

DP08

Retail Financial Services

13 APRIL 2005

1. Time allowed : Three (3) hours
2. Total number of questions : Six (6) questions
3. Number of questions to be answered : Five (5) questions
Part A : Three (3) questions [20 marks each]
Part B : Two (2) questions [20 marks each]
4. Show details of workings, where appropriate. Silent, non-programmable calculators may be used.
5. Begin each answer to a new question on a fresh page.
6. Answer **all** questions in **English**.
7. Blank pages are provided at the end of the question paper for rough work.

PART A

ANSWER ALL THREE (3) QUESTIONS

1. (a) Bank Bagus Bhd approved a housing loan for En Nizam. The loan of RM200,000 was fully drawn down on 1 August 2004 with the final progressive release of 5.0% amounting to RM10,000.
- (i) Calculate the interest payable for the month of July 2004, assuming that the interest rate charged by the bank was 5.0%. [3]
- (ii) Calculate the interest payable for the month of August 2004, assuming that the interest rate charged by the bank after full drawdown was 6.5%. [3]
- (b) What are the differences in the repayment schedule of a fixed (term) loan and an overdraft? [5]
- (c) State **three** disadvantages of using unquoted shares as collateral. [3]
- (d) (i) Briefly describe **three** common types of share financing facilities offered by a financial institution. [3]
- (ii) What are **three** options available to a borrower when fluctuation in share prices causes a breach of the security margin? [3]

(Total:20 marks)

2. (a) The following are the Balance Sheet and Income Statement of Maximus Sdn Bhd (Maximus) as at 31 July 2004:

BALANCE SHEET AS AT 31 JULY

Item	2004 RM'000	2003 RM'000
Non-current assets		
Property, plant and equipment	26,430	27,814
Investment in associate	566	755
	26,996	28,569
Current assets		
Inventories	20,990	19,941
Trade receivables	11,118	8,643
Other receivables	1,308	966
Tax refundable	905	1,370
Cash and bank balances	32,408	31,274
	66,729	62,194
Current liabilities		
Trade payables	5,524	2,103
Other payables	3,691	3,632
	9,215	5,735
Net current assets	57,514	56,459
	84,510	85,028
Financed by:		
Share capital	44,405	43,673
Reserves	37,504	38,758
Shareholders' equity	81,909	82,431
Deferred taxation	1,375	1,402
Minority interests	1,226	1,195
	84,510	85,028

INCOME STATEMENT FOR THE YEAR ENDED 31 JULY

Item	2004 RM'000	2003 RM'000
Revenue	46,575	52,301
Other operating income	969	1,049
Changes in inventories	(527)	675
Raw materials and consumables used	(26,062)	(28,424)
Purchase of trading inventories	(2,742)	(3,180)
Staff costs	(8,397)	(9,187)
Depreciation	(2,335)	(2,283)
Other operating expenses	(4,127)	(4,786)
Profit from operations	3,354	6,165
Share of results of associate	1,133	3,031
Profit before taxation	4,487	9,196
Taxation	(1,567)	(2,440)
Profit after taxation	2,920	6,756
Minority interests	(31)	(6)
Net profit for the year	2,889	6,750
Earnings per share (sen)		
- Basic	6.5	15.5
- Diluted	6.2	14.3

Based on the financial statements provided, compute the following financial ratios for Maximus for years 2003 and 2004:

- (i) Current ratio [2]
 - (ii) Net profit margin [2]
 - (iii) Gearing ratio [2]
 - (iv) Stock turnover days [2]
- (b) Based on the financial ratios calculated in (a) above, comment on the performance of Maximus and state whether you would recommend for an increase in credit facilities for Maximus. [5]
- (c) Apart from financial analysis, what other factors would you take into consideration when evaluating a credit proposal for additional credit facilities? [7]

[7]
(Total:20 marks)

3. (a) Chong bought a new car costing RM100,000 from a dealer. Your bank is agreeable to provide a 90% margin of finance with an interest rate of 3.0% per annum for a nine-year term under hire-purchase.
- Calculate the following:
- (i) Term charges [3]
 - (ii) Monthly instalment [2]
 - (iii) Statutory rebate, assuming that Chong settles the hire-purchase agreement at the end of the fourth year [3]
 - (iv) Early settlement amount at end of the fourth year, assuming that there is no overdue interest [3]
- (b) An owner may allow a hirer to assign the right, title and interest of the goods under the hire-purchase agreement to a third party. Under section 12(4) of the Hire-Purchase Act 1967 (HPA), the owner can impose three conditions when giving consent for the assignment.
- What are these **three** conditions? [3]
- (c) Where the value of the goods at the time when it is returned to the owner is more than the balance outstanding under the hire-purchase agreement, the hirer is entitled to the difference from the owner.
- State the formula under section 14(1) of the HPA to calculate the net balance outstanding under a hire-purchase agreement. [3]
- (d) A hirer can regain possession of the goods within 21 days after the repossession if the hirer gives a notice to the owner.
- State **three** conditions under section 19 of the HPA that the hirer must comply with before he can regain possession of the goods. [3]
- (Total:20 marks)

