

**CASE STUDY
YOUR BANK**

FROM: Bill.Banker@YourBank.com
TO: Angela.Cummings@YourBank.com
SENT: Tuesday, May 19, Year 5 9:15 AM
SUBJECT: Anderson Steel, Inc.

This is the credit we discussed briefly the other day. Since then, there have been several developments which have placed a premium on providing a prompt response if we are to obtain the Anderson Steel business. I am enclosing the credit file we have developed to date.

The company has three funding needs, according to Mark Green, president:

1. A new computer system costing \$250,000. It will be used to upgrade accounting software for tracking and collecting A/R, plus link the various production facilities to eventually reduce inventory levels.
2. New office space within the existing Birmingham plant, costing \$80,000 to build. The costs will be capitalized.

Anderson Steel has about \$1,200,000 outstanding on an existing long-term loan, and Green is willing to consider refinancing this loan. As a combined package, we are being asked to consider a \$1,500,000 long-term loan that will fully amortize over seven years, plus a \$500,000 operating line of credit. If we are successful in obtaining the loan business, the company will move its primary depository accounts and cash management business to us.

While Green and I discussed some preliminary rates and terms, I think he is anxious to get a proposal from us. Therefore, I am sending the attached financial statements to you before the credit department has had a chance to complete the spread and an updated analysis. I look forward to your thoughts and suggestions. I used your electronic calendar to set a meeting at 1:00 p.m. tomorrow.

Simpson, Otter & Simpson, P.C.
Certified Public Accountants
1221 Southside Park
Birmingham, AL 35201

May 12, Year 5

Board of Directors
Anderson Steel, Inc.
Birmingham, AL 35242

We have reviewed the accompanying balance sheet of Anderson Steel, Inc. for the years ending December 31, Year 1 through December 31, Year 4 and the related statements of income and retained earnings. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America and for designing and implementing internal control relevant to the preparation and fair presentation of the financial statements.

Our responsibility is to conduct the review in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the financial statement. We believe that the results of our procedures provide a reasonable basis for our report.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

Simpson, Otter and Simpson, P.C.

ANDERSON STEEL, INC.
Balance Sheet (\$ in 000s)
As of December 31

Assets	Year 1	Year 2	Year 3	Year 4
Current Assets				
Cash	\$ 3	\$ 33	\$ 37	\$ 56
Accounts Receivable (Net)	660	945	1,408	1,277
Inventory	360	685	1,268	1,197
Prepays	43	81	214	221
Other Current Assets	7	12	39	56
Total Current Assets	<u>\$1,073</u>	<u>\$1,756</u>	<u>\$2,966</u>	<u>\$2,807</u>
Fixed Assets				
Cost	356	547	1,122	1,335
Accumulated Depreciation (Note 1)	(99)	(227)	(352)	(521)
Net Fixed Assets	<u>\$ 257</u>	<u>\$ 320</u>	<u>\$ 770</u>	<u>\$ 814</u>
Other Assets				
Due from Officer			27	20
Intangibles	1	1	14	20
TOTAL ASSETS	<u>\$1,331</u>	<u>\$2,077</u>	<u>\$3,777</u>	<u>\$3,661</u>
Liabilities				
Current Liabilities				
Notes Payable – Banks (Note 2)			\$ 186	\$ 128
Accounts Payable	\$ 409	\$ 623	1,261	1,142
Income Taxes Payable	3	93	9	41
Other Accrued Expenses	122	317	63	22
Current Maturities of Long-Term Debt	234	252	188	236
Total Current Liabilities	<u>\$ 768</u>	<u>\$1,285</u>	<u>\$1,707</u>	<u>\$1,569</u>
Other Liabilities				
Long-Term Debt	312	241	1,087	990
Deferred Taxes (Note 3)			111	101
Due to Stockholder		10		
Total Liabilities	<u>\$1,080</u>	<u>\$1,536</u>	<u>\$2,905</u>	<u>\$2,660</u>
Stockholders' Equity				
Common Stock, no par value	205	234	311	311
Retained Earnings	46	307	561	690
Total Stockholders Equity	<u>\$ 251</u>	<u>\$ 541</u>	<u>\$ 872</u>	<u>\$ 1,001</u>
Total Liabilities and Stockholders Equity	<u>\$1,331</u>	<u>\$2,077</u>	<u>\$3,777</u>	<u>\$3,661</u>

ANDERSON STEEL, INC.
Statement of Income and Retained Earnings (\$ in 000s)
For the Year Ended December 31

