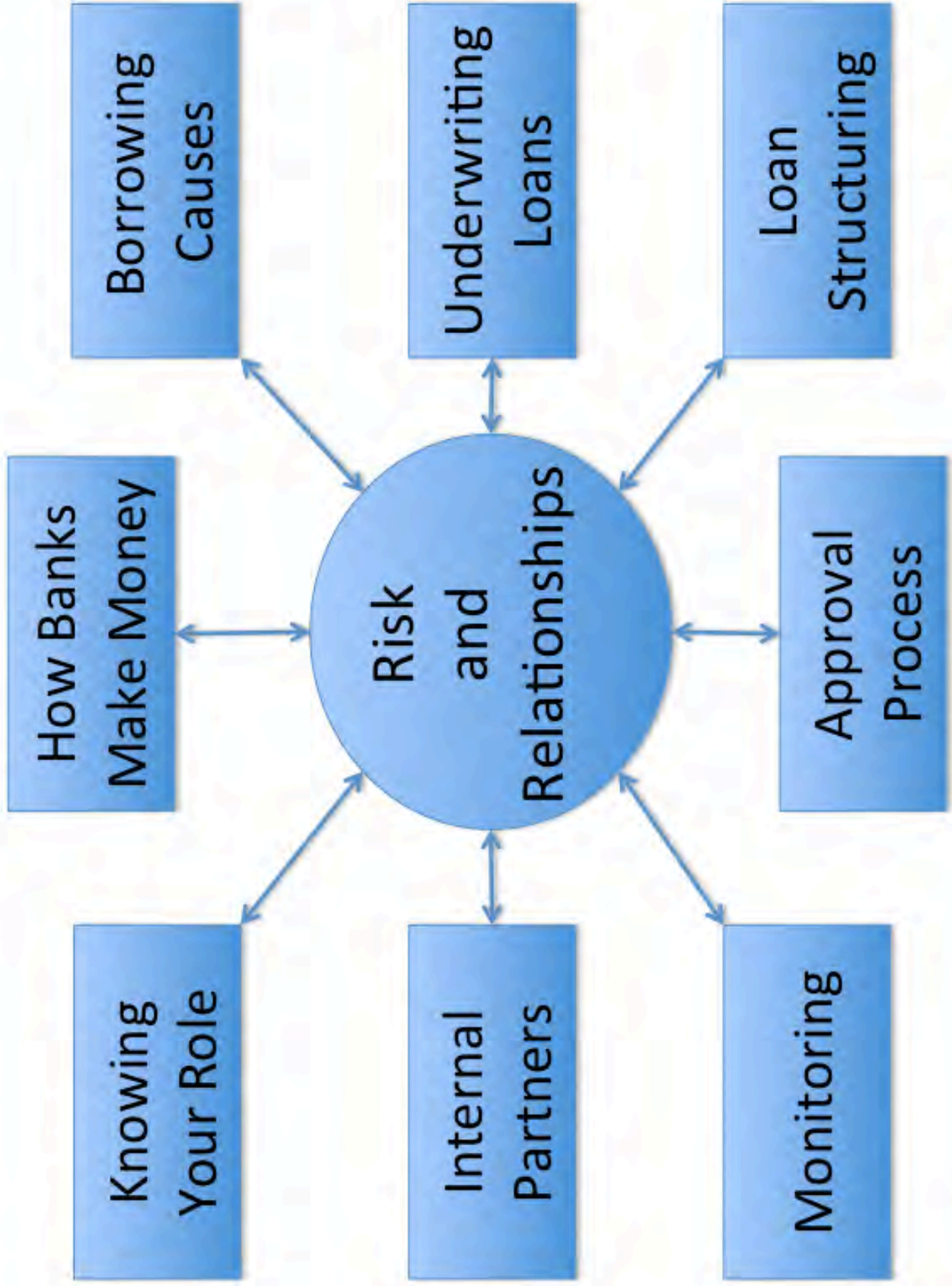




# Reference Guide

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1,000 commercial customers each keep an average of \$15,000 on deposit at Example Bank, totaling \$15MM. The bank pays 1% interest on these deposits for a total of \$150,000 in year 20XX.



\$15 MM DEPOSITS

\$150,000 INTEREST

\$15 MM LOAN

\$600,000 INTEREST



The bank lends the \$15,000,000 to a commercial customer at 4% interest, thus earning  $4\% \times \$15\text{MM} = \$600,000$  in interest income that year.

