

Credit Evaluation & Management of Troubled Credits

2 Days

COURSE OVERVIEW

This program looks at credit analysis from the approach of identifying underlying warning signs in credit evaluation, analysis and management of troubled credits. The program involves the application of exercises and case studies.

LEVEL

Intermediate - Advanced

WHAT DO I GET OUT OF IT?

Participants will:

- Learn lending principles, risk and lending management as the foundation for a holistic approach to managing troubled credits.
- Understand the various components of the asset conversion cycle (operating cycle and capital investment cycle), and how they operate in troubled credits.
- Learn how these timing differences cause borrowing needs and the credit impacts for businesses
- Learn about industry risk and how the use of financial statements can help in understanding the characteristics of the asset conversion cycle unique to an industry.
- Analyze risks related to the general nature of a business, the product-market match, supply and production risks, sales and distribution risks, and the ability of its management.
- Be able to determine the degree of accounting risk in a trading and profit and loss statement
- Understand the effects of different accounting methods on the trading and profit and loss statement and balance sheet.
- Perform a common-size analysis and interpret the results

WHO'S IT FOR?

Delegates could come from a broad range of backgrounds, such as:

- Commercial credit analysts
- Commercial lenders, loan officers, relationship managers
- Investors
- Other financial professionals

COURSE CONTENT

Understand the Risk

- Principles of Sound Lending
 - Personal or Corporate Equation (or Personal Factor)
 - Ability and Capacity to Repay
 - Willingness to Repay
 - Security
- Preliminary Assessment of Loan Proposals
 - Screening Applications
 - Amount of Loan
 - Purpose of Loan
 - Reason (Cause) of Borrowing
 - Lending Policies
 - The Applicant's Business
 - Collecting Information
 - Continue or Decline

The concept of lending principles, risk and lending management are introduced as the foundation for a holistic approach to managing troubled credits. The principles of sound lending are considered as a means of minimizing the risk of default, and to provide the basis for this segment of the program. In this respect, participants will consider the personal or corporate equation as a basis of relationship with the borrower, the ability or capacity to repay, as well as the willingness to repay, and the provision or availability of support through security covering the loan. Their considerations then focus on the preliminary screening of a loan proposal to determine whether it appears reasonable, legal and within the bank's policy. Participants will consider the appropriate questions to be asked about the applicant's business so that they will be better placed to understand what it presented in the financial statements. As a final step in this process, participants will consider the types and sources of information available to them in their analysis. Participants will apply principles learnt through a series of exercises and/or case studies.

The Asset Conversion Cycle

- Asset Conversion Cycle Components
- Timing Differences and Financing Needs

Participants will consider the various components of the asset conversion cycle (operating cycle and capital investment cycle), and how they operate in troubled credits. The concept of cash flow timing differences is introduced and the impact of these timing differences on the operations of a troubled business are discussed. How these timing differences cause borrowing needs and the credit impacts for businesses is the main focus of the segment. Participants will apply principles learnt through a series of exercises and/or case studies.

Causes of Borrowing

- Borrowing Caused by Sales Growth
 - Seasonal Sales Growth
 - Long-term Sales Growth
- Borrowing Caused by Slowdowns in the Operating Cycle
 - Slowdowns in Inventory Turnover

- Slowdowns in Collection of Accounts Receivable
- Borrowing Caused by Purchases of Fixed Assets
 - Replacement of Fixed Assets
 - Increase in Fixed Assets
- Borrowing Caused by Other Factors
 - Asset Growth
 - Other Borrowing Causes

This step considers how borrowing is caused by changes in the operating and capital investment cycles of a business, and by other reasons not directly connected to the asset conversion cycle, such as changes in equity structure or unprofitable operations. How to identify and diagnose each cause of borrowing is considered in four major segments; ie., sales growth, operating cycle slowdowns, fixed asset purchases, and other factors. Again participants will apply principles learnt through a series of exercises and/or case studies.

Analyzing Industry Risk

- Industries
- Industry Risk Characteristics
 - Cost Structure
 - Industry Maturity
 - Industry Cyclicalities
 - Profitability, Dependence, Substitutes and Regulation

The industry risk analysis step addresses the question of what is likely to happen in the environment in which the borrower operates. It develops a working definition of industry and shows how the use of financial statements can help in understanding the characteristics of the asset conversion cycle unique to an industry. Several industry risk characteristics are considered in the segment and the means of assessing the level of risk are discussed. Participants will apply principles learnt through a series of exercises and/or case studies.

Analyzing Business Risk

- Business Analysis Perspective
- General Characteristics
- Product-Market Match
- Supply and Production Analysis
- Sales and Distribution
- Analyzing Management
- Drawing Your Conclusion

Initially participants will consider where business analysis fits into loan analysis and how it will help integrate information gathered and lead to a loan decision. Analysis of business risk involves assessment of the strategic plans and systems within a business and evaluating management's ability to carry out those plans. In this segment participants analyse risks related to the general nature of a business, the product-market match, supply and production risks, sales and distribution risks, and the ability of its management. Methods of approach in analysing different types of business and management risks are discussed and considered, as well as how the various degrees of risk can be assessed and evaluated. Participants will apply principles learnt through a series of exercises and/or case studies.

Financial Statement Analysis

- Balance Sheets
 - What is a Balance Sheet?
 - What are you, as a Lender, looking for?
 - Is the financial position sound?
 - Are earnings satisfactory and can proposed borrowings be comfortably serviced?
 - What are the future prospects?
 - Is it a sound, worthwhile business?
 - How can you assess these matters?
 - Developing Your Expectations
 - Assessing Operations Management
 - Accounting Risk in the Income Statement
 - Common-size Analysis
 - Comparative Analysis
 - Analyzing Asset and Liability Management
 - Accounting Risk in the Balance Sheet
 - Common-size Analysis
 - Operating Efficiency Analysis
 - Capital Structure and Leverage
 - Liquidity Analysis
 - Working Capital

In this step, participants will consider how they can form hypotheses about the structure and content of financial statements they will analyze, how to analyze a company's trading and profit and loss statement, and how to analyze a balance sheet to more fully understand the prospective borrower's lending-worthiness and management expertise. The segment will enable participants to recognize typical asset and liability structures of different types of businesses; determine the degree of accounting risk in a trading and profit and loss statement; understand the effects of different accounting methods on the trading and profit and loss statement and balance sheet; perform a common-size analysis and interpret the results; undertake industry comparisons to determine whether performance is better or worse than the industry average; calculate liquidity, capital structure and operating efficiency ratios; determine historical trends in the ratios; and interpret these trends by examining changes in ratio components. Participants will apply principles learnt through a series of exercises and/or case studies.

Wrap Up

Presentation and discussion, summarizing the program and setting lending objectives back on the job.