Readers Digest Association:
Debt or Equity

Susan White, University of Maryland

ABSTRACT

The Readers Digest Association case is about a decision that RDA must make concerning the financing of its new acquisition. The firm has traditionally be conservative, financing with little or no debt. The company must choose between straight debt, new common equity or preferred stock. The case explores the tax impacts of each decision, along with the implications for control, risk and shareholders' income.

INTRODUCTION

Debt? Equity? Preferred stock? Mark Lee knew all the terms from his finance classes – after all he had only graduated nine months ago. He was contemplating his biggest assignment ever – helping to prepare a report for the big boss, Michael Geltzeiler, senior vice president and chief financial officer of Reader's Digest Association. It was June 17, 2002, and Reader's Digest was getting ready to finalize its acquisition of Reiman Holding Company and its subsidiaries for $760 million in cash. The firm's senior management was about to present financing alternatives to the Board of Directors. Should the acquisition be financed with debt? With equity? With preferred stock? With some combination of these financing alternatives?

READER'S DIGEST ASSOCIATION

Reader's Digest Association (RDA) is a diversified media company, producing books, magazines and other products worldwide. RDA was incorporated in New York in 1922 and reincorporated in Delaware in 1951. The firm's flagship is Reader's Digest magazine, which has a worldwide circulation of 23 million. Published in 48 editions and 19 languages, it has over 100 million readers a month.

RDA operated in three major segments:

1. North American Books and Home Entertainment. This group publishes and markets, primarily through direct marketing, books and home entertainment products in the U.S. and Canada. For example, this division sold Reader's Digest and other magazines through youth fundraising campaigns of Quality Services Programs Inc. in Canada and through independent sales representatives of Books Are Fun, Ltd. in the U.S.
2. U.S. Magazines. This division publishes and markets Reader's Digest and special interest magazines in the U.S. It sells RDA and other publisher's magazines through QSP, Inc. and Books Are Fun.
3. International Businesses. This segment publishes and sells Reader's Digest worldwide. Display and youth-fundraising marketing were introduced in some of its international markets.

RDA's long term growth goals include:

- revitalizing its flagship magazine
- marketing in ways other than sweepstakes direct mail
- attracting new customers through new products and services and building deeper relationships with existing customers
- offering products in addition to published products
- integrating the internet into its businesses

Reader's Digest describes itself as a reader-driven, family magazine. Its editorial mission "is to inform, enrich, entertain and inspire."[1] Many magazine selections are written by freelance or staff writers. The remainder are chosen from existing publications and are condensed or excerpted by Reader's Digest editors. International Reader's Digest editions contain material considered relevant for their audiences. RDA has created a Reader's Digest website, rd.com to expand the print version of Reader's Digest through the use of audio, graphic, text and video enhancements, interactive discussions and reader involvement and additional content.

REIMAN HOLDING COMPANY ACQUISITION

Purchasing Reiman would fit in with RDA's long-term strategy. Reiman publishes magazines and books about cooking, gardening, country lifestyle, nostalgia and crafts. About 62% of its revenues come from magazine publishing, 23% from books and 15% from other businesses. Reiman's philosophy includes focusing on positive aspects of people and their lifestyles, maintaining low editorial costs and emphasizing product quality. About 85-90% of its magazine content is contributed by readers. Reiman's magazines do not accept ads and rely on subscriptions for almost all revenues. It markets the magazines through direct mail and cross-promotion of titles within its magazine group. Its book publishing operation complements its magazines, with books created from magazine content published in prior years. Reiman's other business include Country Store, catalog sales of country lifestyle products; World Wide Country Tours, offering motorcoach and river barge tours; Reiman Advertising & Promotion, offering savings packs of coupons and promotional advertising in conjunction with the firm's magazines and books; and Homemaker Schools, providing cooking school demonstrations by professional home economists in small and medium size communities across the U.S. Reiman's magazines are listed in Exhibit 1.

In addition to the $760 million cash cost of the Reiman purchase, acquisition costs were expected to total $8.2 million. The fair value of Reiman assets is shown in Exhibit 2. Information about pro forma results, as if the acquisition took place at the beginning of the period presented is in Exhibit 3.

RDA OPERATIONS

In addition to the acquisition, RDA was working to improve its financials in other ways as well. For example, it anticipated that cash and cash equivalents would increase to $108 million in June 2002, up from $35 million the prior year. Its current assets were expected to increase from $$770.6 million to $863.7 million in June 2002. The increase resulted from:

- Lower inventory in the QSP and North American Books and Home Entertainment businesses through better timing of purchases and inventory management practices

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[1] RDA 2001 10K filing

- Lower levels of incentive compensation in 2002, compared to 2001.
- Increased focus on working capital management

RDA just switched from the last-in, first out (LIFO) method of inventory accounting to the first in, first out method. Management believed the change was beneficial because provided greater consistency in accounting for inventories globally[2] and allowed more accurate reporting of the current value of the inventory. Management did not expect the inventory method change to have a material impact on its earnings. In fiscal 2002, the change would mean an increase in inventory of $5.8 million, increase in retained earnings by $3.6 million ($5.8 million minus deferred taxes of $2.2 million).