Net interest income earned by the bank in year 20XX from these customers is  $\$600,000 - \$150,000 = \$450,000$

Figure 1.1

**Example Bank**

Income Statement

A bank's primary sources of revenue

**Interest & Fee Income**

(Interest Expense)

Interest paid by bank to depositors

Net Interest Income

(Provision for Credit Losses)

Money set aside based on the Expected Loss of all existing loans

Net Interest Income after Provision

Other Income

(Personnel Expense)

(Other Expenses)

Profit Before Taxes

(Income Tax Expense)

**Net Income**

**Figure 1.2**

# Operating (Cash) Cycle



**Collect A/R**



**Buy Raw  
Materials**



**Add Value**



**Pay  
Suppliers**

**Sell INV**

**→ A/R**





## The 5 C's of Credit

<b>C</b> onditions:	Qualitative factors impacting a borrower's financial performance Do the borrower's non-financial indicators predict success?
<b>C</b> haracter:	Borrower's intent and willingness to honor the loan agreement Do you trust your borrower?
<b>C</b> apital:	Borrower's equity or willingness to share in the risk Does the borrower have "skin in the game?"
<b>C</b> apacity:	Sufficiency of borrower's cash flow to service its obligations Are the borrower's coverage ratios acceptable?
<b>C</b> ollateral:	Bank's backup plan if borrower cannot repay its loan Will the borrower pledge its assets to make the bank whole?

## Detailed Comprehensive Income Statement - Actual and %

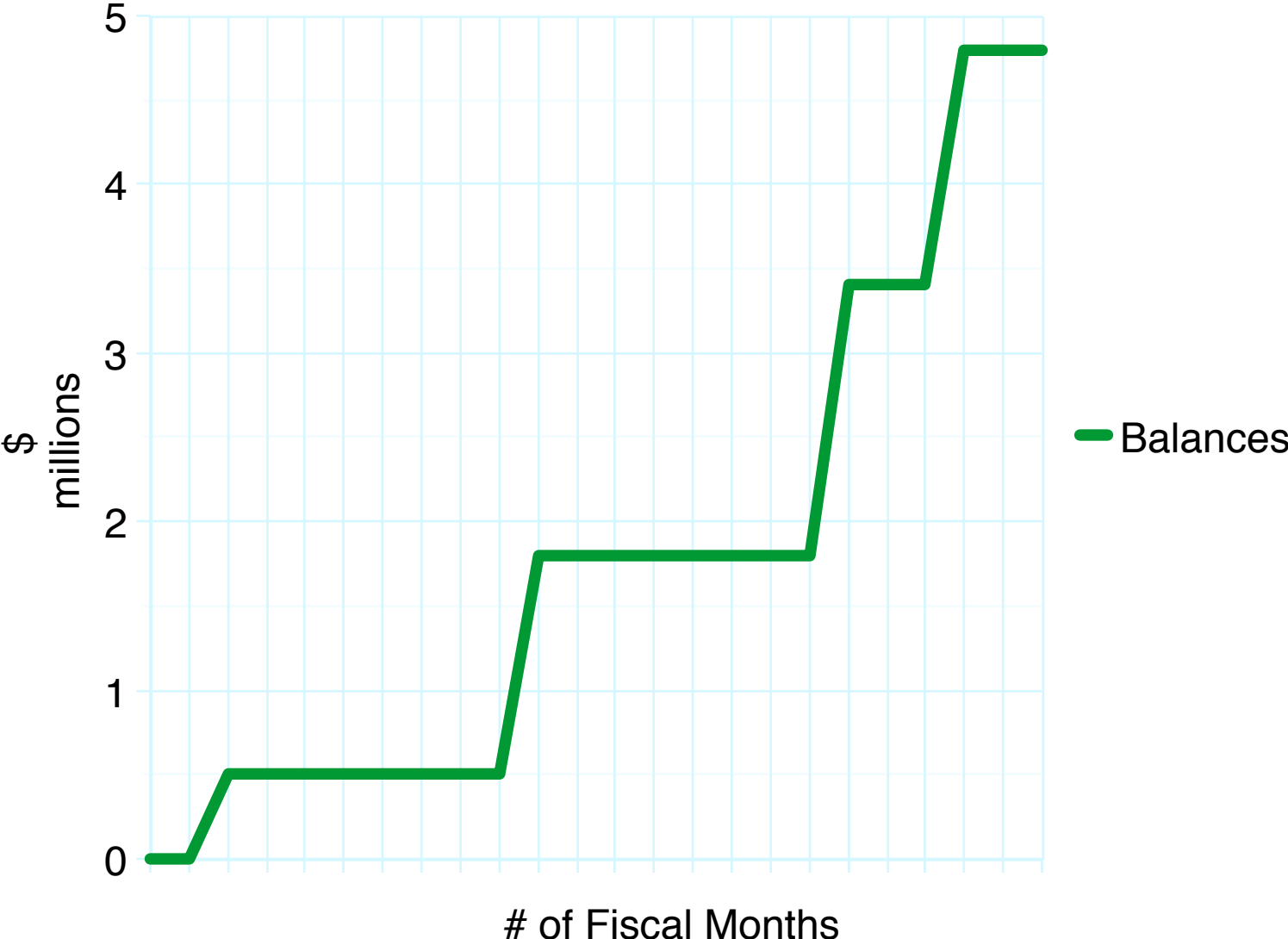
GGH Company, Inc.