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>
Net Sales	\$2,485	\$6,586	\$7,859	\$9,980
Cost of Goods Sold	<u>1,805</u>	<u>4,615</u>	<u>5,655</u>	<u>7,248</u>
Gross Profit	\$ 680	\$1,971	\$2,204	\$2,732
Depreciation	76	128	125	169
Executive Autos (Note 6)		20	36	43
Insurance	22	42	70	98
Miscellaneous			20	43
Occupancy (Note 6)	126	268	271	356
Payroll and Benefits	207	551	879	1,138
Pension Fund		78	55	66
Professional Fees	27	75	89	124
Profit Sharing				26
Selling	20	83	100	110
Supplies	15	59	57	71
Taxes	25	81	13	11
Telephone	<u>18</u>	<u>55</u>	<u>72</u>	<u>105</u>
Total Operating Expenses	<u>\$536</u>	<u>\$1,440</u>	<u>\$1,787</u>	<u>\$2,360</u>
Operating Profit	\$144	\$ 531	\$ 417	\$ 372
Interest Expense	37	65	108	157
Other Expense (Note 4)				98
Other Income (Note 5)			(41)	(49)
Profit Before Taxes	<u>\$107</u>	<u>\$466</u>	<u>\$350</u>	<u>\$166</u>
State and Federal Income Taxes	<u>13</u>	<u>205</u>	<u>96</u>	<u>37</u>
NET PROFIT	<u>\$ 94</u>	<u>\$261</u>	<u>\$254</u>	<u>\$129</u>

RETAINED EARNINGS RECONCILEMENT

Beginning Retained Earnings	(\$48)	\$ 46	\$307	\$561
Add: Net Profit	<u>94</u>	<u>261</u>	<u>254</u>	<u>129</u>
Ending Retained Earnings	<u>\$ 46</u>	<u>\$307</u>	<u>\$561</u>	<u>\$690</u>

ANDERSON STEEL, INC.
Notes to Financial Statements

1. Depreciation is taken on a straight-line basis over useful lives ranging from 3-15 years.
2. Notes payable-banks represents amounts payable under a \$250,000 revolving line of credit in place for both Year 4 and Year 3. The line of credit started in Year 2 with a \$100,000 limit and is secured by accounts receivable and inventory.
3. Deferred income taxes arise primarily from timing differences in the recognition of depreciation between tax returns and management's financial statements.
4. Other expense in Year 4 arises from a one-time charge for disposal of waste materials found in a previously purchased warehouse.
5. Other income arises from rental of excess warehouse space in the Birmingham location to unrelated concerns. Leases are on a year-to-year basis and have been renewed for calendar Year 5.
6. The company leases automobiles and buildings from unrelated parties. A summary of lease obligations follows (\$ in 000s):

Years ending December 31	<u>Buildings</u>	<u>Other</u>
Year 5	\$390	\$52
Year 6	\$332	\$50
Year 7	\$319	\$49
Year 8	\$319	\$49
Thereafter	\$1,276	\$88

CASE STUDY - CONTINUED

FROM: Bill.Banker@YourBank.com
TO: Angela.Cummings@YourBank.com
CC: Credit.File@YourBank.com
SENT: Wednesday, May 20, Year 5 4:27 PM
SUBJECT: Anderson Steel, Inc. (ASI)

Today I visited with Mark Green, president. I have been calling on him for several years, and he is giving us a chance to submit a proposal for refinancing of term debt and new funds for several needs. (See prior e-mail to Angela Cummings dated May 19, Year 5). This message summarizes the background and history of Anderson Steel.

- Distributor of steel products, primarily plates, sheets and rods both in carbon steel and various alloys, founded as Decatur Specialty Metals thirteen years ago
- 80% of revenues from wholesaling, 20% from simple fabrication such as cutting, shaping, drilling and welding; has recently started to acquire small machinery to enable diversifying into contract manufacturing
- Customer list dominated by (1) manufacturers of specialty components for the aerospace and defense industry under contracts lasting as long as three years, (2) machine and equipment replacement parts manufacturers, and (3) heavy repair contractors for bridges, airport runways, overhead cranes and asphalt plants
- Mike Anderson bought the company six years ago and combined it with his existing operations here in Birmingham; has opened or acquired smaller operations in Memphis, TN and Anniston, AL; wants to expand by acquisition or opening a facility in the Atlanta, GA area
- Memphis acquisition in Year 3 cost \$704,000 and provided the fabrication capabilities; all growth in Year 4 was organic – not due to any acquisitions
- Anderson is 68 years old and serves as chairman with 48% ownership; Green is 51 and became president when Anderson Steel acquired his Memphis business five years ago, and owns 33% with an employment contract extending for another five years; Jonathon Hughes owns the remaining 19% as sole heir to a portion formerly owned by Mr. Anderson's sister
- Simpson, Otter and Simpson (SOS) CPAs obtained the Anderson Steel account after the Memphis acquisition was made; SOS upgraded the statements from a compilation to a review, with plans to move to an audit in Year 5
- One of the recent contributions of SOS has been to improve A/R collections performance by recommending the addition of personnel to the function and also by instituting a sales commission forfeiture on related A/R that go past due more than 90 days
- Inventory levels doubled from Year 2 to Year 3 due to excess raw materials from the purchase of the fabrication facility. The excess has been reduced, but will not be reduced much more until a centralized inventory control system (part of the current loan request) is installed
- Green blames lower gross margins on pricing resistance at all levels of government, which affects the contractors that his company supplies

Overall, Anderson Steel appears to be on a growth pace, with a steady customer base in an industry with good prospects for continued growth.