FINANCING THE ACQUISITION

To finance the Reiman acquisition and other planned projects, RDA was looking at a $950 million term loan agreement with a syndicate of banks and other financial institutions. In addition to paying for the $760 million acquisition, the term loan would be used to repurchase $100 million in shares from the DeWitt Wallace-Reader's Digest Fund, Inc. and the Lila Wallace Reader's Digest Fund, Inc., philanthropic funds that held RDA shares. Fiscal year 2002 repurchases already included buying back 3.6 million shares of stock for a total of $641 million.

The loan was secured by the firm's assets and included covenants limiting additional debt, minimum interest coverage and maximum leverage ratios. The loan agreement called for quarterly principal repayments, starting in the first quarter of fiscal 2003, with the final payment due in 2008. The repayment schedule is detailed in Exhibit 4. The interest is variable rate, reset periodically for six month periods. The interest rate is LIBOR plus a spread based on RDA's credit rating at the time the rate is established. For example, if RDA's credit rating decreased by one increment, then the interest rate would increase by 43 basis points. If the credit rating improved by one increment, then the interest rate would decrease by 13 basis points.

RDA was required by the term loan agreement to hedge at least a third of the outstanding borrowings using interest rate swaps. RDA was looking at agreements to cap at 6% the first $400 million of its borrowings for the first three years of the loan. Because interest rates were low, it anticipated the interest rate on all of its borrowings would be 3.8% for 2002.

FINANCING POLICY

RDA had been conservative in its financing choices in the past. For example, in October 1999 RDA purchased Books Are Fun, Ltd, a company that sold books and gift items by displaying its products on-site and schools and corporate businesses. The purchase price of $393.2 was financed with internal funds and $120 million in bank borrowings. The bank borrowings were repaid during the second quarter of 2000. Since this was before the close of the 2000 fiscal year, the borrowings did not appear on RDA's 2000 annual report. The average interest rate for its borrowings was 6.4%.

While RDA used debt sparingly, it had about $29 million of preferred stock. The preferred and common stock issues are listed in Exhibit 5. RDA also makes use of operating leases for some of its facilities, detailed in Exhibit 6.

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[2] International Financial Reporting Standards (IFRS) require the use of FIFO accounting. The European Union and China, among others, require companies in their countries to use IFRS.

RDA paid an annual dividend of $0.20 on its 102.7 million shares in 2001. The 2002 was expected to remain at $0.20. At a stock price of $20.85 on June 17, 2002, this represents a dividend yield of under 1% on common stock. With expected earnings per share of $1.12 anticipated for fiscal 2002, the $0.20 dividend is a payout of about 18%, compared to 12-13% in the immediate prior years. RDA used to payout a substantially higher amount in dividends until the company reduced dividends dramatically in 1998 and 1999. The firm expects current dividend policies to be more representative of the future than in the late 1990s. RDA's dividend history is detailed in the income statement in Exhibit 7 and Exhibit 8 contains RDA's past balance sheets. Exhibit 9 provides information about Treasury securities, Exhibit 10 contains RDA's past betas and Exhibit 11 industry ratio data.

THE FUTURE FOR RDA

RDA management expected a strong year for fiscal 2003, with EPS of $1.20 to $1.30 expected in 2003. The growth in EPS was expected to come from reduced losses at U.S. Books and Home Entertainment, growth in Books Are Fun and QSP and the contribution that Reiman was expected to make to earnings. Growth was expected to be partially offset by a decline at U.S. Reader's Digest magazine, due in part to expected lower circulation, from 12.5 million to 1 million copies of the magazine by the end of fiscal year 2003. The decline in Reader's Digest subscriptions was attributed in part to the September 11 terrorist attack and the subsequent anthrax scare which made RDA mailings less effective.

THE DECISION

The Board of Directors needed to determine what was the best alternative for financing the Reiman acquisition. The term loan was certainly a good possibility. The board was concerned while they could be certain of the rate today, they could not predict the interest rate very far into the future. What about financing with common equity? Book value per share ranged from $4.40 to $4.75 during the past year, compared to a $23 market price. The board thought this might be a good time to issue common equity, since the firm was experiencing such a high market to book ratio. The dividend yield was so low, the board did not believe it was appropriate to use it as a proxy for the cost of equity, but were unsure about what would be an appropriate cost. The firm believed it could issue $950 in new common stock at a share price of $20.00. RDA had also successfully financed with preferred stock in the past. The dividend yield on $100 par value stock would be 5%, and RDA expected it could issue $950 in preferred stock if it chose not to take the term loan.

