
Report prepared for: DeWitt Construction**Industry:** 236115 - New Single-Family Housing Construction (Except Operative Builders)**Periods:** 12 months against the same 12 months from the previous year

LIQUIDITY**PROFITS & PROFIT MARGIN****SALES****BORROWING****ASSETS****EMPLOYEES**

LIQUIDITY

Generally, what is the company's ability to meet obligations as they come due?**Operating Cash Flow Results**

Cash flow from operations is reasonable for the period, but not terrific. Profits are also adequate. Since overall liquidity conditions are less than great (as will be discussed below), it is good to know how cash is coming into and going out of the company, since it seems like the company may need to keep liquid assets on its Balance Sheet in the future. Look for ways to unleash cash through better working capital management.

General Liquidity Conditions

Even though **sales have improved** this period, the firm's liquidity is still poor. In fact, there are fewer cash and near-cash assets relative to short-term obligations than last period, which is clearly not good. Moreover, as evidenced by the quick ratio, there generally are not sufficient resources invested in the top liquid accounts.

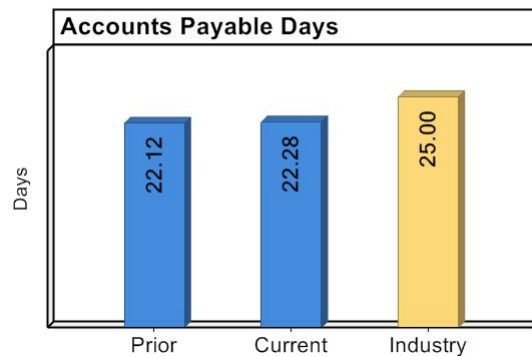
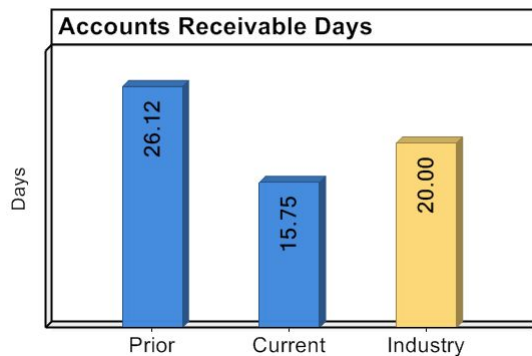
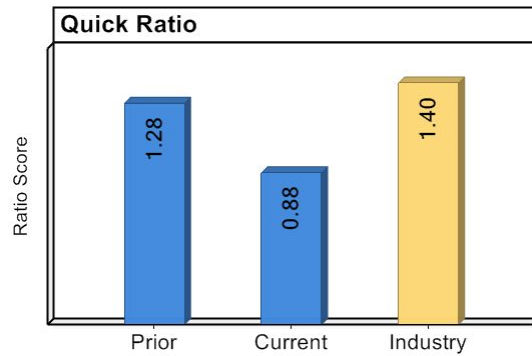
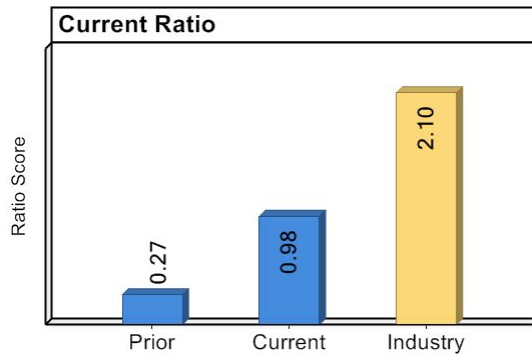
There are two challenges in this area. The first is to monitor the decline in the company's net profit margin. It is detrimental for net margins to be falling when liquidity is also poor. **Profits also fell on higher sales volume.** The second is to try to capture some of the profits and retain them in the company. In the present condition, it may be difficult to pay bills readily over the long run.

If the firm's liquidity cannot be improved by generating more cash in the normal operating cycle, it may be necessary to invest more cash into the business from outside sources.

