

Background:

Callaway Golf Company was incorporated in 1982 with the purpose of designing, manufacturing and selling high quality golf clubs. The Company became a publicly traded corporation in 1992. Callaway Golf has evolved over time from a manufacturer of golf clubs to one of the leading manufacturers and distributors of golf equipment and accessories. Callaway designs its products to be technologically advanced and invests substantially in research and development each year. The Company's golf products are designed for golfers of all skill levels including amateur and professional golfers. Callaway Golf generally sells its products to retailers, directly and through its wholly-owned subsidiaries, and to third-party distributors. It also licenses its trademarks and service marks in exchange for a royalty fee to third parties for use on golf related accessories, including golf apparel and footwear, golf gloves, prescription eyewear and practice aids. The Company's products are sold in the United States and in over 100 countries around the world. For purposes of this assignment, assume that your focus is Drive It Long, which is a close competitor to Callaway Golf. Drive It Long similarly sells golf clubs, golf balls and golf accessories. These products are recreational in nature and are therefore discretionary purchases for consumers. Both firms are affected by the fact that consumers are generally more willing to make discretionary purchases of golf products during favorable economic conditions and when consumers are feeling confident and prosperous. Discretionary spending is also affected by factors including general business conditions, interest rates, consumer confidence in future economic conditions, and the availability of consumer credit. Purchases of these firms' products may decline during periods when disposable income is lower, or during periods of actual or perceived unfavorable economic conditions. A significant or prolonged decline in general economic conditions or uncertainties regarding future economic prospects that adversely affect consumer discretionary spending would have a negative impact on these firm's results of operations, financial condition and cash flows.

This paper is an exercise designed to better acquaint students with the four main categories of ratio analysis. Financial ratios are a standardized means of comparing information presented in financial statements, in order to analyze the operations of a firm, and to compare operations against certain benchmarks that assist us in drawing conclusions about the firm's performance. This exercise requires students to compute common financial ratios in the four areas in which these are most often applied to analyze firm performance. This will strengthen the student's ability to understand what aspects of a firm's activities that a particular ratio characterizes, and where this information can be found in financial statements. The student will additionally be asked to draw conclusions regarding financial performance using computed ratios.

Assume that you are a Senior Financial Manager for Drive It Long Golf, Inc. A close competitor is Callaway Golf Co. (ELY). You are preparing to address the Board of Directors regarding the current financial picture of the firm, following the release of the firm's Audited Financial Statements. Drive It Long Golf, Inc. has 25,000 shares of common stock outstanding, and the market price for a share of stock at the end of 2016 was \$58. Assume that this company's growth rate is 9%. As Drive It Long's Senior Financial Manager, you are assumed to be able to

offer an authoritative interpretation of the firm's recent performance.

Financial Ratios, Drive It Long Golf, Inc.

Short-term solvency ratios:

2015

2016

a. Current ratio

1.1

1.15

b. Quick ratio

0.65

0.68

c. Cash ratio

0.43

0.42

Asset utilization ratios:

Period

d. Total asset turnover

0.88

e. Inventory turnover

8.93

f. Receivables turnover

23.09

Long-term solvency ratios:

2015

2016

g. Total debt ratio

0.37

0.38

h. Debt–equity ratio

0.58

0.6

i. Equity multiplier

1.58

1.6

Period

j. Times interest earned ratio

5.73

k. Cash coverage ratio

7.99

Profitability ratios:

Period

l. Profit margin

11.94%

m. Return on assets

10.53%

n. Return on equity

16.85%

Table 1. Financial Ratios, Drive It Long Golf, Inc.

Drive It Long, Inc.

Statement of Cash Flows for 2016

Cash, beginning of the year

\$26,450

Operating activities

Net income

\$50,376

Plus:

Depreciation

\$37,053

Increase in accounts payable

4,883

Increase in other current liabilities

5,161

Less:

Increase in accounts receivable

(\$4,589)

Increase in inventory

(4,655)

Net cash from operating activities

\$88,229

Investment activities

Fixed asset acquisition

(\$78,233)

Net cash from investment activities

(\$78,233)

Financing activities

Increase in notes payable

(\$2,340)

Dividends paid

(20,000)

Increase in long-term debt	
15,000	
Net cash from financing activities	
(\$7,340)	
Net increase in cash	
\$2,656	
Cash, end of year	
\$29,106	

Table 2. Statement of Cash Flows, Drive It Long, Inc.

Drive It Long, Inc.
2014 and 2015 Balance Sheets

2014	
2015	

2014	
2015	
Current assets	

Current Liabilities

Cash	
\$26,450	
\$29,106	

Accounts payable	
\$30,602	
\$35,485	

Accounts receivable	
13,693	
18,282	

Notes payable	
15,840	
13,500	

Inventory	
27,931	
32,586	

Other

15,280
20,441
Total
\$68,074
\$79,974

Total
\$61,722
\$69,426

Long-term debt

\$95,000
\$110,000

Owner's equity

Common stock & paid-in surplus
\$ 45,000
\$45,000
Fixed assets

Accumulated retained earnings
223,517
253,893

Net plant & equipment
\$357,165
\$398,345

Total
\$268,517
\$298,893
Total assets

\$425,239
\$478,319
Total liabilities & owners' equity

\$425,239
\$478,319

Table 3. Balance Sheets, Drive It Long Golf, Inc.

Drive It Long, Inc.
2015 Income Statement
Sales

\$422,045

Cost of Goods Sold
\$291,090

Depreciation
37,053
Earnings Before Interest and Taxes

\$93,902

Interest Paid
\$16,400

Taxable Income
77,502

Taxes (35%)
27,126
Net Income

\$50,376

Dividends
\$20,000

Retained Earnings
30,376