Amounts Printed in Thousands

Industry Classification: NAICS Code: 123456

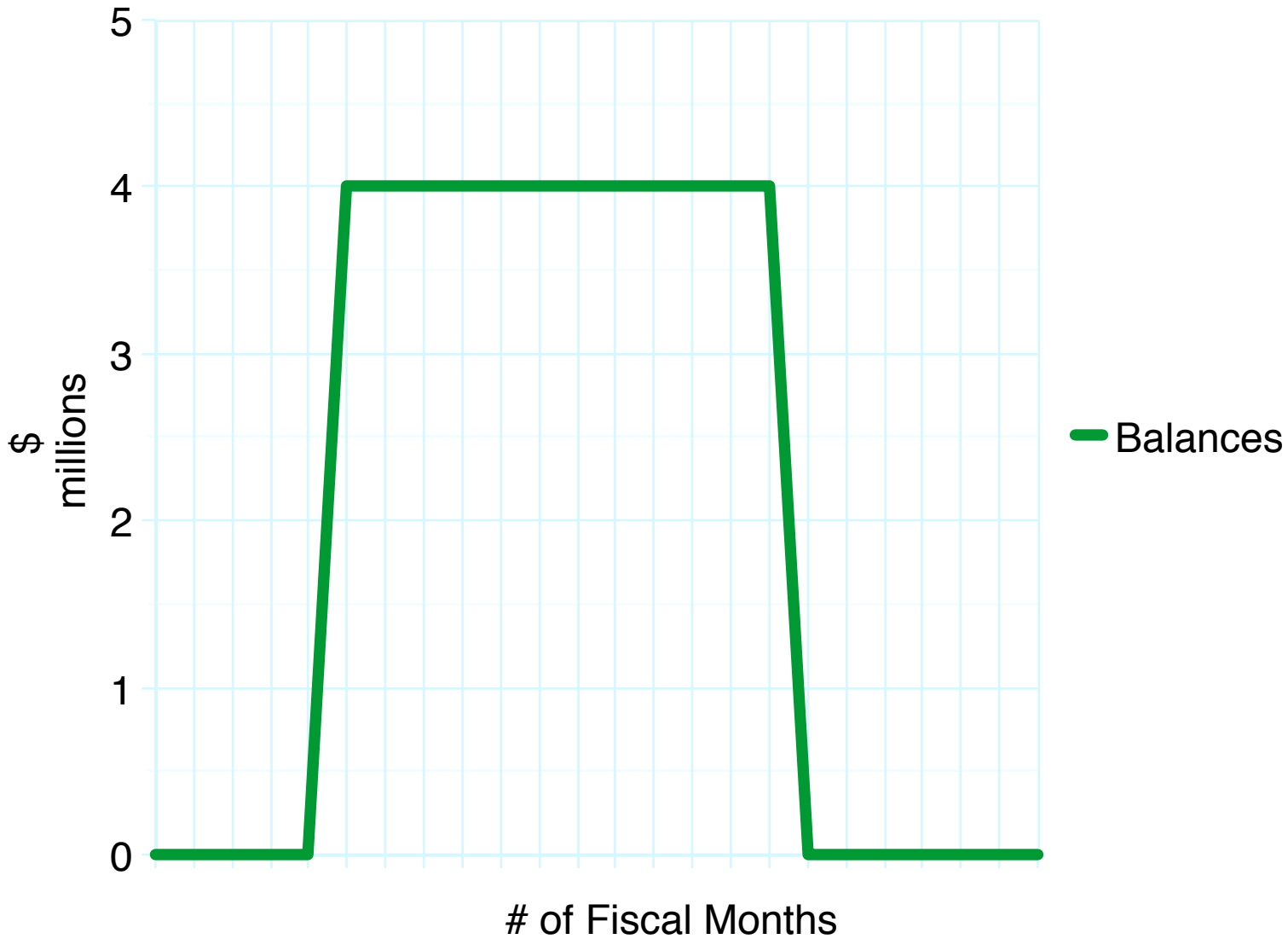
Statement Date	12/31/20X1		12/31/20X2		12/31/20X3	
Months Covered	12		12		12	
Audit Method	Reviewed		Reviewed		Reviewed	
Accountant	C. Brown, CPA		C. Brown, CPA		C. Brown, CPA	
Analyst	KTA		KTA		KTA	
Stmnt Type	Annual		Annual		Annual	
<hr/>						
SALES / REVENUE	\$156,510	100.0	\$170,920	100.0	\$183,335	100.0
Cost of Goods Sold	87,319	55.8	99,014	57.9	111,996	61.1
<hr/>						
GROSS PROFIT	69,191	44.2	71,906	42.1	71,339	38.9
SG&A Expense	11,040	7.1	12,558	7.3	12,993	7.1
Depreciation	2,381	1.5	3,875	2.3	5,041	2.7
<hr/>						
TOTAL OPERATING EXP	13,421	8.6	16,433	9.6	18,034	9.8
NET OPERATING PROFIT	55,770	35.6	55,473	32.5	53,305	29.1
Interest Expense	2,016	1.3	1,993	1.2	1,802	1.0
Other Income	441	0.3	312	0.2	711	0.4
<hr/>						
PROFIT BEFORE TAXES	54,195	34.6	53,792	31.5	52,214	28.5
Current Income Tax	15,175	9.7	15,062	8.8	14,620	8.0
<hr/>						
NET PROFIT	\$39,020	24.9	\$38,730	22.7	\$37,594	20.5