There are a few other observations that have been made. First, both accounts receivable turnover and accounts payable turnover are "average" relative to other similar companies. Second, managers may have some limited discretion in collecting accounts receivables more quickly and paying vendor accounts more slowly in order to improve the specific cash accounts of the company **if need be**. Of course, careful consideration would have to be applied before these techniques were used since they have serious implications for customer and vendor relations. Also, managers would have to assess their effectiveness.

Liquidity can be improved in any business through more effective management of existing resources (and through good Income Statement management). Here are some ideas that managers **might** think about:

- Set longer terms with subcontractors for expenses associated with their work (when agreed upon by the subcontractor). For example, move a 30 day payment window to 60 days. A business should not only maximize trade credit, but stretch its terms if needed.
- Complete jobs on a timely basis. If completion takes longer than expected, soft costs such as interest and penalties can start to drain the money coming into the business.
- Monitor the amount of money that is being used for activities unrelated to the business. An example could be money taken out of the business on draws to principals.
- Increase prices selectively where possible. Done effectively, this can boost cash flow and liquidity. Good Income Statement management helps Balance Sheet performance.



PROFITS & PROFIT MARGIN



Are profitability trends favorable in the company?

The company has several issues to address in the profitability area at this time. The first is its gross profit margin. Although sales rose by 4.92%, the company's gross profits stayed relatively flat. This is because costs of sales rose significantly relative to each sales dollar. The company's cost of sales seems out of line compared to what it was last period. Increased costs of sales lowered the gross margin. The company will want to watch the gross margin area, because changes here can cause even larger changes in net profitability.

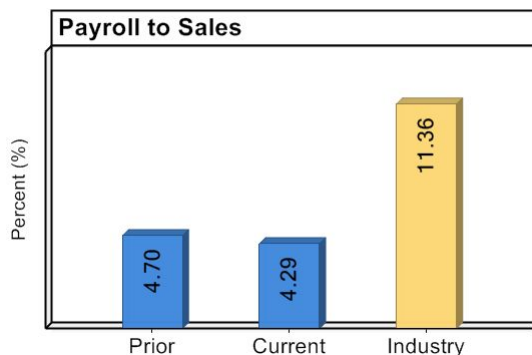
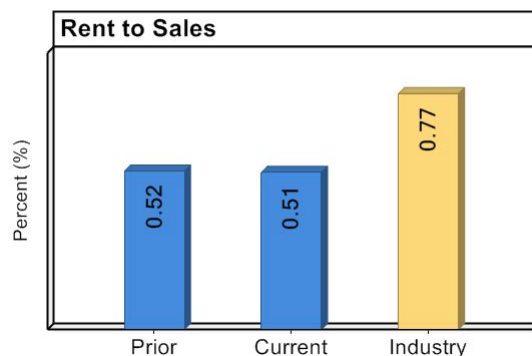
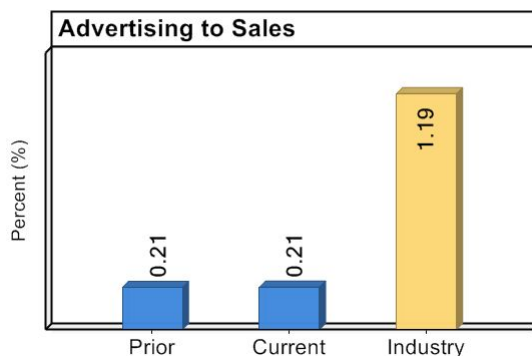
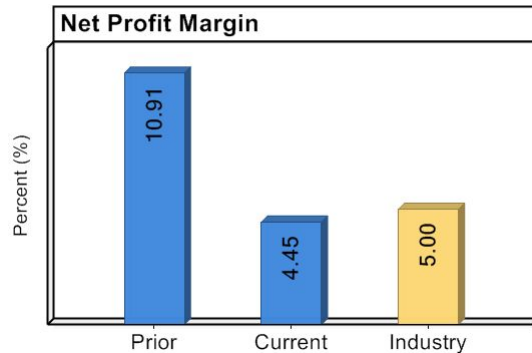
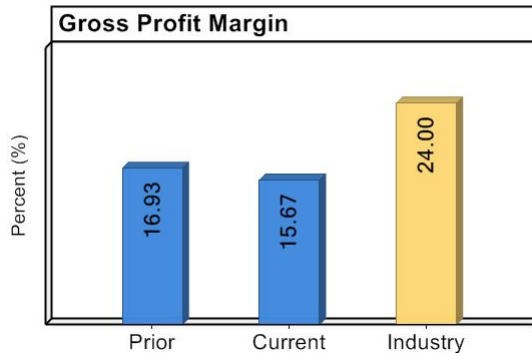
This being said, the company's other concern should be with the net profit area. Net profits and net profit margins fell from last period because the company increased its operating costs. This means that, even though sales rose, both cents of net profit per sales dollar and total net profit dollars have fallen from last period. Companies do not usually mind seeing small increases in operating costs in the short run. However, in the long run, operating costs should help produce higher profits just like any other form of investment.

