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**Analysis of financial risk  
management**

The article describes the main participants of the factoring operations. Disclosed are two main types of factoring, which are widespread in Kazakhstan: factoring with recourse and non-recourse factoring. Analyzed types of factoring operations risks. The author analyzes the main activities of factoring companies in terms of the need to minimize the risks. In Kazakhstan, along with banks, which are reluctant to provide factoring services, as has its own banking products, have already appeared the first specialized factoring companies. Subjects of small and medium-sized businesses with stable debit payments, interested in urgent funding cash shortages. However, factoring potential is not fully used. There are two main problems hindering the development of factoring in Kazakhstan. The first is the low awareness of the business opportunities of factoring transactions, the second – in the absence of state support. Both problems are interrelated.

**Key words:** factoring, risk management, financial market, the methods of minimizing risks.

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**Қаржылық тәуекелдерді  
басқару, талдау**

Мақалада автор тәуекелдерді азайту қажеттілігі тұрғысынан факторингтік компаниялардың негізгі қызметін талдайды. Қазақстанда өз банктік өнімдері бар, факторинг қызметтерін қамтамасыз ету үшін құлықсыз банктерге, бірге қазірдің өзінде алғашқы мамандандырылған факторингтік компаниялар пайда болды. Шұғыл қаржыландыру қолма-қол ақша тапшылығы мүдделі тұрақты дебеттік төлемдер отырып, шағын және орта бизнестің субъектілері. Алайда, факторингтік әлеуеті толық қолданылмайды. Қазақстанда факторинг дамуына кедергі екі негізгі проблемалар бар. Мемлекеттік қолдау болмаған кезде бірінші факторингтік операциялардың бизнесмүмкіндіктері, екінші төмен хабардарлығы болып табылады. Екі проблемалар өзара байланысты болып табылады.

**Түйін сөздер:** факторинг, тәуекелдерді басқару, қаржы нарығы, тәуекелдерді барынша азайту әдістері.

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**Анализ управления  
финансовыми рисками**

В статье были рассмотрены основные участники факторинговых операций. Раскрыты два основных типа факторинга, которые широко распространены в Казахстане: факторинг с правом регресса и факторинг без регресса. Проанализированы виды рисков факторинговых операций. Автором проанализированы основные направления деятельности факторинговой компании с точки зрения необходимости минимизации рисков. В Казахстане, наряду с банками, которые не очень охотно оказывают услуги факторинга, поскольку есть собственные банковские продукты, уже появились первые специализированные факторинговые компании. Субъекты малого и среднего бизнеса, имеющие стабильные дебетовые платежи, заинтересованы в срочном финансировании кассовых разрывов. Однако факторинговый потенциал пока используется не полностью. Есть две основные проблемы мешающие развитию факторинга в Казахстане. Первая заключается в слабой информированности бизнеса о возможностях факторинговых операций, вторая, – в отсутствии государственной поддержки. Обе проблемы взаимосвязаны.

**Ключевые слова:** факторинг, риск-менеджмент, финансовый рынок, методы минимизации рисков.

## **ANALYSIS OF FINANCIAL RISK MANAGEMENT**

Factoring as a financial instrument for business began the formation in Kazakhstan not so long ago. This type of operation provides collection of receivables of the client, crediting and a guarantee from currency and credit risks. Practice showed that factoring proved as the effective tool for financing of small and medium business. According to the experts International Factors Group, it is possible to estimate volume of the Kazakhstan market of factoring at \$2 billion. Services of factoring assume fast receiving the most part of payment on debts, decrease in expenses on maintaining accounts, improvement of control of receivables. Thus the factoring structure (bank or the company) plays a role of the credit manager, operating risks on this service, the account and collection of accounts payable and control over the payment scheme of the debtor.

In the conditions of the competition the factoring companies expand the range of offered products, and the organizations representing other segments of the financial market (for example, insurance companies, banks, collector agencies, etc.), start to develop the specialized directions for mutually beneficial cooperation with the factoring companies. Thus, naturally, there is a need for a return assessment from investments and efficiency of activity in the factoring market, to carry out which it is impossible without an assessment of the corresponding risks. Absence of significant researches on the matter even more raises a problem urgency. First of all, we will list the main participants of factoring operation (see drawing 1). In the standard transaction participate a factor (the factoring company or bank), rendering services to the client, the client and his buyers receivables on which the client transfers to a factor. Two main types of factoring are widespread in Kazakhstan: factoring with recourse and factoring without recourse. In the first case a factor, without having received in time payment from buyers – debtors, has the right after a certain period (so-called preferential) to demand duty payment in the full size from the client (the supplier to whom financing was provided). Respectively, as recourse with reference to factoring understand the right of the return requirement of a factor to the supplier in case of insolvency of the debtor.