# 24-Month Construction Draw Loan

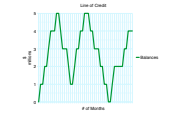
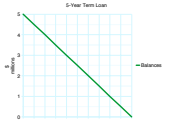

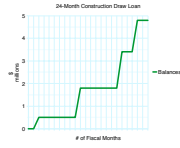
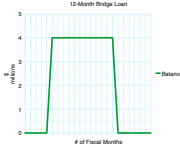




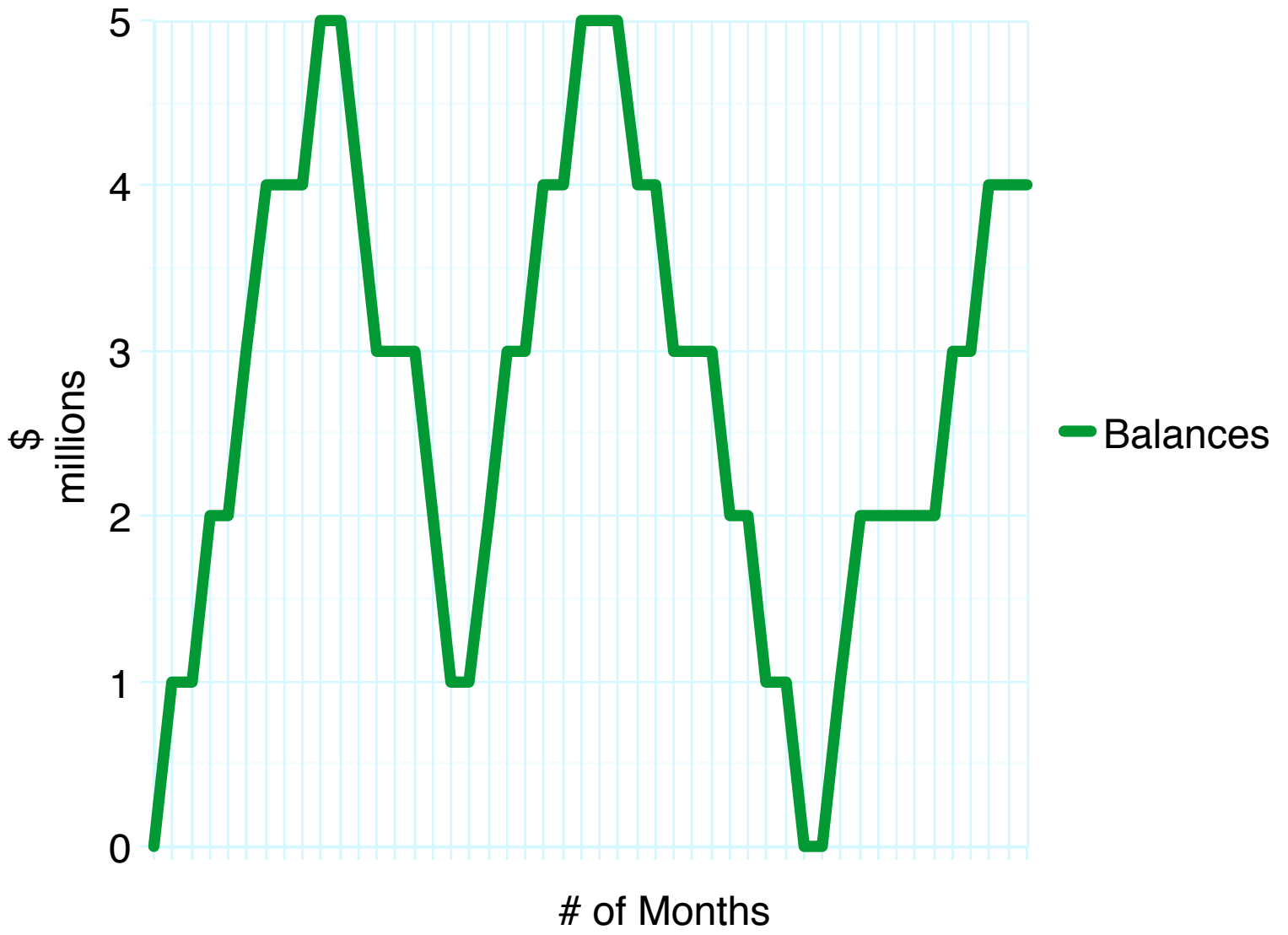
# 12-Month Bridge Loan



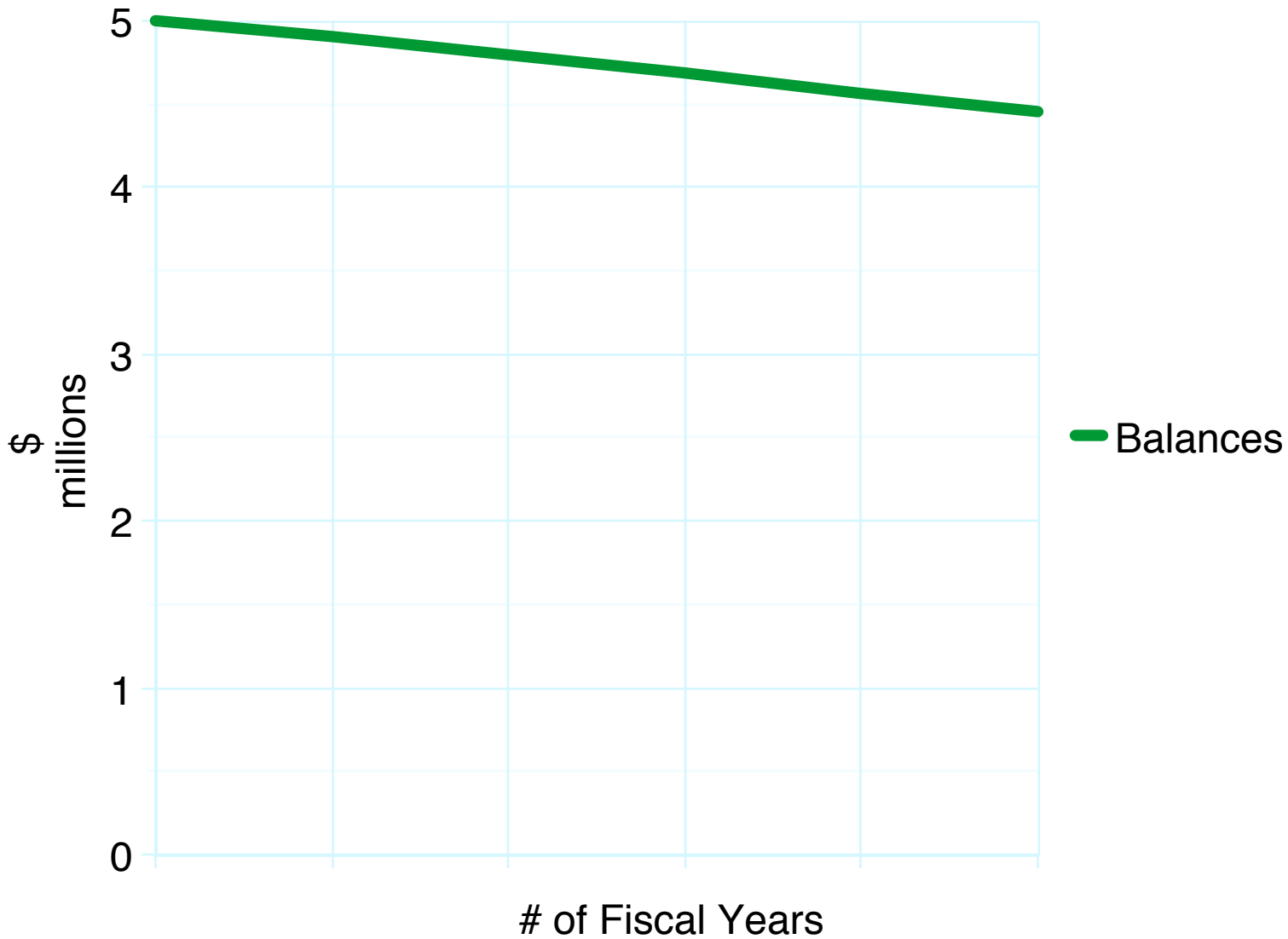
## Facility Types

Facility Type	Typical Borrowing Need	When Funds Disbursed	Amortization	Repayment Source	Able to Re-draw?	Graph of Loan Balances
Line of Credit	Working Capital	Multiple times as needed by borrower	Interest monthly, principal on demand / maturity	Conversion of INV and A/R to cash	Yes - unlimited # of times	
Term	Piece of Equipment	100% up front (at closing)	Monthly payments of P&I or P+I	Cash flow from operations over many years	No	
Mortgage	Real Estate purchase	100% up front (at closing)	Monthly payments of P&I or P+I	Cash flow from operations over many years OR tenant's rent payments	No	
Mult-Draw	Construction or multiple pieces of equipment	In large chunks during limited time period	Interest only during draw period, then monthly payments of P&I or P+I	N/A during draw period, then cash flow from operations or rent payments	Yes - only during draw period	
Bridge	Purchase distressed real estate to rehab or sell	100% up front (at closing)	Interest only during bridging period, then full principal at maturity	Liquidity event (sale of large asset) or long-term financing	No	

