

Introduction to Financial Statement Analysis for the Boardroom

December 7, 2017



The Speakers



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Reading Financial Statements

Analyzing Financial Statements

Applicable Example

- **Three Primary Statements:**



- **Balance Sheet**

What is the company's current financial position?

- **Income Statement (Statement of Operations)**

What were the company's operating results for the period?

- **Cash Flow Statement**

How did the company generate and use cash during the period?

- **The Fourth Statement: Statement of Shareholders' Equity**
 - Details changes to equity over a specified period
 - retained earnings, stock, additional investments by shareholders, dividends, etc.
 - This information can be derived from both the balance sheet and income statement

- **Footnotes provide other important information**
 - Nature of the business and organization (C-corp, S-corp, etc.)
 - Accounting methods and policies (i.e., revenue recognition, inventory, leases, etc.)
 - Debt obligations
 - Business segments
 - Material lawsuits or contingent liabilities

- **Purpose**
 - To **summarize** the performance and financial position of an entity for a given period of time.
- **Reporting standards**
 - The SEC has the authority to set and enforce accounting standards to be followed by U.S. public companies
 - The Financial Accounting Standards Board (“FASB”) advises and provides input on generally accepted accounting principles (“GAAP”)
- **Reporting frequency**
 - Annually, quarterly, monthly
- **Users**
 - Internal – management, internal auditors, owners
 - External – lenders, stockholders, investors

- The Balance Sheet Equation:



- This equation **must always balance**
 - Nearly every transaction that occurs in an entity will be reflected in the Balance Sheet
 - Displays the information for a specific point in time (a specific day)

- **The Balance Sheet provides insight on two key measures:**
 - **Liquidity**
 - How fast an entity can turn its assets into cash (and therefore pay its debt and other obligations)
 - Shown in order of declining liquidity
 - **Leverage**
 - How an entity is financed (debt vs. equity)
 - Segmented between short and long-term obligations

ABC Company, Inc. Balance Sheet	
<i>In U.S. Dollars</i>	<u>12/31/2016</u>
1 Cash and Cash Equivalents	\$ 11,240
2 Accounts Receivable	10,500
3 Inventory	14,500
4 Prepaid Expenses and Other	500
5 Total Current Assets	<u>36,740</u>
6 Gross Property and Equipment	32,000
7 Accumulated Depreciation	(9,500)
8 Net Property and Equipment	<u>22,500</u>
9 Other Long-Term Assets	150
10 Goodwill and Intangible Assets	15,000
11 Total Assets	<u>\$ 74,390</u>
12 Accounts Payable	\$ 6,000
13 Accrued Expenses	2,500
14 Short-Term Debt	500
15 Total Current Liabilities	<u>9,000</u>
16 Long-Term Debt	4,000
17 Other Long-Term Liabilities	250
18 Total Long-Term Liabilities	<u>4,250</u>
19 Total Liabilities	13,250
20 Total Stockholders' Equity	<u>61,140</u>
21 Total Liabilities & Stockholders' Equity	<u>\$ 74,390</u>

**Both sides
must balance**



- Shows accounts only at a single point in time
- Reflects assets at their historical cost basis
- Omits certain assets and liabilities
- Deviates from market value

- **The Income Statement Equation:**



- **Presents the results of an entity's operating activities**
- **Displays sources of revenues and costs during the specific time period**
- **Shows how profitably (or not) a company is able to convert its inputs to saleable outputs**

ABC Company, Inc.	
Income Statement	
<i>In U.S. Dollars</i>	<u>12/31/2016</u>
1 Total Net Sales	\$ 200,000
2 Cost of Goods Sold	110,000
3 Gross Profit	<u>90,000</u>
4 Operating Expenses	
5 Selling and Marketing	23,500
6 General and Administrative	17,500
7 Other	7,500
8 EBITDA	<u>41,500</u>
9 Depreciation	4,500
10 Amortization	1,000
11 EBIT	<u>36,000</u>
12 Interest Expense / (Income), Net	350
13 Pretax Income	<u>35,650</u>
14 Income Taxes	14,260
15 Net Income	<u><u>\$ 21,390</u></u>

- **Impacted by selected accounting policies**
 - Inventory recognition
 - Depreciation and amortization periods

- **Impacted by asset ownership**
 - Owned vs. leased properties

- **Impacted by business model**
 - One-time sale vs. on-going subscription

- **Income can be materially different from cash**

- Demonstrates an entity's ability to generate future cash flow and pay returns to its lenders (via debt service) and owners (via dividends)
- Three types of cash flow activities:



- **Operating** – Enters into the determination of net income
- **Investing** – Relates to the purchase/sale of assets
- **Financing** – Shows capital structure flows

	Operating	Investing	Financing
Inflows	<ul style="list-style-type: none"> - Collecting receivables - Realization of prepaid assets 	<ul style="list-style-type: none"> - Sale of capital assets - Repayments received on loans made 	<ul style="list-style-type: none"> - Debt borrowings - Stock sales



Cash Pool



	Operating	Investing	Financing
Outflows	<ul style="list-style-type: none"> - Inventory purchases - Payments to suppliers 	<ul style="list-style-type: none"> - Purchase of capital assets - Making a loan 	<ul style="list-style-type: none"> - Principal payments - Shareholder dividends

