

Community bank lending decisions: a case illustration

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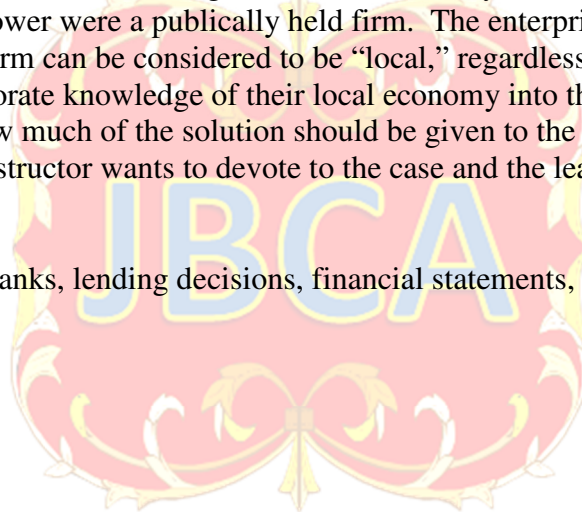
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ABSTRACT

This case requires students to analyze the financial position of a small private venture as if they were a loan officer in a community bank. The information presented is less formal than what would be required at a national or regional bank, and many of the issues in the case would not be present if the borrower were a publically held firm. The enterprise being analyzed is generic enough that the firm can be considered to be “local,” regardless of the location. This allows students to incorporate knowledge of their local economy into the case. Furthermore, this case is very flexible. How much of the solution should be given to the students is a function of the amount of time the instructor wants to devote to the case and the learning objectives to be achieved.

Key words: community banks, lending decisions, financial statements, financial analysis



PURPOSE OF THE CASE

This case is designed to mimic what a loan officer might experience at a community bank. A community bank is “an independent, locally-owned commercial bank. It operates exclusively in and derives its funds from the community in which it is based” (Farlex Financial Dictionary, 2011). Thus, the information presented is less formal than would typically be required at a regional or national bank. The firm being analyzed is a small “mom and pop” operation, a restaurant/bar. Many issues in the case would not be present if the potential borrower was a publically held firm with audited financials and a secondary market for their securities. The enterprise being analyzed is generic enough that the firm can be considered to be “local,” regardless of the location. This allows students to incorporate knowledge of their local economy into the case. Furthermore, this case is very flexible. How much of the solution should be given to the students is a function of the amount of time the instructor wants to devote to the case and the learning objectives to be achieved. This is also an opportunity to encourage students to use a spreadsheet program by providing little or none of the solution and requiring them to construct everything on their own. If time is at a premium, all of the financials can be provided, with the students only focusing on analysis of the statements. The included industry information, although consistent with data from sources that cover privately held firms in this industry, is not drawn from any specific source or for any specific year. The people in the case are fictional and any resemblance to a real enterprise is purely coincidental.

MY BROTHER JOE’S GRILL AND SPIRITS

The current owners of My Brother Joe's Grill and Spirits are Charles (“Charlie”) and Ethel Jones. They acquired the business on June 15, 1999 from its founder, Mr. John Johnson. Mr. Johnson started the business in 1948. Originally, Mr. Johnson was to name the establishment J.J.'s (after himself and his younger brother Joe, a minor league baseball player), but later settled on My Brother Joe's Grill and Spirits (hereafter known as MBJ's). Charlie and Ethel decided not to change the name, since MBJ's was a relatively successful business at the time of purchase. Since acquisition, Charlie has been head cook, and Ethel has run “the front of the house” (restaurant terminology for any place where customers might be). Their daughter, Susie, and some of her friends wait tables and tend bar. The business is open daily, 10 A.M. to midnight. After a couple of years, the stress and strain of operating a business, 7 days a week, 365 days a year began to wear down the Joneses. After much discussion, Ethel's sister, Betty Joe, and her daughter, Janie, were hired to operate the bar and grill on Mondays, giving Charlie and Ethel a much needed respite. Charlie and Ethel hope to cultivate valuable relationships among trustworthy, reliable employees to a point where they would be able to take more time off each week, as well as take an annual vacation of one-two weeks in length. All of the principals are in good health and expecting the bar and grill to be a long term success.

In order to renew MBJ's operational license for another year, a mandatory physical inspection was performed last week. The inspector found several violations with current building codes. The most serious infraction involved the discovery of substandard wiring in the kitchen, and replacement would be a requirement for license renewal.

While soliciting bids in order to make the necessary repairs, Charlie and Ethel noticed that the bar and grill were getting a little shabby; much physical and functional deterioration were present. The Joneses decided that while MBJ's was temporarily closed to replace the

electrical system, they might as well renovate the customer area. After all, the only expenditure they had made during their tenure of ownership was for replacement tables and chairs.

