

EXAMINATION

24 May 2022

Subject F207/B200 – Banking Specialist Applications

Time allowed: Three hours and fifteen minutes, plus an additional five minutes to allow for uploading your file in the ASSA Exam Platform

Total marks: 100

INSTRUCTIONS TO THE CANDIDATE

1. Ensure that you are logged in and authenticated through Examity before you attempt the examination.
2. The question paper is only available in the ASSA Exam Platform as a PDF download and may not be printed. Copy/paste of questions or parts thereof is only allowed between the Exam Platform and the Word answer document.
3. You are required to submit your answers in Word format ONLY using the answer template provided. No uploads of answers (handwritten or otherwise) will be accepted.
4. Ensure that your Candidate Number appears in the “header” of your Word answer template. [Select “Insert”, then “Header”, input your candidate number on the blank header template and select “Close Header”]. **Do not use your name or member number on your answer script.**
5. You may not access any file from your PC, use any other computer program (e.g. Email or Excel), or open any other browser during the examination.
6. You may not use any other material (e.g. a Formulae and Tables book) during the examination. Any such information that may be required will be provided to you within the examination.
7. You are strongly encouraged to use the first 15 minutes as reading time only, however, you may start answering the paper whenever you are ready.
8. Mark allocations are shown in brackets.
9. Attempt all questions.
10. Show calculations where appropriate. You may use blank paper to carry out rough work calculations. You may use a calculator from the approved list only.
11. Upload your Word answer file only into the ASSA Exam Platform. Once you have uploaded your file, you must click on **Finish Attempt** to save your file. You will still be allowed to go back and make changes (**Review Attempt**) if you have time.
12. Once you are satisfied with your uploaded file, click **Finish attempt** and **Finish all and Submit**. Once you have submitted you will not be able to make more changes.
13. **You must submit your answer file BEFORE the end of the allotted examination time.** Take this into account when planning your review and submission. There will be no time announcements.
14. An option to opt out of the exam will become available 1 hour after the official examination start time. If you select the Opt-Out option, you agree and understand that your entire script/answers will be deleted and cannot be retrieved at a later stage and that your script or part thereof will not be put forward for marking.

Note: The Actuarial Society of South Africa will not be held responsible for loss of data where candidates have not followed instructions as set out above.

END OF INSTRUCTIONS

QUESTION 1

You are the head of SABank's Balance Sheet Management team. SABank offers mainly retail products in South Africa, but also has non-retail offerings across the rest of Africa.

- i. Briefly explain the basic requirements to be considered in the production of an ICAAP.

[5]

- ii. SABank have been exploring expanding their footprint through the acquisition of other Banks (potentially outside of South Africa). The table below illustrates the relative risk indicators for Bank A and Bank B and the relative changes in these risk indicators over the course of the COVID-19 pandemic. Discuss the relative profiles of Bank A and Bank B, including commentary on the appropriate measurement approach for each of the risk types.

Risk Indicator	Risk Subtype	Before COVID-19		After COVID-19	
		Bank A	Bank B	Bank A	Bank B
General Risk Indicators (size)		Small	Large	Small	Large
Specific Risks					
Credit Risk	Counterpart Credit Risk / Default Risk	L	H	H	H
	Equity Risk	L	M	M	H
	Concentration Risk				
	Foreign currency loans	L	H	L	M
	Industries	L	M	H	H
	Size classes	L	H	M	M
	Country risk	L	H	L	M
Market Risks		L	M	M	H
Interest Rate Risk in the Banking Book		L	M	M	H
Operational Risks		L	H	H	H
Liquidity Risks		L	M	M	H
Other Risks		L	L	M	M

H	High Significance
M	Medium Significance
L	Low Significance

[25]

- iii. The bank regulator has indicated that they may require SABank to consider climate risks as part of their ICAAP exercise in 2023. Discuss the considerations in preparing for an effective ICAAP exercise, as well as how considerations around climate risk may be incorporated in the overall ICAAP.

