



CENTRAL UNIVERSITY COLLEGE

RESIT EXAMINATION: 2016/2017

DEPARTMENT OF BANKING AND FINANCE

CBBF 305

CREDIT MANAGEMENT (3 Credits)

LEVEL 300 (MATAHEKO & MIOTSO)

(MORNING, AFTERNOON, EVENING & WEEKEND)

August 2017

3 Hours

STUDENT ID No.....

INSTRUCTIONS

SECTION A

Answer ALL questions from this section (Answers should be provided on the question paper in the **template supplied on page 4**)

SECTION B

Answer FOUR questions from this section (Answers should be provided in the answer booklet)

DO NOT TURN OVER THIS PAGE UNTIL YOU HAVE BEEN TOLD TO DO SO BY THE INVIGILATOR

SECTION A: ATTEMPT ALL QUESTIONS FROM THIS SECTION (20 marks)

Multiple Choice

Identify the choice that best completes the statement or answers the question.

1. On which one of the following sources do banks lay primary emphasis for repayment of business loans?
 - A. Cash generated from the operations of business.
 - B. Cash from liquidating the business itself.
 - C. Cash from the sale of non-operating assets of the business.
 - D. Cash from additional equity contribution by shareholders

2. "Accounts receivable turnover days" is a calculation that shows:
 - A. The rate at which the company is adding new customers who buy on credit
 - B. The average balance per customer of accounts receivable
 - C. The average number of days it takes to collect the cash related to a sale
 - D. The number of days the business gives its customers to pay its invoices

3. A bank is likely to take security from a borrower under all the following conditions EXCEPT:
 - A. The borrower's leverage is higher than average.
 - B. The borrower's business has only a short track record.
 - C. The proposed facility is medium to long-term.
 - D. The borrower has given a negative pledge to another lender.

4. If a company is suffering from declining gross margins, it could be due to:
 - A. Higher selling prices
 - B. Lower raw material costs
 - C. Lower depreciation expense
 - D. Higher labor costs

5. Which of the following statements is CORRECT?
 - A. Company shareholders are exposed to unlimited liability.
 - B. The sole partner in a partnership is exposed to unlimited liability.
 - C. The liability of a general partner in a partnership is limited.
 - D. The owner of a sole proprietorship has unlimited liability.

6. Which of the following is the LEAST likely to be taken as security from a typical business for a short-term working capital loan?
 - A. Marketable securities
 - B. Machinery and equipment
 - C. Accounts receivable and inventory
 - D. Cash and deposit accounts

7. Which of the following is part of the CAMPARI lending framework?
- A. INTEREST
 - B. CAPACITY
 - C. ABILITY
 - D. RETURN
8. If a company's accounts receivable days decreases from 43 days to 32 days it means that the company is:
- A. Experiencing higher sales volumes
 - B. Overall less liquid than before
 - C. Having to wait longer to collect its receivables
 - D. Collecting its accounts receivable more quickly
9. On the income statement, Gross Profit represents:
- A. Profits before owner salaries
 - B. Sales minus the cost of the goods sold
 - C. Sales minus the company's operating expenses
 - D. Profits before income taxes
10. Which of the following is NOT considered to be part of the "working capital assets" of a business?
- A. Accounts receivable
 - B. Inventory
 - C. Cash
 - D. Manufacturing equipment
11. Which of the following BEST describes the Credit Policy of a bank?
- A. A format for periodic reports to the bank's management on the loan portfolio
 - B. A historical record of the bank's performance in giving out loans to its customers
 - C. A description of the bureaucratic approaches adopted by a bank in giving loans
 - D. A statement of basic guidelines that governs the extension of credit in a bank.
12. "Default risk" is defined as the risk that a borrower:
- A. May not disclose appropriate information to the bank
 - B. Will experience a decline in its operating results
 - C. Sells assets that are important to the bank
 - D. Will not make required payments to the bank
13. Which of the following is a common primary source of repayment for working capital loans?
- A. Equity injection
 - B. Conversion of short-term assets into cash
 - C. Sale of fixed assets
 - D. Liquidation of collateral
14. One of the credit risks of offering an overdraft that is too large is that the company may:

- A. Use the funds for unintended purposes
 - B. Pay a higher rate of interest
 - C. Not have enough money to meet its objectives
 - D. Not use the entire facility
15. Other things remaining equal, if a company's inventory turnover decreases from 63 days to 48 days, it means that the company is:
- A. Overall more liquid than before
 - B. Moving its inventory more slowly
 - C. Waiting longer to pay its suppliers
 - D. Experiencing higher sales volumes
16. Which characteristic given below is NOT a characteristic of an overdraft facility?
- A. It is provided by the bank up to a stated limit.
 - B. Interest is payable only on the overdrawn balance.
 - C. Interest is payable on the total amount of the facility.
 - D. It is granted by the bank for a given period of time.
17. Which of the following could cause a company's inventory turnover to improve?
- A. Higher sales prices
 - B. Better inventory management
 - C. Obsolete inventory
 - D. Expansion of the product line
18. Current assets on the balance sheet of a typical business are those that are:
- A. Listed as "cash" or "cash equivalents"
 - B. Expected to be converted to cash within one year
 - C. Borrowed temporarily from the business owner
 - D. Expected to be collected or sold within 30 days
19. Purchases of fixed assets such as equipment are usually financed through:
- A. Cash on hand
 - B. Commercial mortgages
 - C. Term loans
 - D. Lines of credit
20. In general, all successful managers of businesses need to have all of the following management skills EXCEPT:
- A. Ability to play either golf or tennis well
 - B. Knowledge of the markets, and products
 - C. Communication skills
 - D. Leadership ability

MULTIPLE CHOICE ANSWER GRID

1		11	
2		12	
3		13	
4		14	
5		15	
6		16	
7		17	
8		18	
9		19	
10		20	

SECTION B: ATTEMPT FOUR (4) QUESTIONS FROM THIS SECTION (80 marks)

QUESTION 1 (20 marks)

- a) The extension of credit should follow a laid down policy. Explain what is meant by credit policy. (5 marks)
- b) The issue of overtrading should be of concern to any lending institution or bank when dealing with both its existing and prospective borrowers. As a Credit Officer in a bank evaluating a business customer:
- i. Explain overtrading. (5 marks)
 - ii. State and comment briefly on five (5) of the indicators of overtrading. (10 marks)

QUESTION 2 (20 marks)

- a) A collateral or security better aligns the interests of the lender and borrower and facilitates lending. State four (4) categories of items that can be used as security in lending, giving an example in each category. (6 marks)

- b) The canons or basic principles of lending provide the banker with tried and tested models for credit evaluation. One of the well-known and tested models for lending is the CAMPARI framework. State and explain each of the items that make up the CAMPARI framework. (14 marks)

QUESTION 3 (20 marks)

- a) From experience, one of the key differences between lending to large businesses and small businesses relates to the level of information provided by the business to the lender. Discuss the problem(s) with information provided by the typical small business to a lender, and the challenges this poses in appraising small business credits. Provide examples. (4 marks)
- b) Discuss the importance of four (4) of the following factors in appraising small business credits.
- i. The owner(s) of the business
 - ii. The physical and production resources of the business
 - iii. The profitability of the business
 - iv. The cash flow of the business
 - v. The capital resources of the business
- (16 marks)

QUESTION 4 (20 marks)

- a)
- i. "If loans are not properly managed, the efforts invested in the initial credit analyses and the decisions to grant them may be wasted". Discuss this statement. (4 marks)
 - ii. List four (4) major sources of information that a bank may use for monitoring its borrowers and the loans in its loan portfolio. (4 marks)
 - iii. Identify four (4) early warning signs that may arise from loan monitoring to indicate that a loan is deteriorating. (4 marks)
- b) Explain the following terms in relation to credit risk:
- i. Asymmetric information (4 marks)
 - ii. Adverse selection. (4 marks)

QUESTION 5 (20 marks)

- a) Review each of the scenarios described below and provide the following:
- i. An appropriate type of credit facility for the prospective borrower and suggested repayment period. Explain why.

- ii. The expected primary source of repayment of the proposed facility.

Scenario 1

A manufacturer of household textiles (towels, table napkins etc.) occasionally needs bank financing to support its receivables and inventory for short periods of time

(4 marks)

Scenario 2

The owner of a beauty shop and salon has been offered the opportunity to buy the building in which it is located, and intends to carry out significant renovations

(4 marks)

Scenario 3

A local catering company specializing in corporate events is seeking financing to support its activities for its corporate clients during the busy period just before the companies break for the Christmas holidays. The caterer expects to be paid by its clients by the end of January in the new year.

(4 marks)

- b) Discuss four (4) key qualities of a good security to back a lending proposition.

(8 marks)