It was determined that approximately \$175,000 would be sufficient to take care of all their needs. An itemized list of their anticipated expenditures follows:

<u>Description</u>	<u>Amount</u>
Electrical Repairs	\$125,000
New Carpet	12,000
New Chairs	7,000
Cash Register	2,000
New Paneling	24,000
New Pictures	2,500
Miscellaneous	2,500
Total Amount Needed	<u>\$175,000</u>

The Joneses have decided to approach PeopleBank, a community bank which is headquartered and operated in the same town as MBJ's. The financial statements for MBJ's last four years of operation, as indicated in Table 1 (Appendix), were presented to the lending officer, Cameron Woods, at PeopleBank (Mr. Woods is a frequent diner at MBJ's, as are many of the area's businesspeople). The terms PeopleBank generally offers on loans of this nature are 9%, 10 years.

The electrical repairs are absolutely necessary for MBJ's to stay in business. Charlie and Ethel were given a temporary license for ninety days to allow them to come into compliance. If the work is not done by that time, the Joneses must close the business or relocate to a building with an adequate electrical system. The other expenditures, although not required, should improve business. Charlie and Ethel estimate that with these renovations, their volume of business should improve by ten to fifteen percent.

QUESTIONS [Note: Questions 4, 5, 6, 8, and 9 may be omitted if all of the financials are provided, with the students only focusing on analysis of the statements.]

1. Is MBJ's a proprietorship, corporation, LLC, or some other form of business organization?
2. Should Mr. Woods, the PeopleBank lending officer, offer advice to the owners of MBJ's concerning their form of business organization?
3. Do MBJ's financial statements in Table 1 conform to generally accepted accounting principles (GAAP)? If not, what alterations are necessary to the income statements and balance sheets in order to achieve compliance?
4. Produce the growth rate income statement and balance sheet (i.e, find the growth rate for each account in each statement for each year, 2008 – 2011).
5. Produce a Statement of Cash Flows for the following years: 2009, 2010 and 2011.
6. Common-size the income statements and balance sheets for MBJ's.
7. Calculate the following ratios:
 - a. Liquidity measures: current ratio, quick ratio, net working capital, cash turnover.

- b. Asset management measures: inventory turnover, average age of inventory, accounts receivable turnover, accounts payable turnover, fixed asset turnover, total asset turnover.
- c. Debt management: debt ratio, times interest earned, fixed charge coverage.
- d. Profitability measures: return on total assets, return on operating assets, return on total equity, return on common equity.

Perform a time series and cross sectional analysis where appropriate. Select industry averages for small, privately owned bar and restaurants can be found in Table 6.

- 8. Use different methods to estimate MBJ's 2012 annual sales (such as long term growth rate, regression, owner's estimates, etc.)
- 9. Provide one year of pro forma financial statements under each of the following assumptions: (1) the lender provides enough money to only perform the required repairs, and (2) the lender grants the entire loan request.
- 10. Should Mr. Woods of PeopleBank grant MBJ's loan request? If so, what should be the amount of the loan? Justify your answer.
- 11. Would it make any difference if MBJ's is an existing customer of PeopleBank, or a potential new customer?

INSTRUCTOR'S MANUAL

- 1. The base information of the case does not indicate the firm's legal form of business organization. Since there is no use of INC, LLC, LLP, or other designation to indicate a limited liability status, it is natural for the students to assume that it must be a proprietorship. However, examination of the income statement reveals that the venture pays income taxes. A look at the balance sheet also shows an equity section that is organized as a corporation. Thus, the implication is that the firm is a corporation, and has not filed for Subchapter S status.
This lack of clarity provides a good opening discussion about the implications of making assumptions. An assumption can have serious consequences if it is not correct. At this point, the class should focus on acquiring information rather than making assumptions. It is also established at this time that the instructor can ask the business owners for additional information. Although the instructor would normally respond that MBJ's is in fact a corporation, any alternative could be chosen. The spreadsheet with the solution would have to be modified accordingly if a different alternative is used in any given semester.
- 2. This is a good time to bring up whether the banker should act as a "consultant," offering business advice to the venture owners. For example, if the business is positioned to be a corporation, should the banker reveal that the owners are endangering their limited liability status by not including "INC" in their company name (and everywhere it is used)? Furthermore, based on their profits, should the banker suggest Sub S status? Every suggestion made by the banker in this capacity exposes the bank to liability (especially if the client takes the advice and something unfortunate occurs).
- 3. The MBJ's financials are unaudited statements; they do not conform to GAAP. Actually, several adjustments need to be made prior to actually beginning the analysis. It is an interesting exercise to tell the students that there are accounts that are misplaced; it allows students to enhance their knowledge of basic financial statement structure.