[15]

[Total 45]

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QUESTION 2

You are the risk head of the home loans division of We Care Bank based in Southern Africa. Your bank offers a full suite of banking products to retail customers. Your sales head has recently proposed to launch a new product called “Home Equity Release Finance”. This aims to enable customers to access any equity they have in their property without selling the property. The product would allow the borrower to withdraw capital from their property, and to negotiate delayed repayment terms based on the remaining equity within their property and their financial means. The target market is retired individuals. There are 3 possible repayment options that could be offered to customers:

- No repayment at all
- Repayment of interest only (or part thereof)
- Repayment of interest and capital (or part thereof)

- i. Discuss the benefits of this product to the customer. [2]
- ii. Discuss the inherent risks of this product to We Care Bank. [8]
- iii. Explain how you would go about developing the product to create an economically viable offering.
The following should be addressed:
 - a. Qualifying criteria [4]
 - b. Accommodating the alternative repayment options [4]
 - c. Other considerations [4]
- iv. Detail the considerations needed to price for this product. [8]
- v. How could you go about estimating the size of the target market for such a product? [3]

[Total 33]

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QUESTION 3

“Life Bank” is a publicly listed bank operating in an emerging market focussed on providing transactional, savings and lending products to the retail market, with a special focus on private individuals in the top income deciles (high-income segments).

Life Bank financial fact sheet:

Balance sheet: Local Dollar (millions)

	Notes	31-Dec-20	31-Dec-21
Assets			
Cash and balances at central bank		500	300
Property and equipment		1 000	1 000
Loans and advances to retail market		12 000	13 000
Local sovereign debt securities		7 500	8 900
Liabilities			
Customer deposits		15 000	17 000
Debt securities in issue		4 000	4 000
Total equity			
		2 000	2 200
Actual liquidity coverage ratio		180%	160%
Actual net stable funding ratio		160%	200%

Income statement: Local Dollar (millions)

	Notes	31-Dec-20	31-Dec-21
Net interest income		438	481
Impairment charge		- 60	- 65
Non-interest revenue		200	180
Costs		- 200	- 205
Pre-tax earnings		378	391
Pre-tax return on equity			
		18.9%	17.8%
Price-to-earnings ratio			
	1	12	11

1. Based on 30 day value weighed trading price post dividend declaration date

- i. Define the liquidity coverage ratio and the net stable funding ratio and explain the risk it is intended to measure. [4]

“CareFree” is a privately listed consumer finance company operating in the same territory providing unsecured term loans to the retail market, with a special focus in the lower-to-middle income market segments.

CareFree financial fact sheet:

Balance sheet: Local Dollar (millions)

	Notes	31-Dec-20	31-Dec-21
Assets			
Cash and cash equivalents		200	100
Property and equipment		300	400
Loans and advances to retail market		8 000	10 000
Liabilities			
	2		
Senior interest bearing debt		4 500	5 000
Sub-ordinated interest bearing debt		2 000	3 300
Total equity			
		2 000	2 200

Income statement: Local Dollar (millions)

	Notes	31-Dec-20	31-Dec-21
Net interest income		560	600
Impairment charge		- 320	- 400
Non-interest revenue		100	150
Costs		- 100	- 100
Pre-tax earnings		240	250
Pre-tax return on equity			
		12.0%	11.4%
Price-to-earnings ratio			
	1	15	16

1. Based on 30 day value weighed trading price post dividend declaration date

2. Maturity profile	31-Dec-20	31-Dec-21
Within 12 months	1 500	2 500
12-36 months	3 000	2 800
36 month+	2 000	3 000

- ii. Define sub-ordinated debt and explain the benefit to company in issuing sub-ordinated debt. [3]

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The CEO of Life Bank has asked you to evaluate the potential financial and strategic benefits of acquiring “Carefree”.

iii. Using the financial factsheet provided, detail your preliminary findings regarding the potential financial benefits of the transaction and further information that you would require. [10]

iv. Outline the additional potential strategic benefits related to the acquisition, and further information that you would require. [5]

[Total 22]

[Grand Total 100]

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END OF EXAMINATION