FORMAT REQUIREMENTS:

The group paper should

- be typed and double spaced;
- flow as a well-documented coherent, committee paper;
- cite all sources;
- have correct formats for the bibliography, footnotes, and references;
- have on the first page of the paper, the title of the paper, the authors' names, and respective tutorial groups; and
- have an executive summary.

Quality is the most appropriate determinant of the grade awarded, but it is suggested that approximately **3,000 words** be a suitable length.

Part A: Athletequip Company Inc Analysis [35 marks]

SPECIFIC REQUIREMENTS / QUESTIONS:

1. Would you grant the loan requested by Mr. Ball? If so, on what terms and conditions?

2. Why does this company need this level of financing?

3. What special risks do you see in this situation:
    - To the bank?
    - To the company?

Note: Students should answer the preceding questions and ignore the questions presented on page 516 of the case.

CASE 11 ATHLETEQUIP COMPANY, INC.

BACKGROUND

Athletequip Company was founded in Toledo, Ohio, in 1964 as a partnership by Mr. Charles O. Ball and Mr. Clark L. Alexander. Mr. Alexander died in 1969, leaving his share of the partnership to his wife, Sharon, who sold it back to Charles Ball. Mr. Ball continued the business with the assistance of his wife, Elizabeth, and his two sons, Gregory and Phillip, who were then students of business administration at the local state university. The company was incorporated in 1974, with Charles Ball as president and Gregory and Phillip, who had at that time completed their degrees, as vice-president and treasurer, respectively. In 1979 the Balls moved the business to Alhambra, California, its present site. The elder Ball died in 1980, leaving the bulk of his estate—and controlling interest in the company—to his wife and sons.

Athletequip, Inc., was engaged in the manufacture of athletic garments, specializing in uniforms and jackets. About half of the inventory on hand usually consisted of football practice pants, with the balance consisting of yardage goods and goods-in-process on firm purchase orders. Because of the nature of these products, a substantial portion of sales was made on a specific order basis, with orders taken throughout the year as institutions were able to anticipate their needs. This enabled the company to maintain a fairly level production cycle.

Goods were distributed throughout the United States. Sales were made to sporting goods stores and directly to high schools and colleges. Although the market was highly competitive, Athletequip had been quite successful, particularly in the area of football uniforms. Of the 1,330 U.S. colleges that play football, Athletequip outfitted 330 teams. In fact, the company estimated that it manufactured at least 25 percent of all football game pants used in the country last year.

Selling terms extended by Athletequip were 3/10–net 30 to stores, and extended terms were given to high schools and colleges, with those invoices being payable in October of each year.

The company employed 89 persons and had 6 salesmen on commission and salary.

MANAGEMENT

Gregory S. Ball assumed the presidency of the company upon the death of his father in 1980. At that time he was 31 years old and had been involved in the company for 11 years. In spite of his youth, he had shown great skill in his trade, and under his direction, Athletequip had grown in the past 12 years from a company with total assets of $238,000 and net sales of $756,000 to one with $698,000 in total assets and $1,727,000 in net sales.

Phillip M. Ball had served as vice-president and chief financial officer since 1980. Currently 39, he was highly regarded in the industry for his integrity and entrepreneurship.

John T. Ryan, age 36, joined the company in 1985 as sales manager. He held a BBA in marketing from California State University and, upon coming to Athletequip, had 12 years' sales experience with a nationally known firm.

The company was well thought of in the community, and the Ball brothers were actively involved in both civic and business organizations.

BANK RELATIONSHIPS

Athletequip, Inc., had been a customer of the Third First State Bank in Alhambra since the company's arrival in 1979. However, ownership of that bank changed hands about six months ago, accompanied by a change in management personnel. Therefore, those familiar with the principals of Athletequip, Inc., were no longer with the bank.

There was also some question regarding the Third First Bank's ability to meet the increasing credit requirements of the company, as these would likely exceed the bank's legal lending limit.

Athletequip had inquired at various times regarding services such as payroll and account reconciliation; however, the bank's response had been largely unsatisfactory.