Despite these declines, the company still has a net profit margin that is about average for this industry; its performance is fair, which is illustrated in the graph area of the report. However, the company did perform better last period, and it would be good to see it improve from its current point.

It may be the case that the company needed to spend more money on operating costs to support its growth. Managers may therefore want to focus on improving gross margins at this time. Gross margins are a crucial part of management work; in fact, they are often the best way to evaluate a company's managerial performance. Many times managers cannot control overhead or operating costs -- they are fixed. Managers should be able to control prices and direct costs by offering high-quality products that generate healthy gross margins.

Profit and loss management is all about continually finding ways to change things in the business to improve profits. Managers **might** think about the following ideas/hints/tips:

- Lock in prices for materials in advance when anticipating future price increases.
- Get on the standing offer list with the government and establish the business as credible with the government.
- Monitor the costs going into all office supplies. With more important costs being monitored closely, many businesses forget to look at this smaller cost, and often allow it to be higher than necessary.
- Invest in activities that can yield positive returns. For example, advertising and employee training can often improve performance for the business.



SALES



Are sales growing and satisfactory?

Most managers are fairly aware of sales trends -- they generally know whether sales are increasing or decreasing at a given point in time. This company's sales are higher this period, which is clearly a good result. The company increased its fixed asset base this period as well. Managers may want to investigate

whether this fixed asset purchase drove the sales increase, or if other factors were at work here.

BORROWING



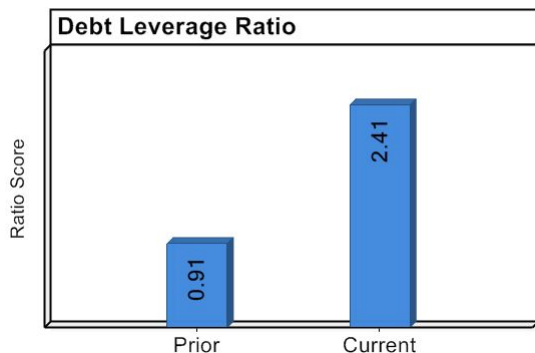
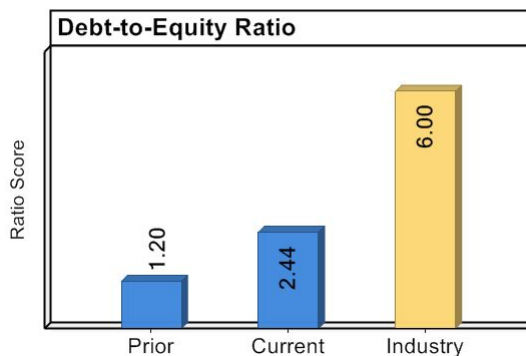
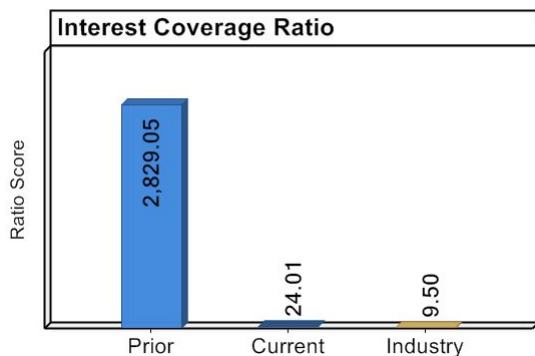
Is the company borrowing profitably?