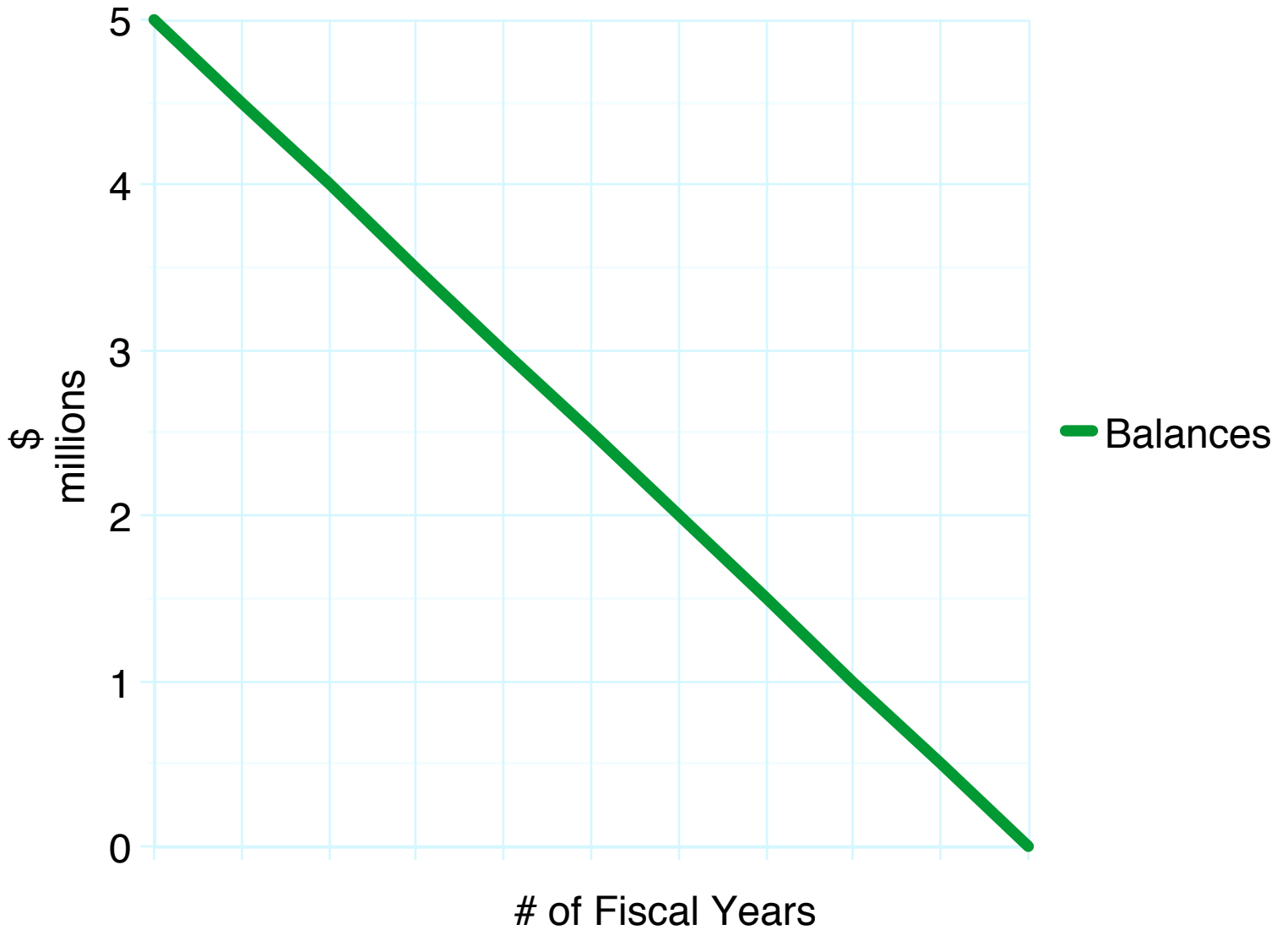
# Line of Credit



# 5-Year Mortgage Loan (25-year Am.)



# 5-Year Term Loan



## The 6 C's of Credit

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<b>C</b> ollateral:	Bank's backup plan if borrower cannot repay its loan Will the borrower pledge its assets to make the bank whole?
<b>C</b> ompetition:	Banks must be disciplined and guard against overaggressive structure What are other banks in the market offering to customers?