On the Income Statement, there are a few items that clearly need help. First, Interest Expense is included in operating expenses; it should be reported separately after the operating expenses. Second, MBJ's has both Advertising and Business Promotion accounts. In reality, there is no difference between these two accounts; they should be combined to give a better indication of how the firm is using its promotions. Another Income Statement account that is troubling is Charitable Contributions. If these amounts are truly charitable contributions, they certainly are not required to operate the business. They should be moved to Other Gains/Losses. On the other hand, if these amounts are used only for public recognition, they are just another form of advertising/promotion and should be grouped with those accounts. The suggested solution is based on the later situation.

On the Balance Sheet, the account Due from Employees is troubling. It is currently listed as a liquid account. Based on the progression of the balance, it seems there is much borrowing, but little repayment. Conservatively, this should be treated as a long term asset. This is again a point that the students might ask for clarification from the owners. The suggested solution is based on this account being considered long term.

The adjusted statements are presented in Table 2 (Appendix).

4. Growth rate statements can be found in Table 3 (Appendix).
5. The Statement of Cash Flow, years 2009, 2010 and 2011, are presented in Table 4 (Appendix).
6. The common size statements can be found in Table 5 (Appendix).
7. The calculated ratios can be found in Table 7 (Appendix).

While discussing the pros and cons of granting the loan, discussion should bring up the above average COGS and the high level of inventory. Since this is a family-owned business, this is a great time to bring up the possibility that the Joneses may be running some personal expenses, in particular all of the food they eat at home and/or use for entertaining, through the business. Some small business owners feel they are over taxed and skim sales in order to "level the playing field." However, it is illegal. This presents an opportunity to discuss ethics and conflicts of interest faced by the banker. If the banker can confirm that the firm is committing tax fraud, should he turn the business owners in to the IRS?

Another unusual item on MBJ's statements is the growing Accounts Receivable balance. Based on the industry, some concern should be raised about this potentially being uncollectable bar tabs. Most restaurants/bars no longer offer in-house accounts to patrons. They rely on customers using credit cards. The instructor typically indicates that after discussing it with the owners, it is determined that the accounts are valid and represent sales people from various businesses in the area that bring customers in for meals. They do not have company credit cards and are reimbursed once a month. By offering these patrons credit accounts, it influences where they take their customers. All of the accounts are current without the need for charge offs.

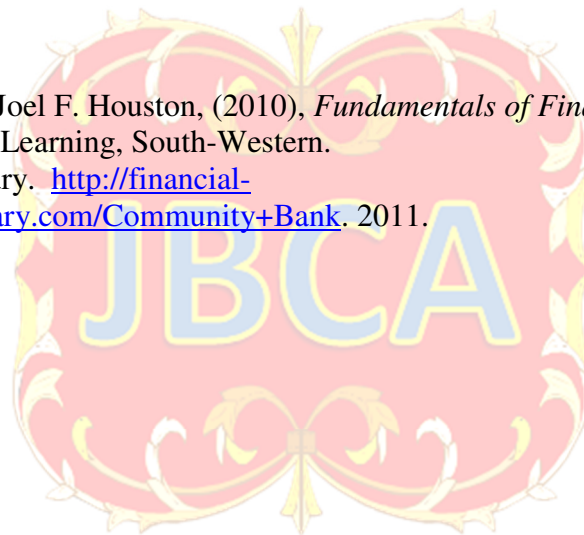
8. Answers will vary. See Table 8 (Appendix) for possible solutions.
9. These solutions will vary based on student assumptions. Answers which students can justify and are realistic should be accepted. A lending decision needs to include a consideration of the future health of the firm. Two alternative projections are provided. One projection is based on the lender only providing enough money to do the required repairs, and the venture can remain in open. The other projection is based on granting the

entire loan request. One set of pro forma statements (accompanying assumptions specified) are presented in Table 9 (Appendix). It should be noted that the future sales level is a projection that is subject to error. The pro forma statements are built in a way that “what if” analysis can be readily accomplished by varying the projected sales level. However, most pro forma statements will generally point to the same conclusion.

10. In polling a class, some students will want to grant the loan, while others will not. If it is granted, all of the outstanding debt should be consolidated into one heavily secured loan. It is also likely that a counteroffer is in order: the loan amount would be somewhere between the minimum amount they need to stay open and the maximum amount they have requested.
11. If the applicant is not already a customer of the bank, they are likely deemed too questionable to grant the loan request. Their current bank has either declined the loan request or is offering terms that are unsatisfactory to the borrower. If the owners of MBJ’s are a current customer and their payment record has been good, there is room for discussion.

REFERENCES:

- Brigham, Eugene F. and Joel F. Houston, (2010), *Fundamentals of Financial Management*, 6th Edition, Cengage Learning, South-Western.
- Farlex Financial Dictionary. <http://financial-dictionary.thefreedictionary.com/Community+Bank>. 2011.



