

Business Performance Review



Sample Company

as of

December 31, 2008

BUSINESS VALUATIONS & STRATEGIES

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Table of Contents

Financial Analysis	3
Approach.....	3
Results.....	4
Comments & Suggestions	4
Ratio Analysis	5
Summarized Financial Data.....	13
Historical Data.....	13
Common-Sized Data.....	14
Industry Scorecard	15

Financial Analysis

Approach

Historical & Common-size Financial Data

This analysis includes an evaluation of the Company's summarized financial information from federal income tax returns on a historical basis. In order to portray the relative size of financial statement items for comparison over time, each line item in the common-size financial statements is expressed as a percentage of total assets or total revenue.

Financial Ratios

This analysis includes an evaluation of commonly used financial ratios. These ratios fall within the following categories:

- Liquidity ratios measure the ability to meet short-term obligations,
- Leverage ratios (borrowing) measure reliance on debt and overall vulnerability to business downturns,
- Activity or operating ratios (assets) measure how effectively assets are used to produce revenue, and
- Profitability ratios measure overall performance.

Although industry statistics are a useful source of general analytical data, there can be significant variation in the reporting practices and operational methods of companies within a given industry. Therefore, industry statistics as used throughout this report should not be regarded as absolute norms or standards.

Ratio Analysis

Each section of the ratio analysis (Liquidity, Profits & Profit Margin, etc.) contains a numerical score/grade, which is a rough measure of overall performance in the area. The scores are derived by evaluating the company's trends, either positive or negative, over time and by comparing the company to industry averages for different metrics. Each grade represents a score from 1 to 100, with 1 being the lowest score and 100 being the highest.

The Scoring results represent the following levels of performance:

- 0 – 20 = Low (Very poor)
- 21 – 40 = Below average (Poor)
- 41 – 60 = Average (Okay)
- 61 – 80 = Above average (Good)
- 81 – 100 = High (Excellent)

Sample Company

Business Performance Review

Results

Based on the procedures described above here are your company's scores:

- Overall 65
- Liquidity 57
- Profits & Profit Margins 39
- Sales 79
- Borrowing 89
- Assets 61

Comments & Suggestions

Strengths

Your company's greatest financial strength is its ability to consistently increase sales while reducing debt significantly. These conditions have produced a strong balance sheet with good liquidity. The balance sheet represents a snap-shot of your company's current financial condition.

Weaknesses

The biggest weakness is your payroll costs. They are way out of line with the industry. High payroll costs are the primary reason your company scored poorly in profits & profit margins. Your company's gross profit margins look misleadingly good because your cost of sales does not include direct labor, like the industry does. Net profit margins are a better indicator of performance and yours are not good. Over time, consistently low profits will erode the strength in your balance sheet.

Suggestions

Monitor your payroll costs closely to cut costs. An accurate job costing system will help monitor labor costs for each job. Consider removing any excess staff through attrition and retirement incentives. Incentive-based compensation and/or a profit-sharing plan can encourage employees to be more efficient and productive.

Please contact me if you have any questions about this report or our analysis. I will gladly review this report with you at your earliest convenience. We welcome your comments and suggestions about how to make the Business Performance Review better.



David Coffman

Ratio Analysis

LIQUIDITY

57 out of 100

Generally, what is the company's ability to meet obligations as they come due?

Operating Cash Flow Results

Cash flow results for the company are mixed and slightly unusual. Cash flow is at a healthy level, although it has declined relative to sales since last period. The company is generating this cash flow despite weak profitability, which is not typical. It may be helpful to investigate where the cash flow is coming from – is it related to operations, or is it due to Balance Sheet transactions that will not be repeated in the future?

General Liquidity Conditions

It could be possible that the company has a targeted liquidity position. Notice that sales and profits have risen, yet the company still only has a fair position. It might be the case that management is pushing extra current asset resources into growing the company, which would be good.

The company's liquidity position has stayed about the same as it was last period. Liquidity is "fair" in several of the ways it is calibrated. Although it is not certain that it will be difficult to meet obligations as a result, it is often the case that only having "fair" scores here means that the firm may possibly have periodic trouble.

More importantly, in this current position the company may concede to the competition the ability to spend more money to grow their businesses. The true benefit of strong liquidity is the ability to invest in the "growth factors" that drive **future** profitability. Profits are necessary to have liquidity, but present liquidity is necessary to push future profits. Liquidity analysis is generally too limited to make broad conclusions.