Exhibit 1 – Reiman Magazines and Year of First Issue

Light & Tasty (2001)
Country Discoveries (2000)
Quick Cooking (1997)
Birds & Blooms (1998)
Taste of Home (1993)
Reminisce Extra (1993)
Reminisce (1991)
Country Extra (1990)
Country (1987)
Crafting Traditions (1982)
Farm & Ranch Living (1978)
Country Woman (1970)

Exhibit 2 – Assets Acquired from Reiman Holding Company, LLC and its subsidiaries

Reiman assets (in millions)

Current assets	$101.1
Property, plant and equipment	10.7
Identified intangible assets*	206.8
Goodwill	651.7
Other noncurrent assets	23.6
Total assets acquired	$991.9
Current liabilities	(154.2)
Long-term liabilities	(69.5)
Net assets acquired	$768.2

- Identified intangible assets include trade names and customer lists. The fair value of the trade names is estimated at $89.7, assuming an indefinite life. The subscriber lists have a fair value of $117.1 and are amortized over their estimated useful lives, ranging from three to six years. The weighted average useful life of the customer lists is about 3.5 years.

Exhibit 3 – Pro forma results, with the acquisition

	2002	2001
Revenues	$2,648.2	$2,824.4
Operating Profit	$ 184.4	$ 263.1
Net Income	$ 92.3	$ 110.9
Earnings per share		
Basic	$0.91	$1.07

Diluted	$0.90	$1.06

* Note that these numbers are from the RDA June 2001 annual report and represent the company's predictions for June 2002.

Exhibit 4 – Term Loan Repayment Schedule

Mandatory principal repayments in each fiscal year

2003: $132 million
2004: $32 million
2005: $57 million
2006: $82 million
2007: $82 million
2008: $565 million

Total: $950 million

Exhibit 5 – Capital Stock

	2002 (estimated)	2001
First preferred stock		
Par value $1		
Outstanding shares: 2,972,000	$ 3.0	$ 3.0
Dividend: $4/share		
Second preferred stock		
Par value $1		
Outstanding shares: 10,320,000	$10.3	$10.3
Dividend: $4/share		
Third subordinated preferred stock		
Par value $1		
Outstanding shares: 15,502,200	$15.5	$15.5 Dividend: $5/share
Total Preferred Stock*	$28.8	$28.8
Class A nonvoting common stock		
Par value: $0.01		
Outstanding shares: 119,428,472	$ 1.2	$1.2
Class B voting common stock		
Par value $0.01		
Outstanding shares: 21,716,057	$ 0.2	$ 0.2
Total Common Stock	$ 1.4	$ 1.4
Unamortized restricted stock	(4.7)	(0.6)
Total Capital Stock	$25.5	$29.6

* All preferred shares have a liquidation preference of $100 per share. Preferred stock is redeemable at any time for $105 per share plus accrued dividends.

Exhibit 6 – Lease Obligations

Rental expense and sublease income:

	2002 (estimate)	2001	2000
Rental expense	$ 18.9	$17.1	$20.6
Sublease income	(4.9)	(2.6)	(1.6)
Net rental expense	$ 14.0	$14.5	$19.0

Future minimum rental commitments, for noncancelable operating leases are:

	Minimum rental payments	Minimum sublease income	Net
2003	$17.0	$(5.0)	$12.0
2004	14.1	(4.8)	9.3
2005	12.6	(4.9)	7.7
2006	10.7	(4.9)	5.8
2007	10.2	(4.8)	5.4
Later years	64.2	(33.3)	30.9

READERS DIGEST ASSN ANNUAL INCOME STATEMENT

RDA Income Statement ($ MILLIONS, EXCEPT PER SHARE)

	Jun01	Jun00	Jun99	Jun98	Jun97	Jun96	Jun95
Sales							
Cost of Goods Sold	2,518.200	2,553.700	2,532.200	2,633.700	2,839.000	3,098.100	3,068.500
	914.400	901.200	919.800	942.800	980.000	1,031.000	1,149.600
Gross Profit	---------------	---------------	---------------	---------------	---------------	---------------	---------------
	1,603.800	1,652.500	1,612.400	1,690.900	1,859.000	2,067.100	1,918.900
Selling, General, &							