# Credit Approval Process Flow Chart

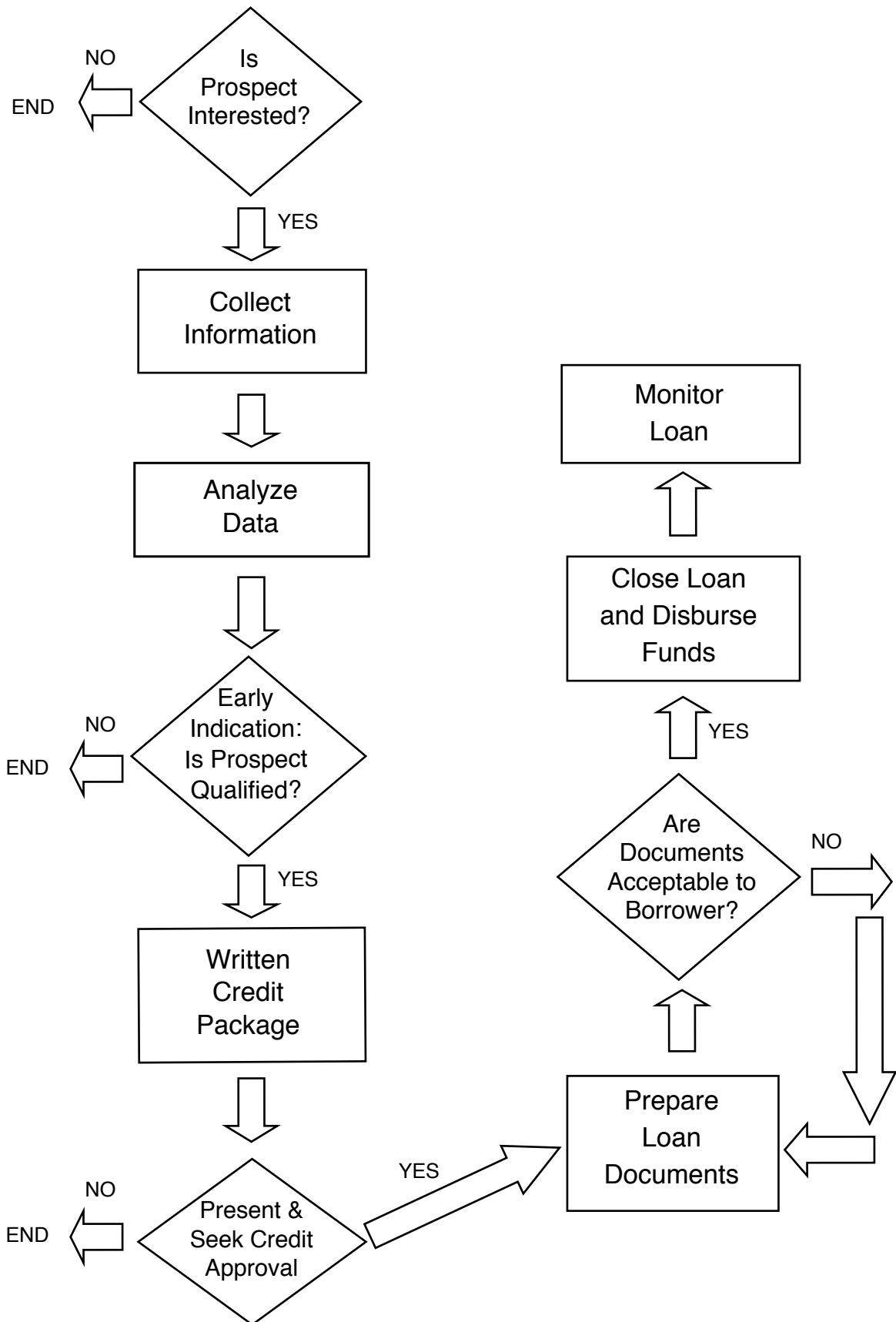


Figure 5.1

**Borrowing Base Certificate**

		<b><u>Accounts Receivable</u></b>	<b><u>Inventory</u></b>	<b><u>Total</u></b>
Collateral as of:	12/31/20XX	\$8,000,000	\$12,000,000	\$20,000,000
Less Ineligible Accounts as of:	12/31/20XX	\$1,500,000	\$3,500,000	\$5,000,000
Eligible Collateral		\$6,500,000	\$8,500,000	\$15,000,000
Rate of Advance:		80%	50%	
Net Collateral		\$5,200,000	\$4,250,000	\$9,450,000
Line of Credit Limit:				11,000,000
Less Line Balance as of:	12/31/20XX			\$6,250,000
<b>Net Availability as of:</b>	<b>12/31/20XX</b>			<b>\$3,200,000</b>

Corinne's Confections, Inc.

Loan Covenant Compliance  
As of 12/31/20XX

Ratio of *Total Liabilities to Tangible Net Worth* must not exceed  
3.0x at the end of any fiscal year  
(tested annually beginning 12/31/XX)

Total Liabilities = \$2,340,655  
Tangible Net Worth = \$1,400,722  
Ratio = 2,340,655 / 1,400,722 = 1.67x

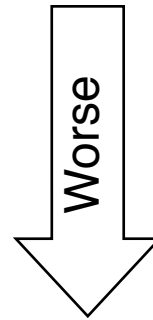
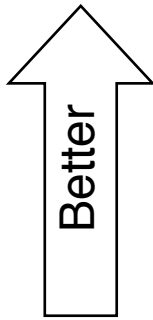
Result: In Compliance

Income Statement Data (\$000)

	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Interest Income	\$2,238,142	\$2,145,392	\$1,970,226	\$1,930,263	\$1,860,637
Interest Expense	<u>\$813,855</u>	<u>\$526,587</u>	<u>\$341,056</u>	<u>\$219,739</u>	<u>\$156,029</u>