Sample Statement of Cash Flows



ABC Company, Inc.	
Cash Flow Statement	
<i>In U.S. Dollars</i>	<u>12/31/2016</u>
1 Net Income (Loss)	\$ 21,390
2 Depreciation and Amortization	5,500
3 Change in Accounts Receivable	(2,000)
4 Change in Inventory	(4,500)
5 Change in Prepaid Expenses and Other	100
6 Change in Other Long-Term Assets	(150)
7 Change in Accounts Payable	1,000
8 Change in Accrued Expenses	(500)
9 Change in Other Long-Term Liabilities	150
10 Net Change in Operating Activities	<u>20,990</u>
11 Purchases of Marketable Securities	0
12 Sale of Property, Plant, and Equipment	0
13 Purchases of Property, Plant, and Equipment	(9,000)
14 Net Change in Investing Activities	<u>(9,000)</u>
15 Proceeds from Borrowings	0
16 Principal Payments on Interest-Bearing Debt	(250)
17 Dividends	(5,000)
18 Net Change in Financing Activities	<u>(5,250)</u>
19 Net Change in Cash and Cash Equivalents	6,740
20 Cash and Cash Equivalents at Beginning of Year	4,500
21 Cash and Cash Equivalents at End of Year	<u>\$ 11,240</u>

- **Income Statement**

- Net income appears in the form of retained earnings on the balance sheet and is also the first line on the operations section in the statement of cash flows

- **Balance Sheet**

- Ensures the balances of all accounts across all the financial statements
- Retained earnings is derived from the income statement, that is made up of net income

- **Cash Flow Statement**

- Net Income is the first line stated in the Operating Cash Flows section
- Ending cash balance flows to the cash account in the Balance Sheet

Tying the Three Statements Together – Step 1



ABC Company, Inc. Income Statement	
<i>In U.S. Dollars</i>	<u>12/31/2016</u>
1 Total Net Sales	\$ 200,000
2 Costs and Expenses	164,350
3 Taxes	14,260
4 Net Income	<u><u>\$ 21,390</u></u>

ABC Company, Inc.				
Changes in Balance Sheet Accounts				
<i>In U.S. Dollars</i>	<u>12/31/2016</u>	<u>12/31/2015</u>	<u>Change</u>	<u>CF Stmt</u>
1 Accounts Receivable	\$ 10,500	\$ 8,500	\$ 2,000	Operating
2 Inventory	14,500	10,000	4,500	Operating
3 Prepaid Expenses and Other	500	600	(100)	Operating
4 Gross Property and Equipment	32,000	23,000	9,000	Investing
5 Accumulated Depreciation	(9,500)	(5,000)	(4,500)	Operating
6 Other Long-Term Assets	150	0	150	Operating
7 Goodwill and Intangible Assets	15,000	16,000	(1,000)	Operating
8 Accounts Payable	6,000	5,000	1,000	Operating
9 Accrued Expenses	2,500	3,000	(500)	Operating
10 Short-Term Debt	500	550	(50)	Financing
11 Long-Term Debt	4,000	4,200	(200)	Financing
12 Other Long-Term Liabilities	250	100	150	Operating

“Missing” Accounts:

- Cash and Cash Equivalents
- Total Stockholders’ Equity

Tying the Three Statements Together – Step 2b



ABC Company, Inc. Cash Flow Statement

<i>In U.S. Dollars</i>	<u>12/31/2016</u>
1 Net Income (Loss)	\$ 21,390
2 Depreciation and Amortization	5,500
3 Change in Accounts Receivable	(2,000)
4 Change in Inventory	(4,500)
5 Change in Prepaid Expenses and Other	100
6 Change in Other Long-Term Assets	(150)
7 Change in Accounts Payable	1,000
8 Change in Accrued Expenses	(500)
9 Change in Other Long-Term Liabilities	150
10 Net Change in Operating Activities	<u>20,990</u>
11 Purchases of Marketable Securities	0
12 Sale of Property, Plant, and Equipment	0
13 Purchases of Property, Plant, and Equipment	(9,000)
14 Net Change in Investing Activities	<u>(9,000)</u>
15 Proceeds from Borrowings	0
16 Principal Payments on Interest-Bearing Debt	(250)
17 Dividends	(5,000)
18 Net Change in Financing Activities	<u>(5,250)</u>
19 Net Change in Cash and Cash Equivalents	6,740
20 Cash and Cash Equivalents at Beginning of Year	<u>4,500</u>
21 Cash and Cash Equivalents at End of Year	\$ 11,240

Net Income (Loss)	\$ 21,390
Total Cash Inflows	6,750
Total Cash Outflows	(21,400)
Net Change in Cash	<u><u>\$ 6,740</u></u>