APPENDIX

Table 1: MBJ's Financial Statements, last four years of operation

INCOME STATEMENT	12/31/2011	12/31/2010	12/31/2009	12/31/2008
Net Sales	1,306,576.80	1,283,245.00	1,235,681.05	1,249,328.55
COGS	589,265.30	567,147.75	530,450.85	512,230.10
Gross Profit	717,311.50	716,097.25	705,230.20	737,098.45
Accounting	31,157.55	30,761.20	30,403.50	30,351.70
Advertising	118,190.40	132,573.50	123,795.60	124,800.65
Business Promotion	39,458.55	37,740.70	35,576.15	36,105.05
Charitable Contributions	27,500.00	27,500.00	27,000.00	27,000.00
Depreciation - Building	11,213.25	11,213.25	11,213.25	11,213.25
Depreciation - Furn & Fix	20,246.60	20,246.60	20,246.60	20,246.60
Insurance	43,247.65	42,205.45	41,082.05	40,478.25
Interest Expense	10,307.70	11,408.95	17,616.75	20,935.30
Payroll	277,385.85	271,645.00	268,175.00	263,250.00
Payroll Taxes	30,789.85	29,880.95	29,449.25	28,957.50
Printing	11,798.15	12,259.05	12,095.35	12,192.75
Telephone	11,597.70	11,326.90	10,389.45	10,764.10
Utilities	66,836.00	66,757.85	66,309.30	65,706.00
Total Operating Expenses	699,729.25	705,519.40	693,352.25	692,001.15
Operating Profit	17,582.25	10,577.85	11,877.95	45,097.30
Other Gains/Losses	-11,367.20	-9,105.75	-7,586.30	-5,630.05
Profit Before Taxes	6,215.05	1,472.10	4,291.65	39,467.25
Income Taxes (Fed. & State)	1,367.31	323.86	944.16	8,682.79
Net Income	4,847.74	1,148.24	3,347.49	30,784.45

Table 1, continued

BALANCE SHEET	12/31/2011	12/31/2010	12/31/2009	12/31/2008
ASSETS				
Cash	62,005.90	62,325.20	55,310.79	42,426.96
Trade Receivables - Net	25,708.10	18,082.15	10,446.00	8,791.60
Due From Employees	11,096.65	5,832.95	6,178.40	4,627.15
Inventory	63,202.60	58,912.80	36,452.55	29,613.75
All Other Current	15,826.90	15,998.60	10,560.55	11,105.15
Total Current	177,840.15	161,151.70	118,948.29	96,564.61
Furniture and Fixtures - Net	23,531.25	43,777.85	62,764.45	83,011.05
Building - Net	140,165.25	151,378.50	162,591.75	173,805.00
Land	55,370.60	55,370.60	55,370.60	55,370.60
Intangible Assets - Net	24,488.30	24,488.30	24,488.30	24,488.30
All Other Non-Current	51,153.35	52,402.25	65,675.00	56,329.55
Total Assets	472,548.90	488,569.20	489,838.39	489,569.11
LIABILITIES				
Trade Payables	35,100.60	33,831.10	29,656.30	21,927.35
Current Mat. L/T Debt	20,915.35	20,415.35	23,623.05	23,691.00
Notes Payable	53,156.00	52,830.20	51,898.50	46,734.20
Income Taxes Payable	341.83	80.97	236.04	2,170.70
All Other Current	91,751.25	95,660.40	82,172.70	71,913.95
Total Current	201,265.03	202,818.02	187,586.59	166,437.20
Long Term Debt	84,503.20	105,418.55	125,833.90	149,456.95
Other Non-Current Debt	13,016.55	11,416.25	8,649.75	9,254.30
Total Liabilities	298,784.78	319,652.82	322,070.24	325,148.45
EQUITY				
Capital Stock	100,000.00	100,000.00	100,000.00	100,000.00
Retained Earnings	73,764.12	68,916.39	67,768.15	64,420.66
Total Net Worth	173,764.12	168,916.39	167,768.15	164,420.66
Total Liabilities & Net Worth	472,548.90	488,569.20	489,838.39	489,569.11

