

Jones electrical distribution electric suppliers finance essay



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Introduction

Jones Electrical Distribution is an Electrical company which has predicted that sales for the company will increase. However, over the years the company has experienced some difficulties in its cash flow and decided that in order to keep the company in operation, it was evident that additional financing would be needed in the form of a loan. However, the loan limit for borrowing could not have exceeded \$250, 000. 00. This amount was the maximum limit their local bank, Metropolitan would offer to any company. It must be pointed out that from the inception of Jones Electrical, Metropolitan Bank was the only financial provider used by the company. In light of the foregoing, Jones had to seek alternative financial assistance from another bank - Southern Bank and Trust. The credit line offered Jones Electrical a loan would be in the amount of \$350, 000. 00, \$100, 000. 00 more than what Metropolitan would have offered. Jones Electrical needed to decide which loan will be more beneficial, less risky and the least expensive for the company. They needed to consider the proposition of receiving the loan from Southern Bank Trust as opposed to remaining with Metropolitan Bank.

Another issue arising from the case is the way in which Jones Electrical did its operations. He had over 100 suppliers from which he credited inventory, and he paid his accounts within the 10-day period in order to benefit from a 2% trade discount. The industry being large, fragmented and highly competitive, Jones Electrical had to decide whether they needed to restructure their company's operation and expand same and also what financial decision that had to be made for the continued operations of the Company. Jones Electrical would have much limitations with respect to borrowing from

Southern Bank and Trust such as; additional investments in fixed assets could only be made with prior approval of the bank, consumption of the credit line would have a limit of \$350, 000 of Accounts Receivable and 50% of Inventory and also, there will be limitations on withdrawals of funds from the business by Jones. Should Jones accept the loan from Southern Bank and Trust, his relationship with Metropolitan Bank will have to be will no longer. (Piper and DeVolder, n. d). A number of factors would be discussed later on in this case which include the financial projections of Jones Electrical. In addition, Jones' financial statements will be analyzed and we will also look at the sustainability growth for this small company. The cash flow of Jones Electrical will also be addressed in this case.

Problems faced by Jones Electrical Distribution

Jones Electrical needs to decide whether or not it will accept the offer of the loan from Southern Bank and Trust or from the Metropolitan Bank. The company needs to maintain its sales, needs to expand, satisfy its liabilities but would need funding in order to do so.

Some main problems identified in the case:

Jones bought Dave Verdent, his former business partner out for \$250, 000. 00. His repayment plan was a \$2000. 00 per month with 8% interest per annum. The interest rate he is paying is relatively high and this means it will take Jones over ten years to repay this loan with an interest payment in excess of \$200, 000. 00 in interest only. Therefore Jones will have to pay approximately \$458, 400. 42 in interest and principal. This occurred because of a fallout Jones had with his partner Dave Verdent over the aggressive

growth of the business, which has put the company in financial debt because Jones has to repay Verdent in full for buying out the company.

From the financial information provided in the Balance Sheet of Jones Electrical Distribution it shows that there was an increase in accounts receivables, inventory, property and equipment. This increase would permit an increase also in liabilities and equity to be able to finance the aforementioned assets. On the other hand, the balance sheet also shows an increase in accounts payable, line of credit payable and accrued expenses. The above increases would therefore warrant financial assistance from the Bank for the expansion of the business.

Another issue is that Jones Electrical had to resort to approaching the bank to receive a loan for his company in order that his business would grow profitably, to develop with respect to opening other locations and to survive on a highly competitive market.

Jones needed to make a decision whether he should receive a loan from Metropolitan Bank or from Southern Bank and Trust. If Jones decide to go with Southern Bank and Trust, there will be implications which were mentioned earlier (additional investments in fixed assets could only be made with prior approval of the bank, consumption of the credit line would have a limit of \$350, 000 of Accounts Receivable and 50% of Inventory and also, there will be limitations on withdrawals of funds from the business by Jones. Should Jones accept the loan from Southern Bank and Trust, his relationship with Metropolitan Bank will no longer be. He needed to weigh his options between the two banks.

Competition in the market: Jones Electrical was faced with a lot of competition from national distributors, home centers and other small supply house. The industry was a very large and fragmented one, and despite the competition, Jones Electrical was able to increase its sales; however, Jones was still in a position where he needed to inject some cash into the business.

Solutions or Recommendations

Jones should accept the loan from Southern Bank and Trust, since he will be receiving more funding. The funding from Southern Bank and Trust was more than what the company would have received from Metropolitan Bank.

Although, the requirements of Southern Bank and Trust Bank seem to be rigid, the more monies that he receives can however be used in the firm's expansion as well as paying off some of the company's liabilities. As a result, Jones will be allowed more flexibility in the operations of the business. He will then be able to increase his assets in the form of inventory and capital, which in turn will result in his business being in a better position to finance its operations. In addition, Jones Electrical will be able to benefit from the trade discounts which are offered by his suppliers because this arrangement would allow him to pay his creditors.

With respect to the early payment discount of only 2%, it is advisable that the Company, continue to credit its supplies and make alternative arrangements with respect of repayment to its suppliers. The company needs cash and the discount of the 2% does not put the company in a better financial position. It is always important to inject equity so that your company will be able to increase its assets, which will eventually lead to an increase in sales and revenue.

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Another issue is that with respect to the proposed growth of the company, Jones had predicted forecasting in sales to increase significantly therefore the urgent need for a very large cash flow into the company would help significantly.

Evaluate solutions

Pros

Cons

Should Jones Electrical decide to accept the loan from Southern Bank and Trust, it will receive funds to be able manage and expand its operations and pay off his debt.

A loan is a liability and this will mean the firm will have another expense to pay at the end of every month.

Benefits from trade discounts offered by his suppliers. He can use this opportunity to get discounts from his suppliers.

Trade discounts can have a negative impact in that if Jones does not stay within the time frame in paying for his goods.

With the increase in bank borrowing, this can contribute to a number of aspects. One main aspect is the increase in sales, which in turn will result in increase revenue.

Increase in bank borrowing can result in a decrease in cash flow. As stated earlier, Southern Bank and Trust has limitations in borrowing money from them.

Conclusion

With respect to the various financial data presented in this case, Jones Electrical forecasts predicted that its sales would increase with favorable prospects and at the same time the company was in dire need of a significant cash inflow. It is however advisable that Jones Electrical accepts the offer made by Southern Bank and Trust despite the specific restrictions that would be placed on the Company. This offer would provide for long term financing of the company and as a result the limitations with respect to borrowing would eventually be removed, thus enabling the Company to utilize the credit line specifically if it foresees forecast would be favorable.

The credit line offered by Southern Bank and Trust would be significantly more than what Metropolitan would ever offer. Eventually, this budding financial relationship between Jones Electrical and Southern Bank and Trust would enable Jones Electrical to even borrow much more than what they would have been offered initially. Jones now will be able to be more flexible with its business decisions with respect to expansion.