

POKHARA UNIVERSITY

Level: Bachelor
Programme: BBA-BI
Course: Credit Risk Management

Semester: Spring

Year: 2021
Full Marks: 100
Pass Marks: 45
Time: 3 hrs.

Candidates are required to answer in their own words as far as practicable. The figures in the margin indicate full marks.

Section "A"

Very Short Answer Questions

Attempt all the questions. [10×2]

1. Why credit information is important in lending process?
2. Differentiate between fixed term and working capital loan?
3. Define the term "Credit Committee".
4. What does an increase in the average collection period suggest?
5. Define the term "Credit Scoring"?
6. What do you mean by KYC & why its important?
7. How Ussance LC is different from Sight LC?
8. List out the methods of creating charge over securities.
9. Highlight the characteristics of residential mortgaged loan.
10. What are the indicators of credit risk?

Section "B"

Descriptive Answer Questions

Attempt **any six** questions. [6×10]

11. What are the principal of lending activities? Also discuss about structuring commercial loan agreements.
12. How asymmetric information play role in lending decision making in competitive environment.
13. What are the characteristics of mortgage loan? Elaborate the alternative mortgage instruments in lending process.

OR

Define the commercial real estate and differentiate it from residential mortgage loan.

14. Explain various types of consumer and business loans offered by Nepalese banks.
15. Explain the indicator of problematic loan and what measures / mechanism can be taken for monitoring problem loans.
16. What is credit scoring and how its used in commercial lending?

17. Following are the projected financial information relevant to business of loan applicant:

Sales	500M
Total Asset	600M
Total Equity Capital	200M
5% Long term Loan	200M
Short term loan	100M
Other interest free loan and Liabilities	100M
Income Tax	20M
Net Profit	60M

Suppose that the application is for short term loan of Rs.100M and interest rate is 10%. Bank is very strict in evaluating the loan application. It doesn't grant the loan if applicant does not meet any of following Financial Criteria

ROA	5%
ROE	20%
Debt service Ratio	4 times
Profit Margin	10%

Section "C"

Case Analysis

18. *Read the case situation given below and answer the questions that follow:*
[20]

How are the lending practices of banks in Nepal today different from traditional moneylenders? i.e. taking pledge of assets and extending loans, irrespective of the borrower's capacity to pay. In fact, the money lenders wish the borrowers to default, so that they can take possession of pledged assets, at negligible cost. Banking is said to be a specialized business or process, run under certain norms. Do the banks in Nepal follow the same prudential norms that are followed universally? While it may be difficult to validate, there are strong suspicions that not all banks in Nepal adhere to prudential practices.

The basic philosophy of lending is primarily to assess the borrower's "ability or capacity to pay" and "willingness to pay" aspects. The entire credit process revolves around these two fundamental questions. There are numerous credit tools available to determine the 'capacity to pay' aspect viz assessing the historical financials of the borrowing company, business risk, industry risk, management risk, past track record of the borrower and the bank's judgment on their future prospects/projections, which establishes their ability to repay the debt.

However, there are limited tools to test the willingness to pay aspect. Many

cases of default may be caused by the inability to manage the underlying risks as originally envisaged, which is though a normal scenario since banks are in the risk business. As opposed to this, if a borrower utilizes the loan proceeds for purposes other than the approved one, with the intention of willful default it may trigger the 'willingness to pay'. Hence, the willingness to pay aspect characterizes the credibility of the borrower. Any prudent banker would not normally want to deal with people, having questionable integrity, at any cost.

The credit officer should be able to assess all the risks inherent to subject credit, weigh the borrower's strengths and weaknesses and find reasonable mitigants before arriving at a decision to lend. There should be a control mechanism to ensure that the borrower utilizes the funds for the intended purpose and a proper mechanism should be in place, to monitor the performance of the borrower. The loan should be self-liquidating in nature. For instance, if the loan is extended against any specific receivable or sales proceeds the same should repay the loan and not through the sale of property or other sources, where the repayment becomes uncertain.

- a) How are the lending practices of banks in Nepal today different from traditional moneylenders?
- b) What factors need to be considered while analyzing the credit worthiness of borrower?
- c) As a lender what types of ratios a bank needs to analyze before granting loan to business? Explain