

DP03

Principles of Lending

5 SEPTEMBER 2007

1. Time allowed : Three (3) hours
2. Total number of questions : Four (4) questions
3. Number of questions to be answered : All four (4) questions
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.

ANSWER ALL FOUR (4) QUESTIONS

1. Outline the framework of a loan life cycle and briefly describe the components and activities involved in each stage of the cycle. (Total:26 marks)

2. Comment on the 5Cs of credit and its relevance in the assessment of loan applications. (Total:20 marks)

3. List and describe **eight** causes of problem loans in financial institutions. (Total:24 marks)

4. Compare and contrast between business lending and consumer lending. Your answer should include similarities and differences with emphasis on the key differences between the two types of lending. (Total:30 marks)

– END OF QUESTION PAPER –

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

- No comments were provided for this question.

1. Please refer to page 44, unit 4.1, of “Bank Lending – Assessment and Management” by Howard Choo.

Question 2

- No comments were provided for this question.

2. Please refer to page 86, unit 6.3, of “Bank Lending – Assessment and Management” by Howard Choo.

Question 3

- No comments were provided for this question.

3. Please refer to page 165, unit 12.2, of “Bank Lending – Assessment and Management” by Howard Choo.

Question 4

- Candidates were unable to state the similarities of the two types of lending.

4. Similarities between Business lending and Consumer lending:

- Both evaluate the ability to repay a bank from future cashflows
- Both are a form of loan products financial institutions offer
- Both can be evaluated using a credit-scoring model
- Both can be in the form of short-term lending and long-term lending
- Pricing of both types of lending are generally based on base lending rate
- Both require credit checks

Differences between Business lending and Consumer lending:

Business lending

- Looks at financial accounts to evaluate performance
- Requires periodic review and site visits
- Governed by loan agreement, debenture and mortgage
- Substantial legal fees incurred
- Requires thorough and in-depth credit analysis
- Requires slightly more complex credit scoring models

Consumer lending

- Looks at income tax returns and pay slips to ascertain income
- Review is only done in the loan processing stage
- Governed by hire-purchase agreement, loan agreement and charge or just the application form in the case of credit cards
- Minimal legal fees incurred
- Simpler in evaluation
- Uses simple credit scoring models