Exhibit 7 – Income statement

Administrative Expense	1,299.600	1,347.800	1,401.700	1,544.500	1,584.500	1,674.000	1,482.300
Operating Income Before Deprec.	304.200	304.700	210.700	146.400	274.500	393.100	436.600
Depreciation, Depletion, & Amortization	56.800	47.500	43.700	46.200	46.700	48.800	44.700
Operating Profit	247.400	257.200	167.000	100.200	227.800	344.300	391.900
Interest Expense	18.300	5.600	5.700	9.400	7.000	2.400	3.300
Non-Operating Income/Expense	(1.900)	15.800	5.900	(49.300)	(10.600)	(204.200)	33.900
Special Items	(39.400)	(3.600)	44.500	0.000	0.000	0.000	0.000
Pretax Income	187.800	263.800	211.700	41.500	210.200	137.700	422.500
Total Income Taxes	55.700	90.000	85.100	23.600	76.700	57.100	158.500
Income Before Extraordinary Items & Discontinued Operations	132.100	173.800	126.600	17.900	133.500	80.600	264.000
Preferred Dividends	1.300	1.300	1.300	1.300	1.300	1.300	1.300
Available for Common	130.800	172.500	125.300	16.600	132.200	79.300	262.700
Earnings Per Share Basic -	1.270	1.630	1.160	0.160	1.240	0.730	2.350
Earnings Per Share Diluted-	1.270	1.161	1.150	0.160	1.240	0.730	2.350
EPS Basic from Operations	1.530	1.650	0.960	0.160	1.240	0.730	2.350
EPS Diluted from Ops	1.510	1.620	0.960	0.160	1.240	0.730	2.350
Dividends Per Share	0.200	0.200	0.375	0.900	1.800	1.750	1.550
Com Shares for Basic Eps	102.700	106.000	107.300	106.500	106.700	107.900	112.000
Com Shares for Diluted EPS	103.700	107.000	108.000	106.700	106.700	107.900	112.000

* Note: Operating Profit is Earnings Before Interest and Taxes (EBIT).

Exhibit 8 – Balance Sheet

READERS DIGEST ASSN — ANNUAL BALANCE SHEET
TICKER: RDA — ($ MILLIONS)

	Jun01	Jun00	Jun99	Jun98	Jun97	Jun96	Jun95
ASSETS							
Cash & Equivalents	35.400	49.700	413.400	122.800	71.700	277.000	307.600
Net Receivables	305.100	285.300	319.900	376.400	426.300	412.400	396.400
Inventories	161.600	120.300	94.900	162.200	167.800	204.400	188.600
Other Current Assets	268.500	317.200	318.300	311.200	260.000	310.300	322.500
Total Current Assets	770.600	772.500	1,146.500	972.600	925.800	1,204.100	1,215.100
Gross Plant,Property & Equipment	350.400	419.300	447.700	622.400	670.000	604.400	592.300
Accumulated Depreciation	190.200	266.900	299.300	337.000	355.200	342.900	335.700
Net Plant,Property & Equipment	160.200	152.400	148.400	285.400	314.800	261.500	256.600
Investments at Equity	10.800	0.000	0.000	0.000	0.000	0.000	0.000
Other Investments	2.500	173.500	0.000	0.000	73.000	137.000	267.600
Intangibles	409.800	438.800	68.500	41.800	59.100	58.400	77.600
Deferred Charges	0.000	0.000	78.200	0.000	0.000	0.000	0.000
Other Assets	321.200	221.600	268.900	264.200	271.100	243.100	141.800
TOTAL ASSETS	1,675.100	1,758.800	1,710.500	1,564.000	1,643.800	1,904.100	1,958.700
LIABILITIES							
Long Term Debt Due In One Year	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Notes Payable	160.300	89.400	0.000	0.000	30.400	0.000	0.000
Accounts Payable	86.400	146.400	130.700	172.100	211.800	216.000	224.800
Taxes Payable	41.200	38.700	56.000	21.000	22.100	67.300	79.000
Accrued Expenses	251.100	309.600	352.200	377.400	373.600	457.300	358.700
Other Current Liabilities	320.500	320.300	447.400	445.400	375.200	372.400	409.600
Total Current Liabilities	859.500	904.400	986.300	1,015.900	1,013.100	1,113.000	1,072.100
Long Term Debt	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Deferred Taxes	9.900	8.100	23.300	11.100	9.800	13.200	12.800
Investment Tax Credit	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Minority Interest	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Other Liabilities	349.500	342.000	319.400	278.400	274.900	299.000	233.000
TOTAL LIABILITIES	1,218.900	1,254.500	1,329.000	1,305.400	1,297.800	1,425.200	1,317.900
EQUITY							
Preferred Stock - Redeemable	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Preferred Stock - Nonredeemable	28.800	28.800	28.800	28.800	28.800	28.800	28.800
Total Preferred Stock	28.800	28.800	28.800	28.800	28.800	28.800	28.800

Common Stock	1.400	1.400	1.400	1.400	1.400	1.400	1.400
Capital Surplus	225.500	221.800	140.800	131.200	140.600	136.500	117.600
Retained Earnings	1,103.100	1,137.600	898.800	795.200	890.500	968.500	1,098.300
Less: Treasury Stock	902.600	885.300	688.300	698.000	715.300	656.300	605.300
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Common Equity	427.400	475.500	352.700	229.800	317.200	450.100	612.000
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TOTAL EQUITY	456.200	504.300	381.500	258.600	346.000	478.900	640.800
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TOTAL LIABILITIES & EQUITY	1,675.100	1,758.800	1,710.500	1,564.000	1,643.800	1,904.100	1,958.700
COMMON SHARES	102.650	102.900	107.633	107.162	106.318	107.650	108.213

