

DP08

Retail Financial Services

10 OCTOBER 2001

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. You have been asked by your local consumer association to answer the following questions on the rights of hirers in the event of repossession of motor vehicles financed under hire-purchase.
- (a) How many instalments in default must there be before an owner can repossess his motor vehicle due to non-payment of monthly instalments by the hirer? [4]
 - (b) How many instalments in default must there be before an owner can repossess his motor vehicle if the hirer is deceased? [2]
 - (c) What are the statutory notices to be served on the hirer before the owner can initiate repossession? [4]
 - (d) If a reposessor carries out the repossession, what documents must the reposessor produce to identify himself? [4]
 - (e) What is the statutory notice that must be served on the hirer, and how many days from the date of the notice can the owner sell the repossessed motor vehicle? [2]
 - (f) Apart from the amount outstanding under the hire-purchase agreement and interest on overdue instalments, what must the hirer pay the owner before he can claim the motor vehicle that has been repossessed and continue with the hire-purchase agreement? [4]
- (Total:20 marks)
2. (a) Labu Estate intends to purchase machinery for its rubber and oil palm plantations. The company's financial controller is in your branch to explore the possibility of getting a leasing facility for the machinery. You want to sell the leasing facility to the financial controller by explaining the advantages of leasing to a lessee.
- Explain any **six** of these advantages. [12]
- (b) When analysing Labu Estate's leasing application, you need to consider the high risks associated with the agricultural sector.
- List **six** factors contributing to the risks in the agricultural sector. [6]
- (c) If Labu Estate is a wholly Bumiputra-owned company with shareholders' funds of RM8.0million, which of Bank Negara Malaysia's or Credit Guarantee Corporation's financing schemes can Labu Estate apply for? [2]
- (Total:20 marks)
3. (a) Jasa Enterprise (Jasa) manufactures Styrofoam lunch boxes which are sold in Peninsula Malaysia. Due to increased demand for lunch boxes, Jasa would like to expand its operations to provide enough stock to its customers. The Managing Director of Jasa was introduced to you by one of your customers for the purpose of obtaining financing to expand Jasa's productive capacity.
- (i) As part of the credit proposal, you are required to state the problems faced by Small and Medium Size Entrepreneurs (SMEs) like Jasa, which can increase the credit risks. [14]
 - (ii) If Jasa takes a short-term financing to purchase a long-term asset, what are the potential problems? [4]
- (b) What is SMI Development Corporation and the Ministry of International Trade and Industry's definition of SMEs? [2]
- (Total:20 marks)

PART B

ANSWER TWO (2) QUESTIONS ONLY

4. (a) (i) Although the risks of housing loan financing (to the financial institution) are lower than other forms of lending, there are specific risks facing housing loan financiers. What are these risks? [6]
- (ii) Apart from careful attention to credit analysis procedures, what other risk reduction measures are available to a housing loan financier? [6]
- (b) What are the advantages of unit trust investment? [8]
- (Total:20 marks)

5. Ms Julie Tan entered into a hire-purchase agreement with ABBA Finance on 6 October 2000, for the purchase of a car at the price of RM55,000. Ms Julie Tan had earlier paid RM10,000 as a deposit to the car dealer. The period of financing is **four** years and the interest rate is 6.0% per annum.

The first instalment was made on 6 November 2000 and thereafter instalments were paid promptly on the sixth of each month. On 6 November 2001, Ms Julie Tan went to ABBA Finance to complete the purchase of the car.

- (a) (i) Calculate the term charges for the above hire-purchase agreement. [2]
- (ii) What is the monthly instalment payment? [2]
- (iii) Assuming that there are no other payments outstanding, how much must Ms Julie Tan pay to complete the purchase of the car on the stated date? (Round up your answer to the nearest sen) [6]
- (b) Upon settling her hire-purchase loan, Ms Julie Tan would like to apply for a fixed loan to renovate her house.
- (i) What is the maximum amount of fixed loan that Ms Julie Tan can obtain from ABBA Finance without providing collateral? [2]
- (ii) How is repayment and prepayment for fixed loans different from overdrafts? [4]
- (iii) If Ms Julie Tan needs more than the maximum amount of fixed loan that ABBA Finance can offer, what type of loan can she apply for and how is the loan repaid? [4]
- (Total:20 marks)
6. (a) What are the **four** risks in providing Internet banking that were highlighted by Bank Negara Malaysia as being of the greatest concern? [12]
- (b) Name **four** trade services that can help local Small and Medium Size Entrepreneurs enter into the international arena, and state the purpose of **each** of these trade services. [8]
- (Total:20 marks)

- END OF QUESTION PAPER -

OUTLINE ANSWERS

Part A

Question 1

This question tested the candidates on repossession of motor vehicles. Only a few candidates stated that defaults have to be successive/consecutive, or that an owner can initiate repossession upon default of the last payment. Many were not able to name the statutory notices to be served on the hirer before repossession. There were also candidates provided the list of repossession documents when asked for a repossessioner's identification.

