7.16 Credit Analysis for Corporate Issuers

Question 1
In a bankruptcy reorganization, which of the following categories of creditors is *most likely* to have the highest recovery rate?
A. Second lien
B. Senior unsecured
C. Senior subordinated

Question 2
Which of the following choices lists the securities in the proper priority of claims, from most senior to most junior?
A. Preferred stock, second-lien debt, junior subordinated debt
B. Second-lien debt, junior subordinated debt, preferred stock
C. Junior subordinated debt, second-lien debt, preferred stock

Question 3
The following information is from a company's income statement:

	€ millions
Gross profit	7,294
Other operating income	314
Other operating expenses	6,910
Operating profit	698
Interest income	54
Interest expense	169
Income before taxes	583
Income taxes	172
Net income	411

Depreciation and amortization were €207 million for 20X0. Based on only this information, the company's EBITDA interest coverage ratio is *closest* to:
A. 4.13
B. 5.36
C. 7.87

Question 4
In traditional credit analysis, collateral is *most likely* concerned with which of the following?
A. Asset values relative to level of indebtedness
B. Projected cash flow from company operations
C. Affirmative and restrictive indenture provisions

Question 5
A company has recently declared bankruptcy and defaulted on its senior unsecured debt. Bondholders include:

	Maturity	Par value owned (USD)
Investor A	6 months	1,000,000
Investor B	6 years	5,000,000
Investor C	2 years	10,000,000

Which of the following *best* describes the right-to-payment rankings of these bondholders?
A. All have equal priority.
B. Investor A has priority.
C. Investor C has priority.

Question 6
An analyst gathered the following company data:

	SAR millions
Shareholders' equity	16.31
Total assets	40.82
Total debt	7.05
Total liabilities	24.51

Based on this information, the company's debt/capital ratio is *closest* to:
A. 17.27%
B. 30.18%
C. 43.23%

Question 7
Debtholders of a subordinated bond recovered 15% of their bond's value during a bankruptcy while the holders of a senior secured bond recovered 75% of their bond's value. The *most likely* explanation is that the:
A. various classes of claimants agreed to a negotiated settlement.
B. value of the secured property was less than the amount of the claim.
C. preferred shareholders received distributions first based on the priority of claims.

Question 8
Regarding the four Cs of credit analysis, character is *most likely* concerned with:
A. asset values relative to level of indebtedness.
B. affirmative and restrictive indenture provisions.
C. aggressive accounting policies and tax strategies.

Question 9
Which of the following is *most likely* considered strict adherence with the priority of claims in a bankruptcy proceeding?
A. All creditor classes receiving only partial settlement of their claims
B. Preferred stockholders receiving distributions only after all creditors are paid in full
C. Secured lenders receiving 100% of collateral sale proceeds to fully retire their claims

Question 10
An analyst compiles the following data for three companies:

	Total debt/total capital	Total debt/EBITDA	EBITDA/interest expense
Company X	84%	1.80	4.46
Company Y	73%	1.30	4.71
Company Z	67%	1.20	6.04

The company with the highest credit quality is *most likely*:
A. Company X.
B. Company Y.
C. Company Z.

Question 11
With regards to credit analysis, management's strategy and execution *most likely* affects:
A. capacity.
B. collateral.
C. character.

Question 12
If a corporate bond issuer defaults, which of the following categories of bondholders is *most likely* to realize the lowest recovery rate?
A. Second lien
B. Senior secured
C. Senior subordinated

Question 13
For credit analysis, limitations on dividend payments or mergers and acquisitions are *most likely* evaluated under:

A. capacity.
B. collateral.
C. covenants.

Question 14
A credit analyst has the following industry and company financial ratios:

	Total Debt / Total Capital	Total Debt / EBITDA	EBITDA / Interest Expense
Company Y	0.41	3.2	6.1
Company Z	0.62	5.7	4.6
Industry average	0.48	4.7	5.2

Based on this data, the credit rating of Company Z is *most likely*:
A. lower than Company Y.
B. the same as Company Y.
C. higher than Company Y.

Question 15
In credit analysis, collateral assessments are *most likely* to be a significant concern if a company:
A. has stock that is trading below book value.
B. carries high-quality intangibles on its balance sheet.
C. reports large capital expenditures relative to depreciation expense.

Question 16
An analyst compiles the following information for a company:

£	20X1	20X2	20X3
Total debt	912	1,200	2,010
Shareholders' equity	165	173	186
Total capital	1,077	1,373	2,196
Operating profit	246	210	205
Depreciation and amortization	262	146	314
Interest expense	114	75	100

Based on the trends in the company's ratio of total debt to total capital and its ratio of EBITDA to interest expense over the three-year period, the *most appropriate* conclusion is that the company's ability to pay interest payments is:

A. increasing and its ability to repay principal is increasing.
B. increasing and its ability to repay principal is decreasing.
C. decreasing and its ability to repay principal is increasing.

Question 17
For credit analysis, when assessing an issuer's capacity an analyst should *most appropriately* consider:
A. management's track record.
B. EBITDA and coverage ratios.
C. asset values versus outstanding debt.