

## **Internal Analysis for Financial Recovery of NUB Club: A Case Study**

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## **Background of the Case**

The purpose of this case study focuses on conducting an internal analysis regarding NUB Club's financial state as a possible basis to influence its management decision with regards on how it can effectively handle its finances and operations sustainability. The NUB Club is a non-profit organization that is based on membership fees to accumulate its resources to provide quality food services, recreation, and entertainment for members of the club. Subsidies have been also their source of money but due to budget cuts by the government, the university was no longer in the position to subsidize the operation of the club.

This case study is developed to analyze the prior and current years' financial statements of the NUB club which causes its financial distress. The reason behind this case study is to recognize the demand for action on the recovery of incurred losses for several years' experience by the club through the increase in membership fee, to increase the number of members or to close the club. And, to give recommendations on proper utilization of ratio analysis to help NUB Club cope up with its current and future operation.

## **Statement of the Problem**

This study aims to identify the optimal course of action for the NUB Club, whether to continue its operation by having an additional membership fee, increase the number of members or to liquidate the club. To analyze the financial statements using financial ratio analysis to assess the club's ability to meet its short-term liabilities, manage its assets, determine the level of debt financing, and evaluate its profitability status of in order to cope up with its financial difficulties.

## **Assumptions**

The NUB Club is currently facing financial difficulties that threatens its long-term ability to survive. There is a possibility that the club may not be able to meet its short-term liabilities, by reason of difficulty in managing its assets effectively or debt financing may be a factor in its financial difficulties, as well as there is uncertainty as to whether the club is currently profitable.

The possible course of action, which is the increase in membership fee, to consider the higher fee on covering the losses would be unfavorable for the members to have an additional membership fee. There would be discouragement for new people to become a member of the club. Some might take into consideration dropping out of the club than to cost them a lot without their full willingness. It would also be possible to decrease the expenses of the club by cutting down some of its services, but it may affect the members' satisfaction and may even result in a decrease in membership.

The decision to liquidate the club may seem like the easiest and straightforward solution, but it may have financial implications that need to be considered carefully. Therefore, the study may provide insights into the club's financial condition and can help identify areas that need improvement. By examining its financial statements, the study can assess whether there is possibility to generate source of financial to meet its long-term obligations or opportunities to increase revenue and decrease its costs.

## **Analysis**

### **Liquidity Ratio Analysis**

Evaluation of the club's ability to meet its short-term obligations using its liquid assets is termed as the liquidity ratio analysis. It focuses on the company's ability to convert its current assets into cash to pay its short-term liabilities. The club shows that it has a current ratio of below 1 which indicates that the club is having difficulty paying its bills on time. NUB club has .81 which is lower than the 2 other university club that has 1.11 capability to pay its liabilities. The two other university clubs have greater ratio that implies that their clubs' assets are greater than its liabilities. In terms of a more conservative measure of liquidity, quick ratio or acid test ratio had been used to consider the most liquid assets that can be quickly converted to cash to satisfy its short-term liabilities. In every 1 peso of the liability of the NUB Club for current year 2016 only 0.38 ratio is the capacity to pay its liabilities which shows a bad indication that the club struggled to meet its short-term obligations using its most liquid assets.

Computation:

Current Ratio (2016) = Current Assets / Current Liabilities

$$= 135,857.32 / 166,970.29$$

$$= 0.81$$

Quick Ratio (2016) = Current Assets-Inventory / Current Liabilities

$$= 25,070.41 + 38,968.40 / 166,970.29$$

$$= 0.38$$

### **Activity Ratio Analysis**

To analyze a company's operational efficiency and effectiveness by measuring its ability to convert its assets into revenue or cash, the technique activity ratio analysis was used. It involves the calculation of various turnover ratios such as total asset turnover, inventory turnover ratio, days in inventory, accounts receivable turnover ratio, and average turnover ratio.

Based on the financial data of NUB Club, the proponents have assessed that the ability of the club to generate revenue in relation to its total assets indicated that it has been able to generate sales from its assets at a moderate rate of which in every 1 asset, the company can make 3.74-peso sales on the year 2016. Although it declines from 5.49 in 2009 to 3.04 as the lowest in 2014, it is better than the average comparable total asset turnover of the two other university clubs which is only 1.5 in that of 3.47-peso sales of the NUB Club.

