

Case 6

Financial Analysis

Joyner Lumber Company, Inc.

E. N. Roussakis

On May 15, 1991, National Bank and Trust Company of New Orleans, Louisiana, opened up a branch in the city of Lake Charles, in an effort to establish a presence in the southwestern part of the state. In the days that followed, George Hartofilax—branch manager—lost no time in soliciting local customers, especially businesses. One of the firms on his list was Joyner Lumber Company, Incorporated. He telephoned its president, Mr. R. Tom Joyner III, and arranged for a meeting with him on May 30.

On that date, George set out to visit Mr. Joyner in his company office. Mr. Joyner received George very cordially and expressed an interest in the bank. He indicated that for some time now he had been toying with the idea of establishing a door manufacturing facility on the premises, to meet his customers' needs. Currently, the company had routinely bought doors from another firm, earning a modest profit. Mr. Joyner went on to clarify that Joyner Lumber Company (JLC) had the funds to finance the project but could perhaps consider a loan, if the terms were attractive enough. He offered to mail JLC's financial statements for the last three years to assist George in his analysis.

As George was about to leave, Mr. Joyner asked him if the bank's philosophy was to work closely with its customers in solving their financial management problems. Mr. Joyner confided that his top priority was a financial analysis of his business to determine the relative strengths and weaknesses of his firm, that is, whether his firm was financially sound and profitable relative to other firms in the industry. Sensing an opportunity to oblige, and perhaps dispose Mr. Joyner favorably for the financing of the door facility, George offered to do the study himself.

Company Background and Operations

JLC is located in the northern outskirts of Lake Charles, a city of 75,000 people. Lake Charles was established in 1852 to promote the exploitation of the heavily timbered pinelands to the north and west. The discovery in the area, in the late 1800s, of mineral deposits—first sulphur, then oil and natural gas—made Lake Charles one of the nation's leading petrochemical production centers. The industrial development of Lake Charles, however, was greatly enhanced by the opening in 1926 of a channel that links the city to the Gulf of Mexico, which lies about 34 miles to the south. As a result, shipping business has grown significantly.

JLC was founded in March 1952 when R. Tom Joyner, Jr., purchased the Elwell Lumber and Supply Company of Lake Charles. At the time of the purchase there were two other small competitors in the area, and the prospects for the company to grow looked good. In the years that followed, the company grew slowly but steadily. Mr. Joyner ran the company very conservatively, relying primarily upon his own funds to meet the firm's financing needs. In the 1960s the company grew faster. Management commitment to quality products and personalized service along with a continuous reinvestment of earnings made JLC a leading independent lumberyard in southwestern Louisiana.

In the 1970s the company began to specialize by concentrating its sales in the home-building industry. This move increased the volume of wholesale business, and contributed significantly to the company's profitability. JLC's performance during this period was greatly enhanced by the unprecedented increase in the price of oil, which created a favorable business climate locally and new opportunities for the company to grow. The ensuing recession of the early 1980s, and the consequent decline in the price of oil, had an adverse effect on local economic activity. JCL managed to overcome the adversity, and as conditions gradually improved, it resumed its growth momentum and profitability record.

As the 1990s were about to unfold, a sudden change took place in the company's management. In February 1990, R. Tom Joyner, Jr., founder and president of the company passed away and his 28-year-old son, R. Tom Joyner III found himself at the helm of the business. Prior to his new duties Tom had significant exposure to the different aspects of the family business, which proved quite helpful when he took control of the company. One of Tom's first tasks was to hire a management consultant to assist in reorganizing the administrative structure and realigning the authorities and responsibilities of management. He felt that such action would increase operational efficiency and enhance the decision-making process. The results of this endeavor are depicted in Exhibit 1.