Tying the Three Statements Together – Step 3



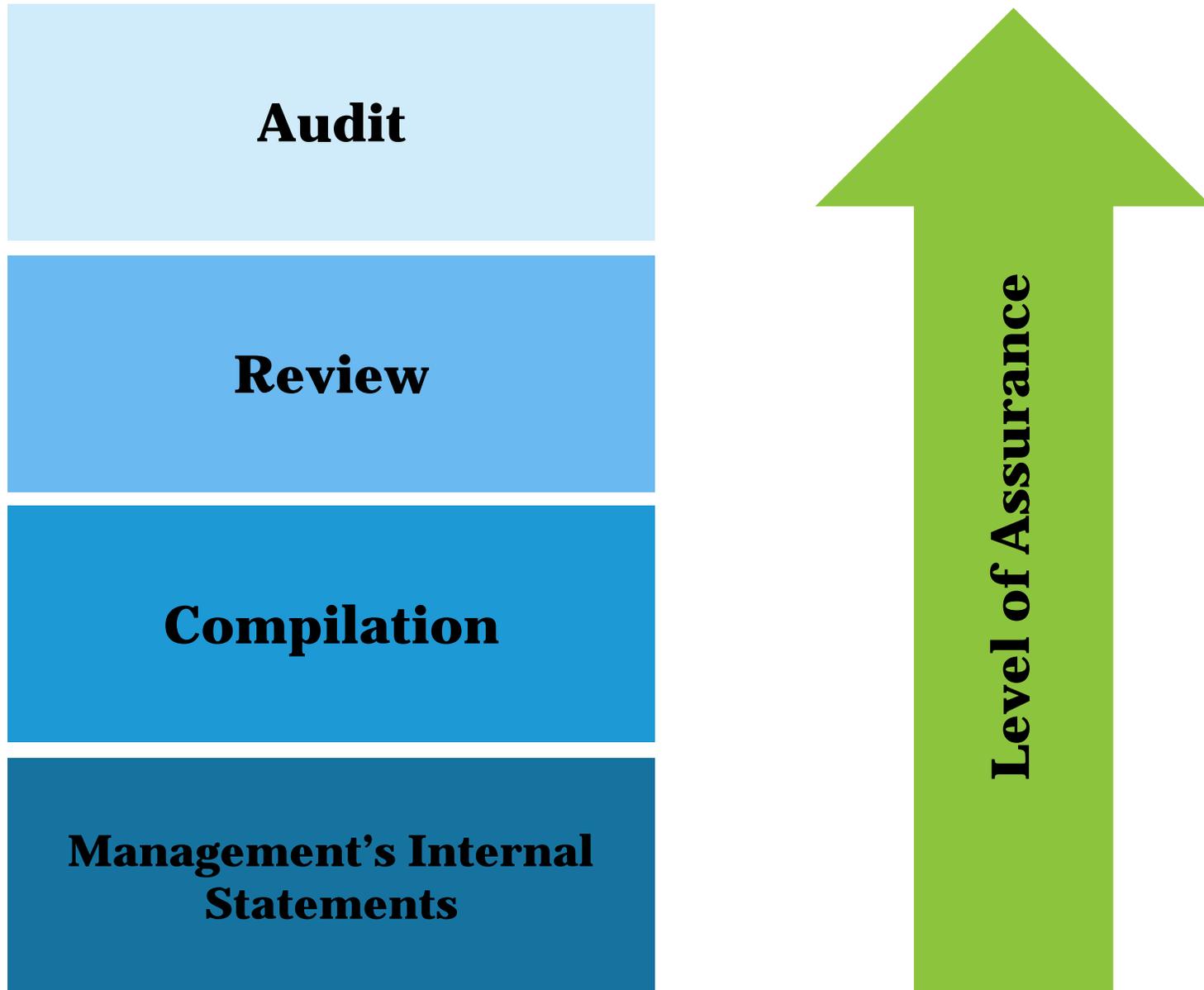
ABC Company, Inc.			
Changes in Balance Sheet Accounts			
<i>In U.S. Dollars</i>	<u>12/31/2016</u>	<u>12/31/2015</u>	<u>Change</u>
1 Cash and Cash Equivalents	\$ 11,240	\$ 4,500	\$ 6,740
2 Total Stockholders' Equity	61,140	44,750	16,390

Net Income (Loss)	\$ 21,390
Total Cash Inflows	6,750
Total Cash Outflows	(21,400)
Net Change in Cash	<u>\$ 6,740</u>

Net Income	\$ 21,390
Less: Dividends	(5,000)
Change in Total Stockholders' Equity	<u>\$ 16,390</u>

- Interim vs. year-end
- Public vs. private company
- Cash basis vs. accrual basis
- Internal vs. external

- **Internally-Prepared**
 - Management uses for periodic review of the operations of the company; May also be provided to investors or lenders
 - No requirements on the format or content of the statements
 - Examples include monthly financial statements, location-specific or product line financial statements, and prospective financial statements
- **Externally-Prepared**
 - Generally prepared in compliance with GAAP or other basis of accounting
 - Compiled, reviewed, or audited statements



Report of Independent Auditors

To the Board of Directors
ABC Company, Inc.

We have audited the accompanying consolidated balance sheets of ABC Company, Inc. as of December 31, 2015 and 2016, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of ABC Company, Inc. at December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Reading Financial Statements

Analyzing Financial Statements

Applicable Example

- **Vertical Analysis**
 - Measuring relationships between items within the statement
 - Expressed as percentages
 - **Income Statement:** Relationship of line item to Net Sales
 - **Balance Sheet:** Relationship of line item to Total Assets, or to Total Liabilities and Stockholder’s Equity