Athletequip, Inc., had been a long-time prospect of the Commerce National Bank in Alhambra and had now requested that Commerce establish a $550,000 line of credit to be used in expanding its operations. The company rented office and plant facilities of approximately 45,000 square feet from a partnership owned by the Balls; however, operating capacity in the present location had been reached, and Athletequip needed to move in the near future. The cost of a new plant and equipment would approximate $400,000, and plans for financing would be considered at a future time.

FINANCIAL INFORMATION

Financial statements of Athletequip, Inc., for the past three calendar years are presented in Exhibits 1–4. Changes in the equity section reflect the purchase by the company from Elizabeth Ball of 700 shares of $10 par value stock for $50 per share. For inheritance tax purposes, Mrs. Ball is contemplating disposal of all of her stock within the next few years. The credit report on the company and its principals appears in Exhibit 5, and industry comparisons are shown in Exhibit 6.

QUESTIONS

1. Consider the loan as requested. Include in the presentation the use of ratios, a source and application of funds statement, reconcilement of net worth, and a basic trend and comparative analysis.

2. Upon conclusion of the analysis, the bank will meet with the principals of Athletequip, Inc., at which time additional information may be obtained. Consider the types of questions to be asked and additional information to be requested, as well as the bank's position in regard to the loan request.

EXHIBIT 1 Athletequip Company, Inc.—Balance Sheet (Prepared without Audit)

	End of Year		
	1992	1991	1990
Assets			
Current Assets			
Cash	$ 55,251	$ 67,261	$ 97,397
Accounts receivable—less allowance for bad debts	169,734	139,442	107,553
Inventory	301,184	295,498	242,674
Prepaid expenses	5,272	4,012	2,120
	$531,441	$506,213	$449,744

[redacted]

EXHIBIT I *(continued)*

	End of Year		
	1992	1991	1990
Fixed Assets			
Machinery and equipment	$189,412	$162,937	$140,739
Automobiles and trucks	14,303	14,545	14,545
Office furniture and equipment	42,228	27,042	23,474
Leasehold improvements	73,688	74,413	73,025
	$319,631	$278,937	$251,783
Less allowance for depreciation and amortization	164,686	137,954	103,939
	$154,945	$140,983	$147,844
Other Assets	11,436	13,336	9,474
Total Assets	$697,822	$660,532	$607,062
Liabilities and Stockholders' Equity			
Current Liabilities			
Accounts payable	$ 88,110	$ 79,621	$ 80,027
Notes payable—secured—Alhambra State Bank—portion due within one year	2,125	8,500	8,500
Contracts payable—autos—portion due within one year	2,846	1,217	4,287
Accrued taxes	14,210	18,000	17,458
Accrued expenses	54,464	11,003	29,997
Deferred income		450	450
Federal taxes on income payable	10,075	45,498	27,969
	$171,830	$164,289	$168,688
Other Liabilities			
Contracts payable—auto—portion due after one year	949		1,217
Notes payable—Elizabeth Ball	35,000		
Notes payable—secured—Alhambra State Bank—portion due after one year		3,125	10,625
	$ 35,949	$ 3,125	$ 11,842
Total Liabilities	144,789	$167,414	$180,530
Stockholders' Equity			
Capital stock—common—authorized 20,000 shares of $10.00 par value per share	$ 93,000	$100,000	$100,000
Paid-in surplus		586	586
Retained earnings	397,043	392,532	325,946
	490,043	$493,118	$426,532
Total Liabilities and Stockholders' Equity	$697,822	$660,532	$607,062

EXHIBIT 2 Athletequip Company, Inc.—Statement of Earnings (Prepared without Audit)