Another important challenge for Tom was to diversify the scope of company business. Excessive reliance on the home-building industry had contributed to a cyclical pattern of company sales. To mitigate the effects of the business cycle, he felt it important for the company to go after the business of commercial and industrial construction firms. The competition was expected to be quite keen since a number of regional chain stores had established a local presence and already catered to that market. However, Tom felt that his company had an important edge over its competitors—a reputation for the sale of quality products and personalized service. At year-end 1990, and 10 months after he took over the company, the sales pattern was as follows:

Type of Sales	Percent of Sales
Home Builders	96%
Commercial and Industrial Construction Firms	3%
Walk-in Retail Trade	1%

The company sells on terms of 2/10, N/30. To encourage early payment, however, the company bills its customers from the 25th day of each month with the discount period beginning from the first day of the following month. In any case, the full amount is due within 30 days from billing date. Past that date, unpaid accounts are charged 1 1/2 percent interest monthly. The company's aging schedule on April 30, 1991 was as follows:

Current	\$268,112.14
1-30 days old	157,585.57
31-60 days old	21,299.12
61-90 days old	63,963.87
91-120 days old	110,711.53
Total	\$621,672.23

The inventory stock is purchased directly from manufacturers within and outside the state (e.g., Canada, Alabama, and Georgia) and is delivered by rail to the company site. The stock consists of steel

lumber products as spruce studs, cedar, yellow pine, sheets of plywood, and two-by-fours. The company also carries limited building material (e.g., a variety of roofing and foundation material, hardware, and moldings).

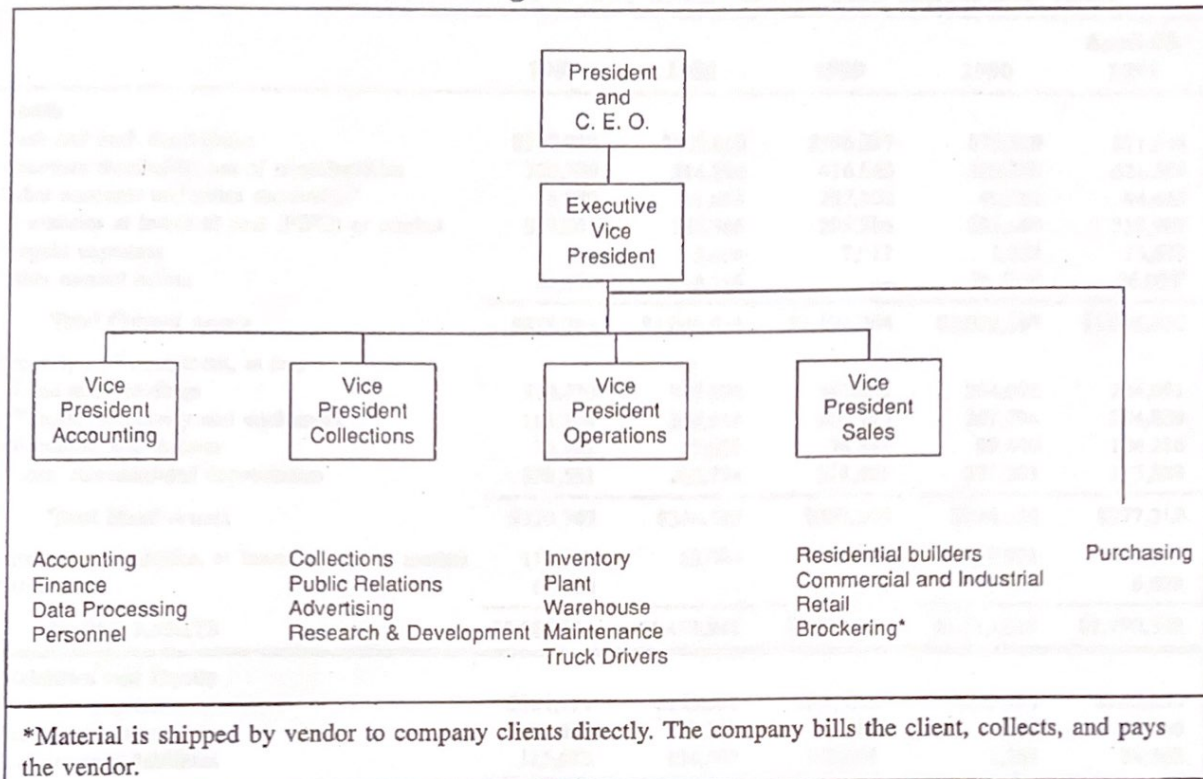
In an effort to maintain better control of the company's investment in inventory, in late 1990 the management organized all the inventory-related data into a computer record system. The use of a computer has made it possible to keep better track of actual inventory levels and generally to improve upon inventory management. A similar effort has been underway with respect to the data relating to accounts receivable. Use of computer controls in both of these areas is expected to contribute to more efficient inventory and credit policies.