The inventory turnover also has significance in assessing the ability of the club to manage its assets, particularly the inventory. The club shows in its data that there are fluctuations in its inventory turnover ratio, which indicates that the higher the turnover is, the more efficient it sells its inventory while when it is lower, may indicate that the company is carrying too much inventory with difficulty in selling its product. However, upon assessing its historical ratios, it is in moderate surveillance that the club makes an effort in order to improve its inventory turnover.

The days in inventory indicator tracks how long it takes a business to sell its stock. A lower number suggests that the business is selling its stock more quickly, which can be a good indicator as it means the business is turning a profit more quickly. The company's days in inventory went from a low of 29.08 in 2009 to a high of 49.32 in 2014, with an average of about 38 days. With some variations from year to year, the trend in days in inventory appears to be generally stable over time. It is important to note that 2014 had

many more days in inventory than previous years, which may call for further research into any possible problems with inventory management that year.

The trend in receivables turnover seems to be increasing from 2007 to 2010, reaching its peak in 2010, and then decreasing in subsequent years. However, there are some fluctuations in the trend, with slight increases and decreases in some years. It is important for companies to keep track of their receivables turnover to ensure efficient management of their accounts receivable and cash flow.

The average collection period was relatively high, indicating that the company was taking longer to collect its accounts receivable. The trend then improved significantly in 2009, with the average collection period dropping to 28.32 days, which is a positive sign. The average collection period then decreased again in 2013, indicating that the company was improving its accounts receivable management. In 2014, the average collection period remained largely stable at 44.99 days. The trend then continued to improve in 2015, with the average collection period dropping to 31.54 days, before decreasing in 2016 to 20.98 days.

#### Computations

Total Asset turnover in 2016 = 10.23

$$= \frac{\text{total operating revenue}}{\text{average total assets}}$$

$$= \frac{909,905.77}{243,206.45}$$

$$= 3.74$$

Days in inventory in 2016 =

$$\frac{\text{days in period (365 days for annual)}}{\text{inventory turnover}}$$

$$= \frac{365}{10.23}$$

Inventory turnover in 2016 = 35.67

$$= \frac{\text{cost of goods sold}}{\text{average inventory}}$$

$$= \frac{215,505.47}{21,067.48}$$

$$\text{Receivables turnover (2016)} = \frac{\text{total operating revenue}}{\text{average accounts receivable}}$$

$$= \frac{813,175.14}{100,220.69}$$

$$= 8.11$$

$$\text{Average Collection Period (2016)} = \frac{\text{days in period (365 for annual)}}{\text{receivables turnover}}$$

$$= \frac{365}{17.40}$$

$$= 20.98$$

#### Summary Activity Ratios from 2007 to 2016

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Total Asset turnover	3.86	4.18	5.49	5.28	3.49	3.27	3.56	3.04	3.33	3.74
Inventory turnover	11.96	12.00	12.55	10.82	7.80	8.66	7.96	7.40	9.78	10.23
Days in inventory	30.50	30.42	29.08	33.69	46.79	42.13	45.81	49.32	37.34	35.67
Receivables turnover	6.75	8.13	12.88	22.90	11.34	7.54	8.93	8.11	11.56	17.40
Average Collection Period	54.07	44.91	28.32	15.93	32.19	48.37	40.84	44.99	31.54	20.98

#### Financial Leverage Ratio

Financial leverage ratio analysis is a technique used to evaluate a company's use of debt to finance its operations and investments. The analysis focuses on the amount of debt a company has relative to its equity and measures the company's ability to meet its debt obligations. The debt ratio of NUB Club as of 2016 shows that its ratio is higher of which 0.92 in contrast with the other university clubs which is only 0.31. It means that the club is taking on too much debt, which negatively impacted its financial health. Although from the past years, it almost reaches halfway of the other clubs' average ratio, but it is possible to improve its debt ratio by reducing the use of debt to finance its assets.

Moreover, the proportion of debt-to-equity ratio indicates the club's financing that comes from debt relative to equity is very high in 2016 which is approximately 10 of the debt to 1 equity. It also means that the club is heavily reliant on debt financing that increases its financial risk in its current years of operation that starts to increase from the year 2014. However, over the past years they manage to control their debt financing

which lowered 0.13 in 2008 but, due to several factors that causes variations over the years, its management can be at poor control that is why it is unable to meet its debt obligations that it faces financial difficulties.

