

AVERAGE JOE'S GYM

Background

You are an Analyst for the professional service firm, BUSI 1043 LLP. Your firm specializes in providing a wide variety of internal business solutions for different clients. After 4 months on the job, you walk into the partner's office to provide him with your two-week notice. Given your excellent performance over the past few months, rival professional service firm, BUSI 2083 LLP has provided you with an offer you cannot refuse by providing you with a promotion to Consultant and a significant raise. Although sad to see you go, lead partner Justin Medakiewicz requested assistance on one last engagement: Average Joe's Gym.

Additional Information

Average Joe's caters to families and gives a substantial discount for families to work out together. Families that workout together reach their goals together. Members receive 2 free training sessions with enrollment so that they may start reaching their goals as soon as they sign up. The exercise specialists that provide the training to the members hold the highest certification credentials and come from accredited universities with a specific degree focus in Exercise Science and or Health Education.

The company has experienced significant growth in the past five years due to an increase in the popularity of health and fitness among social trends. As a result, Average Joe's has applied to TD Bank for a \$1 million long term loan in order to finance further expansion plans. Specifically, the funds would be used to purchase additional gym equipment.

Average Joe's application and financial statements have been provided by Lisa Jennings, a credit analyst with TD Bank. She would like BUSI 1043 to conduct a preliminary review of Average Joe's financial statements and determine whether Average Joe's should proceed further into a more detailed analysis. Lisa would like BUSI 1043 to document the recommendations and supporting analysis in a report that will be maintained by the bank.

Lisa: "Average Joe's has provided us with a copy of their most recent Balance Sheet and Income Statement (Exhibit I). I know this may not be enough to make the final decision, but it should be more than enough for you to get started."

You: "Yes, I can obtain much information from these two statements".

Lisa: "Okay, that's great. I took a quick look at the Balance Sheet and am wondering what has caused the change in cash. Cash is needed to pay back the loan. Although I haven't done any rigorous analysis, it is a bit concerning to see the cash decline by such a large amount."

You: "I can definitely look into the decrease in cash."

Lisa: "It may also be useful to give some thought to what the Balance Sheet may look like if the loan is approved. Historical statements are fine, but they will not be able to provide you with this information. Additional information on the use of the loan is provided in Exhibit II."

You: "That is a great point. I will take this into consideration."

Lisa: “Alright. Let me know if I can be of any further assistance. I look forward to reading your report. If you recommend proceeding with further due diligence, can you prepare a list of additional information that would be useful in making our final decision?”

You: “Yes, I can most certainly do that. I will get started right away.”

You are excited with this last assignment and want to leave BUSI 1043 with a good impression. You begin to conduct some preliminary research by requesting industry comparable from the bank. You have located various industry ratios that can be used as a benchmark (Exhibit III).

Exhibit I: Financial Statements

	Average Joe's Gym Statement of Financial Position As at Dec 31	
Current Assets	2014	2013
Cash	235,359	134,550
Marketable Securities	145,780	457,206
Accounts Receivable	223,450	174,930
Inventory	425,770	355,790
Prepaid Expenses	17,500	19,500
TOTAL	1,047,859	1,141,976
Capital	2014	2013
Property and Equipment, net	2,756,950	2,492,655
TOTAL ASSETS	3,804,809	3,634,631

Liabilities and Shareholder's Equity		
Current		
	2014	2013
Accounts Payable	294,305	95,700
Accrued and Other Liabilities	237,595	244,760
Current Portion of Long-Term Debt	375,900	345,900
Total	907,800	686,360
Long Term Debt	1,280,330	1,601,500
Shareholder's Equity		
Common Shares (50,000 Outstanding)	595,817	595,817
Retained Earnings	1,020,862	750,953
Total Liabilities and Shareholders' Equity	3,804,809	3,634,631

Average Joe's Gym		
Income Statement		
For the Year Ended December 31st		
	2014	2013
Sales	2,975,990	2,575,990
Cost of Goods Sold	1,368,955	1,184,955
Gross Profit	1,607,035	1,391,035

Average Joe's Gym
 Income Statement
 For the Year Ended December 31st

	2014	2013
Sales	2,975,990	2,575,990
Cost of Sales	<u>1,368,955</u>	<u>1,184,955</u>
Gross Profit	1,607,035	1,391,035
 Expenses		
Amortization	155,490	125,490
General and Administrative	134,500	102,800
Marketing and Sales	175,680	155,600
Interest Expense	76,820	96,090
Office Expense	295,980	255,000
Wages and Benefits, Administration	<u>315,000</u>	<u>315,000</u>
Total Operating Expenses	1,153,470	1,049,980
 Operating Income	453,565	341,055
Gain (losses) on marketable securities	25,475	9,800
Impairment loss on capital assets	<u>0</u>	<u>0</u>
Income (loss) before taxes	479,040	350,855
Provision for (benefit from) income taxes	<u>134,131</u>	<u>98,239</u>
Net Income	344,909	252,616
 Opening Balance - Retained Earnings	750,953	573,338
Net Income	344,909	252,615
Dividends	<u>75,000</u>	<u>75,000</u>
Closing Balance - Retained Earnings	<u>1,020,862</u>	<u>750,953</u>

Exhibit II – Additional Information Regarding the Loan

- The loan will be used to purchase \$1 million in additional capital assets. The additional assets will result in an increase in revenue of 20%.
- The loan will bear interest at 6%. Principal payments of \$200,000 per annum will be required.
- The company will withhold any dividend payments during the foreseeable future in order to support the debt to equity ratio.
- The capital assets are expected to have a useful life of 15 years with no residual value.
- All other fixed expenses are expected to remain consistent.
- The existing loan will require a principal payment of approximately \$375,900 during the upcoming fiscal year. The payment for the following fiscal year is expected to be \$300,000.
- Accounts receivable, inventory, prepaid expense, and accounts payable will all increase by 40% as a result of the increased sales.
- The marketable securities will be converted to cash at the beginning of the year.

Exhibit III – Industry Benchmarks

Industry Ave	
Ratio on Profitability 2014	
Return of Equity	15.00%
Return on Assets	8.00%
Financial Leverage Percentage	7.00%
Earnings per Share	\$4.40
Quality of Income	75.00%
Profit Margin	10.00%
Fixed Asset Turnover	2.00
Tests of Liquidity	
Cash Ratio	7.00%
Current Ratio	1.00
Quick Ratio	0.75
Receivable Turnover	13.00
Average Days in Accounts	
Receivable	28.08
Payable Turnover	19.00
Average Days in Accounts Payable	19.21
Inventory Turnover	6.50
Average Days in Inventory	56.15
Solvency and Equity Position	
Times Interest Earned	5.40
Cash Coverage	6.30
Debt to Equity Ratio	1.35
Miscellaneous	
Book Value Per Share	\$29.00

Prepare the report. It is to include, organized and presented in a logical manner:

- quantitative analyses;
- ratio analyses;
- qualitative analyses; and
- appropriate recommendations given the case facts and analyses completed.

Evaluation

Final Exam will be marked in its entirety out of 100. The following rubric indicates the criteria students are to adhere to, and their relative weights to the assignment overall.

	Activity/Competencies Demonstrated	% of Final Grade
1.	Identification and Analysis of Issues (80%)	
	a. Quantitative Analysis	/30
	b. Ratio Analysis	/20
	c. Qualitative Analysis	/20
	d. Prepare entries stated in Exhibit II	/10
2.	Recommendation (10%)	
	a. Provides appropriate recommendation given the case facts and analysis completed.	/10
3.	Attention to Detail (10%)	
	a. Spelling, grammar, and formatting	/10
Total		/100