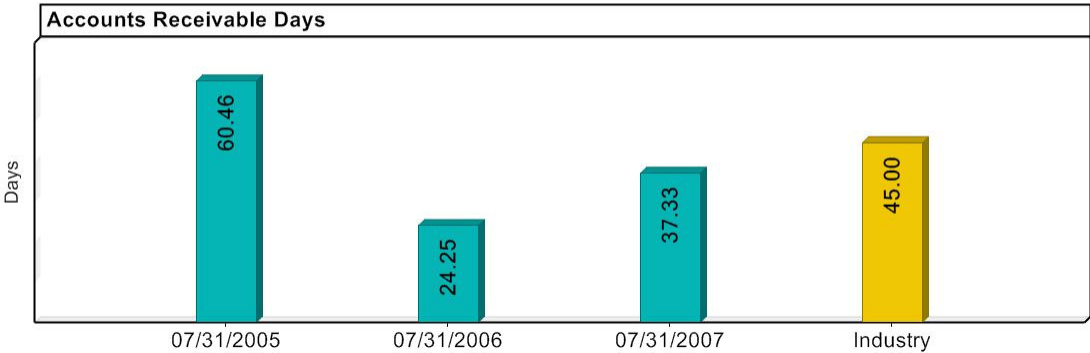
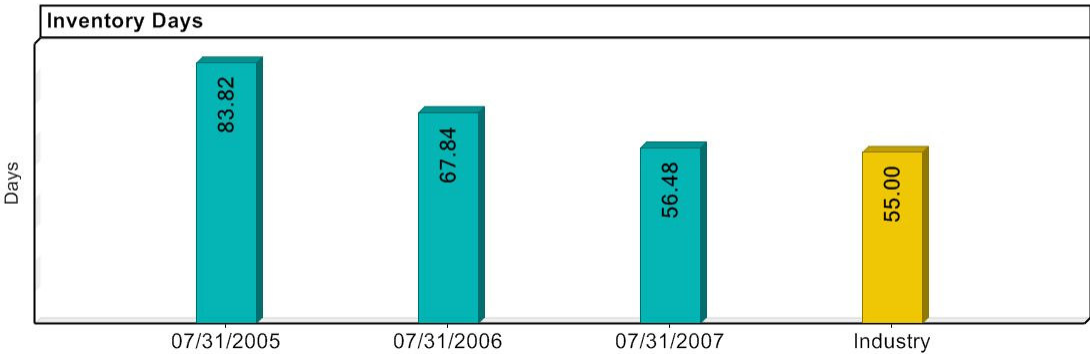
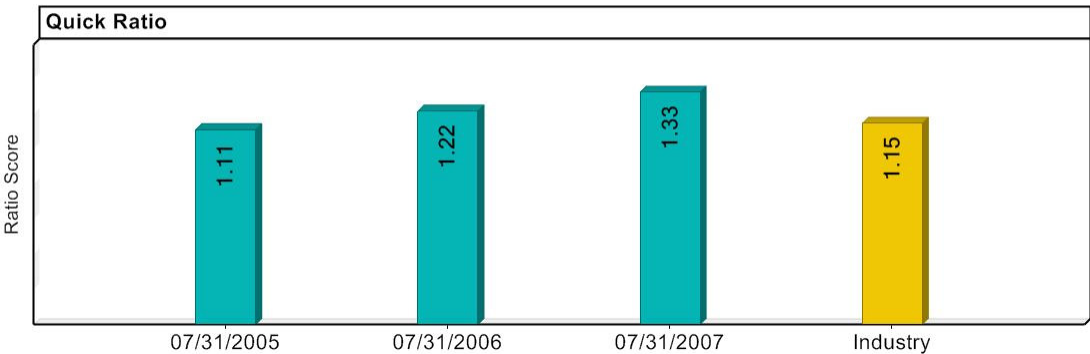
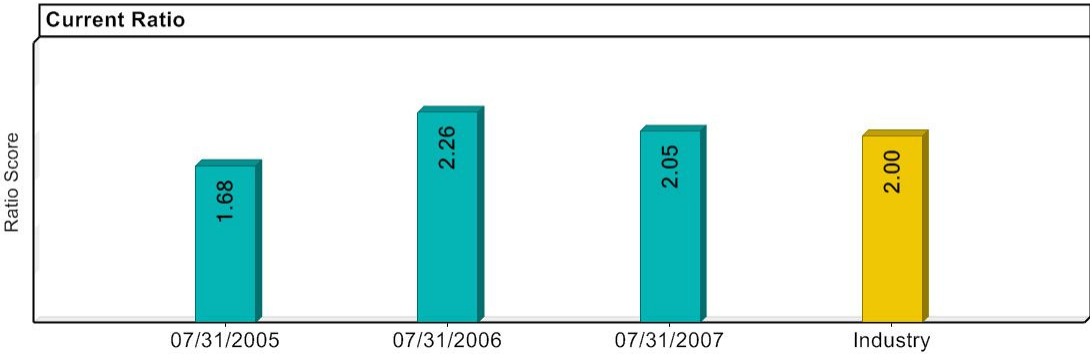
With regard to liquidity turnover performance, the company is operating in the norm. This company's results in terms of inventory days, accounts receivable days, and accounts payable days are all about average right now compared to others in the industry. Nothing drastic needs to take place in terms of these metrics, although turning inventory more quickly and collecting receivables faster could be beneficial to the cash position of the company.