	Year Ending							
	1992		*1991*			*1990*		
	Dollars	% of Sales	Dollars	% of Sales	Increase or Decrease	Dollars	% of Sales	Increase or Decrease
Sales	$1,726,769	100.00	$1,739,224	100.00	$(12,455)	$1,607,121	100.00	$132,103
Cost of Sales	1,093,130	63.30	1,081,909	62.21	11,221	1,036,048	64.47	45,861
Gross Profit on Sales	633,639	36.70	657,315	37.79	(23,676)	571,073	35.53	86,242
Operating Expenses								
Advertising	37,793	2.19	26,154	1.50	11,639	29,081	1.81	(2,927)
Depreciation and amortization	33,001	1.91	34,015	1.96	(1,014)	27,585	1.72	6,430
Discounts on sales	36,743	2.13	36,460	2.10	283	31,739	1.98	4,721
Employees' profit-sharing plan	28,000	1.62	25,966	1.49	2,034	20,000	1.24	5,966
Factory supplies and expense	11,123	.64	17,477	1.01	(6,354)	21,682	1.35	(4,205)
Insurance	21,150	1.22	20,478	1.18	672	16,275	1.01	4,203
Outside sales commissions	65,636	3.80	62,518	3.59	3,118	62,827	3.91	(309)
Rent—net	60,425	3.50	59,586	3.43	839	48,524	3.02	11,062
Salaries	145,778	8.44	132,069	7.59	13,709	116,080	7.22	15,989
Taxes	44,587	2.58	37,661	2.17	6,926	36,316	2.26	1,345
Travel and entertainment	38,607	2.24	29,721	1.71	8,886	22,278	1.39	7,443
Other	76,193	4.41	69,834	4.02	6,359	68,772	4.28	1,062
	599,036	34.68	$ 551,938	31.73	$ 47,098	$ 501,159	31.18	$ 50,779
Net Earnings from Operations	$ 34,603	2.00	$ 105,377	6.06	$(70,774)	$ 69,914	4.35	$ 35,463
Other Income	$ 5,983	.35	$ 6,707	.38	$ (724)	$ 6,687	.42	20
Net Earnings before Provision for Federal Taxes on Income	$ 40,586	2.35	$ 112,084	6.44	$(71,498)	$ 76,601	4.77	$ 35,483
Provision for Federal Taxes on Income	10,075	.58	$ 45,498	2.61	(35,423)	27,969	1.74	17,529
Net Earnings	$ 30,511	1.77	$ 66,586	3.83	$(36,075)	$ 48,632	3.03	$ 17,954

EXHIBIT 3 Athletequip Company, Inc.—Statement of Cost of Sales (Prepared without Audit)

	1992		1991			1990		
	Dollars	% of Sales	Dollars	% of Sales	Increase or Decrease	Dollars	% of Sales	Increase or Decrease
Opening inventory	$ 295,498	17.1	$ 242,674	14.0	$ 52,824	$ 221,284	13.8	$21,390
Purchases	528,647	30.6	539,426	31.0	(10,779)	518,331	32.3	21,095
Supplies	71,141	4.1	88,992	5.1	(17,851)	75,994	4.7	12,998
Labor—plant	427,983	24.8	435,010	25.0	(7,027)	397,517	24.7	37,493
Outside work	71,044	4.1	71,306	4.1	(262)	65,595	4.1	5,711
	$1,394,313	80.7	$1,377,408	79.2	$ 16,905	$1,278,721	79.6	$98,687
Closing inventory	301,184	17.4	295,498	17.0	5,686	242,674	15.1	52,824
Cost of sales	$1,093,129	63.3	$1,081,910	62.2	$11,219	$1,036,047	64.5	$45,863

EXHIBIT 4A General Spread Form—Athletequip Company, Inc. (in thousands of dollars)

NAME ATHLETEQUIP COMPANY, INC.			
1 AUDITED STATEMENT	No	No	No
2 STATEMENT DATE	12-31-90	12-31-91	12-31-92
3 CASH	97	67	55
4 MARKETABLE SECURITIES			
5 NOTES RECEIVABLE			
6 ACCOUNTS RECEIVABLE	108	139	170
7 INVENTORY	243	295	301
8			
9			
10			
11 ALLOW. FOR DOUBT. ACCT.			
12 TOTAL CURRENT ASSETS	448	501	526
13 FIXED ASSETS—NET	148	141	155
14 NON-MARKETABLE SECURITIES			
15 NONCURRENT RECEIVABLES			
16 PREPAID AND DEFERRED EXPENSES	2	4	6
17 OTHER ASSETS	9	14	11
18			
19			
20			
21 INTANGIBLES			
22 TOTAL NONCURRENT ASSETS	159	159	172
23 TOTAL ASSETS (12 + 22)	607	660	698
24 CURRENT MTY. OF TERM DEBT	13	10	5
25 NOTES PAYABLE			
26 ACCOUNTS PAYABLE	80	80	88
27 ACCRUED EXPENSE & MISC.	47	29	69
28 NOTE PAYABLE—ELIZ. BALL			35