Computations:

$$\begin{aligned}\text{Debt Ratio (2016)} &= \text{Total Debt} / \text{Total Assets} \\ &= 166,970.29 / 182,887.95 \\ &= 0.92\end{aligned}$$

$$\begin{aligned}\text{Debt to equity Ratio} &= \text{Total Debt} / \text{Total equity} \\ &= 166,970.29 / 15,917.66 \\ &= 10.49\end{aligned}$$

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Debt Ratio	1.75	1.82	.012	0.32	0.61	0.62	0.52	0.60	0.81	0.92
Debt to equity ratio	2.33	2.22	0.13	0.47	1.58	1.62	1.08	1.49	4.14	10.49

## Profitability Ratio

The Gross Profit Ratio of the NUB Club from 2007 to 2016 ranges from 0.79 to 0.84. A high Gross Profit ratio indicated that the company is being efficient and stable. Based on the information above, the lowest Gross Profit Ratio is 0.79 which can be seen in not consecutive but 3 years which are the years 2007, 2008 and 2010. The highest Gross profit Ratio was achieved in the year 2013 which is 0.84. the information above can be interpreted as a good thing even though there is some decreases it is not that big of a deal as there is also increases in some years.

The Net Profit Margin of the NUB Club from year 2007 to 2016 ranges from -6.57 to 0.06. A negative Net Profit margin means that the club is spending more money than what they are earning. Based on the information above 7 out of 10 years the club has a negative net profit margin. During the year 2008 the lowest Net profit Ratio were recorded at -6.57. Although the next year the Net Profit Ratio became positive at 0.06 it

is still not good as it can still be seen that the club has too much expense than what they earn.

### Computations

#### Gross Profit Margin

$$= \frac{\text{Gross Income}}{\text{Total Operating Revenue}}$$

$$= \frac{740,014.85}{909,905.77}$$

$$= 0.81$$

#### Net Profit Margin

$$= \frac{\text{Net Income}}{\text{Total Operating Revenue}}$$

$$= \frac{-43,144.12}{909,905.77}$$

$$= -0.05$$

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Gross Profit Margin	0.79	0.79	0.80	0.79	0.83	0.82	0.84	0.83	0.81	0.81
Net Profit Margin	0.01	-6.57	0.06	-6.02	-6.02	-0.01	0.04	-0.05	-0.04	-0.05

### Recommendation

The findings of the study allow the proponents to come up with the following recommendations based on the previous and current years' performance of the NUB Club:

1. An increase in the membership fee would increase the assets, particularly in cash, of the club to meet its short-term obligations. This cash should be



managed efficiently through investing in short-term investments such as money market funds or short-term bonds as it can generate a higher return than keeping cash on hand to improve its liquidity.

2. Boost collection efforts. The decline in receivables turnover in the years that followed implies that the business may have issues getting payments from its clients. The business can think about rewarding early payments or punishing late payments to increase collection efforts. It could also follow up with clients who have unpaid amounts in a more proactive manner.
3. The business might want to think about implementing inventory management strategies to increase inventory turnover and improve cash flow. The company should also keep an eye on its days in inventory and inventory turnover to make sure that it is maximizing its inventory management. By optimizing inventory management, the company can reduce costs and improve profitability.
4. Increasing the number of members of the club through hosting events and campaigns would improve the financial leverage or reduce debt financing of the club. It should not only rely on subsidies of the university but to seek donations from individuals, corporations, and foundations. Debt financing is a risk that should be managed effectively thus the club should take lesser borrowing of money from lenders.
5. Investing in long-term growth initiatives that can increase revenue and decrease expenses can also be a factor to be considered in the profitability of the club.
6. Although the Gross Profit Margin is good and can cover the costs for the club, but the negative results of Net Profit Ratio cause a big impact for the club as it may be the reason why the NUB Club wasn't able to earn money rather, they keep on losing it through the years. The NUB Club may consider on keeping their expenses on track or have someone to monitor and budget their finance to avoid too much expense that can help to prolong the activities of NUB Club.