

# Case study on competition bikes inc storyline

[Business](#), [Company](#)



## **Competition Bikes Inc. Storyline**

### Horizontal Analysis

Horizontal analysis involves a comparison of companies' performance over a specific duration. The intent of this paper is to analyze the performance of Competition Bikes Company using various methods. There is a commendable performance in Competition Bikes Inc as is shown by the analysis done on the income statement and the balance sheet. There is a decrease in sales in the year 7, as well as 8 by 15 percent, but an increase in net sales by 33 percent was achieved in year 6 and 7. The decrease in sales could have been attributed by a general increase in prices, recession or increased competition such as with Wheel Racing, Inc. This shows that in the accounting period, in year 6 and 7 net sales, increased, but decreased drastically in years 7 and 8. This has an effect on the gross profit realized by the company. This is evidenced by a decrease of gross profit in year 7 and 8 by 16.3 percent and rose by 37.5 percent in year 6 and 7. This reduction in gross profit in the years 7 and 8 are as a result of a drastic decrease in sales within the period. A decrease in selling expenses is experienced in the year 7 and 8 as compared to 33 percent in year 6 and 7. This was as a result of reduction of costs which contributed to higher profits in the same period. There's an increase in general and administrative costs which described the company weakness of controlling cost and maintaining them as low as possible. This is evidenced by an increase of expenses by 1 percent in year 6 and 8, which was 20 percent in year 6 and 7. In both accounting period, there is an increase in costs, but costs in year 7 and 8 as a result of research and development costs. There is an increase in total cost by 23 percent in year 7

and 8, but decreased from year 6 and 7. With the same proportion, provision for taxes as well as earning before interest and taxes changed as net earnings were changing. Hostile competition leads to decrease in sales.

## **Vertical analysis results**

In vertical analysis, analysis of financial statements is basically on three areas, which includes, assets, liabilities as well as equity. Every balance sheet component is expressed in terms of assets but in the income statement is expressed in terms of sales, that is, sales and assets are the basis of evaluation. This helps the organization to have a clear view of changes in the financial period.

In the Competition Bikes, Inc. the cost of goods sold is approximately 73 percent of sales in all the three accounting periods. Therefore, sales have an effect on the gross profit recorded by the organization. The accounting profit reported by the company in the three accounting period is averaged to 27 percent. The management of Horizontal Bikes Incl should develop strategies for reducing costs. This leads to higher profits as cost of sales is decreased. Its gross profit is averaged to be 27 percent. For an increase in profits, the company should reduce the cost of sales or increase the sales amount or price.

On average, the company average selling expenses were about 6.7 percent in the three periods of time. This is an indication of an effective strategy of reducing the cost. Reduced selling cost lowers operational cost thus higher profits. There is an almost equal administrative and operational costs over the three periods. The proportion of the year 6 was 17 percent, 15 percent in

year 7 and 18 percent in the year 8. In terms of operating income, there is a better performance in year 7 as compared to the other years.

### **The outcome of trend analysis**

This is an analysis of the company's performance through an examination of its annual financial outcomes. From the projected, as well as historical trend analysis, it is evident that the company is performing well. Increase in general performance by 133 percent in year 7 made the company has an improved performance. This performance resulted from an increase in sales as well as the reduction of costs in the same year. This boosted the companies' net earnings. However in the year 8, there was a drastic decrease in sales which made the year's income different from the previous year. This reduction in sales leads to unpleasant performance of the company. The Competition Bikes Inc should set strategies to improve its sales margin so as to gain competitive advantage.

A projected increase in sales by 3.2 percent in year 2009 is made as well as a 4 percent increase in the year 2010. This is an indication of company's improvement in performance in the coming years. The company projects that, it will have a fully implemented strategy of improving sales by eleventh year. This is an indication that the company can increase sales without increasing cost of production. The company is on the right steps in achievement of set goals as evidenced by the expected increase in sales in year 2008 to 2011.

## Ratio analysis

Ratios can also be used to analyze the performance of Competitive Bikes Inc. The current ratio of the company in the year 7 and 8 are given as 5.5. If compared with Two Wheels Racing, Inc. which has a ratio of 4.2, then the Competition Bikes has a more liquidity position than Two wheel Racing Inc. A high liquidity position is recommended since it shows that the company is able to meet its short term obligations when they fall due. The company has an acid test ratio of 4.5, an indication that its current liabilities are 4.5 times less than current assets.

The Competition Bikes has shown a better position of meeting its short run obligations when they fall due as compared to its competitors. The average collection period of the company is 43.8 indicating a good credit policy. However, its competitor has a shorter collection period of 32.5 days than the company thus takes less time to receive the credit sales payment than the company.

## Part B

Cash flow is improved techniques

Strategies that increase annual sales leads to an increase in cash flow. The company should thus develop strategies for improving its sales to raise its cash flow level. Strategies such as advertising, increased production, diversification as well as product promotions are ways of increasing sales level. This makes firms acquire competitive advantage over its competitors. This makes customers loyal to the company. Strategies for reducing production costs which covers 73 percent of the company sales should be established by the company. This can be done by upgrading the company

technology to ensure an efficient and effective production means. Finding the best supplier of raw materials in terms of price, quality and discount are ways that can lead to reduced cost of production. When these strategies are implemented, then an increase in sales is experienced thus an increase in cash inflow to the company.

## **Methods of utilizing surplus working capital**

Part c

Internal controls used in Competition Bikes

- i. Purchasing department has the sole function of purchasing raw materials. This may lead to collusion among employees hence risk to the company.
- ii. The company uses first month projection to make requisition instead of using the historical or market prices.
- iii. The company has a good strategy of storing the raw materials that have not been used at the end of the month. The problems arise when the company fails to document this monthly unutilized raw material.
- iv. Three sources are only used in making decisions. The company ignores other sources.
- v. Writing of checks as well as sending the checks is made by the purchasing department but is supposed to be done by many departments.

## **Corrective measures**

- I. The company should use the historical figures when ordering raw materials but not basing its decision on monthly projections.
- II. Quality of products should also play a part in getting the supplier rather than just getting the lowest bidder.

III. Regular checks on the delivered goods should be done and compared to the ordered ones.

IV. Goods received note after delivery of raw materials and at the same time demand a delivery note should be given by the company.

### **The company's risks and how they can be mitigated**

Insolvency is a risk that a company may face after failing to have a complex and efficient method of recording the transaction. An elaborate bookkeeping system should be created to record the daily transactions of the company.

The company is facing a risk of purchasing low quality goods since it only considers three suppliers. The risk of buying low quality goods can be avoided by accessing all possible sources and implementing strong measures that will guarantee quality products are purchased.

### **Compliance analysis of Sarbanes-Oxley requirements**

Competition Bikes does not comply with the requirements of Sarbanes-Oxley in implementing its internal controls. Annual records can be used to check the strength and weakness of internal control system. Competition Bikes can use its annual records to determine the nature of its internal control system. A weak internal control is evidenced by the purchasing department by having numerous authorities within the organization. Proper documentation should be maintained by the company for internal control system evaluation.

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