Exhibit 9 – Treasury Yields

6 month Treasury		1 year Treasury		5 year Treasury		10 year Treasury	
Jan-02	1.77	Jan-02	2.16	Jan-02	4.34	Jan-02	5.04
Feb-02	1.86	Feb-02	2.23	Feb-02	4.3	Feb-02	4.91
Mar-02	2.06	Mar-02	2.57	Mar-02	4.74	Mar-02	5.28
Apr-02	1.98	Apr-02	2.48	Apr-02	4.65	Apr-02	5.21
May-02	1.91	May-02	2.35	May-02	4.49	May-02	5.16
Jun-02	1.83	Jun-02	2.2	Jun-02	4.19	Jun-02	4.93

Exhibit 10 – Reader's Digest Beta

Date	**5 Year Regression Beta**	3 Year Regression Beta	Research Insight Beta
June-95	**0.724**	0.209	N/A
June-96	**0.440**	0.182	
June-97	**0.153**	0.076	
June-98	**0.172**	0.196	
June-99	**0.740**	0.883	
June-00	**0.687**	0.726	
June-01	**0.674**	0.880	0.632
June-02	**0.870**	0.798	0.844

Historical Market Risk Premium: 6%
Note that the five year regression betas calculate beta from the date listed, including the previous five years of data. The three year regression betas represent beta on the date listed using the previous three years of data.

Exhibit 11 – Industry Ratios

Ratio Analysis (Ratio Except as Noted)

	2001	2000	1999	1998	1997	1996	1995
Leverage							
Debt to Total Equity	0.679	0.357	0.363	0.471	0.461	0.530	0.525
Times Interest Earned	6.302	9.957	7.433	4.914	9.011	4.995	8.383
Liquidity							
Current Ratio	1.152	1.104	1.252	1.227	1.158	1.264	1.231
Cash Flow Per Share ($)	1.674	1.617	1.309	0.984	1.485	0.917	1.235
Activity							
Operating Cycle (Days)	145.089	139.149	144.187	149.898	158.137	148.911	139.149
Fixed Asset Turnover	11.021	11.218	10.852	9.834	9.242	9.958	9.808
Profitability							
Return on Avg Total Assets (%)	8.319	9.630	7.949	5.426	10.286	5.661	9.028
Return on Avg Total Equity (%)	23.091	25.528	22.411	15.968	31.359	17.539	27.526
Profit Margin (%)	7.132	8.050	6.696	4.611	8.973	4.586	7.560
Market Information							
Price Close *	29.977	32.604	29.238	20.735	18.037	27.160	29.001
Dividends Per Share (Exdate) *	0.378	0.351	0.365	0.477	0.848	0.919	0.910
Earnings Per Share *	1.206	1.236	0.957	0.585	1.154	0.658	1.537
EPS from Basic Operations *	1.355	1.207	0.894	0.586	0.831	0.686	1.537
Price-Earnings Ratio *	24.849	26.373	30.537	35.466	15.631	41.281	18.864
Price/EPS from Basic Operations	22.120	27.009	32.718	35.399	21.706	39.596	18.864
Market Value **	18.488	24.090	27.865	26.118	36.787	44.935	51.739
Price to Book Value *	6.189	7.224	7.726	6.812	5.529	6.758	5.777

* Industry figure represents weighted average industry item

** Industry figure represents percentage of total industry known as:

Books: Publishing and Publishing and Printing

Reader's Digest Teaching Note

Case Synopsis

The Reader's Digest Association (RDA) case is a fairly straightforward decision between debt, equity or preferred stock. RDA publishes its flagship magazine, Reader's Digest, along with other periodicals and books. RDA has just agreed make a substantial purchase, acquiring Reiman Holding Company, a book and magazine publishing company which it believes will complement its existing businesses. The company wants to raise $950 million, mostly for the Reiman purchase. The company must choose between a term loan, common equity and preferred stock to finance the purchase.

Audience for the case

This case is intended for an advanced undergraduate or an MBA corporate finance elective.

Teaching Objectives

The objectives of this case include:

- Opportunity to analyze an acquisition financing decision
- Value debt and find the cost of equity
- Use EBIT/EPS analysis to evaluate financing decisions
- Evaluate a firm's creditworthiness

Theory Application

Research Methods

The primary data source is Reader's Digest Association filings with the SEC.

Suggested Teaching Approaches

Discussion Questions and Answers

1. Perform a ratio analysis of RDA. What are RDA's strengths and weaknesses? What is the firm's overall creditworthiness? What is RDA's Altman's Z score?
2. What is an appropriate cost of equity for RDA? How should the board assess the cost of equity if it chooses to finance the acquisition through new common equity? How does the firm's dividend policy impact its financing decision? What are the benefits and costs of issuing common equity?
3. What is the present value of the term loan? Assume a 3.8% cost in the first year of the loan and 6% in subsequent years. What are the benefits and costs of the term loan?
4. How does the preferred stock alternative compare to the debt and equity alternatives?
5. What is the impact on 2002 EPS of each of the financing alternatives? In other words, what EPS would result with each alternative? What is the breakeven EBIT for the debt

alternative vs. the common equity alternative? For the preferred stock alternative vs. the common equity alternative?