29			
30			
31 INCOME TAX LIABILITY	28	45	10
32 **TOTAL CURRENT LIABILITIES**	168	164	207
33 TERM DEBT	12	2	1
34			
35 SUBORDINATED DEBT			
36 TOTAL LIABILITIES (32 + 33 + 34 + 35)	181	166	208
37 MINORITY INTEREST			
38 DEFERRED INCOME/RESERVES			
39 TREASURY STOCK			
40 PREFERRED STOCK OUTSTANDING			
41 COMMON STOCK OUTSTANDING	100	100	93
42 CAPITAL SURPLUS	1	1	—
43 RETAINED EARNINGS (DEFICIT)	326	393	397
44			
45			
46 NET WORTH (39 thru 45)	427	494	490
47 **TANGIBLE NET WORTH (46 − 21)**	427	494	490
48 WORKING CAPITAL (12–32)	280	337	319
49 CUR. ASSETS LESS TOT. LIAB.	267	335	318
50 CURRENT RATIO (12–32)	2.7	3.1	2.5
51 CASH, MKT. SEC. & A/R TO CUR. LIAB.	1.2	1.3	1.1
52 A/R COLLECTION PERIOD—DAYS	24	29	35
53 NET SALES TO INVENTORY	6.6	5.9	5.7
54 COST OF SALES TO INVENTORY	4.3	3.7	3.6
55 INVENTORY TO WORKING CAPITAL	.87	.88	.94
56 SR. DEBT ÷ (TANG. N.W. & SUB. DEBT)	.42	.34	.42
57 NET PROFIT (LOSS) TO AVG. NET WORTH	.11	.15	.06

EXHIBIT 4A *(continued)*

NAME ATHLETEQUIP COMPANY, INC.

58 PERIOD COVERED (MONTHS)	12 mos		12 mos		12 mos					
STATEMENT DATE	12-31-90		12-31-91		12-31-92					
	%		%		%		%		%	
59 NET SALES	1,607		1,739		1,					
60 COST OF SALES	1,036	65	1,082	62	1,093	63				
61 GROSS PROFIT	571	36	657	38	634	37				
62 SELLING EXPENSES	146		155		169					
63 GENERAL & ADMINISTRATIVE EXP.	355		397		430					
64 TOTAL OPERATING EXPENSES (62 + 63)	501		552	32	599	35				
65 OPERATING PROFIT (61 − 64)	70		105	6	35	2				
66 OTHER INCOME (EXPENSE)—NET	7		7		6					
67 NET PROFIT (LOSS) BEFORE TAXES	77		112	6	41	2				
68 INCOME TAXES	28		45	3	10					
69 NET PROFIT (LOSS) AFTER TAXES	49		67	4	31	2				
ADDITIONAL DATA										
70 DIVIDENDS—PREFERRED STOCK										
71 DIVIDENDS—COM. STOCK OR WITHDRAW										
72 OFFICER REMUNERATION										
73 INTEREST EXPENSE										
74 OTHER CHANGES IN WORTH (80 thru 83)										
75 CONTINGENT LIABILITIES										
76 LEASE OBLIGATIONS										
ANALYSIS OF CHANGES IN WORTH OR SURPLUS										
77 AT BEGINNING OF PERIOD			427		494					
78 ADD NET PROFIT			67		31					
79 DEDUCT DIVIDENDS OR WITHDRAW.										
80 TREAS. STK.—PURCH. & CANCEL'D					(35)					