Here are some ideas/actions that managers might consider in managing liquidity:

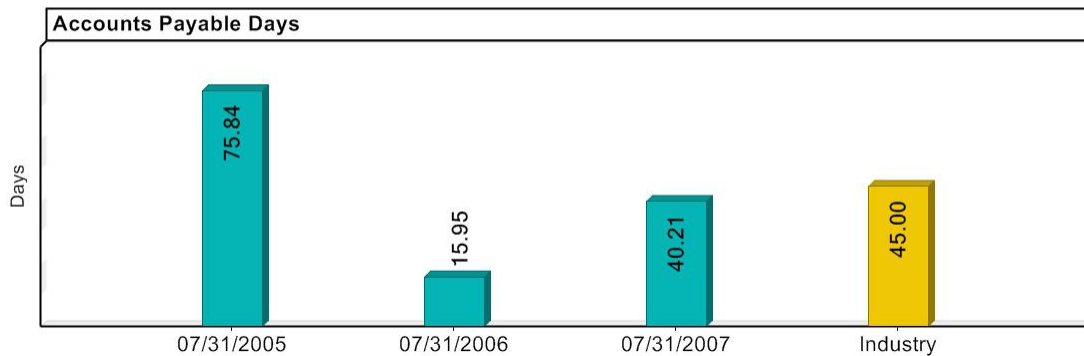
- Monitor accounts receivable on a weekly basis, and charge interest on invoices that are past due.
- Use cash on delivery (COD) for chronically slow payers, when possible. Simply require payment when the service is performed or the product is delivered. This will ensure that compensation is received in a timely manner.
- Monitor invoicing procedures to help ensure correctness. Nothing will delay payment from a customer more than sending out an incorrect invoice. This will extend Accounts Receivable and hurt cash flow.
- Monitor the impact tax payments may have on cash. Keep enough money aside to be able to meet future tax obligations based on earnings.

LIMITS TO LIQUIDITY ANALYSIS: Keep in mind that liquidity conditions are volatile and this is a general analysis looking at a snapshot in time. Review this section, but do not overly rely on it.

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PROFITS & PROFIT MARGIN

39 out of 100

Are profitability trends favorable in the company?

It is positive to see that all of this company's key profitability ratios are moving in the right direction this period. Even though the net profit margin is still weak, it has improved by 54.88% this period, which is very positive. This means that the company is doing a better job of managing the company's growth than it did last period, and that a lower percentage of each sales dollar is being eaten away by operating costs. The company's net profit dollars have increased significantly this period as well. If the company can continue to increase sales and control expenses, it should be able to elevate profitability to an acceptable level.

It is particularly important for the company to control overhead and operating expenses now. The temptation might be to increase spending because the company is doing better than last period. However, the fact is that managers need to remember that **net margins are still weak**. Weak margins and levels of profit make for lower returns on assets and equity. The company should focus on improving its net margins and profits to the point where they are at least in line with the industry average before increasing overhead and operating expenses.