6. Using a FRICT analysis framework, what alternative should RDA choose?

Answers to Study Questions

1. Perform a ratio analysis of RDA. What are RDA's strengths and weaknesses? What is the firm's creditworthiness? What is RDA's Altman's Z score?

A financial statement analysis and ratio analysis of RDA are provided in TN Exhibits 1 and 2.

Liquidity

RDA's current ratio has been consistently low, and well below the industry average. RDA's current ratio ranges from its high of 1.162 (in June 1999) to its low of 0.854 (June 2000); whereas the industry current ratio hit a high in 1999 and 2001 of 1.152 and a low in 2000 of 1.104. In general, lenders prefer a current ratio above 2 times; RDA's has never been this high during the period presented in the case. RDA's quick ratio is especially low, declining from 0.66 in 1995 to 0.4 in 2001. RDA has had negative working capital per share in the most recent years, 2000 and 2001.

Efficiency and Profitability

RDA's inventory turnover has remained reasonably stable during the time period of the case (starting at 6.461 in June '95, and ending at 5.742 in June '02), and its receivables turnover improved slightly. However, its average collection period is well above 30 days. If the firm offers 30 day terms to its customers, then it is slow in collecting. Total asset turnover has been consistently low compared to the industry average. RDA has improved its Sales to Fixed Assets ratio and its operating margin has increased steadily since a low in 1998, as has its net margin. RDA's return on assets has also increased dramatically since 1998 and is generally close to the industry average ROA. Return on equity has been high, except in 1998, and is considerably higher than the industry average ROE. RDA's operating ratios are generally better than industry averages (for example, RDA's net margin ratio is 9.10, compared to the industry 7.13%. RDA's operating cycle is shorter at 107 days than the industry at 145 days. It is utilizing its fixed assets better with a ratio of 15.72 compared to the industry 11.02.

Ratio Analysis (Ratio Except as Noted)

	2001	2000	1999	1998	1997	1996	1995
Current Ratio	1.152	1.104	1.252	1.227	1.158	1.264	1.231
Return on Avg Total Assets (%)	8.319	9.630	7.949	5.426	10.286	5.661	9.028
Return on Avg Total Equity (%)	23.091	25.528	22.411	15.968	31.359	17.539	27.526
Operating Cycle (Days)	145.089	139.149	144.187	149.898	158.137	148.911	139.149
Fixed Asset Turnover	11.021	11.218	10.852	9.834	9.242	9.958	9.808

Debt Ratios

RDA's interest coverage has been consistently higher, and usually considerably greater than the industry average. With no debt, RDA has been very underlevered, compared with the industry, which has had debt ratios ranging from 36% to 68% over the time period of the case.

Industry Ratios

Ratio Analysis (Ratio Except as Noted)

	2001	2000	1999	1998	1997	1996	1995
Debt to Total Equity	0.679	0.357	0.363	0.471	0.461	0.530	0.525
Times Interest Earned	6.302	9.957	7.433	4.914	9.011	4.995	8.383

While RDA's financial statements might raise some questions for lenders, particularly concerning liquidity, RDA seems to be a good candidate for a loan.

The Altman's Z score measures probability of bankruptcy. The lower the score, the higher the odds of bankruptcy. A Z-score of less than 1.8 is an indication that the company may be heading for bankruptcy. Companies with scores above 3 are unlikely to enter bankruptcy. Scores between 1.8 and 3 are a grey area – the company may be healthy and may be in financial difficulty. Altman's Z for publicly traded manufacturers is:

Z = 1.2A + 1.4B + 3.3C + 0.6D + 1.0E, where:
A = working capital/Total Assets
B = Retained earnings/Total Assets
C = Earnings before Interest and Taxes/Total Assets
D = Market Value of Equity/Total Liabilities
E = Sales/Total Assets

For 2001 for RDA,
Current assets = $770.6
Current liabilities = $859.5
Retained earnings = 1,103.1
Total assets = 1,675.1
EBIT = 247.4
Market value of equity = number of shares x price per share = 102.7 x $20.45 = $2,100.215
Total liabilities = 1,218.9
Sales = 2,518.2

A = (770.6-859.5)/1675.1 = -0.053
B = 1103.1/1675.1 = 0.6585
C = 247.4/1675.1 = 0.1477
D = 2100.215/1218.9 = 1.723
E = 2518.2/1675.1 = 1.5033

Z = 1.2*(-0.053) + 1.4*0.6585 + 3.3*0.1477 + 0.6*1.723 + 1*1.5033 = 3.88

For a private, non manufacturer, Altman's Z is:
Z = 6.56A + 3.26B + 1.05C + 6.72D = 6.56*-0.053 + 3.26*.6585 + 1.05*0.1477 + 6.72*0.35 = 4.3

(In this equation, all the variables are the same as above, except for D, which is book value of equity/total liabilities, in this case 427,400/1,218,900 = 0.35.