The issue in this case is that the company increased debt, but profitability actually fell from last period. This situation may simply be because the company has invested in a manner that has not **yet** improved profitability; however, it at least merits some attention.

Another issue to be aware of is that net margins fell, as mentioned previously. Over the short term, it is acceptable to lose a little efficiency while adding debt. However, over the long term, even debt should improve profits and profit margins.

There are some conflicting analytical points here. For example, the company's trend in this area is poor. Yet, the firm seems to be generating ample cash flow from its operations to meet debt obligations. What conclusions can be reached? Perhaps the company is driving enough cash flow **relative** to cost of debt expenses because its debt load is relatively **low** (notice that the debt-to-equity of the company is low, even as compared to the competition). It is difficult to go far in the analysis here, so one might lean on the fact that the overall trend is not favorable.

Income is down, and action is important. This is especially true because the company added significant debt. There are several actions that can be taken in the borrowing area. To start, the company can go through the types of debt on the books right now -- accounts payable, accrued payables, bank financing - - and examine whether it is reasonable to eliminate some debt by selling any underproductive assets associated with the debt. Careful thinking and planning is necessary if this option is considered. Another area to look at is whether some of the debt can be refinanced or restructured, possibly getting longer terms in order to lessen cash outlays. Additionally, the net profit margin is a key indicator: it should be watched closely in the future.



ASSETS



Is the company using gross fixed assets effectively?

The company has invested in more fixed assets but profitability has fallen this period. The company will want to avoid allowing this result to turn into a trend. Over the long run, these types of results could potentially depress profitability. In addition, the company's efficiency has fallen, since the net profit margins have also decreased. Ultimately, fixed asset additions should improve both margins and profitability over time.

It is also important to highlight critical components that are positive. For example, the company has generated above average returns on equity and assets. While it is true that the changing relationship between operating profits and assets will guide long-term returns, in this case, real economic returns in assets and equity are excellent, a fact that needs to be balanced against the overall unfavorable trend.



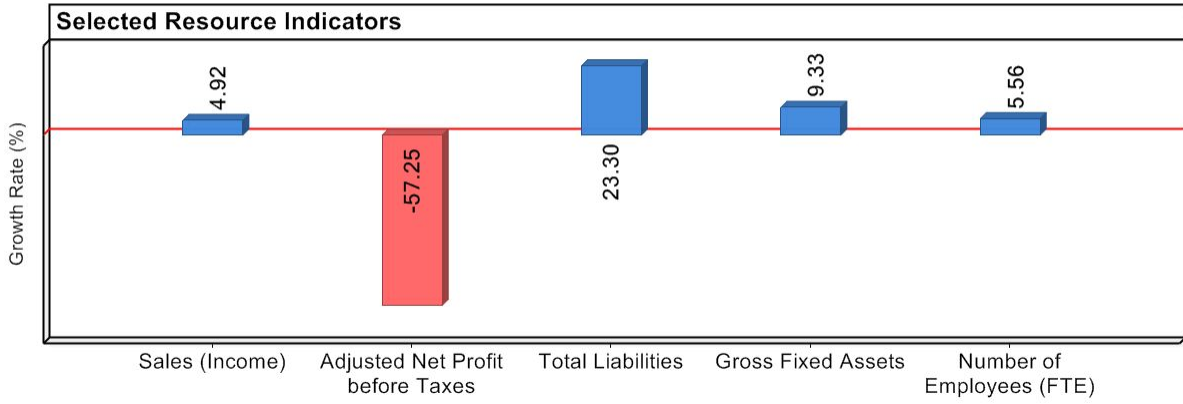
EMPLOYEES



Is the company hiring effectively?