In case of factoring without recourse (sometimes it call factoring with the guarantee) the factor takes up all risks connected with

non-payments. The factor can involve the insurer and insure a part of risk of non-payment. It is natural that this scheme is more risky for factoring, and as a result, factoring cost for the client is quite high.

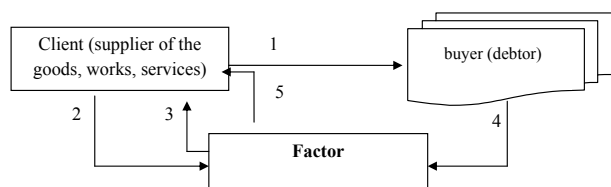


Figure 1 – The scheme of factoring services

It is also important to note the substantial differences in the factoring and its main «competitor» – credit. In lending transactions are only two players (the lender and the borrower), while the factoring of a minimum of three (the client, the creditor and the debtor). The recipient of the money when factoring is one person – the customer (supplier), and their return by another person (the buyer). Thus, the time for completion of the factoring operation is always associated with the term of execution of the transaction for the sale of goods with deferred payment. In principle, the actual user of the loan is the buyer of goods, since it was he interested in obtaining trade credit. Taking the goods, he becomes a debtor in relation to the supplier, who in turn assigns the factor of the right to receive money due to him. This is reflected in the formation of specific risk factors in the provision of factoring services.

Besides, within factoring operation there are risks, not characteristic for crediting. The main difference of factoring from the credit is distribution of a source of credit risk between the client and the buyer whereas when crediting it arises only from the borrower.

So, we will list main types of risks for participants of the factoring transaction. Risks of the factoring company:

1) Credit risk (risk of a non-payment) which source is either the buyer or the client (in case of presentation to it recourse)

2) Risk of loss of liquidity from – for untimely payment of the buyer or the client

3) The risk of fraud caused by difficult structure of the factoring transaction that complicates the full preliminary analysis of all his participants.

The main risks of factoring operations: del credere risk, currency and political. The risk due to the possibility of default del credere / incomplete or late repayment due to dishonesty or breach of the

buyer's solvency or exporter contract conditions (in the case of international factoring). Parties to the transaction face two major types of risk: credit risk and liquidity risk. Credit risk means that the participants in the transaction may not obtain payment of a monetary demand. This risk usually arises when a participant becomes (in the case of factoring, accounts receivable, or a client, which is also important when factoring with recourse).

The risk of liquidity is a risk of that the party – the debtor can't carry out of the obligations in due time, having worsened, thus, liquid position of the recipient of means. In case of factoring, the debtor usually is the buyer. The factoring companies face this type of risk most often as according to the developed trading practice of a delay at payment of deliveries with a delay of payment is a commonplace. The factoring company initially allows possibility of a small delay from the buyer called so-called «the technical reasons» i.e. actually standard practice not to pay precisely in time. It should be noted that the risk of liquidity only in the presence of a number of additional circumstances can develop into credit risk.

Currency risks are caused by change of exchange rates that leads to losses when translating means from currency of the buyer in currency of the seller. Now all calculations between the Kazakhstan companies it is carried out to tenge therefore the currency risk can arise only at transactions of the international factoring. Political risks are connected with impossibility to execute the export contract or to carry out calculations for it from – for changes of a political situation in the country of the seller or in the country of the buyer.

It should be noted that for the factoring business as a sphere characterized by the same risks as the business services sector. All risks of business, depending on the factors influencing their occurrence can be divided into external and internal. External risks from macroeconomic factors, in the case of factoring businesses do not differ fundamentally from those that arise under any other business. To a large extent we are interested in specific internal risks.

So, risks are identified, the following stage is their assessment. As it was already noted, specifics of factoring transactions is that risks proceed not only from the borrower (plus external risks), as in usual crediting, but also also from the client, which can appear unfair, not execute the contract provision with the buyer etc. Therefore it is necessary to estimate all these risks in aggregate. One of weak lines of a risk management of many factoring

companies is that at the conclusion of the contract with the client they, first of all, estimate his own reliability and solvency, without giving sufficient attention to quality of transferred receivables.