The total number of individuals employed is 32, of whom two work in the yard and four drive trucks. When necessary, additional yard workers and drivers are hired on a part-time basis.

Writing Up a Report

With all this information at hand, George set out to analyze the company and make concrete recommendations for improvement. Financial statements of the company since 1987 are presented in Exhibits 2 through 4. Financial data from Robert Morris Associates are reproduced in Exhibit 5.

Exhibit 1 Joyner Lumber Company, Inc. Organization Chart



*Material is shipped by vendor to company clients directly. The company bills the client, collects, and pays the vendor.

Exhibit 2
Joyner Lumber Company, Inc.
Balance Sheets as of December 31, 1987-1990, and April 30, 1991

	1987	1988	1989	1990	April 30, 1991
Assets					
Cash and cash equivalents	\$207,923	\$405,830	\$196,297	\$75,529	\$71,538
Accounts receivable, net of uncollectibles	320,709	314,290	416,865	583,840	621,584
Other accounts and notes receivable ^a	18,950	11,653	257,303	40,062	44,645
Inventories at lower of cost (FIFO) or market	279,651	288,366	295,886	295,886	318,967
Prepaid expenses	—	5,664	7,913	1,137	13,673
Other current assets	44,550	18,115	—	25,713 ^b	26,003 ^b
Total Current Assets	\$871,783	\$1,043,918	\$1,174,264	\$1,022,167	\$1,096,410
Property and equipment, at cost					
Land and buildings	410,779	347,570	347,462	284,091	284,091
Trucks, machinery and equipment	163,209	205,914	208,413	267,796	284,839
Furniture and fixtures	75,292	55,670	56,432	99,440	104,216
Less: Accumulated depreciation	338,531	262,774	318,561	377,201	395,833
Total Fixed Assets	\$310,749	\$346,380	\$293,746	\$274,126	\$277,313
Investment securities, at lower of cost or market	112,101	63,544	59,932	409,998	409,997
Other assets	91,000	—	130	6,628	6,628
TOTAL ASSETS	\$1,385,633	\$1,453,842	\$1,528,072	\$1,712,919	\$1,790,348
Liabilities and Equity					
Accounts payable	\$161,719	\$145,599	\$210,643	\$242,191	\$205,835
Accrued expenses	57,656	52,257	36,206	17,272	29,366
Other current liabilities	115,673	134,507	147,068	1,251	24,562
Total Current Liabilities	\$335,048	\$332,363	\$393,917	\$260,714	\$259,763
Notes payable to banks and others ^c	50,689	50,483	39,086	70,550	90,477
Total Liabilities	\$385,737	\$382,846	\$433,003	\$331,264	\$350,240
Common stock (11,266 shares, \$1 par value)	11,266	11,266	11,266	11,266	11,266
Paid-in capital	161,239	161,239	161,239	161,239	161,239
Retained earnings	827,391	907,343	951,153	1,237,739	1,305,436
Common stock in treasury, at cost	—	(8,852)	(28,589)	(28,589)	(37,833)
Total Equity	\$999,896	\$1,070,996	\$1,095,069	\$1,381,655	\$1,440,108
TOTAL LIABILITIES AND EQUITY	\$1,385,633	\$1,453,842	\$1,528,072	\$1,712,919	\$1,790,348
*Non-trade related (e.g., advances to employees, officers, and a major local business concern).					
^b Short-term securities.					
^c Includes a mortgage note on a residential property.					