1. (a) **Two** successive default of payments or a default in respect of the last payment of instalments.
- (b) After **four** successive defaults of payment.
- (c) Fourth Schedule and a notice informing the hirer that the owner intends to proceed with the repossession of the goods.
- (d) Identity card and authority card.
- (e) Fifth Schedule; 21 days from the date of Fifth Schedule.
- (f) Costs incurred by the owner of the motor vehicles and incidental to his taking possession, and costs of storage, repair or maintenance of the goods.

Question 2

Although the majority of the candidates were able to list the advantages of leasing and the risks associated with the agricultural sector, they were not able to explain them clearly.

2. (a) The advantages of leasing to a lessee:
 - Leasing provides up to 100% of the cost of the equipment
 - Often no deposits or advance payments are required.
 - Leasing conserves valuable working capital or credit lines
 - A leasing facility preserves liquidity.
 - Leasing offers cash flow benefits
 - Rentals fixed at the inception of a lease assist expense budgeting and cash flow forecasting.
 - Leasing provides certainty
 - A lease is non-cancelable, unlike an overdraft, which is repayable on demand, and may be reduced during a credit squeeze.
 - Leasing is a sound hedge against inflation
 - Equipment can be acquired at current prices and rentals met out of future earnings.
 - Leasing preserves existing credit-worthiness
 - As a lease is not a borrowing, it is off balance sheet, and therefore, does not adversely affect balance sheet ratios and existing creditworthiness.
 - Leasing is straightforward
 - Leasing minimises administrative costs and simplifies tax and accounting procedures. Asset depreciation normally becomes the lessor's responsibility. Documentation is simplified.

- Leasing is tax efficient
 - Lease rentals are generally fully tax deductible as operating expenses if the goods or equipment being leased is used for the production of assessable income.
- (b) The factors contributing to the high risks associated with the agricultural sector (any **six** factors):
- The success and output of the sector depends on natural elements such as the weather, soil, pollution, pests, diseases etc.
 - Long gestation periods: 3 – 7 years for yields to be realised.
 - Price variability.
 - Inelastic demand & supply.
 - Comparative cost disadvantage.
 - Perishability.
 - Imperfect market structures.
 - Low investment.
 - Poor distribution network.
 - High wastage.
 - High imported contents and imports.
 - Low mechanisation and modernisation.
 - Labour intensive.
 - In high competition for land resources.
- (c) New Entrepreneurs Fund (NEF).

Question 3

- Candidates were not able to define SMEs and describe the problems faced by them. Many thought shareholders fund must not exceed RM25million although the cap applies to sales turnover.
- Many candidates were not also able to explain how cash a flow problem is caused by taking short-term financing to purchase long-term assets.

3. (a) (i) The problems faced by SMEs (any 14 of the problems):
- Small size
 - Informal business management ways
 - Limited access to working capital and other financial assistance
 - Absence of satisfactory track records
 - Limited collateral offered
 - Reluctance to reveal their operations to the authorities
 - Inadequate levels of technological and managerial skills
 - Lack information technology and R&D capabilities
 - Frequently use out-of-date machinery
 - Operate under conditions which are not conducive to optimising their overall efficiency (factories are not located in proper industrial parks)
 - Shortage of skilled labour and technicians
 - Lack the capacity and capability to have organised marketing
 - Most MNCs bring their own SMEs to support them
 - Lack knowledge in export procedures and overseas market opportunities
 - Have to contend with a high cost of raw materials
 - Lack skills and technical knowledge to add value to their existing products

- Banks have too much bureaucracy, paper work and give lukewarm support
 - Threat of competition from larger industries
- (ii) The loan will have to be repaid before profits are generated from the asset, and the outflow of cash might cause cash flow problems in the business operations.
- (b) Industries and entrepreneurs/enterprises with:
- Annual sales turnover of less than RM25 million.
 - Less than 150 full-time employees.