81				
82				
83				
84	WORTH OR SURPLUS REPORTED (46)		494	490
	ANALYSIS OF WORKING CAPITAL			
85	AT BEGINNING OF PERIOD		280	337
86	ADD: NET PROFIT	49	67	31
87	NON-CASH CHARGES	28	34	33
88	DECR. OTHER DEF'D ASSETS			1
89				
90				
91	MISCELLANEOUS			
92	TOTAL ADDITIONS (86 thru 91)	77	101	65
93	DEDUCT:			
94	DIVIDENDS/WITHDRAWALS			
95	PLANT EXPENDITURES		27	47
96	CANCEL TREAS. STK			35
97	INCR. OTHER DEF'D ASSETS		7	
98	DECR. DEF'D LIABILITIES		10	1
99	MISCELLANEOUS			
100	TOTAL DEDUCTIONS (93 thru 99)		44	83
101	NET CHANGE (+ OR −) (92 − 100)		+57	(18)
102	AT END OF PERIOD (85 + 101)	280	337	319
103				
104	W/C AS ABOVE (102 same as 48)	280	337	319
105	INVENTORY	243	295	301
106	W/C LESS INVENTORY (104 − 105)	37	42	18
	ANALYST INITIALS	JEB	JEB	JEB

EXHIBIT 4B General Spread Form

NAME ATHLETEQUIP COMPANY, INC. (in thousands of dollars)

1 AUDITED STATEMENT	No	No	No	No	No
2 STATEMENT DATE	12-31-91	3-31-92	6-30-92	9-30-92	12-31-92
3 CASH	67	1	4	1	55
4 MARKETABLE SECURITIES					
5 NOTES RECEIVABLE					
6 ACCOUNTS RECEIVABLE	139	443	567	844	170
7 INVENTORY	295	217	257	219	301
8					
9					
10					
11 ALLOW. FOR DOUBT. ACCT.					
12 **TOTAL CURRENT ASSETS**	501	661	828	1,064	526
13 FIXED ASSETS—NET	141	140	139	145	155
14 NON-MARKETABLE SECURITIES					
15 NONCURRENT RECEIVABLES					
16 PREPAID AND DEFERRED EXPENSES	4	9	16	8	5
17 OTHER ASSETS	14	11	11	11	11
18					
19					
20					
21 INTANGIBLES		1	1	1	
22 **TOTAL NONCURRENT ASSETS**	159	161	167	165	171
23 TOTAL ASSETS (12 + 22)	660	822	995	1,229	697
24 CURRENT MTY. OF TERM DEBT	10				5
25 NOTES PAYABLE		145	279	443	
26 ACCOUNTS PAYABLE	80	64	96	125	88
27 ACCRUED EXPENSE & MISC.	29	11	5	19	69
28 NOTE PAYABLE—ELIZ. BALL					35

29					
30					
31 INCOME TAX LIABILITY	45	64	59	70	10
32 **TOTAL CURRENT LIABILITIES**	164	284	439	657	207
33 TERM DEBT	2	5	2	2	1
34					
35 SUBORDINATED DEBT					
36 TOTAL LIABILITIES (32 + 33 + 34 + 35)	166	289	441	659	208
37 MINORITY INTEREST					
38 DEFERRED INCOME/RESERVES					
39 TREASURY STOCK					
40 PREFERRED STOCK OUTSTANDING					
41 COMMON STOCK OUTSTANDING	100	100	100	100	93
42 CAPITAL SURPLUS	1	1	1	1	
43 RETAINED EARNINGS (DEFICIT)	393	432	453	469	397
44					
45					
46 NET WORTH (39 thru 45)	494	533	554	570	490
47 **TANGIBLE NET WORTH (46 − 21)**	494	532	553	569	490
48 WORKING CAPITAL (12–32)	337	377	389	407	319
49 CUR. ASSETS LESS TOT. LIAB.	335	372	387	405	318
50 CURRENT RATIO (12–32)	3.1	2.33	1.89	1.62	2.5
51 CASH, MKT. SEC. & A/R TO CUR. LIAB.	1.3	1.56	1.30	1.29	1.1
52 A/R COLLECTION PERIOD—DAYS[a]	29	78	110	162	35
53 NET SALES TO INVENTORY[a]	5.9	9.4	7.2	8.6	5.7
54 COST OF SALES TO INVENTORY	3.7				3.6
55 INVENTORY TO WORKING CAPITAL	.88	.58	.66	.54	.94
56 SR. DEBT ÷ (TANG. N.W. & SUB. DEBT)	.34	.54	.80	1.16	.42
57 NET PROFIT (LOSS) TO AVG. NET WORTH[a]	.15	.03	.23	.19	.06

[a]Annualized.