ABC Company, Inc. Reported Income Statements		
<i>In U.S. Dollars</i>	For the Fiscal Year Ended 12/31/2016	
		%
1 Total Net Sales	\$ 2,500,000	100.0%
2 Growth Rate	25.0%	
3 Total Cost of Sales	<u>1,700,000</u>	68.0%
4 Gross Profit	800,000	32.0%
5 S,G&A Expenses	293,000	11.7%
6 Depreciation	<u>58,000</u>	2.3%
7 Total S,G&A Expenses	<u>351,000</u>	14.0%
8 Operating Income	449,000	18.0%
9 Other Income (Expense)	<u>50,000</u>	2.0%
10 EBIT	499,000	20.0%
11 Interest Expenses	<u>(20,000)</u>	-0.8%
12 Earnings Before Taxes	479,000	19.2%
13 Income Tax Expense	<u>0</u>	0.0%
14 Net Income	<u>\$ 479,000</u>	19.2%

■ Horizontal Analysis

- Same items on comparative statements over two or more periods
- Describes changes over time
 - **Sales**
 - **Gross Profit:** Net Sales – Cost of Goods Sold
 - **Net Income:** Net Sales – All Costs and Expenses
 - **EBITDA:** Net Sales – All Costs + Interest Expense + Income Taxes + Depreciation + Amortization

ABC Company, Inc. Reported Income Statements											
<i>In U.S. Dollars</i>		For the Fiscal Year Ended									
		12/31/2012		12/31/2013		12/31/2014		12/31/2015		12/31/2016	
			%		%		%		%		%
1	Total Net Sales	\$ 975,000	100.0%	\$ 1,000,000	100.0%	\$ 1,500,000	100.0%	\$ 2,000,000	100.0%	\$ 2,500,000	100.0%
2	<i>Growth Rate</i>	<i>n/a</i>		2.6%		50.0%		33.3%		25.0%	

Basic Financial Statement Analysis – Vertical and Horizontal



ABC Company, Inc.										
Reported Income Statements										
<i>In U.S. Dollars</i>	For the Fiscal Year Ended									
	12/31/2012	%	12/31/2013	%	12/31/2014	%	12/31/2015	%	12/31/2016	%
1 Total Net Sales	\$ 975,000	100.0%	\$ 1,000,000	100.0%	\$ 1,500,000	100.0%	\$ 2,000,000	100.0%	\$ 2,500,000	100.0%
2 Growth Rate	<i>n/a</i>		<i>2.6%</i>		<i>50.0%</i>		<i>33.3%</i>		<i>25.0%</i>	
3 Total Cost of Sales	<u>467,000</u>	47.9%	<u>500,000</u>	50.0%	<u>1,005,000</u>	67.0%	<u>1,300,000</u>	65.0%	<u>1,700,000</u>	68.0%
4 Gross Profit	508,000	52.1%	500,000	50.0%	495,000	33.0%	700,000	35.0%	800,000	32.0%
5 S,G&A Expenses	166,000	17.0%	180,000	18.0%	224,000	14.9%	256,000	12.8%	293,000	11.7%
6 Depreciation	<u>20,000</u>	2.0%	<u>20,000</u>	2.0%	<u>32,000</u>	2.1%	<u>44,000</u>	2.2%	<u>58,000</u>	2.3%
7 Total S,G&A Expenses	<u>186,000</u>	19.1%	<u>200,000</u>	20.0%	<u>256,000</u>	17.1%	<u>300,000</u>	15.0%	<u>351,000</u>	14.0%
8 Operating Income	322,000	33.0%	300,000	30.0%	239,000	15.9%	400,000	20.0%	449,000	18.0%
9 Other Income (Expense)	<u>12,000</u>	1.2%	<u>14,000</u>	1.4%	<u>24,000</u>	1.6%	<u>36,000</u>	1.8%	<u>50,000</u>	2.0%
10 EBIT	334,000	34.3%	314,000	31.4%	263,000	17.5%	436,000	21.8%	499,000	20.0%
11 Interest Expenses	<u>(20,000)</u>	-2.1%	<u>(20,000)</u>	-2.0%	<u>(20,000)</u>	-1.3%	<u>(20,000)</u>	-1.0%	<u>(20,000)</u>	-0.8%
12 Earnings Before Taxes	314,000	32.2%	294,000	29.4%	243,000	16.2%	416,000	20.8%	479,000	19.2%
13 Income Tax Expense	<u>0</u>	0.0%	<u>0</u>	0.0%	<u>0</u>	0.0%	<u>0</u>	0.0%	<u>0</u>	0.0%
14 Net Income	<u>\$ 314,000</u>	32.2%	<u>\$ 294,000</u>	29.4%	<u>\$ 243,000</u>	16.2%	<u>\$ 416,000</u>	20.8%	<u>\$ 479,000</u>	19.2%

- **Common Financial Ratios**
 - **Liquidity**
 - **Current: Current Assets/Current Liabilities**
 - Measures a company's ability to meet present obligations
 - **Leverage**
 - **Debt ratio: Total Liabilities/Total Assets**
 - Provides information about protection of creditors from insolvency and ability to obtain additional financing
 - **Profitability**
 - **Return on Assets: Net Income/Average Total Assets**
 - Measures the company's return on investment or income derived based on assets available

- **Compare to benchmarks:**
 - Industry standards
 - Prior operating years
 - Management goals
 - Competition
 - Lending agreements

Reading Financial Statements

Analyzing Financial Statements

Applicable Example

Key Financials

Exhibit A.1

In Millions of USD, except per share items.