PART B

ANSWER TWO (2) QUESTIONS ONLY

4. (a) (i) Briefly describe **three** main benefits of electronic banking services to each of the following:
- (aa) Customers [3]
 - (bb) Banks [3]
- (ii) Briefly describe **two** disadvantages of electronic banking from a bank's point of view. [4]
- (b) State the key differences between a financial lease and an operating lease in respect of the following:
- (i) Length of the lease tenure [2]
 - (ii) Type of equipment leased [4]
 - (iii) Recoverability of cost of the leased asset over the lease period [4]
- (Total:20 marks)

5. (a) The National Agricultural Policy (NAP3: 1980-2010) outlines the strategies to make agriculture a vibrant economic sector and a growth engine of the Malaysian economy.
State any **four** of these strategies. [8]
- (b) Briefly describe **four** ways how banks can promote the development and growth of Small- and Medium-sized Enterprises in Malaysia. [8]
- (c) (i) Name **one** trade service and state its purpose. [2]
(ii) Name **one** trade financing product and state its purpose. [2]
(Total:20 marks)
6. (a) Briefly describe **three** types of Internet banking services offered by banks. [6]
- (b) Using a diagram, illustrate a hire-purchase transaction and state the role of each of the **three** parties involved in the transaction. [7]
- (c) Briefly describe the differences between an assignment and a charge in the security documentation for a housing loan. [7]
(Total:20 marks)

OUTLINE ANSWERS

The comments given in the boxes below indicate the areas of weaknesses the examiners have identified and their advice to future candidates.

Question 1

Candidates did not know the principles behind the acceptance of unquoted shares as collateral and types of share financing facilities available.

1. (a) (i) Interest (July)
= P x T x R
= 95% X 200,000 X 31/365 X 5%
= RM806.85
- (ii) Interest (August)
= P x T x R
= 200,000 x 1/12 x 6.5%
= RM1,083.33
or
= $\frac{200,000 \times 31 \times 6.5\%}{365}$
= RM1,104.11
- (b) Fixed (term) loan
- Amount and due date of all repayments can be determined at the beginning of the loan and instalments tailored to suit the circumstances of the borrower.
- Overdraft
- Repayment can be made anytime without giving any notice to the lender. Amount prepaid can be redrawn up to the approved limit.
- (c) Disadvantages of unquoted share as collateral:
- Difficult to establish its value
 - Difficult to find a buyer (normally pre-exemption rights given to existing shareholders)
 - Only equitable mortgage is possible. Right to transfer share may be restricted by Articles of Association.
- (d) (i) **Three** types of share finance facilities:
- New public issue – a line of credit will be given where the financier will provide funds up to the full value of the cost of the issued price of the shares applied for.
 - Purchase of shares – the financier will provide funds up to an agreed percentage of the market value of the shares to borrowers who want to buy quoted/unquoted shares or take up an offer of shares during rights issue.
 - Margin account – the financier will provide a line of credit between 1.5 to 3 times will be extended to the borrower based on the value of the security pledged.
- (ii) **Three** options available to borrowers:
- Top-up the shortfall (put in more cash to reduce balance outstanding).
 - Put in additional securities acceptable to the financier.
 - Sell part of the existing holdings to reduce the balance outstanding.

Question 2

Candidates had difficulties in computing the more advanced financial ratios (i.e. gearing and stock turnover) and interpreting financial ratios to comment on the company's performance to recommend for an increase in credit facilities.