EXHIBIT 5A Athletequip Company, Inc.—Credit Report

	Date of Report April 3, 1993	Started	Rating
ATHLETEQUIP COMPANY, INC., MFG ATHLETIC GARMENTS		1964	A+1
ALHAMBRA, CALIF 91103		SUMMARY	
		PAYMENTS	DISC PPT
GENE BALL, PRES., TREAS., & CHIEF EXECUTIVE		SALES	$1,700,000+
PHIL BALL, VICE-PRESIDENT		WORTH	$488,650
ELIZABETH BALL, SECRETARY		EMPLOYS	95
		CONDITION	SOUND
		TREND	UP

PAYMENTS	HC	OWE	P DUE	TERMS	March 11,	SOLD
	27500	11000		1 30	Disc	Over 3 years
	20000	400		30	Ppt	Over 3 years to 6-B
	4000	500		30	Ppt	Over 3 years

HIGHLIGHTS		*Dec. 31, 1992*	*Dec. 31, 1991*
	Net Working Capital	$ 359,611	$ 341,924
	Net Worth	490,043	493,118
	Net Sales	1,726,769	1,739,224

This old, established business has all along maintained a sound financial condition. Net worth has shown increases over the past several years as a result of retention of earnings, but it declined slightly this year. Volume continues to show moderate increases each year.

Current financial statement shows a satisfactory working capital condition despite the slight reduction in sales and net worth.

CURRENT

On March 3, Mrs. Emma Little, bookkeeper, submitted financial statement of Dec. 31, 1992, as the latest available for publication.

While complete operating figures are not submitted for publication, sales for the year ending Dec. 31, 1992, were $1,727,000 compared to $1,739,000 for the previous year.

Mrs. Little stated that sales for the first three months of this year are in excess of $470,000 and that sales for the fiscal year will probably approach $2,000,000.

Banking

Relations are maintained with one local bank, where balances average in high five to low six figures. Loans granted to low five figures secured by accounts receivable, with high four figures currently outstanding. The account is well regarded.

EXHIBIT 5B Athletequip, Inc.—Financial Statement of Principals[a]

	Names			
	Elizabeth Ball	Phillip Ball	Gregory Ball	Combined
Assets				
Cash	$ 18,000	$ 9,434	$ 6,298	$ 33,732
Listed securities	30,000	30,809	27,059	87,868
Unlisted securities	92,232	180,804	180,804	453,840
Co. profit sharing	5,650	12,500	12,500	30,650
Real estate	235,639	281,643	275,100	792,382
Vans Inv.	3,800	3,800	3,800	11,400
C.V.L.I.		2,430	4,529	6,959
Receivables	65,521			65,521
Auto	6,000	3,100	1,500	10,600
Other		2,000		2,000
Total	$456,842	$526,520	$511,590	$1,494,952
Liabilities				
Real estate	$ 28,940	$ 88,945	$ 90,430	$ 208,315
Contracts	2,376			2,376
Taxes	1,967	3,023	5,150	10,140
Total	$ 33,283	$ 91,968	$ 95,580	$ 220,831
Net Worth	423,559	434,552	416,010	1,274,121
Total	$456,842	$526,520	$511,590	$1,494,952
N.W. w/o Athletequip	$331,327	$253,748	$235,306	$ 820,381

[a]All statements dated April 1, 1993.

EXHIBIT 6 Industry Ratios—Manufacturing—Sporting and Athletic Goods

	Low 10%	Average	High 10%
Current ratio	1.2×	1.8×	2.7×
Quick ratio	.5×	.8×	1.2×
Days sales in receivables	72d	54d	36d
Days COGS inventory	166d	111d	72d
Sales/working capital	3.6×	7.2×	12.4×
Sales/net fixed assets	6.5×	10.9×	20.9×
Sales/total assets	1.5×	1.7×	2.4×
EBIT/interest	.7×	2.1×	4.2×
Cash flow/current maturity debt	.3	2.4	7.1
Total debt/equity	351%	168%	94%
Return on assets	.4%	5.0%	15.6%
Return on equity	1.6%	16.4%	37.4%