

THE INSTITUTE OF BANKERS OF ZIMBABWE

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DIPLOMA LEVEL	
SUBJECT	PRACTICE OF BANKING II
DATE	26 OCTOBER 2017
TIME	3 HOURS
MARKS	100
EXAM TYPE	CLOSED BOOK
READING TIME	FIFTEEN MINUTES READING TIME IS ALLOWED FOR THIS PAPER. DURING THIS TIME YOU ARE PERMITTED TO WRITE ON THE QUESTION PAPER BUT NOT IN YOUR ANSWER BOOK
EQUIPMENT REQUIREMENTS	NON –PROGRAMMABLE AND NON SCIENTIFIC CALCULATOR

INSTRUCTIONS TO CANDIDATES

1. Read the instructions CAREFULLY before answering the paper
2. This paper has six (6) questions.
3. Question 1 and 2 are compulsory. Question 1 and 2 carry 30 marks each
4. Answer any other 2 questions from questions 3 to 6
5. Please be neat – illegible handwriting cannot be marked
6. Use black or blue ink
7. Ensure that all information on the cover of your answer book is completed in full.
8. Cheating is not allowed. If anyone is caught cheating, disciplinary measures will be taken by the Institute of Bankers.

GOOD LUCK !

QUESTION PAPER

OCTOBER 2017

SECTION A (COMPULSORY QUESTIONS)

QUESTION 1 (30 MARKS)

Mr. Germaine Mpofo and Mr. Colin Moyo are the directors and shareholders of Germco Steel Fabricators (Pvt) Ltd which started operations in 1987. The directors own equal shareholding in the company and have been banking with you since inception.

The company manufactures fabricated steel works for sale to large multinational companies country wide. Sometimes the company receives large export orders which it manufactures to certain specifications.

Presently the company has an overdraft limit of \$950 000 which is secured by a Notarial General Covering Bond (NGCB) over the company's fixed and floating assets and the directors unsupported guarantees. Your Bank has never solicited for information on the director's personal assets. Currently you have been noticing persistent excesses on the account and your analysis of the account operations reveals a hard-core element in the region of \$750 000. Account operations have tended to continue to deteriorate and you are now concerned with the company's future prospects. During this period while you are nursing your concerns as to what steps to take to address the situation, the company approaches you with a request for an enhanced overdraft facility of \$1 150 000. You see this as an opportunity to probe the company's financial affairs. You ask for an independent accountant's report into the operations of the company.

The report is furnished with the following figures and remarks.

Achievement of the report is dependent on sales volumes and gross margins as overheads are well maintained and under control. Sensitivity analysis reveals the following:

- a) 5% change in sales at budget gross margin: - Effect +/- \$112 800
- b) 5% change in gross margin at budget sales levels: -Effect +/- \$47 000

The budgeted 14.7% increase in sales is dependent on anticipated increased spending by major users of fabricated steel. A high proportion of sales take place in October and November as the company nears its annual shut down. Though the order book looks good, it is not possible to be confident about the outcome for the year as a whole.

The cash flow forecast reveals a requirement of \$1 150 000 at the peak overdraft. However, material suppliers have been lenient in enforcing their credit terms. If all creditors had to be brought up to date, there would be a \$300 000 extra cash requirement.

The directors are believed to have substantial equities in their houses even after increasing their mortgages last year to inject capital into the business.

Required:

In view of the private accountant's report, give with reasons, the response you would make to the directors' request.

GERMCO STEEL FABRICATORS (PVT) LTD STATEMENT OF COMPREHENSIVE SUMMARY \$(000) 12 MONTHS TO 30 JUNE

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
Sales	8 068	6 484	8 192	9 400
Gross margin	1 914	1 602	2 008	2 256
			Draft	Budget
Overheads	(1 106)	(15 10)	(15 96)	(15 80)
Rent & Rates	(4 30)	(4 54)	(3 44)	(2 76)
Interest	(1 00)	(1 18)	(1 26)	(1 18)
Extra-ordinary item	-	2 42	-	-
Profit (Loss) before tax	<u>2 78</u>	<u>(2 38)</u>	<u>(58)</u>	<u>2 82</u>