For the Fiscal Period Ending	12 months Jan-30-2010A	12 months Jan-29-2011A	12 months Jan-28-2012A	12 months Feb-02-2013A	12 months Feb-01-2014A	12 months Jan-31-2015A	Press Release 12 months Jan-30-2016A
Currency	USD						
Total Revenue	902.4	775.9	759.1	784.7	797.8	826.8	800.9
Growth Over Prior Year	(28.1%)	(14.0%)	(2.2%)	3.4%	1.7%	3.6%	(3.1%)
Gross Profit	373.5	308.1	297.9	326.3	333.2	360.2	343.5
Margin %	41.4%	39.7%	39.2%	41.6%	41.8%	43.6%	42.9%
EBITDA	28.4	(10.4)	(24.5)	(5.6)	3.3	8.2	0.7
Margin %	3.1%	(1.3%)	(3.2%)	(0.7%)	0.4%	1.0%	0.1%
EBIT	(42.0)	(66.0)	(62.0)	(33.2)	(18.2)	(11.8)	(16.1)
Margin %	(4.7%)	(8.5%)	(8.2%)	(4.2%)	(2.3%)	(1.4%)	(2.0%)
Earnings from Cont. Ops.	(45.6)	(78.8)	(81.2)	(52.6)	(47.0)	(29.4)	(8.5)
Margin %	(5.1%)	(10.2%)	(10.7%)	(6.7%)	(5.9%)	(3.6%)	(1.1%)
Net Income	(70.3)	(96.6)	(106.4)	(52.1)	(48.7)	(29.4)	(8.5)
Margin %	(7.8%)	(12.5%)	(14.0%)	(6.6%)	(6.1%)	(3.6%)	(1.1%)
Diluted EPS Excl. Extra Items³	(0.7)	(1.19)	(1.22)	(0.78)	(0.69)	(0.42)	(0.12)
Growth Over Prior Year	NM						
Same Store Sales Growth %	(19.1%)	(7.6%)	NA	2.0%	2.0%	3.0%	NA

Source: Capital IQ, Inc.

- Top line growth has been modest for 3 years prior to 2016
- Gross profit margin was reasonably steady to improving for 3 years prior to 2016
- EBITDA had been negative in 2010-2013 with modest improvement in 2014-2015
- Consistently negative earnings 2010-2016

Apparel Retailer – Income Statement



Income Statement

Exhibit A.2

In Millions of USD, except per share items.

For the Fiscal Period Ending	Reclassified 12 months Jan-30-2010	Reclassified 12 months Jan-29-2011	Reclassified 12 months Jan-28-2012	Reclassified 12 months Feb-02-2013	Reclassified 12 months Feb-01-2014	Reclassified 12 months Jan-31-2015	Press Release 12 months Jan-30-2016
Currency	USD						
Revenue	902.4	775.9	759.1	784.7	797.8	826.8	800.9
Other Revenue	-	-	-	-	-	-	-
Total Revenue	902.4	775.9	759.1	784.7	797.8	826.8	800.9
Cost Of Goods Sold	528.9	467.8	461.3	458.4	464.5	466.5	457.4
Gross Profit	373.5	308.1	297.9	326.3	333.2	360.2	343.5
Selling General & Admin Exp.	362.5	330.1	323.8	359.6	351.5	372.1	359.6
R & D Exp.	-	-	-	-	-	-	-
Depreciation & Amort.	53.0	44.0	36.0	-	-	-	-
Other Operating Expense/(Income)	-	-	-	-	-	-	-
Other Operating Exp., Total	415.5	374.1	359.8	359.6	351.5	372.1	359.6
Operating Income	(42.0)	(66.0)	(62.0)	(33.2)	(18.2)	(11.8)	(16.1)
Interest Expense	-	(0.9)	(4.4)	(13.3)	(14.1)	(15.8)	(17.3)
Interest and Invest. Income	-	-	-	-	-	-	-
Net Interest Exp.	-	(0.9)	(4.4)	(13.3)	(14.1)	(15.8)	(17.3)
Other Non-Operating Inc. (Exp.)	(0.3)	-	(5.0)	0	(10.6)	2.3	27.7
EBT Excl. Unusual Items	(42.2)	(67.0)	(71.4)	(46.6)	(43.0)	(25.3)	(5.6)
Impairment of Goodwill	-	-	-	-	-	-	-
Asset Writedown	(14.5)	(10.8)	(8.7)	(5.2)	(3.2)	(3.3)	(1.9)
Other Unusual Items	-	-	-	-	-	-	-
EBT Incl. Unusual Items	(56.7)	(77.7)	(80.1)	(51.7)	(46.2)	(28.6)	(7.6)
Income Tax Expense	(11.1)	1.1	1.1	0.8	0.8	0.7	0.9
Earnings from Cont. Ops.	(45.6)	(78.8)	(81.2)	(52.6)	(47.0)	(29.4)	(8.5)
Earnings of Discontinued Ops.	(24.7)	(17.8)	(25.3)	0.5	(1.7)	-	-
Extraord. Item & Account. Change	-	-	-	-	-	-	-
Net Income to Company	(70.3)	(96.6)	(106.4)	(52.1)	(48.7)	(29.4)	(8.5)
Minority Int. in Earnings	-	-	-	-	-	-	-
Net Income	(70.3)	(96.6)	(106.4)	(52.1)	(48.7)	(29.4)	(8.5)

Source: Capital IQ, Inc.