- 2 (a)
- | | <u>2003</u> | <u>2004</u> |
|-------|---|--|
| (i) | Current ratio
= Current assets/Current liabilities
= 62,194/5,735
= 10.84 | Current ratio
= 66,729/9,215
= 7.24 |
| (ii) | Net profit margin
= $\frac{\text{Net profit after tax} \times 100\%}{\text{Revenue}}$
= $6,756 \times 100\% / (52,301 + 1,049)$
= 12.66% | Net profit margin
= $2,920 \times 100\% / (46,575 + 969)$
= 6.14% |
| (iii) | Gearing ratio
= $\frac{\text{Current liabilities} \times 100\%}{\text{Shareholders funds}}$
= $(5,735/82,431) \times 100\%$
= 6.96% | Gearing (debt-equity) ratio
= $(9,215/81,909) \times 100\%$
= 11.3% |
| (iv) | Stock turnover (days)
= $\frac{\text{Inventory} \times 365}{\text{Cost of goods sold}}$
= $(19,941 \times 365) / (28,424 + 3,180 - 675)$
= 235 | Stock turnover (days)
= $(20,990 \times 365) / (0.527 + 26,062 + 2,742)$
= 261 |
- (b) The performance of Maximus deteriorated in 2004, as reflected by the following:
- Percentage of current assets that can be liquidated at book value declined.
 - A lower gross profit margin denotes that profitability has declined.
 - The rise in gearing ratio denotes an increase debt with creditors.
 - Inventory takes longer to be sold off as the stock turnover days increased by 26 days.
- Therefore, it is not recommendable to approve higher credit facilities for Maximus.
- (c) Factors for consideration:
- Purpose of the loan.
 - Length of company in business, reputation and customer loyalty/relation- ships.
 - Character: conduct of existing accounts and willingness to repay loan.
 - Capital available: willingness to inject more capital and effectiveness of capital management.
 - Capacity: ability of its people to manage business; succession plan.
 - Condition: changes in external economic and industry conditions and demand.
 - Collateral: availability of collateral to be pledged to offset the other 4Cs.

Question 3

- Candidates were not conversant with the calculation of statutory rebate and early settlement amount and could not state the formula to calculate the net balance outstanding under a hire-purchase agreement.
- They also could not state the conditions that a hirer must comply with before regaining possession of repossessed goods and erroneously stated the steps for repossession instead.

3. (a) (i) Purchase price: RM100,000
Amount financed
 $= 90\% \times 100,000 = \text{RM}90,000$
Term charges
 $= 90,000 \times 3\% \times 9$
 $= \text{RM}24,300$
- (ii) Monthly instalments
 $= \frac{90,000 + 24,300}{9 \times 12}$
 $= \text{RM}1,058$
- (iii) Statutory rebate
 $= \frac{60(60 + 1) \times 24,300}{108(108 + 1)}$
 $= \text{RM}7,555$
- (iv) Early settlement amount
 $= \text{Outstanding amt} - \text{Statutory rebate} + \text{Overdue interest}$
 $= [(90,000 + 24,300) - (1,058 \times 48)] - 7,555 + 0$
 $= \text{RM}55,961$
- (b) Section 12 (4) allows the owner giving the consent to impose three conditions:
- Pay up all defaulted instalments.
 - Require the hirer and assignee to execute and deliver to the owner an assignment in an approved form, without prejudicing the continual personal liability of the hirer, the assignee agrees to be personally liable to the owner to pay the instalments remaining and to observe all obligations of the hirer.
 - Pay reasonable cost incurred in stamping and registering the assignment.
- (c) Net balance due is the balance originally payable under the HP agreement *less*:
- Any amounts already paid (except deposit) by hirer.
 - Statutory rebate for term charges.
 - Statutory rebate for insurance, if any contract of insurance is to be cancelled.
- (d) Section 19 allows the hirer to regain possession of the goods after:
- Paying or tendering to the owner any amount due in respect of the period of hiring up to the date of payment/tender.
 - Remedying any breach of the agreement or where he is not able to remedy the breach because the owner has taken possession of the goods, pays or tender to the owner the cost and expenses reasonably and actually incurred by the owner in remedying the breach.
 - Paying or tendering to the owner the reasonable costs and expenses incurred in taking possession of the goods and returning them to the hirers.

Question 4

Candidates could not differentiate between a financial lease and an operating lease.

4. (a) (i) (aa) Benefits to customers
- Convenience of e-channel (24 x 7).
 - Ease of management and integration; consolidation and integration of banking transaction and reporting for financial management.
 - Wider range of services with electronic infrastructure, e.g. ETPOS.
- (bb) Benefits to banks
- Lower transaction costs. Cost based on per transaction lower for smaller value transaction thus enabling banks to concentrate on higher quality/value transaction at the frontline.
 - Consistency/lower error rate. Ensure consistency, speed and accuracy of transactions, lower error rates and risks.
 - Globalisation of banking services. Deliver financial services globally in a cost-effective manner.
- (ii) Risks/disadvantages of technology-based banking (choose any **two**):
- High capital investment – technological obsolescence.
 - Commoditising of banking service and products easily duplicated.
 - High strategic risk – choice of investment in wrong technology.
 - Security risk – clone/duplicated cards and unauthorised access.
- (b) Comparison between financial and operating lease

No.	Item	Financial lease	Operating lease
(i)	Tenor	Long-term	Short-term
(ii)	Type of equipment	Wide range of lease equipment for commercial, industrial and professional uses. Lessor selects the equipment from supplier and submits it for lease finance.	Confined to equipment with high resale/second-hand value, mainly for commercial activities. Not suitable for products easily affected by obsolescence.
(iii)	Cost recoverability of leased assets	Full recoverability; often 100% finance and zero residual rates for full payment lease at end of primary period.	Usually not fully recovered during primary period. Depends on residual value of the equipment to recover balance of net investment and earn profit.