This company has about the same number of employees that it had last period, but net profitability has fallen. This means that the company's profitability per employee statistic (which is a rough measure of efficiency) is lower now than it was last period. At this time, managers **might** want to consider delaying any additional hiring until the company can improve net profitability, especially given the additional fixed assets that were added this period. Managers should always carefully consider all hiring decisions, regardless of profitability levels.

"Obstacles are those frightful things you see when you take your eyes off the goal." -- Henry Ford



A NOTE ON SCORING: Each section of this report (Liquidity, Profits & Profit Margin, etc.) contains a star rating which measures the company's overall performance in the area at the time of the report's generation. One star indicates that the company is below average or may possibly need improvement in the area. Three stars indicate that the company is about average for the area. Five stars indicate that the company is above average or performing quite well in the area.

RAW DATA

	Prior	Current
<u>Income Statement Data</u>		
Sales (Income)	\$2,332,578	\$2,447,454
Cost of Sales (COGS)	\$1,937,688	\$2,063,986
Gross Profit	\$394,890	\$383,468
Gross Profit Margin	16.93%	15.67%
Payroll / Wages / Salary	\$109,560	\$105,023
Rent	\$12,025	\$12,523
Advertising	\$4,985	\$5,256
Depreciation and Amortization	\$8,500	\$8,500
Interest Expense	\$93	\$5,099
Net Profit before Taxes	\$254,509	\$108,814
Adjusted Net Profit before Taxes	\$254,509	\$108,814
Net Profit Margin	10.91%	4.45%
EBITDA	\$263,102	\$122,413
Net Income	\$254,509	\$108,814
<u>Balance Sheet Data</u>		
Cash (Bank Funds)	\$77,193	\$125,718
Accounts Receivable	\$166,940	\$105,583
Inventory	\$0	\$0
Total Current Assets	\$51,555	\$258,151
Gross Fixed Assets	\$143,368	\$156,750
Total Assets	\$439,535	\$416,200
Accounts Payable	\$117,450	\$125,994
Total Current Liabilities	\$190,282	\$262,785
Total Liabilities	\$239,408	\$295,189
Total Equity	\$200,127	\$121,011
Number of Employees (FTE)	18.0	19.0

COMMON SIZE STATEMENTS

	Prior	Current
<u>Income Statement Data</u>		
Sales (Income)	100%	100%
Cost of Sales (COGS)	83%	84%
Gross Profit	17%	16%
Payroll / Wages / Salary	5%	4%
Rent	1%	1%
Advertising	0%	0%
Depreciation and Amortization	0%	0%
Interest Expense	0%	0%
Net Profit before Taxes	11%	4%
Adjusted Net Profit before Taxes	11%	4%
EBITDA	11%	5%
Net Income	11%	4%
<u>Balance Sheet Data</u>		
Cash (Bank Funds)	18%	30%
Accounts Receivable	38%	25%
Inventory	0%	0%
Total Current Assets	12%	62%
Gross Fixed Assets	33%	38%
Total Assets	100%	100%
Accounts Payable	27%	30%
Total Current Liabilities	43%	63%
Total Liabilities	54%	71%
Total Equity	46%	29%

