

AEB 4138 – Assignment 2

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1. Consider the bank balance sheet presented in Table 1 compute the capital adequacy of this bank. How should you rate “Preferred stock” (is it Tier 1 or Tier 2)?
2. Assume that Deposits from other banks earn 1.5 %, Mortgaged Backed Securities earn 3.5 % and Home Mortgages earn 5.0 % (also assume that the bank received \$ 15,000 in principal payments during the year, but made an additional \$ 17,500 in loans). Assume further that the operating expenses were \$ 7,500. Make the accounting entries to recognize this year’s transactions assuming that \$ 2,500 is paid in dividends. Create the income statement and balance sheets for the bank at the end of the year.
3. How did the capital adequacy change? Is that better or worse?

Table 1: Balance Sheet for the First National Bank of Delhi

Asset	Value	Net Value	Equity	Value
Cash (C_1)		25,000	Deposits	375,000
Deposits in Other Banks (C_2)		5,000	Common Stock ($T1$)	15,000
Mortgaged Backed Securities (C_3)		125,000	Preferred Stock ($T?$)	5,000
Home Mortgages (C_4)	250,000		Retained Earnings ($T1$)	5,000
Allowance for Bad Debt	5,000	245,000		
Total Assets		400,000	Total Debt and Equity	400,000