SG&A exceeded gross profit 2011-2016

- With no apparent attempt to right-size SG&A

Apparel Retailer – Industry Specific



Industry Specific

Exhibit A.3

In Millions of USD, except per share items.

For the Fiscal Period Ending	12 months Jan-30-2010	12 months Jan-29-2011	12 months Jan-28-2012	12 months Feb-02-2013	12 months Feb-01-2014	12 months Jan-31-2015	Press Release 12 months Jan-30-2016
Currency	USD						
Retail Specific Data							
Stores Closed	40	44	119	92	30	18	15
Total Stores	894	852	613	615	618	605	601
Total Same Store Sales Growth	(19.1%)	(7.6%)	-	2.0%	2.0%	3.0%	-
Gross Margin	25.3%	22.6%	22.0%	25.0%	25.0%	27.0%	-
Operating Margin	(6.3%)	(9.9%)	(9.3%)	(4.9%)	(2.7%)	(1.8%)	-
Merchandise Margin	48.8%	47.4%	46.7%	48.9%	49.1%	50.8%	-
Retail Revenues	902.4	775.9	759.1	784.7	797.8	826.8	800.9
Total Retail Sq. Ft. (Gross)	-	-	-	-	-	2,400,000	-
Sales/Sq. Ft., Comparable (Gross)	\$297.0	\$284.0	\$289.0	\$298.0	\$302.0	\$310.0	-
Growth in Avg. Value Per Transaction	-	-	-	-	1.0%	8.0%	-
Owned / Operated Store Data							
Owned/Operated Stores Closed	40	44	119	92	30	18	15
Total Owned/Operated Stores	894	852	613	615	618	605	601
Owned/Operated Same Store Sales Growth	(19.1%)	(7.6%)	-	2.0%	2.0%	3.0%	-

Source: Capital IQ, Inc.

Number of closed stores peaked in 2012

Number of total stores stayed essentially flat 2012-2016

Sales/Sq. Ft. had been improving since 2011

Apparel Retailer – Balance Sheet



Balance Sheet

Exhibit A.4

In Millions of USD, except per share items.

Balance Sheet as of:	Jan-30-2010	Jan-29-2011	Jan-28-2012	Reclassified Feb-02-2013	Feb-01-2014	Jan-31-2015	Press Release Jan-30-2016
Currency	USD	USD	USD	USD	USD	USD	USD
ASSETS							
Cash And Equivalents	93.1	63.7	50.3	48.7	27.8	22.6	6.2
Total Cash & ST Investments	93.1	63.7	50.3	48.7	27.8	22.6	6.2
Accounts Receivable	-	-	-	-	-	-	-
Total Receivables	-	-	-	-	-	-	-
Inventory	89.7	95.7	88.7	90.7	83.1	81.7	96.5
Prepaid Exp.	10.8	11.7	15.5	12.8	13.4	12.7	12.4
Restricted Cash	-	-	8.6	-	-	-	-
Other Current Assets	5.4	4.8	6.3	2.9	6.1	4.0	5.0
Total Current Assets	198.9	175.9	169.4	155.1	130.3	120.9	120.1
Gross Property, Plant & Equipment	641.1	619.5	566.1	481.6	473.0	467.8	461.3
Accumulated Depreciation	(392.1)	(426.3)	(416.3)	(370.9)	(376.2)	(379.1)	(376.0)
Net Property, Plant & Equipment	249.0	193.2	149.7	110.7	96.8	88.8	85.3
Long-term Investments	-	-	23.0	23.0	23.0	23.0	23.0
Other Intangibles	-	-	-	14.1	13.0	11.1	10.5
Deferred Tax Assets, LT	4.0	6.2	6.6	6.2	6.2	6.0	3.3
Other Long-Term Assets	25.3	26.0	6.4	4.6	3.4	2.5	1.1
Total Assets	477.2	401.3	355.1	313.8	272.6	252.3	243.3
LIABILITIES							
Accounts Payable	38.5	41.0	38.9	50.0	46.0	36.8	43.3
Accrued Exp.	16.8	14.2	14.7	15.6	9.4	16.2	13.4
Short-term Borrowings	-	-	-	-	-	-	18.0
Curr. Port. of LT Debt	-	-	-	-	-	0.5	77.4
Curr. Port. of Cap. Leases	-	-	-	-	-	1.0	-
Unearned Revenue, Current	12.6	12.0	10.8	9.5	9.0	8.9	9.1
Def. Tax Liability, Curr.	-	2.1	2.2	-	-	-	-
Other Current Liabilities	14.3	13.8	40.7	38.5	49.6	49.9	17.9
Total Current Liabilities	82.2	83.2	107.3	113.6	114.0	113.4	179.1
Long-Term Debt	-	29.1	73.9	79.6	86.1	94.4	26.8
Capital Leases	-	-	-	-	-	1.0	-
Pension & Other Post-Retire. Benefits	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Other Non-Current Liabilities	86.3	72.6	58.8	54.2	52.4	50.9	50.9
Total Liabilities	170.5	186.9	242.0	249.5	254.5	261.7	258.9
Common Stock	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Additional Paid In Capital	7.3	11.6	16.8	20.1	22.6	24.4	26.7
Retained Earnings	298.7	202.1	95.7	43.6	(5.1)	(34.5)	(43.0)
Treasury Stock	-	-	-	-	-	-	-
Comprehensive Inc. and Other	-	-	-	-	-	-	-
Total Common Equity	306.7	214.3	113.1	64.4	18.1	(9.4)	(15.5)
Total Equity	306.7	214.3	113.1	64.4	18.1	(9.4)	(15.5)
Total Liabilities And Equity	477.2	401.3	355.1	313.8	272.6	252.3	243.3

Cash is dwindling over time

Total debt = \$122.2 M (up from \$0)

While debt climbs

Source: Capital IQ, Inc.