1. Accounting Ratios

As at 31 December	<u>2015</u>	<u>2016</u>	<i>Draft</i> <u>2017</u>	Budget <u>2018</u>
Gross margin (%)	23,7	24,7	24,5	24,0
Net margin (%)	3,4	(3,7)	(0,7)	3,0
Interest cover (times)	3,8	-	0,5	3,4
Net gearing (%)	209	859	156	-
Current ratio	1,01:1	0,77:1	1,03:1	-
Acid test	0,51:1	0,33:1	0,59:1	-
Credit given (days)	55	36	59	-
Credit taken (days)	103	125	118	-
Stock turnover (days)	89	102	91	-

Statement of Financial Position as at 30 June S(000)

	<u>Forecast as at</u> <u>30/09/18</u>	<u>Draft Accounts at</u> <u>30/09/17</u>	<u>Audited Accounts</u> <u>30/09/16</u>
2. Fixed Assets			
Leasehold improvements	1 98	1 99	1 98
Equipment Plant & machinery	1 50	1 50	1 72
Motor vehicles	<u>1 50</u>	<u>1 54</u>	<u>2 04</u>
	4 98	5 03	5 74
<u>Current Assets</u>			
Trade Debtors	12 80	13 24	6 44
Other debtors & payments	12	4	4
Stock & Work in progress	10 20	10 20	8 58
Corporate tax refund	12	12	-
Cash at Bank and hand	<u>2</u>	<u>2</u>	<u>2</u>
	23 26	23 62	15 08
3. Current Liabilities			
Trade creditors	10 18	11 04	7 28
Other creditors & Accruals	72	18	32
PAYE & N SSA	46	1 18	-
Corporate Tax	1 94	1 66	78
Bank Overdraft	9 04	8 12	7 46
Hire Purchase/Lease balances	16	18	26
Directors Loans	<u>59</u>	<u>58</u>	<u>3 14</u>
	2309	22 94	19 24
		<u>17</u>	
	<u>5 15</u>	<u>68</u>	<u>(4 16)</u>
		<u>5 71</u>	<u>1 58</u>

Represented By:

Share Capital		6 00		6 00		100
Profit & Loss Account Bal b/f	(30)		28		2 38	
Current period	(55)	<u>(85)</u>	<u>(57)</u>	<u>(29)</u>	(180)	<u>58</u>
		<u>5 15</u>		<u>5 71</u>		<u>1 58</u>

QUESTION 2 (30 MARKS)

Techno Tech Manufacturing (Pvt)Limited have made reasonable profits over 10 years and on 30 June 2016 the Statement of Financial Position showed a capital base of \$100 000. Accounts are normally produced six months after year-end and form the only financial summary. Last year, when reviewing the overdraft facility you suggested more regular financial information might be beneficial and now you see in the latest accounts to 30 June 2017 a loss of \$150 000 even after the directors' salaries had been reduced.

The company borrowing has become hardcore and additionally, there have been bad debts of \$100 000 and a resistance from customers to price increases. PAYE has not been paid and the Revenue Authorities are pressing. The Managing Director feels he does not get sufficient advice from the accountants and wishes to reopen the discussion with you on financial control. How would you respond to his request for advice?

(Total 30 marks)

SECTION B (Answer any (2) Questions)

QUESTION 3 (20 MARKS)

Below are financial statements of Farm House Cooperative Union, a client of the Bank. You are required to analyse the information provided and perform a profitability assessment supported by appropriate financial ratios.