Table 2: MBJ's Adjusted Financial Statements

INCOME STATEMENT	12/31/2011	12/31/2010	12/31/2009	12/31/2008
Net Sales	1,306,576.80	1,283,245.00	1,235,681.00	1,249,328.50
COGS	589,265.30	567,147.75	530,450.85	512,230.10
Gross Profit	717,311.50	716,097.25	705,230.20	737,098.45
Advertising	118,190.40	132,573.50	123,795.60	124,800.65
Business Promotion	39,458.55	37,740.70	35,576.15	36,105.05
Charitable Contributions	27,500.00	27,500.00	27,000.00	27,000.00
Total Advertising	185,148.95	197,814.20	186,371.75	187,905.70
Accounting	31,157.55	30,761.20	30,403.50	30,351.70
Depreciation - Furn & Fix	20,246.60	20,246.60	20,246.60	20,246.60
Depreciation - Building	11,213.25	11,213.25	11,213.25	11,213.25
Total Depreciation	31,459.85	31,459.85	31,459.85	31,459.85
Insurance	43,247.65	42,205.45	41,082.05	40,478.25
Payroll	277,385.85	271,645.00	268,175.00	263,250.00
Payroll Taxes	30,789.85	29,880.95	29,449.25	28,957.50
Printing	11,798.15	12,259.05	12,095.35	12,192.75
Telephone	11,597.70	11,326.90	10,389.45	10,764.10
Utilities	66,836.00	66,757.85	66,309.30	65,706.00
Total Operating Expenses	689,421.55	694,110.45	675,735.50	671,065.85
Operating Profit	27,889.95	21,986.80	29,494.70	66,032.60
Other Gains/Losses	-11,367.20	-9,105.75	-7,586.30	-5,630.05
Interest Expense	-10,307.70	-11,408.95	-17,616.75	-20,935.30
Profit Before Taxes	6,215.05	1,472.10	4,291.65	39,467.25
Income Taxes (Fed. & State)	1,367.31	323.86	944.16	8,682.79
Net Income	4,847.74	1,148.24	3,347.49	30,784.46

Table 2, continued

BALANCE SHEET	12/31/2011	12/31/2010	12/31/2009	12/31/2008
ASSETS				
Cash	62,005.90	62,325.20	55,310.79	42,426.96
Trade Receivables - Net	25,708.10	18,082.15	10,446.00	8,791.60
Inventory	63,202.60	58,912.80	36,452.55	29,613.75
All Other Current	15,826.90	15,998.60	10,560.55	11,105.15
Total Current	166,743.50	155,318.75	112,769.89	91,937.46
Furniture and Fixtures - Net	23,531.25	43,777.85	62,764.45	83,011.05
Building - Net	140,165.25	151,378.50	162,591.75	173,805.00
Land	55,370.60	55,370.60	55,370.60	55,370.60
Intangible Assets - Net	24,488.30	24,488.30	24,488.30	24,488.30
All Other Non-Current	51,153.35	52,402.25	65,675.00	56,329.55
Due From Employees	11,096.65	5,832.95	6,178.40	4,627.15
Total Assets	472,548.90	488,569.20	489,838.39	489,569.11
LIABILITIES				
Trade Payables	35,100.60	33,831.10	29,656.30	21,927.35
Current Mat. L/T Debt	20,915.35	20,415.35	23,623.05	23,691.00
Notes Payable	53,156.00	52,830.20	51,898.50	46,734.20
Income Taxes Payable	341.83	80.97	236.04	2,170.70
All Other Current	91,751.25	95,660.40	82,172.70	71,913.95
Total Current	201,265.03	202,818.02	187,586.59	166,437.20
Long Term Debt	84,503.20	105,418.55	125,833.90	149,456.95
Other Non-Current Debt	13,016.55	11,416.25	8,649.75	9,254.30
Total Liabilities	298,784.78	319,652.82	322,070.24	325,148.45
EQUITY				
Capital Stock	100,000.00	100,000.00	100,000.00	100,000.00
Retained Earnings	73,764.12	68,916.39	67,768.15	64,420.66
Total Net Worth	173,764.12	168,916.39	167,768.15	164,420.66
Total Liabilities & Net Worth	472,548.90	488,569.20	489,838.39	489,569.11

Table 3: MBJ's Growth Rate Statements

INCOME STATEMENT	Average	12/31/2011	12/31/2010	12/31/2009
Net Sales	1.50	1.82	3.85	-1.09
COGS	4.78	3.90	6.92	3.56
Gross Profit	-90	.17	1.54	-4.32
Advertising	-1.80	-10.85	7.09	-.81
Business Promotion	3.00	4.55	6.08	-1.46
Charitable Contributions	.61	.00	1.85	.00
Total Advertising	-.49	-6.40	6.14	-.82
Accounting	.88	1.29	1.18	.17
Depreciation - Furn & Fix	.00	.00	.00	.00
Depreciation - Building	.00	.00	.00	.00
Total Depreciation	.00	.00	.00	.00
Insurance	2.23	2.47	2.73	1.49
Payroll	1.76	2.11	1.29	1.87
Payroll Taxes	2.07	3.04	1.47	1.70
Printing	-1.09	-3.76	1.35	-.80
Telephone	2.52	2.39	9.02	-3.48
Utilities	.57	.12	.68	.92
Total Operating Expenses	.90	-.68	2.72	.70
Operating Profit	-24.97	26.85	-25.46	-55.33
Other Gains/Losses	26.39	24.84	20.03	34.75
Interest Expense	-21.04	-9.65	-35.24	-15.85
Profit Before Taxes	-46.00	322.19	-65.70	-89.13
Income Taxes (Fed. & State)	-46.00	322.19	-65.70	-89.13
Net Income	-46.00	322.19	-65.70	-89.13