For a start on available for the supplier or bank to statistics of payments the payment discipline of the debtor is estimated. The probability of failure to pay of debt can be measured as a share of unpaid accounts ( $S_{unpaid}$ ) in total of the conceded accounts ( $S$ ) in a money equivalent:

$$P(\text{unpaid}) = S_{unpaid}/S, \quad (1)$$

The probability of delay of payment is estimated similarly: a share of back payments ( $S_{delayed}$ ) in total of the conceded accounts in a money equivalent:

$$S(\text{delayed}) = S_{delayed}/S, \quad (2)$$

To carry out such appraisal expediently concerning each debtor. Than more share of back payments, subjects a high probability of that at the debtor can arise problems with repayment of the obligations. For calculation of probability of this event it is possible to determine by each client for a number of the periods specific weight of accounts on which there were refusals of payment from debtors for the specified reasons, and also growth rates of number of such accounts. If there is a tendency to growth of unpaid accounts or rates of their growth advance growth rates of total number of accounts, with this client it is necessary to recognize carrying out factoring operations inefficient. So, because of the supplier it is possible to define probability of non-payment as follows:

$$P(\text{supplier}) = N_{\text{deviation}}/N, \quad (3)$$

where  $N$  – total number of deliveries,

$N_{\text{deviation}}$  – number of deliveries on which there were refusals of payment because of the supplier.

The probability of a non-return of the credit will develop of probability of bankruptcy (insolvency) of the debtor, probability of default by the supplier of contract provisions and probabilities of a default for the external reasons not depending on the parties:

$$P(\text{not return}) = P_{\text{unpaid}} + P_{\text{supplier}} + n, \quad (4)$$

It should be noted that the reason for non-repayment of debt the debtor may also be a fraud

on his part, and from the supplier. To assess the likelihood of fraud is difficult to quantify, but qualitative assessment can be obtained by studying the firm's reputation and client companies debtors. Due to the fact that not all factoring companies and even banks have accumulated enough statistical base of clients and their customers to assess credit risk and liquidity risk is also proposed to use traditional methods for assessing the solvency of the debtor, such as rating and expert methods. The credit rating is made by evaluating the financial condition of the borrower (his solvency and financial stability) on the basis of financial statements (balance sheet, income statement). The main criteria of insolvency, which characterize the structure of the balance sheet are as follows: the coefficient current liquidity ratio of own funds, and the coefficient of restitution (loss) to pay. Based on the above system parameters can be estimated probability of insolvency of the company (Table 1).

1) Current ratio is calculated as follows:

$$\text{Current ratio} = \text{current assets}/\text{short-term obligations}, \quad (5)$$

i.e. as relation of size of current assets to size of short-term obligations;

2) The factor of security is defined by own current assets as the relation of own current assets to the sum of current assets:

$$\begin{aligned} \text{Factor of security with own current assets} &= \\ &= \text{Own current assets} - \text{Non-current assets} / \text{current} \\ &\quad \text{assets}, \end{aligned} \quad (6)$$

3) If at least one of the above-stated factors matters, indicating on an inadmissible or high risk level, the factor of restoration (loss) of solvency pays off. It is defined as follows:

$$\text{Factor of solvency} = FCLB + Y/T(FCLB - FCLE)/2, \quad (7)$$

where  $FCLE$  – value of factor of the current liquidity for the end of the reporting period,  $FCLB$  – value of factor of the current liquidity for the beginning of the reporting period,  $T$  – duration of the reporting period in months,  $Y$  – the period of restoration (loss) of solvency. At calculation of factor of restoration of solvency of  $Y =$  to 6 months. At calculation of factor of loss of solvency of  $Y =$  to 3 months. In the analysis of data of the annual reporting duration ( $T$ ) is accepted to equal 12 months, for the first quarter – to 3 months etc.

**Table 1** – Assessment of solvency of the buyer

Indicator	Meaning	Quality assessment	Quantitative assessment
Factor of the current liquidity (1)	<1	Inadmissible risk	50-100%
	From 1 to 1,5	High risk	10-50%
	From 1,5 to 2	Moderate risk	5-10%
	>2	Low risk	1-5%
Factor of security with own current assets (2)	<0,1	Inadmissible risk	50-100%
	From 0,1 to 0,4	High risk	10-50%
	From 0,4 to 0,7	Moderate risk	5-10%
	>0,7	Low risk	1-5%
Factor of restoration (loss) of solvency (3)	<1	Inadmissible risk	50-100%
	From 1 to 1,2	High risk	10-50%
	From 1,2 to 1,5	Moderate risk	5-10%
	>1,5	Low risk	1-5%

Thus, if value of one of the two first factors is lower standard, and the factor of restoration of solvency accepts value less than 1, the structure of balance of the enterprise can be recognized unsatisfactory, and the enterprise – insolvent.

