|  |
| --- |
| You have just been hired as a loan officer at Fairfield State Bank. Your supervisor has given you a file containing a request from Hedrick Company, a manufacturer of auto components, for a $1,000,000 five-year loan. Financial statement data on the company for the last two years are given below: |

|  |
| --- |
| Hedrick CompanyComparative Balance Sheet |
|  | This Year | Last Year |
| **Assets** |  |  |  |  |
| Current assets: |  |  |  |  |
| Cash | $ | 337,000  | $ | 421,000  |
| Marketable securities |  | 0  |  | 96,000  |
| Accounts receivable, net |  | 901,000  |  | 602,000  |
| Inventory |  | 1,400,000  |  | 880,000  |
| Prepaid expenses |  | 72,000  |  | 59,000  |
|  |  |  |  |  |
| Total current assets |  | 2,710,000  |  | 2,058,000  |
| Plant and equipment, net |  | 3,261,400  |  | 3,234,000  |
|  |  |  |  |  |
| Total assets | $ | 5,971,400  | $ | 5,292,000  |
|  |  |  |  |  |
| **Liabilities and Stockholders' Equity** |  |  |  |  |
| Liabilities: |  |  |  |  |
| Current liabilities | $ | 1,350,000  | $ | 900,000  |
| Bonds payable, 10% |  | 1,180,000  |  | 1,200,000  |
|  |  |  |  |  |
| Total liabilities |  | 2,530,000  |  | 2,100,000  |
|  |  |  |  |  |
| Stockholders' equity: |  |  |  |  |
| Preferred stock, 8%, $30 par value |  | 600,000  |  | 600,000  |
| Common stock, $40 par value |  | 2,000,000  |  | 2,000,000  |
| Retained earnings |  | 841,400  |  | 592,000  |
|  |  |  |  |  |
| Total stockholders' equity |  | 3,441,400  |  | 3,192,000  |
|  |  |  |  |  |
| Total liabilities and stockholders' equity | $ | 5,971,400  | $ | 5,292,000  |
|  |  |  |  |  |
|  |

|  |
| --- |
| Hedrick CompanyComparative Income Statement and Reconciliation |
|  | This Year | Last Year |
| Sales (all on account) | $ | 5,280,000  | $ | 4,290,000  |
| Cost of goods sold |  | 4,110,000  |  | 3,190,000  |
|  |  |  |  |  |
| Gross margin |  | 1,170,000  |  | 1,100,000  |
| Selling and administrative expenses |  | 510,000  |  | 520,000  |
|  |  |  |  |  |
| Net operating income |  | 660,000  |  | 580,000  |
| Interest expense |  | 118,000  |  | 120,000  |
|  |  |  |  |  |
| Net income before taxes |  | 542,000  |  | 460,000  |
| Income taxes (30%) |  | 162,600  |  | 138,000  |
|  |  |  |  |  |
| Net income |  | 379,400  |  | 322,000  |
|  |  |  |  |  |
| Dividends paid: |  |  |  |  |
| Preferred stock |  | 48,000  |  | 48,000  |
| Common stock |  | 82,000  |  | 41,000  |
|  |  |  |  |  |
| Total dividends paid |  | 130,000  |  | 89,000  |
|  |  |  |  |  |
| Net income retained |  | 249,400  |  | 233,000  |
| Retained earnings, beginning of year |  | 592,000  |  | 359,000  |
|  |  |  |  |  |
| Retained earnings, end of year | $ | 841,400  | $ | 592,000  |
|  |  |  |  |  |
|  |

|  |
| --- |
| Marva Rossen, who just two years ago was appointed president of Hedrick Company, admits that the company has been “inconsistent” in its performance over the past several years. But Rossen argues that the company has its costs under control and is now experiencing strong sales growth, as evidenced by the more than 22% increase in sales over the last year. Rossen also argues that investors have recognized the improving situation at Hedrick Company, as shown by the jump in the price of its common stock from $70 per share last year to $54 per share this year. Rossen believes that with strong leadership and with the modernized equipment that the $1,000,000 loan will enable the company to buy, profits will be even stronger in the future. |
| Anxious to impress your supervisor, you decide to generate all the information you can about the company. You determine that the following ratios are typical of companies in Hedrick’s industry: |

|  |  |  |
| --- | --- | --- |
|  |  |  |
| Current ratio | 2.3 |  |
| Acid-test ratio | 1.2 |  |
| Average collection period | 31 | days  |
| Average sale period | 60 | days  |
| Return on assets | 9.5 | %  |
| Debt-to-equity ratio | 0.65 |  |
| Times interest earned ratio | 5.7 |  |
| Price-earnings ratio | 10 |  |
|  |

|  |
| --- |
| **Required:** |
| **1.** | Present the balance sheet in common-size format. **(Leave no cells blank - be certain to enter "0" wherever required. Round your answers to 1 decimal place. Due to rounding, figures may not fully reconcile down a column. Omit the "%" sign in your response.)** |

|  |
| --- |
| Hedrick CompanyComparative Balance Sheet |
|  | This Year | Last Year |
| **Assets** |  |  |  |  |
| Current assets: |  |  |  |  |
| Cash |  | % |  | % |
| Marketable securities |  |  |  |  |
| Accounts receivable, net |  |  |  |  |
| Inventory |  |  |  |  |
| Prepaid expenses |  |  |  |  |
|  |  |  |  |  |
| Total current assets |  |  |  |  |
| Plant and equipment, net |  |  |  |  |
|  |  |  |  |  |
| Total assets |  | % |  | % |
|  |  |  |  |  |
| **Liabilities and Stockholders' Equity** |  |  |  |  |
| Liabilities: |  |  |  |  |
| Current liabilities |  | % |  | % |
| Bonds payable, 10% |  |  |  |  |
|  |  |  |  |  |
| Total liabilities |  |  |  |  |
|  |  |  |  |  |
| Stockholders' equity: |  |  |  |  |
| Preferred stock, 8%, $30 par value |  |  |  |  |
| Common stock, $40 par value |  |  |  |  |
| Retained earnings |  |  |  |  |
|  |  |  |  |  |
| Total stockholders' equity |  |  |  |  |
|  |  |  |  |  |
| Total liabilities and stockholders' equity |  | % |  | % |
|  |  |  |  |  |
|  |

|  |  |
| --- | --- |
| **2.** | Present the income statement in common-size format down through net income. **(Input all amounts as positive values. Round your answers to 1 decimal place. Due to rounding, figures may not fully reconcile down a column. Omit the "%" sign in your response.)** |

|  |
| --- |
| Hedrick CompanyComparative Income Statements |
|  | *This Year* | *Last Year* |
| Sales | %  | %  |
| Cost of goods sold |  |  |
|  |  |  |
| Gross margin |  |  |
| Selling and administrative expenses |  |  |
|  |  |  |
| Net operating income |  |  |
| Interest expense |  |  |
|  |  |  |
| Net income before taxes |  |  |
| Income taxes (30%) |  |  |
|  |  |  |
| Net income | %  | %  |
|  |  |  |