Exhibit 3
Joyner Lumber Company, Inc.
Operating Statements for Years Ended December 31, 1987-1990
and for Four Months Ended April 30, 1991

	1987	1988	1989	1990	1991	
					April 30	Year-to-Date
Net sales	\$2,832,803	\$3,148,875	\$3,403,999	\$3,283,010	\$370,993	\$1,345,370
Cost of sales	2,017,963	2,259,277	2,409,538	2,336,793	274,075	982,107
Gross Profit	\$814,840	\$889,598	\$994,461	\$946,217	\$96,918	\$363,263
Operating Expenses						
General and administrative	\$267,735	\$342,442	\$403,405	\$412,737	\$44,111	\$143,600
Salaries and wages	253,698	349,418	407,413	360,908	36,203	152,541
Officers' salaries	197,111	220,200	166,400	152,874	11,317	44,617
Total Expenses	\$718,544	\$912,060	\$977,218	\$926,519	\$91,631	\$340,758
Operating income	\$96,296	\$(22,462)	\$17,243	\$19,698	\$5,287	\$22,505
Other income, net ^a	31,840	125,848	54,166	327,071	2,223	55,292
Income before taxes	128,136	103,386	71,409	346,769	7,510	77,797
Taxes	37,332	23,434	27,599	60,183	1,186 ^b	10,100 ^b
Net Income	\$90,804	\$79,952	\$43,810	\$286,586	\$6,324	\$67,697

^aIncludes dividends, interest income from securities, and rent income from the ownership of a residential property. This is true in all cases except for 1988 and 1990 which include in addition extraordinary income in the amounts of \$101,238 and \$238,645, respectively. In the former instance this income resulted from the sale of a fixed asset while in the latter it resulted from the sale of unaccounted inventory.

^bEstimates.

Exhibit 4
Joyner Lumber Company, Inc.
Statements of Retained Earnings as of December 31, 1987-1990,
and April 30, 1991

	1987	1988	1989	1990	1991 (1/1 - 4/30)
Retained earnings, beginning of the year	\$736,587	\$827,391	\$907,343	\$951,153	\$1,237,739
Add: Net income for the year	90,804	79,952	43,810	286,586	67,697
Less: Dividends	—	—	—	—	—
Retained earnings, end of the year	\$827,391	\$907,343	\$951,153	\$1,237,739	\$1,305,436

Exhibit 5 Industry Statistics for Wholesalers: Lumber & Millwork (SIC #5031)