Net Interest Income	\$1,424,287	\$1,618,805	\$1,629,170	\$1,710,524	\$1,704,608
<b>Provision for Credit Losses</b>	<u>\$2,074,671</u>	<u>\$634,547</u>	<u>\$174,059</u>	<u>\$147,388</u>	<u>\$90,045</u>
Net Interest Income after Provision	<b>\$650,384</b>	\$984,258	\$1,455,111	\$1,563,136	\$1,614,563
Net Income (loss)	<b>\$3,097,179</b>	\$312,347	\$542,613	\$641,022	\$638,741

**Regulatory Grades**

**PASS**



**(WATCH)**

**SPECIAL MENTION**

**SUBSTANDARD**

**DOUBTFUL**

**LOSS**

Criticized

Classified

### Special mention (SM)

"A special mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification."

### Substandard

"A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected."

### Doubtful

"An asset classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable."

### Loss

"Assets classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future."



## Who They Are and What They Do

Credit Administration	<i>Approving the risks</i>
Lending	<i>Winning new customers</i>
Commercial Real Estate	<i>Financing bricks and sticks</i>
Leasing	<i>Financing heavy equipment</i>
Collateral Services	<i>Trusting but verifying</i>
Private Banking	<i>Wooing the wealthy</i>
Special Loans	<i>Rehabilitating the wounded</i>
Loan Review	<i>Checking and reporting</i>
Treasury Management	<i>Generating fee income</i>
Legal	<i>Defending and protecting</i>
Regulators	<i>Looking over your shoulder</i>