Table 3, continued

BALANCE SHEET	Average	12/31/2011	12/31/2010	12/31/2009
ASSETS				
Cash	13.48	-0.51	12.68	30.37
Trade Receivables - Net	43	42.17	73.1	18.82
Inventory	28.75	7.28	61.62	23.09
All Other Current	12.54	-1.07	51.49	-4.9
Total Current	21.95	7.36	37.73	22.66
Furniture and Fixtures - Net	-34.31	-46.25	-30.25	-24.39
Building - Net	-6.92	-7.41	-6.9	-6.45
Land	0	0	0	0
Intangible Assets - Net	0	0	0	0
All Other Non-Current	-3.16	-2.38	-20.21	16.59
Due From Employees	33.85	90.24	-5.59	33.52
Total Assets	-1.17	-3.28	-0.26	0.06
LIABILITIES				
Trade Payables	16.98	3.75	14.08	35.25
Current Mat. L/T Debt	-4.07	2.45	-13.58	-0.29
Notes Payable	4.39	0.62	1.8	11.05
Income Taxes Payable	-46	322.19	-65.7	-89.13
All Other Current	8.46	-4.09	16.41	14.27
Total Current	6.54	-0.77	8.12	12.71
Long Term Debt	-17.31	-19.84	-16.22	-15.81
Other Non-Current Debt	12.04	14.02	31.98	-6.53
Total Liabilities	-2.78	-6.53	-0.75	-0.95
Capital Stock	0	0	0	0
Retained Earnings	4.62	7.03	1.69	5.2
Total Net Worth	1.86	2.87	0.68	2.04
Total Liabilities & Net Worth	-1.17	-3.28	-0.26	0.06

Table 4: MBJ's Statement of Cash Flows

	12/31/2002	12/31/2010	12/31/2009
OPERATING ACTIVITIES			
Net Income	4847.74	1148.24	3347.49
+ Depreciation	31459.85	31459.85	31459.85
Provided by operations	36307.59	32608.09	34807.34
Trade Receivables - Net	-7625.95	-7636.15	-1654.4
Inventory	-4289.8	-22460.25	-6838.8
All Other Current Assets	171.7	-5438.05	544.6
Trade Payables	1269.5	4174.8	7728.95
Notes Payable	325.8	931.7	5164.3
Income Taxes Payable	260.86	-155.08	-1934.66
All Other Current Liabilities	-3909.15	13487.7	10258.75
Net Operating Activities	22510.55	15512.76	48076.08
INVESTING ACTIVITIES			
Furniture and Fixtures	0	-1260	0
Building	0	0	0
Land	0	0	0
Intangible Assets	0	0	0
All Other Non-Current Assets	1248.9	13272.75	-9345.45
Due From Employees	-5263.7	345.45	-1551.25
Net Investing Activities	-4014.8	12358.2	-10896.7
FINANCING ACTIVITIES			
Current Mat. L/T Debt	500	-3207.7	-67.95
Long Term Debt	-20915.35	-20415.35	-23623.05
Other Non-Current Debt	1600.3	2766.5	-604.55
Capital Stock	0	0	0
Net Financing Activity	-18815.05	-20856.55	-24295.55

Table 5: MBJ's Common Size Statements

INCOME STATEMENT	12/31/2011		12/31/2010		12/31/2009		12/31/2008	
	Co.	IND	Co.	IND	Co.	IND	Co.	IND
Net Sales	100	100	100	100	100	100	100	100
COGS	45.1	37.6	44.2	38.4	42.93	39.2	41	42.7
Gross Profit	54.9	62.4	55.8	61.6	57.07	60.8	59	57.3
Advertising	9.05		10.33		10.02		9.99	
Business Promotion	3.02		2.94		2.88		2.89	
Charitable Contributions	2.1		2.14		2.19		2.16	
Total Advertising	14.17		15.42		15.08		15.04	
Accounting	2.38		2.4		2.46		2.43	
Depreciation - Furn & Fix	1.55		1.58		1.64		1.62	
Depreciation - Building	0.86		0.87		0.91		0.9	
Total Depreciation	2.41		2.45		2.55		2.52	
Insurance	3.31		3.29		3.32		3.24	
Payroll	21.23		21.17		21.7		21.07	
Payroll Taxes	2.36		2.33		2.38		2.32	
Printing	0.9		0.96		0.98		0.98	
Telephone	0.89		0.88		0.84		0.86	
Utilities	5.12		5.2		5.37		5.26	
Total Operating Expenses	52.77	58.1	54.09	57.2	54.69	54.1	53.71	50.3
Operating Profit	2.13	4.3	1.71	4.4	2.39	6.7	5.29	7
Other Gains/Losses	-0.87		-0.71		-0.61		-0.45	
Interest Expense	-0.79		-0.89		-1.43		-1.68	
Profit Before Taxes	0.48	3.3	0.11	2.6	0.35	5.9	3.16	5.2
Income Taxes	0.1		0.03		0.08		0.69	
Net Income	0.37		0.09		0.27		2.46	