Part B

Question 4

Many candidates were not able to explain the risks facing housing loan financiers or the risk reduction measures. However, many candidates were able to describe the advantages of unit trust investment.

4. (a) (i) Specific risks facing housing loan financing:
- *Default risk* – Failure to repay a loan is most likely to occur during the early years of the loan and is influenced by many unforeseen conditions such as bad health, unemployment, and marriage breakdown.
 - *Interest rate risk* – Times of rising interest rate cause difficulties to housing loan financiers who have to pay for long term relatively low interest rate loans with more costly short-term deposits.
 - *Liquidity risk* – A lack of liquidity could cause a failure to meet withdrawal demands, which could have disastrous consequences.
- (ii) Risk reduction measures available to a housing loan financier? (candidates should list at least **three** measures)
- *Guarantees* – A personal guarantee may be accepted from a third party where the applicant's income appears insufficient to meet repayment.
 - *Periodic review* – A system of periodic review.
 - *Variable interest rate loans* – Protect the lender by passing the risk to the customers.
 - *Proper security documentation* – Protect the financier's interest in the security.
- (b) Advantages of unit trust investment are:
- *Professional management* – unit trusts are managed by professional fund managers who are specialists in investment matters;
 - *Diversification* – allow individual investors with small capital to have access to certain investments otherwise unavailable to them & give them better spread of risks;
 - *Liquidity* – there is a ready market for the units, the investor is able to liquidate his investment without much difficulty; and
 - *Flexible and affordable* – investment in unit trust is not only available to institutions but also to an individual with low investment funds. Some initial investment in unit trusts is as low as RM10 per unit.

Question 5

This question on hire-purchase calculations and fixed/housing loan of personal lending was generally well answered.

5. (a) (i) Term charges = $RM45,000 \times 6\% \times 4$
= **RM10,800**
- (ii) Monthly instalment = $\frac{RM(45,000 + 10,800)}{48}$
= **RM1,162.50**
- (iii) Statutory rebate = $\frac{36(36+1) \times RM10,800}{48(48+1)}$
= **RM6,116.33**
- Outstanding amount = $RM55,800 - RM13,950$
= **RM41,850**
- Early settlement amount = $RM41,850 - RM6,116.33$
= **RM35,733.67**
- (b) (i) RM10,000
- (ii) Fixed loans have fixed repayment schedule where the amount and due date of all repayments is determined at the beginning of the loan. Prepayments can be made at any time subject to the borrower's prior notice to the lender.
- The outstanding debt in an overdraft account may be repaid at anytime, as there is no fixed repayment schedule. There is no prior notice required from the borrower to the lender.
- (iii) Housing Loan. Repayments are due at regular intervals throughout the term of the loan.

Question 6

While many of the candidates were able to explain the risks associated with Internet banking, they had difficulty stating and explaining the trade services available for SMEs.

6. (a) The risks highlighted are:
- *Transaction risk* – Possibility of security breaches as transactions transverse an open, unsecured public network, e.g. unauthorised access, disclosure of confidential information, denial of service and the repudiation of transactions. The detection and subsequent recovery of these security breaches requires substantial expertise and resources.
 - *Legal risk* – The legal infrastructure concerning Internet transactions has not been tested extensively, e.g. legality and enforceability of contracts made through the Internet, compliance to existing local and foreign laws. Financial institutions may be exposed to legal action due to the inadequate disclosure of information to customers or failure to protect customers' privacy.
 - *Reputation risk* – Any breach of security, whether real or perceived, can seriously damage the trust a financial institution commands with its customers and the general public.
 - *Strategic risk* – As substantial ongoing resources are needed in capital expenditure, highly skilled human resources etc., a wrong decision would result in a waste of resources and may place the organisation in an inappropriate market positions not in line the financial institution's overall business strategy.

- (b) The available trade services are (any **four**):
- *Import Letters of Credit* – Facilitate the purchase of goods/materials either locally or overseas.
 - *Export Letters of Credit Advising/Confirmation* – Mitigate the risk associated with exporting to a new or existing importer, or to a new importing country.
 - *Inward Bills for Collection (Clean/Documentary)* – A customer can arrange with the seller to forward the bill documents to its bank which will then collect payment from the customer and remit it to the seller.
 - *Outward Bills for Collection (Clean/Documentary)* – Assist customers in collecting their bills drawn on local or overseas buyers.
 - *Shipping Guarantee* – Issued to the owner or agents of the vessel for delivery of goods prior to receipt of the bill of lading.