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DCM LEVEL III

PRACTICE OF CREDIT MANAGEMENT

WEDNESDAY: 27 November 2019. **Time Allowed: 3 hours.**

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

QUESTION ONE

CAWAMATT HOLDINGS

Cawamatt Holdings is a supermarket chain. Until February 2014, Cawamatt Holdings was regarded as the largest retailer in the country with 50 branches across the region. However, Cawamatt's rapid expansion was funded through debt. This included short term borrowings, bank loans and letters of credit to its numerous suppliers. Cawamatt Holdings was overtrading. The retailer also depended heavily on trade credit. Due to a number of reasons, Cawamatt Holdings started experiencing serious cash flow difficulties in the year 2015. The retailer was unable to meet its financial obligations to the landlords, suppliers and employees. It is for this reason that an administrator was appointed by an order of the court pursuant to an application filed by unsecured creditors to put Cawamatt Holdings under liquidation. After looking at the financial health of Cawamatt Holdings, the administrator who is a qualified credit professional, set out to come up with a debt restructuring proposal, which he believed that if properly implemented, would restore Cawamatt Holdings to its original status of a profitable retailer.

Required

(a) (i) Explain the term "overtrading". (2 marks)

(ii) Enumerate four symptoms of overtrading that are identifiable in Cawamatt Holdings. (4 marks)

(b) Cawamatt Holding's rapid expansion was funded through debt and short term borrowing among other sources of finance.

With reference to the above statement:

(i) Analyse three features of short term loans. (6 marks)

(ii) Argue two cases for and two cases against the use of short term loans as a source of finance. (8 marks)

(c) Cawamatt Holdings was in financial distress since it could not meet its financial obligations as they fell due.

Required:
With reference to the above statement, list six actions that creditors and lenders could engage in when dealing with Cawamatt Holdings. (6 marks)

(d) Cawamatt Holdings relied heavily on trade credit from its suppliers.

With reference to the above statement:

(i) Explain the term "trade credit". (2 marks)

(ii) Propose two advantages of trade credit to Cawamatt Holdings. (4 marks)

(e) (i) Explain the term "debt restructuring". (2 marks)

(ii) Analyse three benefits that could accrue to Cawamatt Holdings after undertaking debt restructuring. (6 marks)

(Total: 40 marks)

QUESTION TWO

(a) Digital lending is one of the main directions of financial technology (Fintech) software development. Fintech organisations are transforming the lending process so that customers no longer need to submit physical documents to banks to get loans.

With reference to the above statement:

(i) Highlight five benefits of a loan origination software. (5 marks)

(ii) Identify three key features of a loan origination software. (6 marks)

(b) List four documents required for opening a letter of credit (LC). (4 marks)

(Total: 15 marks)

QUESTION THREE

(a) Explain the following terms as used in foreign exchange:

(i) Transaction risk. (2 marks)

(ii) Translation risk. (2 marks)

(iii) Hedging transaction. (2 marks)

(iv) Contingent risk. (2 marks)

(b) Describe seven sources of credit risk in commercial banks. (7 marks)

(Total: 15 marks)

QUESTION FOUR

(a) Examine three types of invoices used in export credit. (6 marks)

(b) Explain the term "credit reference bureau". (1 mark)

(c) With reference to credit reference bureau regulations and credit sharing information, distinguish between the following terms:

(i) "Notice of change" and "notice of resolution". (4 marks)

(ii) "Credit report" and "credit information". (4 marks)

(Total: 15 marks)

QUESTION FIVE

(a) Analyse five in-house collection strategies that a credit controller could implement to speed up debt collection in an organisation. (10 marks)

(b) (i) Explain the term "risk preference". (1 mark)

(ii) Distinguish between "risk averse preference" and "risk neutral preference". (4 marks)

(Total: 15 marks)

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