In this case the cumulative indicator of credit risk will represent average these indicators. If to consider them as equivalent, level of credit risk will be their arithmetic-mean. For an assessment of credit risk and risk of liquidity it is possible to calculate also growth rates of non-payments (back payments) and to compare them to growth rates of payments as a whole (if the first above, the situation becomes complicated).

If all levels of separate risks expressed as a percentage (i.e. probabilities) are known, it is possible to calculate the general level of risks of the factoring transaction which will represent the following:

$$P_{\text{fact.}} = (P_{\text{s.t.}} + P_{\text{liq.}}) P_{\text{curr.}} P_{\text{per.}} P_{\text{curr.}} P_{\text{polit.}}$$

$P_{\text{legisl.}}$   $P_{\text{operat.}}$ ,

Let's try to analyses from the point of view of need of minimization of risks the main activities of the factoring company:

- Fond;
- Risk management;
- Internal business – processes;
- IT providing;
- Marketing;
- Sale and regional network;
- Personnel.

As the main components of competitiveness factoring the companies act as IT – providing, internal operational processes, system risk – management, cost of monetary resources. Cost of

monetary resources is the main element of prime cost of factoring products. Finally it defines the price of a factoring product, so, and competitiveness of the factoring company to the sphere of sales. IT providing and internal operational processes form key competitive advantages on each factoring product at a stage of its creation, sale and service.

The system risk – management also is of great importance, as principles of a risk management define, what products the company can offer the clients.

Main ways of minimization of risks of the current activity of the factoring company it: Use of three-level model of a risk management; Creation of multilevel system of decision-making; Automation of processes; Flexible regulation of working conditions with the client; Application of scoring -rating model of an assessment of clients and debtors; Division of operational and strategic functions of client service.

Application of three-level system of a risk management provides control and the analysis of actions of the client at all stages of existence of a factoring product. At a stage of sales this function is carried out originally by the seller, then risk manager, and at a stage of service of the client – the manager on clients and risk manager.

The multilevel system of the decision-making, concerning interaction with the client and transaction parameters, allows to minimize risk of the wrong assessment. At an initial stage the analysis of the transaction is carried out by the seller, then risk – the manager, the final decision is accepted jointly with participation of the management of factoring division.

Automation provides a choice and control of the specialized factoring software for maximum quantity processing business – processes that will allow to reduce service terms to clients and will reduce probability of the mistakes resulting influence of a human factor. The specialized software allows to automate the majority of stages of the factoring transaction.

As shows world experiment, in providing the enterprises with fast and short working capital factoring just is engaged. In Kazakhstan, along with banks which not so willingly render factoring services as there are own bank products, already there were first specialized factoring companies. The subjects of MSB having stable debit payments, interested in urgent financing of the cash gaps became their clients.

However the factoring potential while is used not completely. There are two main problems disturbing to development of factoring in Kazakhstan. The first consists in weak awareness of business on the factoring possibilities, the second as it was noted, – in absence of state support. Both problems are interconnected.

That business, especially in regions, knew about factoring more, it is necessary to open

regional representations, to carry out explanatory work. All this demands additional resources which developing subjects of factoring simply don't have. As participants of a meeting, by big incentive for development of factoring both in Russia specified, and in Kazakhstan absence of regulation is from a financial regulator. Because the factoring companies, unlike banks, shouldn't carry out standards for sufficiency of the capital, they have good possibilities to finance current assets, demand on which from real sector the very big. Benefit of factoring at the correct use is obvious to MSB – the company spends the received means on purchase the new goods or raw materials at the expense of what can increase considerably sales volumes of finished goods, thus his buyers will receive a desirable delay of payment. At the same time, at interest of the client, the factoring company can take up risks of a non-payment of delivery from the debtor, i.e. actually insure the client from financial losses. The bank credit of such possibility of MSB won't give.

As a whole, development of factoring will promote in many respects to decrease in dependence of MSB from bank crediting. And also to competition strengthening in financial sector that will favorably affect quality of its development.

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