RDA's Z score is in the positive, financially healthy area – low risk of bankruptcy.

2. What is an appropriate cost of equity for RDA? How should the board assess the cost of equity if it chooses to finance the acquisition through new common equity? How does the firm's dividend policy impact its financing decision? What are the benefits and costs of issuing common equity?

RDA's cost of equity can be computed using the capital asset pricing model and information from the case.

$$k_e = k_{rf} + \beta(k_m - k_{rf})$$

Using the 10 year Treasury rate of 4.93% as the risk-free rate, 6% as the historical risk premium, and 0.87 as RDA's beta, the cost of equity is 4.93 + 0.87(6) = 10.15%. Shareholders are expecting RDA to earn at least a 10% return on their stock investment.

However, these numbers will change if RDA does take on $950 million in debt. Its new book value debt ratio would be: 950/1675.1 = 0.57 and its new market value debt equity ratio would be 950/2141 = 0.44. (Market value of equity = 102.7 million shares x $22,85 = 2,141. Re-levering RDA's beta, using market value weights:

$\beta_L = \beta_u(1 + \frac{D}{E}(1-T))$ yields $\beta_L = 0.87(1 + 0.44(1-0.34)) = 1.12$

The new cost of equity reflecting the higher risk because of the additional debt would be:
4.93 + 1.12(6) = 11.65%.

RDA's cost of equity is the sum of its dividend yield and its growth rate. The board cannot use dividend yield as a proxy for cost of equity – shareholders are expecting their investment to grow in value through reinvestment of the earnings that are retained in the firm.

The discounted cash flow model cannot be easily used in this case to calculate a cost of equity:

$$k_e = \frac{\text{Dividend}_1}{P_0} + g$$

RDA is expected to pay of dividend of $0.20 in a few weeks. This can be use as dividend_0.
RDA's current stock price is $20.85. RDA's past growth in dividends can be calculated:
1995-6: 12.9%
1996-7: 2.9%
1997-8: -50%
1998-9: -58.3%
1999-2000: -46.7%
2000-2001: 0%
This is an arithmetic average of -23% and a geometric growth of -22%.
Arithmetic Average=(12.9+2.9+-50+-58.3+-46.7+0)/6=-23.2%

Geometric growth= (12.9)(2.9)(-50)(-58.3)(-46.7)^(1/5)=-21.947%

The dividend does not enter explicitly into the financing decision. However, any funds paid out as dividends are not available for reinvestment in the firm. The firm must seek outside funds if its investing needs are greater than its retained earnings.

Issuing equity usually has higher costs than issuing debt and preferred stock. At a cost of $0.85 per share, to raise $950 million at $20 a share, RDA would need to issue 47,500,000 new common shares. The total cost would be $0.85 x 47,500,000 = $40,375,000. In addition, existing shareholders would have their equity position diluted. RDA has 102,650,000 common shares. Adding 47.5 million shares would mean dilution of 47.5/(47.5+102.65) or 32%, a substantial amount of dilution. Firms may choose to issue equity to avoid overlevering the firm – this is not the case with RDA which has no debt at the time of the case.

Benefits of issuing common equity include:

- There is no obligation to declare a monetary dividend. The corporation cannot default on an undeclared dividend.
- Different classes of common equity can be issued to maintain the rights and privileges of existing shareholders.
- No maintenance of debt covenants or collateral.

Costs of issuing common equity include:

- 10-15% discount for additional common equity compared to the market share price.
- High transaction cost of issuing new common equity (7-10%, on average)
- Dilution of control over the company
- Additional shares in the market may lower the market price
- Cost of equity is higher than the cost of debt
- No deductibility of dividends for tax purposes, unlike debt interest payments, which are tax deductible.

3. What is the present value tax shield of the term loan? Assume a 3.8% cost in the first year of the loan and 6% in subsequent years. What are the benefits and costs of the term loan?

The term loan would have the following cash flows:

Term loan cash flows							
	2002	2003	2004	2005	2006	1007	2008
Balance	950	818	786	729	647	565	0
Principal repayment		132	32	57	82	82	565
Interest expense		36.1	49.08	47.16	43.74	38.82	33.9
Tax shield (35% tax rate)		12.635	17.178	16.506	15.309	13.587	11.865
Present value tax shield		76.82					

This assumes a 35% tax rate, 3.8% interest on a 950 million principal amount in 2003, and 6% interest on the remaining loan balances. The tax shield is discounted at a 3.8% discount rate.

The loan is the only alternative which provides a tax shield. The term loan has less of a tax shield than permanent debt. The present value tax shield of permanent debt is the amount of debt times the tax rate, or $950 million x 0.35 = $332.5 million. RDA is losing a great deal of potential tax shield by choosing a term loan instead of permanent debt. $76.82M is significantly less than $332.5M.