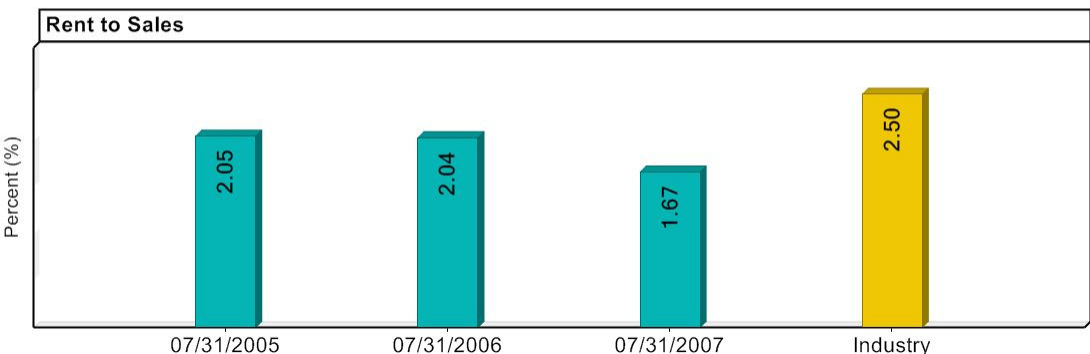
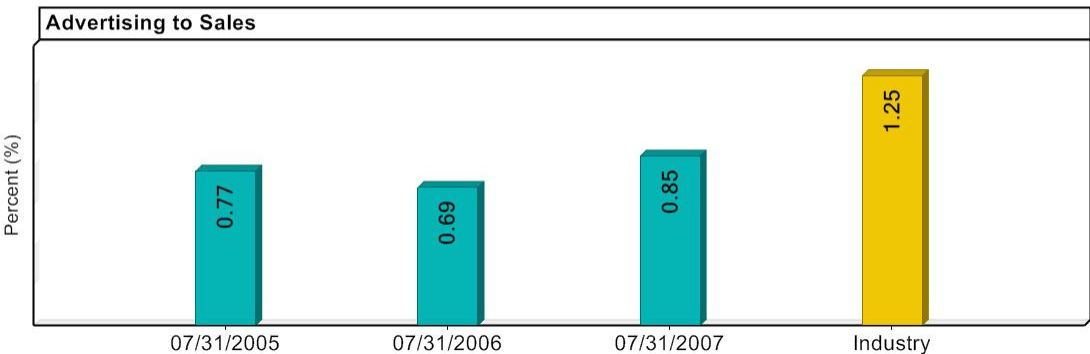
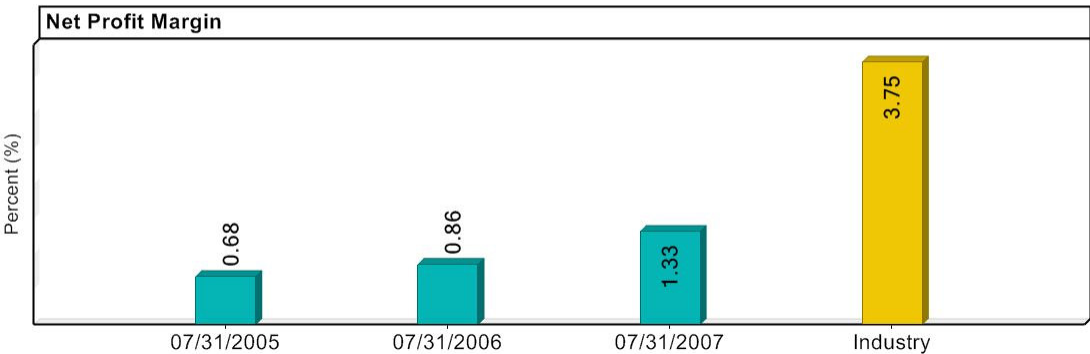
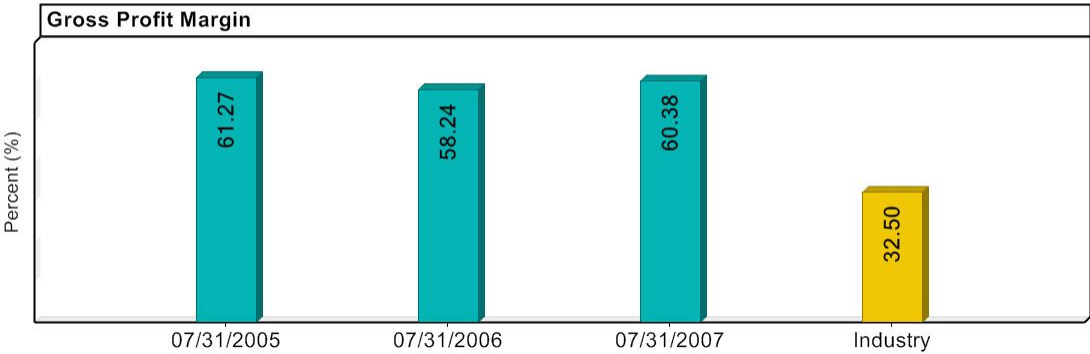
Finally, although the company's sales have risen from last period, they are only rising at healthy levels, not at excellent levels. Therefore, managers should not expect to see expenses decrease at a great rate relative to sales volume unless the company is managing expenses very well. In general, if the company is increasing its sales at the current rate, it will need to keep its operating expenses in control in order to boost net margins.

The following ideas to improve profitability might be useful and can be thought-through by managers:

- Use systems that can track sales of products at varying prices. This can help determine an ideal price where sales and revenue are maximized. Also, keeping track of sales per customer can help the business determine if additional items, similar to the current offering, can be sold as a way to increase sales.
- Obtain an annual business check-up. Meet with an accountant or banker to review financial statements and get advice on how to improve performance.
- Generate accurate financial reports on a timely basis -- within 40 days of the end of the financial period. This will help ensure the usefulness of the data for examination purposes. Good financial reports are the backbone of management decisions.
- Reduce payroll costs, including any overtime expenses as applicable, by maintaining an ideal number of employees and monitoring the number of hours that each employee works.

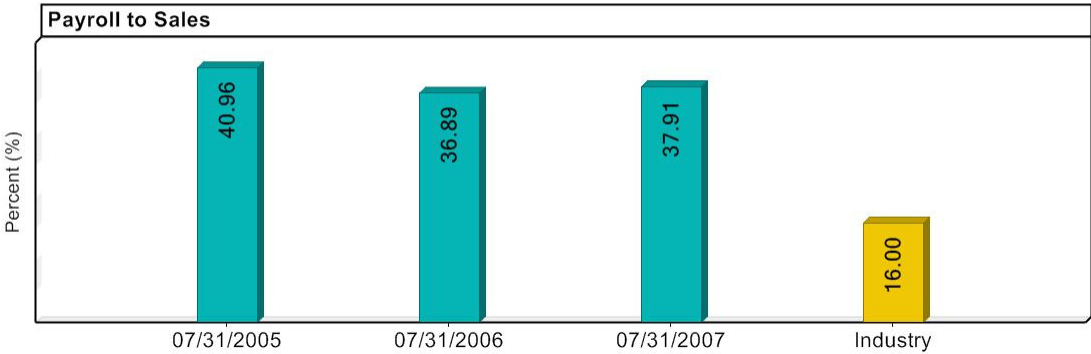
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Business Performance Review



