

# [Cartwright lumber company case](https://assignbuster.com/cartwright-lumber-company-case/)

Company Background & Situation Cartwright lumber company was located in a suburb of a large city in the Pacific Northwest; its operations were limited to the retail distribution of lumber products in the local area. In 1994, Cartwright Lumber Company was established as a partnership by Mark Cartwright and his brother-in-law Henry Stark. However, in 2001, Cartwright brought out Henry’s interest for $105, 000 and incorporated the company. About 55% of the total sales of Cartwright Lumber Company were made in the six months from April through September. There were no sales representative; orders were taken exclusively over telephone. Sales volume had been largely on the basis of successful price competition, made possible by careful control of operating expenses and by quantity purchases of material at substantial discounts.

Besides, good relationship with suppliers and high loyalty of employees contributed to its success. Cartwright Lumber Company’s financial status was promising; from 2001 to 2004, they experienced an average sales increase rate of about 29. 7% yearly. However, debt existed. In order to buy off Stark’s interest, Cartwright got a loan of $70, 000 in late 2001; the loan was secured by land and buildings, carried an interest rate of 11%, and was repayable in quarterly installments at the rate of $7, 000 a year over the next 10 years. During the last two years, Cartwright Lumber Company was short for funds arising from the purchase of Stark’s interest in the business and the additional investment in working capital associated with the company’s increasing sale volume. The tentative discussions between Northrop Bank and Cartwright Lumber Company had been about a revolving secured 90-day note not to exceed $465, 000. Interest would be set on a floating-rate basis, which was about 10. 5% under conditions in effect in early 2004. The problems were, how much should Cartwright borrow, should Northrop Bank approve the loan?

II. Financial Analysis Based on the company background and situation analysis, we do the historical record for financial analysis, including profitability, assets management, liquidity, working capital and cash flow. 1. Profitability

Profitability ratios are functions of both the industry and a company’s position within the industry. The boundaries are set by the operating characteristics of the industry, within these boundaries profitability ratios are determined by a player’s relative position. Gross profit margin should stay constant or increase because cost of goods sold should be a constant percentage of sales or should decrease as the company’s price increases and/or volume discounts. Gross profit margin was slightly favorable stable at 28%. The horizontal analysis information showed that sales had been averagely increased by 26% from 2001 to 2003. However the operating cost had been averagely increased by 27%.

Assets Management

For the assets management, we are looking for receivable turnover, payable turnover, inventory turnover. Turnover ratios measure how many times per year a given resource is consumed. Management’s objective is to stretch out the accounts payable period (low accounts payable turnover) and shorten the periods for accounts receivable and inventory (high accounts receivable and inventory turnover). The average of 2001 to 2003 was 10, 9. 2 and 5. 1 times respectively. And according to horizontal analysis from 2001 to 2003, the assets and liabilities were keeping increasing.

Liquidity & Working

Capital Current ratio measures the firm’s ability to meet short-term obligation. The average of 2001 to 2004 was 1. 55. Asset-liability ratio measures the firm’s ability to meet its long-term obligation. The average of 2001 to 2004 was 0. 61. Those were within acceptable level. Besides the liquidity, the working capital was keeping increasing from $ 208 thousand to $ 242 thousand.

Cash Flow

Based on the income statement and balance sheet, we can get the cash flow statement for year 2002, 2003 and the first quarter of 2004. From the cash flow, it is obviously see that the main use of fund is for operations, materials purchasing, wages payment, interest payment etc. While the source of fund is from financing, bank loan and trade notes payables.

III. Credit Assessment & Industry Analysis With understanding of historical financial situation, we still need to know how company’s credit report demonstrates. And for a corporate form of organization, how it plays about the owner of the company’s personal credit. 1. Credit Assessment on Company

Company Credit Assessment: For the Cartwright Lumber could get 2% discount payment within 10 days from suppliers, but it had taken few purchase discount because of the shortage of funds, while there was no bad record of lagged payment, so the company still owned good credit assessment.

Credit Assessment on Mark

Administer Credit Assessment: Mark Cartwright was the sole owner of Cartwright Lumber Company. Per one of his supplier evaluated, Mark kept close check on his own credits, and had good personality. Situation for Cartwright Lumber were good. It was located in the growing suburb of a big city. The growing suburb will need a big sum of construction material such as a molding, sash and door. And the Pacific Northwest area was covered by plenty of forestry, and this forestry supply enough raw materials for Cartwright Lumber. Trees had seldom been harvested during the grow season, March to September, so the best choice for Cartwright Lumber was to purchase abundant raw material before March.

As the gross profit rate was 28%, if the sales forecast $3. 6 million, the raw material would cost $2. 6 million. American financial policies would continue keep the low interest rate in 2004, this policy would be sustainable to incentive the real estate development. There were some risks for Mark Cartwright. Firstly, for the long history of wood production mill was easy to catch the fire for electronic wire and poor operation or smoking cigarette. Secondly, Mark was the sole owner of mill and controlled all the line, if his health condition went bad, it was a potential risk for Cartwright Lumber. Thirdly, turnover was another risk for Cartwright, because Mark had only 10 staff and $3. 6 million sales, if any staff left the mill, it would have negative influence.

IV. Financial Forecasting According to the industrial analysis and company analysis, we predict the sales forecast as the following chart: On the assumption of 20% increasing of sales, the net income would be 18, 000 in second quarter, 18, 000 in the third quarter and 17 in the fourth quarter. By this way, we assume the accounts receivable and accounts receivable were the some ratio of sales between the different quarters, so we could make the balance sheet according to the sales forecast.

After adjust the income statement and balance sheet, we could conclude the statement of cash flow. So, the lumbers needed 236, 000 cash in the second quarter. With considering the previous loan balance, we needed to apply the loan from Northrop National Bank with amount $ 400, 000.

V. Conclusion According to the financial analysis, credit assessment, industry analysis and financial forecasting, we can make decisions below. For Cartwright Lumber Company, they needed to apply the loan from Northrop National Bank. The amount should be $ 400, 000. And for the further expansion, they needed to keep the sales growth and more debt financing if necessary. For Northrop National Bank, they could approve the loan with conditions below: 1) Interest would be set on floating-rate basis; 2)90 – days due, unsecured; 3) net working capital would be kept above $ 400, 000; 4) additional investment in fixed assets could be made only with the prior approval of the bank; 5) limitations would be placed on withdrawals of funds from the business by Cartwright.