Apparel Retailer – Cash Flow



Statement of Cash Flow

Exhibit A.5

In Millions of USD, except per share items.

For the Fiscal Period Ending	Reclassified	Reclassified	Reclassified	Reclassified	12 months	12 months	Press Release
	12 months	12 months	12 months	12 months	12 months	12 months	12 months
Currency	Jan-30-2010	Jan-29-2011	Jan-28-2012	Feb-02-2013	Feb-01-2014	Jan-31-2015	Jan-30-2016
	USD	USD	USD	USD	USD	USD	USD
Net Income	(70.3)	(96.6)	(106.4)	(52.1)	(48.7)	(29.4)	(8.5)
Depreciation & Amort.	70.4	55.6	37.5	27.6	21.5	20.0	16.7
Depreciation & Amort., Total	70.4	55.6	37.5	27.6	21.5	20.0	16.7
Other Amortization	-	-	5.0	7.5	6.2	7.0	8.0
(Gain) Loss From Sale Of Assets	1.0	0.9	0.2	0.3	0.2	0.3	0.1
Asset Writedown & Restructuring Costs	14.5	10.8	8.7	5.2	3.2	3.3	1.9
Stock-Based Compensation	6.4	4.0	3.2	2.8	2.6	1.6	2.6
Tax Benefit from Stock Options	(2.0)	-	-	-	-	-	-
Net Cash From Discontinued Ops.	12.5	4.8	6.1	0.2	0.0	-	-
Other Operating Activities	-	-	14.4	(0.3)	10.4	(2.5)	(27.7)
Change In Inventories	17.5	(6.3)	7.0	(1.9)	7.6	1.4	(14.9)
Change in Acc. Payable	(6.8)	2.5	(16.3)	11.1	(4.0)	(9.3)	6.6
Change in Other Net Operating Assets	44.3	(16.6)	(6.7)	6.0	(6.7)	18.2	0
Cash from Ops.	87.5	(40.9)	(47.4)	6.4	(7.7)	10.7	(15.1)
Capital Expenditure	(23.5)	(17.2)	(13.2)	(15.4)	(12.3)	(15.6)	(17.6)
CFO less Capital Expenditure	64.0	(58.1)	(60.6)	(9.0)	(20.0)	(4.9)	(32.7)
Sale of Property, Plant, and Equipment	3.7	-	-	-	-	-	-
Cash Acquisitions	-	-	-	-	-	-	-
Divestitures	-	-	-	-	-	-	-
Invest. in Marketable & Equity Secur.	-	-	-	-	-	-	-
Net (Inc.) Dec. in Loans Originated/Sold	-	-	-	-	-	-	-
Other Investing Activities	-	-	(8.3)	9.2	-	-	-
Cash from Investing	(19.8)	(17.2)	(21.5)	(6.1)	(12.3)	(15.6)	(17.6)
Short Term Debt Issued	-	-	-	-	-	-	85.0
Long-Term Debt Issued	-	29.8	81.3	-	-	15.6	-
Total Debt Issued	-	29.8	81.3	-	-	15.6	85.0
Short Term Debt Repaid	-	-	-	-	-	-	(67.0)
Long-Term Debt Repaid	(0.1)	(0.5)	(20.9)	(2.4)	(1.1)	(16.2)	(1.4)
Total Debt Repaid	(0.1)	(0.5)	(20.9)	(2.4)	(1.1)	(16.2)	(68.4)
Issuance of Common Stock	0.7	0.5	0.5	0.6	0.2	0.4	0.3
Total Dividends Paid	-	-	-	-	-	-	-
Special Dividend Paid	-	-	-	-	-	-	-
Other Financing Activities	-	(1.2)	(5.3)	-	-	(0.1)	(0.6)
Cash from Financing	0.6	28.7	55.5	(1.9)	(0.9)	(0.3)	16.4
Net Change in Cash	68.3	(29.4)	(13.4)	(1.6)	(21.0)	(5.2)	(16.4)

Source: Capital IQ, Inc.

CFO fluctuated between marginal and negative 2011-2016

CFO less capital expenditures was consistently negative 2011-2016

Apparel Retailer – Ratios



Ratios

Exhibit A.6

In Millions of USD, except per share items.