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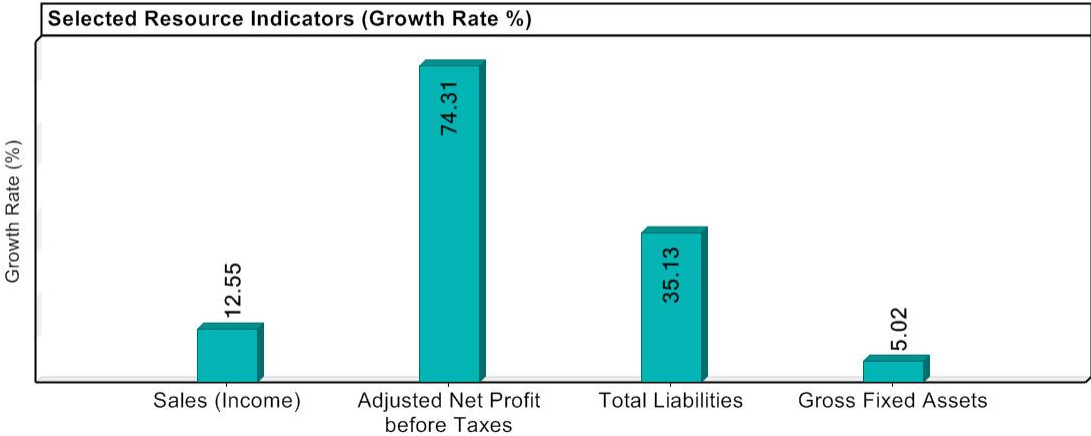


SALES

79 out of 100

Are sales growing and satisfactory?

Sales increases by themselves do not mean much; companies are typically more interested in net profitability results. Sales changes are also relatively easy to interpret -- sales are either up or down. However, this company's sales results for this period are a bit deeper and more intriguing. The company has increased sales with about the same amount of fixed assets. Basically, the company is "driving" more sales through relatively the same level of resources. This is a good dynamic in the sales area that will **potentially** yield higher net profitability in the long run.



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Business Performance Review

BORROWING

89 out of 100

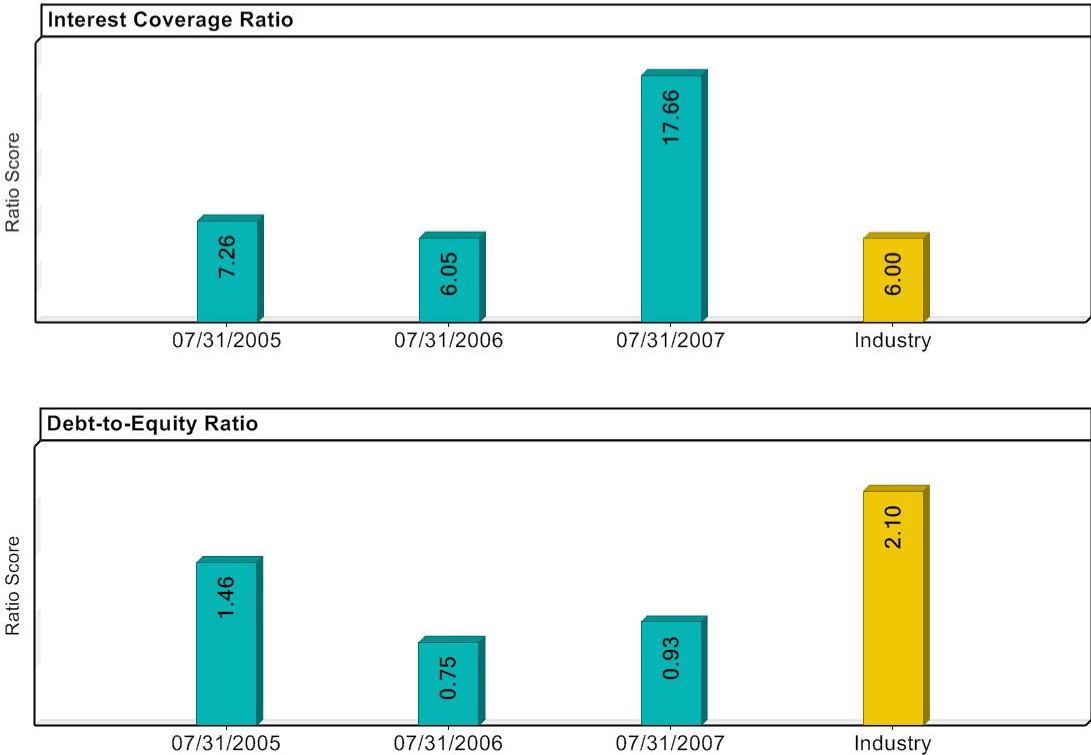
Is the company borrowing profitably?

Borrowing (using leverage) is a valuable tool for a business -- borrowing can improve profitability significantly. The only problem is that the effectiveness of leverage depends upon how well the company is using it. Borrowing has great power. However, it must be applied under the right terms, for the right assets, and in the right environment.