FARM HOUSE COOPERATIVE UNION

STATEMENT OF FINANCIAL POSITION AS AT 30 JUNE 2016

	Notes	2015	2016
		\$	\$
ASSETS			
NON- CURRENT ASSETS		245 986	261 099
Tangible fixed assets	4	102 216	117 329
Goodwill		143 770	143 770
CURRENT ASSETS		296 905	317 537
Inventory		56 001	110 410
Accounts receivable		240 515	204 971
Cash & cash equivalents		389	2 156
TOTAL ASSETS		542 891	578 636
EQUITY & LIABILITIES			
CAPITAL & RESERVES		43 559	(31 729)
Members contribution		100	100
Accumulated profits		43 459	(31 829)
NON-CURRENT LIABILITIES		215 040	246 299
Long term liabilities	3	0	66 999
Members loans	2	215 040	179 300

CURRENT LIABILITIES		284 292	364 066
Accounts payable		182 426	192 688
Current portion of long-term debt		20 418	0
Taxation		1 407	538
VAT		10 443	8 112
Bank overdraft		69 598	162 728
TOTAL EQUITY & LIABILITIES		542 891	578 636

STATEMENT OF COMPREHENSIVE SUMMARY FOR THE YEAR ENDED 30 JUNE 2016

	Notes	2016	2015
TURNOVER	1.1	1 597 651	1 318 720
COST OF SALES		1 046 027	838 192
Opening stock		110 410	121 491
Purchases		1 023 952	827 111
Recovery account		-32 334	0
Closing stock		-56 001	-110 410
GROSS PROFIT		551 624	480 528
SUNDRY INCOME		496	209
Discount received		300	281
Handling charges		196	-72
GROSS INCOME		552 120	480 737
LESS: Expenditure as per schedule		472 926	548 074
PROFIT / (LOSS) for the year before tax		79 194	-67 337
Taxation		3 906	0
PROFIT / (LOSS) for year after tax		75 288	-67 337
UNDRAWN INCOME AT THE BEGINNING OF THE YEAR		-31 829	35 508
UNDRAWN INCOME END OF YEAR		43 459	-31 829

SCHEDULE OF EXPENSES

	2016	2015
Accounting fees	5 270	4 450
Advertising & promotion	219	3 320
Bad debts	10 004	0
Bank charges	6 895	6 738
Cleaning	0	58
Computer expenses	3 132	1 974
Consulting fees	0	1 268
Postage	1 329	796
Depreciation	22 473	28 243
Discount allowed for cash	1 229	1 239
Donations	961	202
Electricity & water	2 241	3 606
Entertainment	3 362	3 162
Finance charges	5 510	0
General expenses	207	126
Insurance	9 842	8 876
Interest paid	8 515	21 319
Member's salary	50 246	31 674
Motor vehicle expenses	37 013	91 774
Photocopy	2 045	1 359
Printing & stationery	6 245	4 688
Rental of equipment	13 362	9 671
Rent paid	46 628	52 764
Repairs & maintenance	316	799
RSC Levies	3 674	3 329
Salaries & wages	179 504	218 622
Security	1 654	1 520
Staff welfare	2 431	2 594
Subscriptions	2 848	2 589
Telephone & fax	44 153	40 332
Travel & accommodation	1 618	982
TOTAL EXPENSES	472 926	548 074

QUESTION 4 (20 MARKS)

Mr. John Brown, aged 51, married with a grown up family and owner of his own house on which there is a mortgage of \$70 000, calls to say he has won Lotto in the amount of \$200 000.

His small account has been trouble-free and he has never borrowed from the bank or sought financial advice. Understandably, he is worried by the financial responsibilities stemming from managing such a large sum and realizes he must do something with the money. Above all else he would like to provide a secure future for his wife and two children. What bank services would be appropriate for Mr. Brown? Explain briefly the benefits of each.

(Total 20 marks)

QUESTION 5 (20 MARKS)

- a) Briefly describe credit risk. (5 marks)
- b) What is the purpose of credit risk analysis? (5 marks)
- c) What do you understand by credit scoring? (5 marks)
- d) When a company goes into liquidation what items take precedence over a notarial general covering bond (NGCB) (5 marks)

(Total 20 Marks)

QUESTION 6 (20 MARKS)

As Branch Manager you have identified the need to increase substantially the Retail deposits generated from personal customer and Small to Medium Size Enterprises (SMEs) and the informal sector. How would you go about the task of achieving growth in retail deposit mobilization?

(Total 20 Marks)