Comparative Historical Data			Type of Statement	Current Data Sorted By Sales													
186	172	177	Unqualified	2	7	8	36	57	67								
21	6	12	Qualified			1	3	5	3								
249	228	222	Reviewed	6	29	39	66	64	18								
209	190	206	Complied	8	81	37	50	22	8								
127	113	138	Other	7	46	19	22	29	15								
8/30/87- 2/31/88	8/30/88- 3/31/89	8/30/88- 3/31/90		221(6/30-9/30/89)			534(10/1/89-3/31/90)										
ALL	ALL	ALL		0-1MM	1-3MM	3-5MM	5-10MM	10-25MM	25MM & OVER								
792	709	755	NUMBER OF STATEMENTS	23	163	104	177	177	111								
			ASSETS	%	%	%	%	%	%								
5.3	5.6	5.1	Cash & Equivalents	4.6	6.6	4.0	4.4	5.9	4.2								
38.0	38.5	37.4	Trade Receivables - (net)	38.4	33.7	38.1	38.7	38.0	39.0								
31.5	32.2	33.8	Inventory	25.6	34.6	35.9	35.1	33.9	30.5								
2.0	1.8	2.0	All Other Current	.4	1.9	2.0	1.5	2.0	3.5								
76.7	78.0	78.4	Total Current	69.0	76.8	79.9	79.8	79.8	77.1								
16.2	15.2	15.3	Fixed Assets (net)	24.2	16.9	13.9	14.8	13.9	15.1								
.4	.5	.5	Intangibles (net)	1.0	.3	.3	.4	.4	1.3								
6.6	6.2	5.8	All Other Non-Current	5.8	6.0	5.9	5.0	5.9	6.5								
100.0	100.0	100.0	Total	100.0	100.0	100.0	100.0	100.0	100.0								
			LIABILITIES														
20.4	20.8	21.3	Notes Payable-Short Term	20.1	16.7	21.4	21.5	22.7	25.7								
3.6	3.0	3.2	Cur. Mat.-L/T/D	7.9	4.2	3.9	2.8	2.1	2.1								
17.1	17.4	16.9	Trade Payables	14.6	18.1	19.1	16.8	16.4	14.5								
1.0	.7	.5	Income Taxes Payable	.8	.3	.5	.5	.5	.7								
8.9	7.4	6.5	All Other Current	7.8	5.0	6.1	7.2	7.1	7.0								
50.9	49.2	48.4	Total Current	51.2	44.4	51.0	48.7	48.8	50.1								
11.3	10.8	11.1	Long Term Debt	16.3	13.1	11.3	10.2	8.5	12.7								
.4	.4	.3	Deferred Taxes	1.2	.5	.2	.2	.2	.5								
1.8	2.0	2.2	All Other Non-Current	2.5	2.8	3.3	1.7	1.8	1.5								
35.6	37.8	38.0	Net Worth	28.8	39.2	34.2	39.2	40.8	35.1								
100.0	100.0	100.0	Total Liabilities & Net Worth	100.0	100.0	100.0	100.0	100.0	100.0								
			INCOME DATA														
100.0	100.0	100.0	Net Sales	100.0	100.0	100.0	100.0	100.0	100.0								
19.8	19.3	19.4	Gross Profit	26.8	22.7	20.5	18.9	17.8	16.0								
16.8	16.5	16.7	Operating Expenses	24.5	19.8	18.3	16.2	15.1	12.8								
3.0	2.8	2.7	Operating Profit	2.1	2.9	2.2	2.7	2.5	3.2								
.7	.6	.9	All Other Expenses (net)	1.7	.8	.8	1.0	.6	1.3								
2.3	2.2	1.8	Profit Before Taxes	.4	2.1	1.7	1.7	1.9	1.9								
			RATIOS														
2.2	2.4	2.4	Current	2.1	2.7	2.3	2.4	2.4	2.0								
1.5	1.6	1.6	Quick	1.3	1.7	1.5	1.6	1.7	1.5								
1.2	1.2	1.3	Quick	1.1	1.0	1.2	1.2	1.2	1.2								
1.2	1.4	1.3	Quick	1.5	1.4	1.2	1.3	1.3	1.1								
.8	.9	.9	Quick	.8	.9	.9	.8	.9	.8								
.6	.6	.6	Quick	.5	.5	.6	.6	.6	.6								
26	13.9	25	14.5	26	13.9	29	12.5	23	15.7	24	15.1	28	14.1	27	13.7	29	12.6
35	10.3	34	10.7	35	10.3	53	6.9	35	10.5	35	10.5	34	10.6	38	10.1	37	9.8
47	7.7	46	8.0	47	7.8	91	4.0	46	7.9	49	7.5	48	7.9	48	8.0	46	8.1
24	15.3	23	16.2	26	13.9	20	18.3	26	14.5	30	12.1	27	13.7	24	15.1	25	14.4
45	8.2	43	8.5	48	7.8	47	7.8	53	6.9	52	7.0	49	7.4	47	7.7	43	8.5
72	5.1	68	5.4	72	5.1	85	4.3	87	4.2	78	4.8	86	5.5	72	5.1	80	6.1
9	41.2	9	42.5	10	37.3	6	59.3	10	38.0	11	32.3	10	37.8	10	35.4	9	42.5
17	21.0	17	21.1	18	20.8	24	14.9	22	16.6	20	18.5	17	21.7	17	20.9	13	28.3
31	11.6	28	12.9	30	12.1	35	10.5	40	9.2	32	11.3	30	12.0	27	13.7	22	16.7
8.1	7.6	7.0	Sales/Working Capital	4.6	6.7	6.7	7.4	6.8	7.1								
15.3	14.0	13.0	Sales/Working Capital	17.2	11.8	13.4	13.1	13.2	15.3								
41.3	39.4	29.5	Sales/Working Capital	52.5	22.9	25.7	31.7	32.1	32.6								
6.2	6.3	4.7	EBIT/Interest	4.5	5.4	4.1	3.9	5.9	4.5								
(697)	3.0	(607)	2.6	(693)	2.2	(21)	1.5	(146)	2.3	(98)	1.9	(165)	2.1	(159)	2.2	(104)	2.4
1.7	1.4	1.2	EBIT/Interest	.6	1.1	1.0	1.3	1.3	1.4								
7.6	8.3	7.3	Net Profit + Depr., Dep., Amort./Cur. Mat. L/T/D		5.0	7.5	6.8	9.7	8.8								
(425)	2.8	(334)	3.0	(370)	2.7	(54)	2.1	(50)	2.3	(91)	2.6	(98)	3.1	(71)	3.6		
1.1	1.1	.8	Net Profit + Depr., Dep., Amort./Cur. Mat. L/T/D		.3	.1	.8	1.2	1.9								