Table 5, continued

BALANCE SHEET	12/31/2011		12/31/2010		12/31/2009		12/31/2008	
	Co.	IND	Co.	IND	Co.	IND	Co.	IND
ASSETS								
Cash	13.12	9.2	12.76	7.8	11.29	12.9	8.67	11.3
Trade Receivables	5.44	2.6	3.7	3.6	2.13	1.9	1.8	2.7
Inventory	13.37	9.8	12.06	8.6	7.44	7.2	6.05	9
All Other Current	3.35	0.6	3.27	0.4	2.16	1.9	2.27	1.3
Total Current	35.29	22.2	31.79	20.4	23.02	23.9	18.78	24.3
Furniture and Fixtures - Net	4.98		8.96		12.81		16.96	
Building - Net	29.66		30.98		33.19		35.5	
Land	11.72		11.33		11.3		11.31	
	46.36	59.2	51.28	53.7	57.31	56.4	63.77	55.1
Intangible Assets - Net	5.18	9	5.01	10.5	5	10	5	10.9
All Other Non-Current	10.82	9.6	10.73	15.3	13.41	9.8	11.51	9.6
Due From Employees	2.35		1.19		1.26		0.95	
Total Assets	100	100	100	100	100	100	100	100
LIABILITIES								
Trade Payables	7.43	6.9	6.92	9.2	6.05	6.5	4.48	8
Current Mat. L/T Debt	4.43	5.7	4.18	5.9	4.82	5.5	4.84	5.9
Notes Payable	11.25	8.7	10.81	6.3	10.6	3.6	9.55	2
Income Taxes Payable	0.07	0.4	0.02	1.3	0.05	0.7	0.44	0.6
All Other Current	19.42	11.9	19.58	13.2	16.78	10.3	14.69	9.7
Total Current	42.59	33.6	41.51	35.9	38.3	26.6	34	26.1
Long Term Debt	17.88	28.3	21.58	30.3	25.69	28.4	30.53	33.1
Other Debt	2.75	7.2	2.34	5.9	1.77	6.7	1.89	5.5
Total Liabilities	63.23	69.1	65.43	72.1	65.75	61.7	66.42	64.7
EQUITY								
Capital Stock	21.16		20.47		20.41		20.43	
Retained Earnings	15.61		14.11		13.83		13.16	
Total Net Worth	36.77	30.9	34.57	27.8	34.25	38.3	33.58	35.3
Total Lia & Net Worth	100	100	100	100	100	100	100	100

Table 6: Select industry averages for small, privately owned bar and restaurants

Ratio	2011	2010	2009	2008
Current Ratio	.90	.70	.80	.90
Quick Ratio (Acid Test)	.50	.30	.40	.30
Inventory Turnover	19.40	19.40	16.60	19.00
Average Age of Inventory	19.00	19.00	22.00	19.00
Accounts Receivable Turnover	494.00	INF	INF	INF
Accounts Payable Turnover	19.80	25.00	16.50	20.80
Fixed Asset Turnover	3.50	6.20	6.20	4.70
Total Asset Turnover	2.20	2.90	2.90	2.20



Table 7: MBJ's financial ratios

	12/31/2011	12/31/2010	12/31/2009	12/31/2008
Liquidity				
Current Ratio	.83	.77	.60	.55
Quick Ratio (Acid Test)	.44	.40	.35	.31
Net Working Capital	-34,521.53	-47,499.27	-74,816.70	-74,499.74
Cash Turnover	21.07	20.59	22.34	29.45
Activity (Asset Management)				
Inventory Turnover	9.32	9.63	14.55	17.30
Average Age of Inventory	39.15	37.91	25.08	21.10
Accounts Payable Turnover	6.68	6.54	6.50	7.46
Accounts Receivable Turnover				
Fixed Asset Turnover	5.96	5.12	4.40	4.00
Total Asset Turnover	2.76	2.63	2.52	2.55
Debt Management				
Times Interest Earned	1.60	1.13	1.24	2.89
Debt Ratio	.63	.65	.66	.66
Fixed Charge Coverage	.91	.63	.71	--
Profitability				
Return on Total Assets (%)	1.03	0.24	0.68	6.29
Return on Operating Assets (%)	7.32	5.56	7.58	16.61
Return on Total Equity (%)	2.79	0.68	2.00	18.72
Return on Common Equity (%)	2.79	0.68	2.00	18.72

Table 8: MBJ's 2012 Sales Estimates

Annual Sales	
12/31/2011	1,306,576.80
12/31/2010	1,283,245.00
12/31/2009	1,235,681.05
12/31/2008	1,249,328.55
L/T Growth	1.505%
Estimates	12/31/2012
	1,324,255.81 Regression
	1,326,236.68 Long-Term Growth Rate
	1,275,000.00 Guesstimate
	1,315,000.00 Graphical
	1,323,595.11 Forecast (Excel Function)
Variation	51,236.68
Owner Estimates if Loan Granted	
	1,437,234.48 Low
	1,502,563.32 High

