Turnaround Strategies

Below are the balance sheet and income statement for 2005 and 2006 of a company that is in financial distress.

**Balance Sheet for 2005 and 2006**

|  |  |  |
| --- | --- | --- |
|   | **2005 ($)** | **2006 ($)** |
| Cash | 20,000 | 5,000 |
| Accounts receivables | 150,000 | 395,000 |
| Inventories | 300,000 | 200,000 |
| Total current assets | 470,000 | 600,000 |
| Fixed assets, net | 350,000 | 350,000 |
| **Total assets** | **820,000** | **950,000** |
| Accounts payable | 85,000 | 170,000 |
| Accruals | 40,000 | 50,000 |
| Bank loan | 150,000 | 150,000 |
| Total current liabilities | 275,000 | 270,000 |
| Long-term debt | 325,000 | 500,000 |
| Common stock ($5 par) | 100,000 | 100,000 |
| Capital Surplus | 70,000 | 70,000 |
| Retained Earnings | 50,000 | 10,000 |
| **Total liabilities and equity** | **820,000** | **950,000** |

**Income Statement for 2005 and 2006**

|  |  |  |
| --- | --- | --- |
|   | **2005 ($)** | **2006 ($)** |
| Net sales | 800,000 | 600,000 |
| Cost of goods sold | 500,000 | 400,000 |
| Gross profit | 300,000 | 200,000 |
| Marketing | 50,000 | 70,000 |
| General and administrative | 60,000 | 80,000 |
| Depreciation | 20,000 | 30,000 |
| EBIT | 170,000 | 20,000 |
| Interest | 50,000 | 60,000 |
| Earnings before taxes | 120,000 | –40,000 |
| Income taxes (35%) | 42,000 | 0 |
| **Net income** | **78,000** | **–40,000** |

**Your tasks:**

1. Calculate the firm’s total operating cycle for 2005 and 2006.
2. What type of working capital restructuring can the firm do to turn around its performance? What other types of asset restructuring might the firm consider?
3. What type of operations restructuring should the firm consider?
4. What type of financial restructuring should the firm consider?