(Exhibit 5 Continued)

.2	.1	.1		.3	.1	.1	.1	.1	.2
.4	.3	.3	Fixed/Worth	1.0	.3	.3	.3	.3	.4
.9	.7	.8		4.0	.9	.8	.7	.6	.8
1.0	.9	.8		1.3	.7	1.0	.9	.7	1.1
2.1	2.0	1.9	Debt/Worth	2.3	1.5	2.1	1.8	1.9	2.2
4.3	4.1	3.7		13.4	3.5	4.3	3.3	3.7	3.8
42.9	36.3	31.0	% Profit Before Taxes/Tangible	50.4	40.5	28.9	29.6	28.3	28.8
(760)	22.1 (687)	19.8 (730)	Net Worth	(20)	4.9 (154)	12.5 (96)	13.1 (174)	14.4	15.5 (109)
8.6	5.9	4.3		-6.9	2.3	1.6	5.1	5.1	7.0
13.2	13.0	11.1	% Profit Before Taxes/Total	11.1	13.2	10.7	10.4	10.9	10.6
6.5	6.0	4.9	Assets	1.5	4.9	4.0	4.8	4.9	5.7
2.4	1.6	1.0		-3.1	.5	0	1.3	1.4	1.8
86.1	92.1	84.4	Sales/Net Fixed Assets	52.5	85.2	80.7	84.2	93.7	87.7
27.4	30.7	29.9		14.2	30.0	32.7	33.6	32.1	22.1
12.6	14.2	13.6		4.6	12.5	19.7	14.2	12.9	12.4
4.8	4.9	4.7	Sales/Total Assets	4.6	4.5	4.7	4.9	4.8	4.9
3.4	3.5	3.4		3.0	3.2	3.4	3.5	3.4	3.5
2.4	2.6	2.5		1.8	2.4	2.5	2.6	2.6	2.4
.4	.3	.4	% Depr., Dep., Amort./Sales	.9	.4	.5	.4	.3	.3
(673)	.8 (609)	.8 (692)		(21)	1.4 (146)	1.0 (98)	.8 (165)	.8 (161)	.8 (101)
1.5	1.4	1.4		2.3	1.7	1.2	1.3	1.3	1.2
1.4	1.3	1.5	% Officers' Comp/Sales		2.4	1.7	1.3	1.1	.6
(285)	2.3 (275)	2.3 (307)			(80)	3.5 (51)	2.7 (84)	2.4 (62)	2.0 (21)
4.2	4.1	4.3				5.5	3.7	3.8	2.1
1385871M	10981171M	12891685M	Net Sales (\$)	13620M	320907M	416246M	1261271M	2786110M	8073631M
4082911M	3208294M	3943012M	Total Assets (\$)	7367M	114816M	132087M	396347M	850456M	2441939M

M = \$thousand MM = \$million

Source: Robert Morris Associates, *Annual Statement Studies*, Philadelphia: Robert Morris Associates, 1990, pp. 402-403. Reprinted with permission. © Robert Morris Associates 1990.

RMA cautions that the *Studies* be regarded only as a general guideline and not as an absolute industry norm. This is due to limited samples within categories, the categorization of companies by their primary Standard Industrial Classification (SIC) number only, and different methods of operations by companies within the same industry. For these reasons RMA recommends that the figures be used only as general guidelines in addition to other methods of financial analysis.