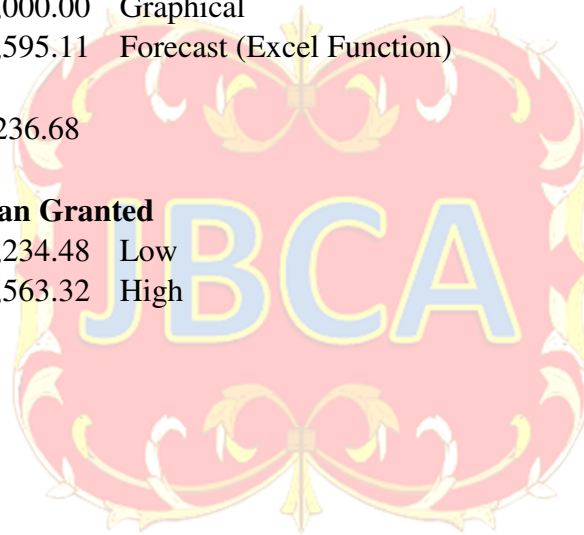


Table 9: MBJ's Pro Forma Statements

Assumptions		\$175,000.00	\$125,000.00
		Full Loan	Minimum Loan
INCOME STATEMENT		12/31/2012	12/31/2012
Net Sales		1,398,037.18	1,320,000.00
COGS	44% of Sales	615,136.36	580,800.00
Gross Profit		782,900.82	739,200.00
Advertising			
Business Promotion			
Charitable Contributions			
Total Advertising	Flat	185,148.95	185,148.95
Accounting	2.4% of Sales	33,552.89	31,680.00
Depreciation - Furn & Fix	5 yr Straight Line	28,846.60	20,246.60
Depreciation - Building	10/20 yr SL	21,063.25	17,463.25
Total Depreciation		49,909.85	37,709.85
Insurance	3.3% of Sales	46,135.23	43,560.00
Payroll	2.2% Growth	283,488.34	283,488.34
Payroll Taxes	2.2% Growth	31,467.23	31,467.23
Printing	Flat	11,798.15	11,798.15
Telephone	1.66% of Sales	23,207.42	21,912.00
Utilities	1.0% Growth	67,504.36	67,504.36
Total Operating Expenses		732,212.41	714,268.88
Operating Profit		50,688.41	24,931.12
Other Gains/Losses	25% Growth	-14,209.00	-14,209.00
Interest Expense	9% Loan	-18,227.87	-13,727.87
Profit Before Taxes		18,251.54	-3,005.74
Income Taxes (Fed. & State)	25% Tax Rate	4,562.89	-751.44
Net Income		13,688.66	-2,254.31

Table 9, continued

		\$175,000.00	\$125,000.00
	Assumptions	Full Loan	Minimum
BALANCE SHEET		12/31/2012	12/31/2012
ASSETS			
Cash	Cash Turnover 21x	66,573.20	62,857.14
Trade Receivables - Net	40% Growth	35,991.34	35,991.34
Inventory	Inventory Turnover 10x	61,513.64	58,080.00
All Other Current	Constant	15,826.90	15,826.90
Total Current		<u>179,905.07</u>	<u>172,755.38</u>
Furniture and Fixtures - Net	Old + Purchases - Depr.	6,184.65	3,284.65
Building - Net	Old + Purchases - Depr.	280,102.00	247,702.00
Land	Constant	55,370.60	55,370.60
Intangible Assets - Net	Constant	24,488.30	24,488.30
All Other Non-Current	Subjective	50,000.00	50,000.00
Due From Employees	Subjective	10,000.00	10,000.00
Total Assets		<u>606,050.62</u>	<u>563,600.93</u>
LIABILITIES			
Trade Payables	A/P Turnover 17x	36,184.49	34,164.71
Current Mat. L/T Debt	10 yr L/T Loan Payoff	31,265.92	26,265.92
Notes Payable	Consolidated with L/T Loan	0.00	0.00
Income Taxes Payable	25% of Annual Tax	1,140.72	-187.86
All Other Current	Subjective	90,000.00	90,000.00
Total Current		<u>158,591.13</u>	<u>150,242.77</u>
Long Term Debt	Per Decision	281,393.28	236,393.28
Other Non-Current Debt	Subjective	12,000.00	12,000.00
Total Liabilities		<u>451,984.41</u>	<u>398,636.05</u>
EQUITY			
Capital Stock	No Change	100,000.00	100,000.00
Retained Earnings	From Income Statement	87,452.78	71,509.82
Total Net Worth		<u>187,452.78</u>	<u>171,509.82</u>
Total Liabilities & Net Worth		<u>639,437.19</u>	<u>570,145.87</u>
Excess Resources		33,386.57	6,544.93