This company has performed well in this area. Profitability was substantially improved by 74.31% as significant debt was added. In fact, even though there is more debt on the books this period, the net profit margin improved as well. It is always positive to not lose margin when adding either short-term or long-term debt.

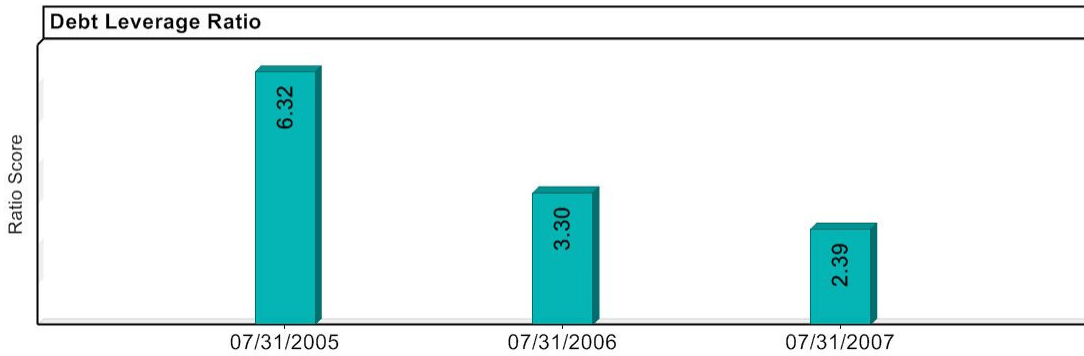
When a company receives a good score in this area, it is still quite important to evaluate real returns. For example, the trend here is good, but the company will still want to determine the rates of return on assets and borrowed money. This report only indicates trends, not acceptable rates of return on borrowed funds.

The overall trend in this area seems to be positive. The company has a relatively low level of debt as compared to its equity, and has demonstrated the ability to generate adequate earnings (before interest and non-cash expenses) to cover its interest obligations. Since the company seems to be able to cover its current debt obligations and is not highly levered, it may be able to borrow effectively to help foster future growth. Of course, this must be carefully evaluated by the company's management.



Sample Company

Business Performance Review



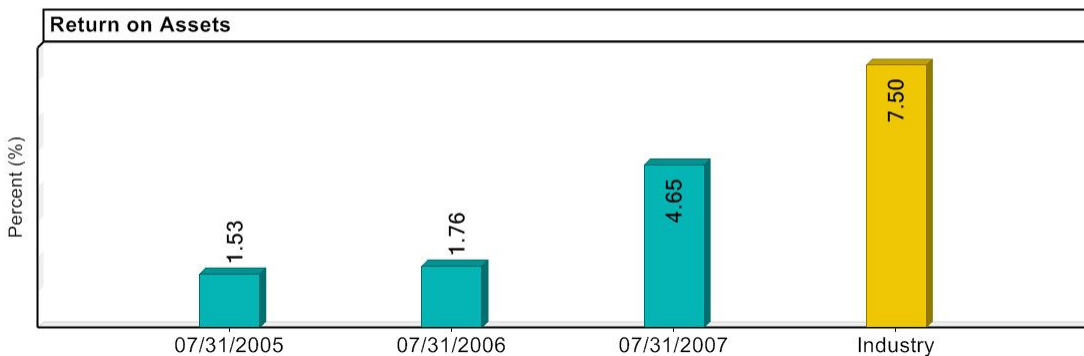
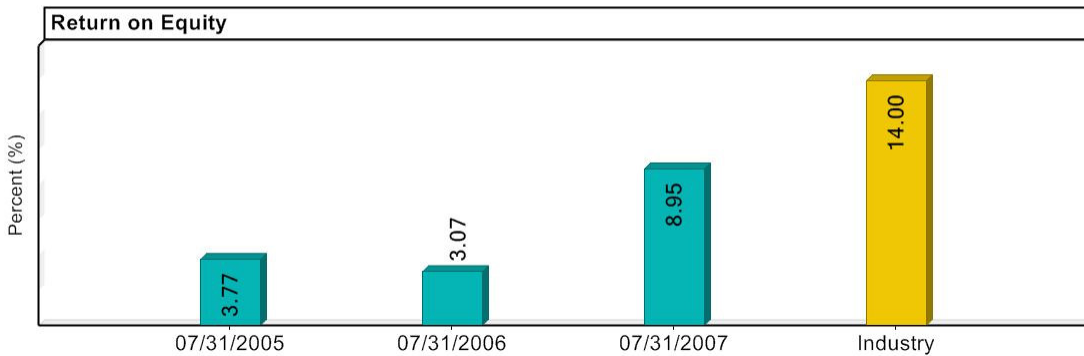
ASSETS