INDUSTRY SCORECARD

Financial Indicator	Current Period	Industry Range	Distance from Industry
Current Ratio = Total Current Assets / Total Current Liabilities	0.98	1.40 to 2.80	-30.00%
<p>Explanation: Generally, this metric measures the overall liquidity position of a company. It is certainly not a perfect barometer, but it is a good one. Watch for big decreases in this number over time. Make sure the accounts listed in "current assets" are collectible.</p>			
Quick Ratio = (Cash + Accounts Receivable) / Total Current Liabilities	0.88	1.00 to 1.80	-12.00%
<p>Explanation: This is another good indicator of liquidity, although by itself, it is not a perfect one. If there are receivable accounts included in the numerator, they should be collectible. Look at the length of time the company has to pay the amount listed in the denominator (current liabilities).</p>			
Accounts Receivable Days = (Accounts Receivable / Sales) * 365	15.75 Days	10.00 to 30.00 Days	0.00%
<p>Explanation: This number reflects the average length of time between credit sales and payment receipts. It is crucial to maintaining positive liquidity.</p>			
Accounts Payable Days = (Accounts Payable / COGS) * 365	22.28 Days	15.00 to 35.00 Days	0.00%
<p>Explanation: This ratio shows the average number of days that lapse between the purchase of material and labor, and payment for them. It is a rough measure of how timely a company is in meeting payment obligations.</p>			
Gross Profit Margin = Gross Profit / Sales	15.67%	20.00% to 28.00%	-21.65%
<p>Explanation: This number indicates the percentage of sales revenue that is paid out in direct costs (costs of sales). It is an important statistic that can be used in business planning because it indicates how many cents of gross profit can be generated by future sales.</p>			
Net Profit Margin = Adjusted Net Profit before Taxes / Sales	4.45%	2.00% to 8.00%	0.00%
<p>Explanation: This is an important metric. In fact, over time, it is one of the more important barometers that we look at. It measures how many cents of profit the company is generating for every dollar it sells. Track it carefully against industry competitors. This is a very important number in preparing forecasts.</p>			
Advertising to Sales = Advertising / Sales	0.21%	0.00% to 2.39%	0.00%
<p>Explanation: This metric shows advertising expense for the company as a percentage of sales.</p>			
Rent to Sales = Rent / Sales	0.51%	0.39% to 1.14%	0.00%
<p>Explanation: This metric shows rent expense for the company as a percentage of sales.</p>			
Payroll to Sales = Payroll Expense / Sales	4.29%	5.11% to 17.61%	+16.07%

Explanation: This metric shows payroll expense for the company as a percentage of sales.

Interest Coverage Ratio = EBITDA / Interest Expense	24.01	4.00 to 15.00	+60.07%
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Explanation: This ratio measures a company's ability to service debt payments from operating cash flow (EBITDA). An increasing ratio is a good indicator of improving credit quality.

Debt-to-Equity Ratio = Total Liabilities / Total Equity	2.44	4.00 to 8.00	+39.00%
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Explanation: This Balance Sheet leverage ratio indicates the composition of a company's total capitalization -- the balance between money or assets owed versus the money or assets owned. Generally, creditors prefer a lower ratio to decrease financial risk while investors prefer a higher ratio to realize the return benefits of financial leverage.

Debt Leverage Ratio = Total Liabilities / EBITDA	2.41	N/A	N/A
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Explanation: This ratio measures a company's ability to repay debt obligations from annualized operating cash flow (EBITDA).

Return on Equity = Net Income / Total Equity	89.92%	8.00% to 20.00%	+349.60%
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Explanation: This measure shows how much profit is being returned on the shareholders' equity each year. It is a vital statistic from the perspective of equity holders in a company.

Return on Assets = Net Income / Total Assets	26.14%	6.00% to 10.00%	+161.40%
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Explanation: This calculation measures the company's ability to use its assets to create profits. Basically, ROA indicates how many cents of profit each dollar of asset is producing per year. It is quite important since managers can only be evaluated by looking at how they use the assets available to them.

Fixed Asset Turnover = Sales / Gross Fixed Assets	15.61	15.00 to 40.00	0.00%
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Explanation: This asset management ratio shows the multiple of annualized sales that each dollar of gross fixed assets is producing. This indicator measures how well fixed assets are "throwing off" sales and is very important to businesses that require significant investments in such assets. Readers should not emphasize this metric when looking at companies that do not possess or require significant gross fixed assets.

NOTE: Exceptions are sometimes applied when calculating the Financial Indicators. Generally, this occurs when the inputs used to calculate the ratios are zero and/or negative.

READER: Financial analysis is not a science; it is about interpretation and evaluation of financial events. Therefore, some judgment will always be part of our reports and analyses. Before making any financial decision, always consult an experienced and knowledgeable professional (accountant, banker, financial planner, attorney, etc.).

Performance Review

For the period ending 12/31/2006

Provided By

By The Book Accounting, Inc.

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1/17/2007

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