For the Fiscal Period Ending	12 months Jan-30-2010	12 months Jan-29-2011	12 months Jan-28-2012	12 months Feb-02-2013	12 months Feb-01-2014	12 months Jan-31-2015	Press Release 12 months Jan-30-2016
Profitability							
Return on Assets %	(5.0%)	(9.4%)	(10.2%)	(6.2%)	(3.9%)	(2.8%)	(4.1%)
Return on Capital %	(7.7%)	(15.0%)	(18.0%)	(12.5%)	(9.2%)	(7.7%)	(10.3%)
Return on Equity %	(13.4%)	(30.2%)	(49.6%)	(59.3%)	(113.9%)	(672.4%)	NM
Return on Common Equity %	(13.4%)	(30.2%)	(49.6%)	(59.3%)	(113.9%)	(672.4%)	NM
Margin Analysis							
Gross Margin %	41.4%	39.7%	39.2%	41.6%	41.8%	43.6%	42.9%
SG&A Margin %	40.2%	42.5%	42.7%	45.8%	44.1%	45.0%	44.9%
EBITDA Margin %	3.1%	(1.3%)	(3.2%)	(0.7%)	0.4%	1.0%	0.1%
EBITA Margin %	(4.7%)	(8.5%)	(8.2%)	(4.2%)	(2.3%)	(1.4%)	(2.0%)
EBIT Margin %	(4.7%)	(8.5%)	(8.2%)	(4.2%)	(2.3%)	(1.4%)	(2.0%)
Earnings from Cont. Ops Margin %	(5.1%)	(10.2%)	(10.7%)	(6.7%)	(5.9%)	(3.6%)	(1.1%)
Net Income Margin %	(7.8%)	(12.5%)	(14.0%)	(6.6%)	(6.1%)	(3.6%)	(1.1%)
Net Income Avail. for Common Margin %	(5.1%)	(10.2%)	(10.7%)	(6.7%)	(5.9%)	(3.6%)	(1.1%)
Normalized Net Income Margin %	(2.9%)	(5.4%)	(5.9%)	(3.7%)	(3.4%)	(1.9%)	(0.4%)
Levered Free Cash Flow Margin %	8.5%	(0.6%)	1.1%	1.6%	0.3%	(0.3%)	(6.8%)
Unlevered Free Cash Flow Margin %	8.5%	(0.5%)	1.4%	2.5%	1.1%	0.6%	(6.0%)
Asset Turnover							
Total Asset Turnover	1.7x	1.8x	2.0x	2.3x	2.7x	3.2x	3.2x
Fixed Asset Turnover	3.2x	3.5x	4.4x	6.0x	7.7x	8.9x	9.2x
Accounts Receivable Turnover	NA						
Inventory Turnover	5.4x	5.0x	5.0x	5.1x	5.3x	5.7x	5.1x
Short Term Liquidity							
Current Ratio	2.4x	2.1x	1.6x	1.4x	1.1x	1.1x	0.7x
Quick Ratio	1.1x	0.8x	0.5x	0.4x	0.2x	0.2x	0.0x
Cash from Ops. to Curr. Liab.	1.1x	NM	NM	0.1x	NM	0.1x	NM
Avg. Days Sales Out.	NA						
Avg. Days Inventory Out.	67.7	72.1	72.8	72.6	68.1	64.3	70.9
Avg. Days Payable Out.	29.8	30.5	32.0	35.8	38.2	32.4	30.9
Avg. Cash Conversion Cycle	NA						
Long Term Solvency							
Total Debt/Equity	NA	13.6%	65.4%	123.6%	474.3%	NM	NM
Total Debt/Capital	NA	12.0%	39.5%	55.3%	82.6%	110.8%	114.5%
LT Debt/Equity	NA	13.6%	65.4%	123.6%	474.3%	NM	NM
LT Debt/Capital	NA	12.0%	39.5%	55.3%	82.6%	109.0%	25.1%
Total Liabilities/Total Assets	35.7%	46.6%	68.2%	79.5%	93.3%	103.7%	106.4%

Source: Capital IQ, Inc.

Current ratio was deteriorating as liquidity dried up

- **Results**

- The Apparel Retailer filed for bankruptcy in April 2016, after continuously negative earnings reported every quarter since 2008.

- **Observations**

- Despite reporting flat to increasing sales and gross profit, the Company's SG&A expenses consistently exceeded its gross profit, resulting in negative operating income for each operating period.
- Cash flow from operations less capital expenditures was also consistently negative.
- Debt ratios and liquidity measures showed that liquidity was drying up over time.
- Why didn't the Company right size SG&A, rationalize capital expenditures and close more stores?



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Marc C. Asbra is a Managing Director in the Valuation Advisory group. He has a broad range of experience in valuation and financial consulting assignments, including M&A and strategic planning analyses. He has provided valuations regarding financial reporting matters including purchase price allocations, goodwill impairment testing, employee stock option plans, corporate tax matters, gift and estate tax planning, collateral lending, and litigation related matters. He has also provided valuation advisory services to public and private companies, boards of directors, and other fiduciaries in connection with strategic planning and other merger & acquisition related initiatives.

Ms. Asbra has over 20 years of experience in the valuation of businesses, securities, and intangible assets for corporate tax, financial reporting, and other purposes.

Prior to joining Stout, Ms. Asbra was a Director at Houlihan Lokey. Previously, he was a senior manager in the Los Angeles office of Ernst & Young's corporate finance practice where he conducted valuations of public and private securities, closely held companies, and intangible assets, with particular emphasis on technology companies.

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Christina E. Carroll is a Managing Director in the Valuation Advisory group where her responsibilities include providing valuation and transaction related advice. For more than 20 years, Ms. Carroll has been a Board and C-suite advisor on complex transactions and strategic issues with a focus on evaluating transactions and assisting her clients in enhancing shareholder value.

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Professional Memberships

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Thank you! Questions?



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