61 out of 100

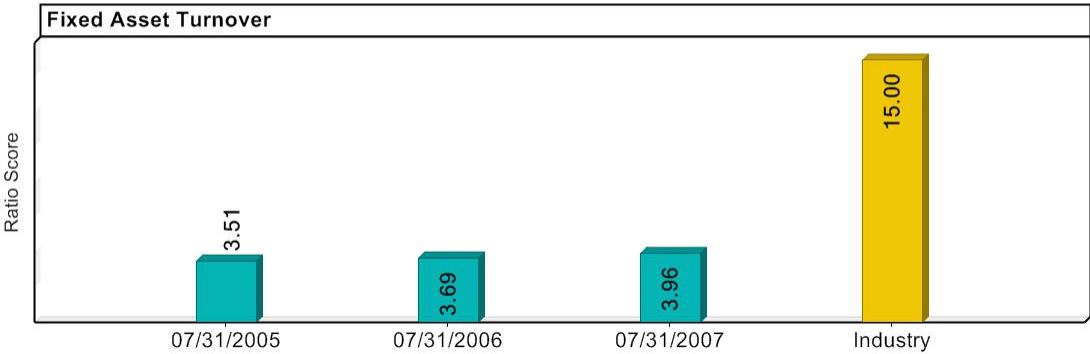
Is the company using gross fixed assets effectively?

These are some very good results, at least for this section. The company considerably improved profitability with about the same level of resources (fixed assets). This means that the company is now using its assets more effectively. It **may** also indicate that the company might have some room to further grow profitability within its current operating environment (while maintaining relatively the same level of assets). Furthermore, note the improvement in the net profit margin. The company has become more efficient within its present structure.

The company generated a relatively poor return on assets, and did not do a good job of using its fixed asset base to produce sales this period. This may be an area of concern in the future, because sales revenue is important for generating returns.



Sample Company Business Performance Review



Sample Company Business Performance Review

Summarized Financial Data

Historical Data

	07/31/2005	07/31/2006	07/31/2007
<u>Income Statement Data</u>			
Sales (Income)	\$3,163,165	\$3,547,770	\$3,992,881
Cost of Sales (COGS)	\$1,225,204	\$1,481,505	\$1,582,150
Gross Profit	\$1,937,961	\$2,066,265	\$2,410,731
Gross Profit Margin	61.27%	58.24%	60.38%
Payroll / Wages / Salary	\$1,295,749	\$1,308,721	\$1,513,540
Rent	\$64,922	\$72,255	\$66,555
Advertising	\$24,430	\$24,508	\$33,815
Depreciation	\$73,259	\$61,428	\$140,721
Interest Expense	\$15,160	\$18,198	\$11,627
Net Profit before Taxes	\$21,622	\$30,408	\$53,004
Adjusted Net Profit before Taxes	\$21,622	\$30,408	\$53,004
Net Profit Margin	0.68%	0.86%	1.33%
EBITDA	\$110,041	\$110,034	\$205,352
Net Income	\$17,975	\$14,937	\$47,324

Balance Sheet Data

Cash (Bank Funds)	\$31,821	\$71,105	\$52,970
Accounts Receivable	\$523,933	\$235,718	\$408,349
Inventory	\$281,364	\$275,351	\$244,830
Total Current Assets	\$838,388	\$566,703	\$712,111
Gross Fixed Assets	\$900,408	\$961,270	\$1,009,503
Total Assets	\$1,171,912	\$848,931	\$1,018,726
Accounts Payable	\$254,583	\$64,750	\$174,285
Total Current Liabilities	\$498,878	\$251,303	\$347,218
Total Liabilities	\$695,689	\$362,741	\$490,182
Total Equity	\$476,223	\$486,190	\$528,544

Sample Company Business Performance Review

Common-Sized Data

	07/31/2005	07/31/2006	07/31/2007	Industry (307)
<u>Income Statement Data</u>				
Sales (Income)	100%	100%	100%	100%
Cost of Sales (COGS)	39%	42%	40%	68%
Gross Profit	61%	58%	60%	32%
Payroll / Wages / Salary	41%	37%	38%	14%
Rent	2%	2%	2%	2%
Advertising	1%	1%	1%	1%
Depreciation	2%	2%	4%	1%
Interest Expense	0%	1%	0%	1%
Net Profit before Taxes	1%	1%	1%	4%
Adjusted Net Profit before Taxes	1%	1%	1%	5%
EBITDA	3%	3%	5%	5%
Net Income	1%	0%	1%	4%
<u>Balance Sheet Data</u>				
Cash (Bank Funds)	3%	8%	5%	13%
Accounts Receivable	45%	28%	40%	31%
Inventory	24%	32%	24%	30%
Total Current Assets	72%	67%	70%	86%
Gross Fixed Assets	77%	113%	99%	22%
Total Assets	100%	100%	100%	100%
Accounts Payable	22%	8%	17%	30%
Total Current Liabilities	43%	30%	34%	51%
Total Liabilities	59%	43%	48%	67%
Total Equity	41%	57%	52%	32%