Question 5

Candidates displayed poor knowledge on agricultural financing and common SME financing facilities.

5. (a) Strategies under the NAP3 (choose any **four**):
- Establishment of agro-forestry for sustainable development (forest plantation).
 - The product approach: Producing value-added agricultural products. End product linking and supporting downstream value-added activities to other economic sectors.
 - Food security and inflation control: reduce food import bill.
 - Reverse investment in agriculture in lower cost developing countries.
 - Improve marketing and distribution: direct marketing to end-consumers.
 - New product development through biotechnology and extraction of industrial materials from agriculture.
 - Shift from labour intensive to high tech agriculture, working in a controlled and scientific environment.
 - Set-up agro-technology growth and central incubators.
 - Hub for halal food export to international market.

- (b) Promoting the development and growth of SMEs:
- Develop innovative financial package to cater for SME needs.
 - Undertake in-depth industry research study and selected industry groups promoted by the Government.
 - Package SME loans with other financial schemes e.g. those under Credit Guarantee Corporation financing schemes into loan package to be more competitive.
 - Hold awareness seminars and road shows with SMIDEC to promote SME financing packages.
- (c) (i) Trade services (choose any **one**):
- Import letters of credit issuance.
 - Export letters of credit advising/confirmation.
 - Inward bill for collection (clean/documentary).
 - Outward bill for collection (clean/documentary).
 - Shipping guarantee.

Candidates need to briefly describe the purpose of the service (please refer to pages 147-148 of the DP08 study manual)

- (ii) Trade financing products (choose any **one**):
- Trust receipt.
 - Banker's acceptance.
 - Local bills of exchange purchase documentary.
 - Foreign bills of exchange purchased.
 - Foreign currency trade finance.
 - Export credit refinancing scheme.
 - Bank guarantee.

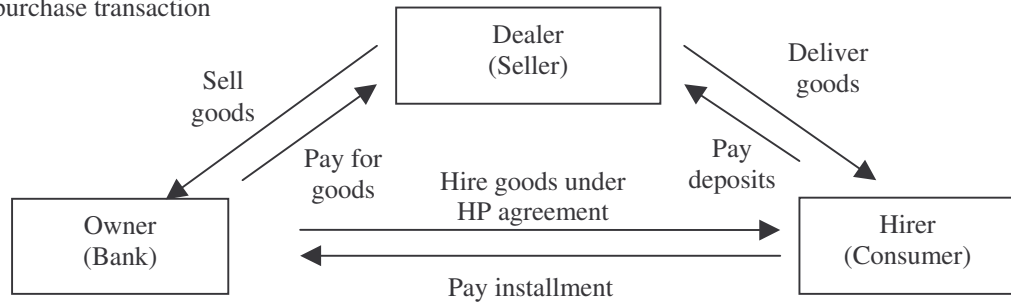
Candidates need to briefly describe the purpose of the product (please refer to page 148 of the DP08 study manual)

Question 6

Candidates were unfamiliar with the security documentation for housing loans involving assignments and charge.

6. (a) Types of Internet banking services
- Informational services – dissemination of information on products and services.
 - Communicative services – communication channel with customers, enquiries, e-mail, customer support services.
 - Transactional services – B2C, B2B transaction services.

(b) A hire-purchase transaction



Hirer – takes goods from owner under HP Agreement.

Owner – let goods to hirer.

Dealer – arrange/negotiate the HP Agreement between the hirer and the owner.

(c) Assignment – a contract in writing whereby the assignor assign all his rights, title and interests in the property to the assignee as security for a loan granted by the lender to the borrower where the master title is not available to be charged. The contractual rights of the assignee under the assignment are subject to any existing registered rights and interests in the master title to the land, to which the assigned property forms a part thereof.

Charge – a transaction or dealing where the registered proprietor of a land or a lease conveys it as security to another for debt repayment or payment of any annuity or other periodic sum. The land must be registered and where the register is clear, the title to the land and the rights of all persons holding leases or charges, once registered, are indefeasible.