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CHRISTIAN SERVICE UNIVERSITY COLLEGE
KUMASI, GHANA
CSUC SCHOOL OF BUSINESS
DEPARTMENT OF ACCOUNTING AND FINANCE

SPECIAL SUPPLEMENTARY, 2018/2019 ACADEMIC YEAR

LEVEL 400
CSBF 415: BANK LENDING

AUGUST, 2019 **TIME ALLOWED: 3HOURS**

GENERAL INSTRUCTIONS TO CANDIDATES:

This paper is in three parts. Part A, B and C

1. **Answer only two questions in Part A. Question one and any other**
2. **Answer only one question from Part B**
3. **Answer all questions in part C**
4. **Provide only your index number on the answer sheet**
5. **No question paper should leave the examination hall. Submit both question paper and answer sheet to the invigilator**
6. **A total of 120marks allocated as follows PART A 50marks, PART B 10marks, PART C 60marks.**

Examiner: R. A. Osei

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PART A

Answer only two questions from this part. Question one and any other.

QUESTION ONE

30marks

An organization wants to embark on a project out of which they expect some returns in a years' time. The organization therefore wishes to finance the project through debt. They have approached a bank which has agreed to advance a loan to finance the project. The bank wishes to use the cashflows from the project as collateral. The organization has therefore prepared a project proposal specifying the proposed cashflows from the project for a period of five years. The initial requirement for the project is GHC700, 000.

YEAR	**0**	**1**	**2**	**3**	**4**	**5**
Cashflow GHC (000)	(700)	200	220	250	350	450

The bank is convinced with the proposal and has agreed to give the said amount at an interest of 12% per annum subject to an expert advice. The bank has therefore hired you as a project financial consultant to advice the management of the bank on the financial viability or otherwise of the project. Your findings will help the bank take a decision in the loan advance. Your presentation must be centered on the following financial appraisal techniques stating your reasons in each case

i. Simple payback method
ii. Net present Value (NPV)
iii. Profitability index (PI)
iv. Internal rate of return (IRR)

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QUESTION 2
20marks

Orchestra is a public trading pharmaceutical company in Ghana. The company has provided the ff. financial statement in its application for a loan.

ASSETS	**GH¢ 000**	**LIABILITIES/EQUITY**	**GH¢ 000**
Cash at bank	50	Trade payables	52
Trade receivables	60	Accruals	34
Stock	105	Short term loan	37
Prepaid expense	20	Long term debt	47
Plant and equipment	145	Share capital	210
Total	**380**	**Total**	**380**

Foot notes	**GH¢ 000**
Turnover	650
Cost of sales	330
Tax	39
Interest payments	37
Net income	50
Dividend payout ratio	55%

Assume the market value of equity is equivalent to its books value

a. As a credit officer of the lending institution, use Altman's linear discriminant model to ascertain the credit worthiness of orchestra pharmaceutical company.

b. Using the answer in *'a'* above should the loan be approved for orchestra pharmaceuticals? Explain your answer.

c. State three criticisms of the Altman's linear discriminant model.

d. i. Using the ***Private firm model***, deduce the ***zone*** in which orchestra pharmaceutical can be found. Explain your answer.

ii. Based on the zone does the private firm model support the conclusion of the Altman's linear discriminant model?

iii. What general conclusions can be drawn from these two models as applied to bank lending?

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QUESTION THREE

20marks

A. Suppose you have a loan of GHC 40,000 with an APR of 5% for 20 years.

i. What will be your monthly payments?

ii. What will be the total interest paid for the entire 20-year period

Suppose you would like to pay off the loan in 10 years instead of the 20 years,

iii. What will be your monthly payment?

iv. What will be the total interest paid for the 10 year period

v. Compare the total amounts you would pay over the course of the loan

B. Mike obtained a loan of GHC 1,000,000 from ABC bank at an APR of 12%. The repayment schedule is for a period of 5 years of equal instalments

i. Calculate the amount per instalment
ii. Prepare a loan amortization schedule for Mike. (*Show working)*
(***Rounding off error allowed***)

PART B

Answer only one question from this section

10marks

QUESTION FOUR

A. One of the risks which lending institutions face in their operations is credit risk. Briefly explain credit risk and show how lending institutions can minimize the occurrence of this risk.

B. Credit ratings of a borrower are of immense significance to lenders. Briefly describe these importance

C. Loans and advances are classified based on certain factors. State and explain four of these factors used in classifying a loan

QUESTION FIVE

A. What is project financial appraisal? Why should lending institutions be so much concerned about project appraisal?

B. Structuring of loans is categorized in three major parts. Briefly describe these parts.

C. Briefly discuss the framework in which lending decisions are taken. (***Diagram not required)***

QUESTION SIX

A. i. Explain risk management in lending

ii.State and explain four types of risk in bank lending

iii.Explain three ways of dealing with these risks.

B. State the steps involved in risk management process of lending

C. In order to originate good quality loans, lenders need to collect relevant and timely information about prospective obligor. The information can either be *hard* or *soft.* Distinguish between hard and soft information as applied to bank lending

PART C

Answer all questions in this section

60marks

1. Differentiate between *direct* and *indirect* financing in the financial system with the aid of a diagram.
2. What is *compensating balance?*
3. State the three attributes of good lending.
4. When is a loan account said to develop a *hardcore?* Briefly explain how it occurs
5. Distinguish between *loan-to-value ratio* and *delinquency ratio in bank lending.*
6. What is the main difference between a *single payment loan* and *instalment loans?*
7. Briefly explain *revolving credit.*
8. State four attributes of a good collateral
9. Give two disadvantages of a loan to lender

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10. What is the main difference between *equity participation* and *equipment leasing* as modern methods of advances.

11. The table below shows the abbreviated forms of some lending principles.

Complete the table by providing the full names of each letter.

Acronym	**Full meaning**
IPARTS	
CAMPARI	
PARSER	
5Cs	
ICE	

12. What is *loan amortization schedule?* Enumerate five information that can be found in a loan amortization schedule

13. Briefly explain the main difference between *moral hazard* and *adverse selection.* How can a lender manage these two problems in lending?

14. Briefly differentiate between *factoring with recourse* and *factoring without recourse.*

15. Enumerate the steps involved in the lending process.

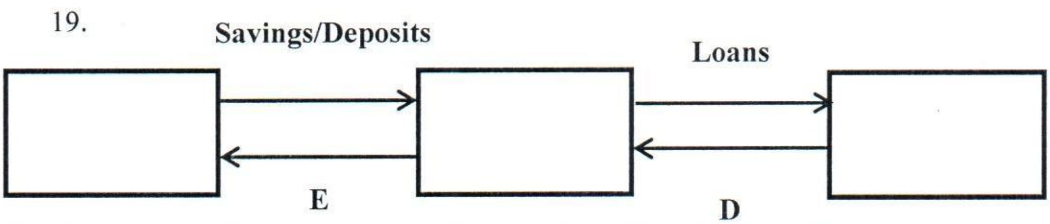
16. What is the main difference between a *loan* and an *overdraft*?

17. What is the main difference between *overcapitalization* and *overtrading* in banking business?

18. i. What is a loan covenant?

ii. Differentiate between *affirmative covenants* and *negative covenants*

19.



Use the process of financial intermediation to identify ***A, B, C and D***

20. A bank lender has a number of aids to assist in monitoring a borrower. Enumerate three of these aids.