Sample Company

Business Performance Review

Industry Scorecard

Financial Indicator	Current Period	Industry Range	Distance from Industry
Current Ratio = Total Current Assets / Total Current Liabilities Explanation: Generally, this metric measures the overall liquidity position of a company. It is certainly not a perfect barometer, but it is a good one. Watch for big decreases in this number over time. Make sure the accounts listed in "current assets" are collectible. The higher the ratio, the more liquid the company is.	2.05	1.40 to 2.60	0.00%
Quick Ratio = (Cash + Accounts Receivable) / Total Current Liabilities Explanation: This is another good indicator of liquidity, although by itself, it is not a perfect one. If there are receivable accounts included in the numerator, they should be collectible. Look at the length of time the company has to pay the amount listed in the denominator (current liabilities). The higher the number, the stronger the company.	1.33	0.70 to 1.60	0.00%
Inventory Days = (Inventory / COGS) * 365 Explanation: This metric shows how much inventory (in days) is on hand. It indicates how quickly a company can respond to market and/or product changes. Not all companies have inventory for this metric. The lower the better.	56.48 Days	40.00 to 70.00 Days	0.00%
Accounts Receivable Days = (Accounts Receivable / Sales) * 365 Explanation: This number reflects the average length of time between credit sales and payment receipts. It is crucial to maintaining positive liquidity. The lower the better.	37.33 Days	30.00 to 60.00 Days	0.00%
Accounts Payable Days = (Accounts Payable / COGS) * 365 Explanation: This ratio shows the average number of days that lapse between the purchase of material and labor, and payment for them. It is a rough measure of how timely a company is in meeting payment obligations. Lower is normally better.	40.21 Days	30.00 to 60.00 Days	0.00%
Gross Profit Margin = Gross Profit / Sales Explanation: This number indicates the percentage of sales revenue that is paid out in direct costs (costs of sales). It is an important statistic that can be used in business planning because it indicates how many cents of gross profit can be generated by future sales. Higher is normally better (the company is more efficient).	60.38%	25.00% to 40.00%	+50.95%
Net Profit Margin = Adjusted Net Profit before Taxes / Sales Explanation: This is an important metric. In fact, over time, it is one of the more important barometers that we look at. It measures how many cents of profit the company is generating for every dollar it sells. Track it carefully against industry competitors. This is a very important number in preparing forecasts. The higher the better.	1.33%	1.50% to 6.00%	-11.33%
Advertising to Sales = Advertising / Sales Explanation: This metric shows advertising expense for the company as a percentage of sales.	0.85%	0.50% to 2.00%	0.00%
Rent to Sales = Rent / Sales Explanation: This metric shows rent expense for the company as a percentage of sales.	1.67%	1.00% to 4.00%	0.00%
Payroll to Sales = Payroll Expense / Sales Explanation: This metric shows payroll expense for the company as a percentage of sales.	37.91%	10.00% to 22.00%	-72.32%
Interest Coverage Ratio = EBITDA / Interest Expense Explanation: This ratio measures a company's ability to service debt payments from operating cash flow (EBITDA). An increasing ratio is a good indicator of improving credit quality. The higher the better.	17.66	3.00 to 9.00	+96.22%

Sample Company Business Performance Review

Financial Indicator	Current Period	Industry Range	Distance from Industry
Debt-to-Equity Ratio = Total Liabilities / Total Equity Explanation: This Balance Sheet leverage ratio indicates the composition of a company's total capitalization -- the balance between money or assets owed versus the money or assets owned. Generally, creditors prefer a lower ratio to decrease financial risk while investors prefer a higher ratio to realize the return benefits of financial leverage.	0.93	1.20 to 3.00	+22.50%
Debt Leverage Ratio = Total Liabilities / EBITDA Explanation: This ratio measures a company's ability to repay debt obligations from annualized operating cash flow (EBITDA).	2.39	N/A	N/A
Return on Equity = Net Income / Total Equity Explanation: This measure shows how much profit is being returned on the shareholders' equity each year. It is a vital statistic from the perspective of equity holders in a company. The higher the better.	8.95%	8.00% to 20.00%	0.00%
Return on Assets = Net Income / Total Assets Explanation: This calculation measures the company's ability to use its assets to create profits. Basically, ROA indicates how many cents of profit each dollar of asset is producing per year. It is quite important since managers can only be evaluated by looking at how they use the assets available to them. The higher the better.	4.65%	5.00% to 10.00%	-7.00%
Fixed Asset Turnover = Sales / Gross Fixed Assets Explanation: This asset management ratio shows the multiple of annualized sales that each dollar of gross fixed assets is producing. This indicator measures how well fixed assets are "throwing off" sales and is very important to businesses that require significant investments in such assets. Readers should not emphasize this metric when looking at companies that do not possess or require significant gross fixed assets. The higher the more effective the company's investments in Net Property, Plant, and Equipment are.	3.96	10.00 to 20.00	-60.40%

NOTE: Exceptions are sometimes applied when calculating the Financial Indicators. Generally, this occurs when the inputs used to calculate the ratios are zero and/or negative.

READER: Financial analysis is not a science; it is about interpretation and evaluation of financial events. Therefore, some judgment will always be part of our reports and analyses. Before making any financial decision, always consult an experienced and knowledgeable professional (accountant, banker, financial planner, attorney, etc.).

Source:

SageWorks Industry Data

NAICS 42369 – Other Electronic Parts & Equipment Merchant Wholesalers