ISQ Examination - Summer-2013
Lending: Products, Operations and Risk Management - Stage- II

Q. The following information is extracted from the latest audited Balance Sheet of Bank 'X':

Surplus/Deficit on Revaluation Reserve (Fixed Assets)	Rs.400 million (Cr.)
Paid up capital	Rs.2,000 million
Reserves	Rs.1,700 million
Un-appropriated profit	Rs.500 million

Note: The exposure should be calculated on the basis of prevailing limits.
Assume that all other terms and conditions are conducive.

With the help of the above information, compute the following:

A. Total equity of the bank

B. Per party exposure limit

C. Group exposure limit which Bank 'X' can allocate to a client, or a single/ group.

Q. A. Discuss the difference between primary security and secondary security.

Q. B. List at least THREE secondary securities against working capital finance, specifying the risks associated with each type of security.

Q. A. Discuss the SBP regulation concerning write off of loans.

Q. B. What is the Prudential Regulation stipulation for reversal of provision when cash recovery is made from a delinquent borrower?

Q. A. Define the following:

I. Hypothecation
II. Mortgage
III. Lien
IV. Floating charge
V. Pledge agreement
VI. Guarantee
VII. Trust Receipt

Q. B. Which of the above is the most secure form of collateral? P provide TWO reasons for your answer.

Q. A trading house has approached your bank for a working capital finance of Rs.15 million. To scrutinize their finance requirements on the basis of cash flows, the prospective borrower was asked to furnish selected information based on projected sales and expenses for the coming year. The trading house has furnished the following data:

Revenue

i) Projected sales (credit) for next year:

1st quarter	Rs. 50 million
2nd quarter	Rs. 60 million
3rd quarter	Rs. 80 million
4th quarter	Rs.100 million

ii) Credit sales – collection pattern:

a. 25% of each quarter sale would be collected during the same quarter.
b. 75% of the balance in the following quarter.

Disbursements

i) Cost of goods sold would be 75% of the amount of sales.
a. 50 % of the cost of goods sold would be paid in the same quarter
b. the remaining 50% in the following quarter.

ii) Operating expenses :

1st quarter	Rs.10 million
2nd quarter	Rs.12 million
3rd quarter	Rs. 8 million
4th quarter	Rs.10 million

iii) Level of minimum cash balance to be maintained Rs.500,000 during each quarter.

iv) No injection or withdrawal of funds by the owners/proprietor during the year.

Required:

A. Prepare projected cash flows of the entity showing receipt and disbursement of funds during each quarter and the shortfall for each quarter separately.

B. If the bank’s policy permits financing to the extent of 50% of the total funds needed during the year, what amount of finance can be extended to the client. Adjustment to the extent of 10% plus minus is admissible. Amount of finance offered to the client may be rounded up in millions.

Q. Waheed Brother has been in the towel manufacturing business since the last 20 years. Your bank has a satisfactory working relationship with them on the trade side for the last 5 years. You have been pursuing them to take a loan from your bank and the company has finally agreed and has sent you the following financial statement:

Waheed Brothers

Assets	(PKR million)
Cash & Cash Equivalents	4,000
Accounts receivable	7,000
Inventory	5,000
Operating Fixed Assets	18,000
Other Assets	5,000
Total Assets	39,000
Liabilities & Stockholder's Equity	
Accounts payable	4,000
Notes payable	7,000
Bonds payable	13,000
Capital	11,000
Retained Earnings	4,000
Total Liabilities & Stockholder's Equity	39,000
Sales	60,000
Cost of Goods Sold	41,800
Gross Margin	18,200
Operating Expenses	
Selling Expenses	9,000
Administrative expenses	4,000
Interest expenses	2,000
Income Tax	1,800
Total Operating expenses	16,800
Net Income	1,400

A. What are your observations on the operating cycle of Waheed Brothers? Please calculate at least 3 ratios in support of your answer.

B. What are your observations on the profitability of the business? Please calculate at least 2 ratios in support of your answer.

C. What are your observations on the gearing and liquidity of the company? Please calculate at least 2 ratios in support of your answer.

D. Based solely on the above analysis, would you lend to Waheed Brothers? If yes, please detail the terms. If no, why not?

Q. You are a credit analyst at Janoobi Bank and you receive an approved credit memo from your Departmental Head with a note saying, “Please process the loan after building appropriate loan covenants/terms.”

You read the credit memo, the salient features of which are:

- The company is a tyre manufacturer and has been in business for the last 7 years but is a new customer for the bank.
- The company has recently expanded its capacity and is now looking to export to East African countries apart from sales to Europe.
- The company allows a dividend of PKR 25 million from business every year but has not done so in 2012.
- Market check of the customer has not been documented.
- Financial snapshot is as under:

Liabilities	**2012**	**2011**	**Assets**	**2012**	**2011**
Accounts Payable	324,000	145,600	Cash	7,282	9,000
Notes Payable	720,000	200,000	Short Term Inv.	20,000	48,600
Accruals	284,960	136,000	Accounts Receivable	632,160	351,200
			Inventories	1,287,360	715,200
Current Liabilities	**1,328,960**	**481,600**	Current Assets	**1,946,802**	**1,124,000**
Long Term Debt	1,000,000	323,432	Net Fixed Assets	939,790	344,800
Equity	557,632	663,768			
Total Liabilities & Owners Equity	**2,886,592**	**1,468,800**	Total Assets	**2,886,592**	**1,468,800**

Income Statement	2012	2011
Sales	5,834,400	3,432,000
Cost of Goods Sold	4,980,000	2,864,000
EBIT	17,440	209,100
Interest Expenses	176,000	62,500
Net Income after tax	**(95,136)**	**87,960**

Based on the information provided, you are not comfortable with allowing them credit.

A. Highlight FIVE potential causes of concern.

B. Make the loan covenants to mitigate the causes highlighted above.

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