The main cost of debt is the increased risk of bankruptcy. If RDA adds $950 million to its assets, and takes on $950 million in debt, its new debt to assets ratio would be:
$\frac{950}{950+1675.1} = 0.36$. This is still well below the current industry average of 0.68. RDA's times interest earned ratio with the debt, assuming the same EBIT as in 2001, would be:
$\frac{247.4}{18.3+36.1} = 4.5 \text{ times}$
This is still a respectable interest coverage ratio.

Benefits of the term loan include:
- Tax deductibility of interest payments on the term loan
- Interest payments are capped. In other words, if the firm does well, bondholders only receive interest payments; shareholders benefit from increased shareholder wealth if the firm is doing well.
- No dilution of control
- Potential increase in value of the firm as long as the debt is manageable and doesn't lead to bankruptcy.

Costs of the term loan include:
- Cost of distress if the firm has too much debt in its capital structure.
- Mandatory fixed payments, even if the firm does not have the income to handle the payments.
- Liquidation preference over common stockholders.

4. How does the preferred stock alternative compare to the debt and equity alternatives?

6% interest on remaining loan balances (beginning in 2003)
35% Tax Rate
The preferred stock alternative does not have the tax advantages of the debt alternative. The after-tax cost of debt is 0.06(1-0.35) = 0.39. The preferred stock alternative costs 5%. (See "The Decision" section of the case.) Preferred stock is not used a great deal by financially healthy companies like RDA. Preferred stock is used the most by regulated utilities which can pass on the costs of preferred stock to their customers and by financially distressed companies. Financially distressed companies may benefit from preferred stock because, first, they may not have any income to shield if they are distressed. Second, preferred stock is generally more flexible than debt when a company is financially distressed. Missing a loan payment can force a firm into bankruptcy. Missing a preferred stock dividend is bad news, but will not automatically force a company into bankruptcy. Most preferred stock issues have cumulative dividends – if a

dividend payment is missed, then it must be made up before common stock dividends may be paid.

5. What is the impact on 2002 EPS of each of the financing alternatives? In other words, what EPS would result with each alternative? What is the breakeven EBIT for the debt alternative vs. the common equity alternative? For the preferred stock alternative vs. the common equity alternative?

An EBIT/EPS analysis can show the benefits to EPS and ROE for each of the alternatives. The analysis makes the following assumptions:

2002

Expected EBIT with the acquisition: $184.4 million (operating profit from Exhibit 3)
Addition to assets: $950 million
Interest expense under the common equity and preferred stock alternatives: $18.3 million
(Interest from revolving credit lines listed on firm's 2001 income statement)
Interest expense under the term loan alternative: $18.3 + 36.1 = $54.4 million
Note that using 2002 interest expense in our EBIT/EPS analysis may understate the true cost of debt because we are only paying 3.8% in 2002 and 6% from 2003 on. The breakeven point using 2003 interest is about 173 million much greater than 132 million.
Preferred dividends under the common equity and term loan alternatives:
2,972,000 x $4 = $11,888,000
10,372,000 x $4 = $41,488,000
15,502,200 x $5 = $77,511,000
Total: $130,887,000

New preferred stock dividends:
$950,000,000 in preferred stock, $100 par value
9,500,000 new preferred stock shares
New dividend: 9,500,000 x $5 = $47,500,000
Total preferred dividends under preferred stock plan: $178,387,000

Number of common shares under the preferred stock and debt plans: 102.65 million
Number of new common shares under the common equity plan:

$$\frac{950{,}000{,}000}{20} = 47{,}500{,}000 \text{ new shares}$$

New common share price $20.
Common shares under the equity plan: 105.65+47.5 = 150.15 million shares

Breakeven point between common stock and debt:

Solving for breakeven EBIT,

$$\text{Breakeven point: } \frac{(\text{EBIT*}-54.4)(1-0.35)}{102.65} = \frac{(\text{EBIT*}-18.3)(1-0.35)}{150.15}$$

The breakeven point between common stock and debt is: $132.414 million in EBIT

Breakeven point: $\frac{(\text{EBIT*-Interest}_{\text{preferred stock}})(1\text{-T})\text{-Preferred dividends}}{\text{Number of common shares}_{\text{preferred stock}}} = \frac{(\text{EBIT*-Interest}_{\text{equity}})(1-\text{T})}{\text{Number of common shares}_{\text{equity}}}$

Solving for breakeven EBIT:

Breakeven point: $\frac{(\text{EBIT*-18.3})(1\text{-0.35})\text{-47.5}}{102.65} = \frac{(\text{EBIT*-18.3})(1-0.35)}{150.15}$

The breakeven point between common stock and preferred stock is: $249.3 million in EBIT. (Note that this calculation ignores existing preferred stock dividends. With existing preferred dividends, the equation becomes:

Breakeven point: $\frac{(\text{EBIT*-18.3})(1\text{-0.35})\text{-178.4}}{102.65} = \frac{(\text{EBIT*-18.3})(1-0.35)\text{-130.9}}{150.15}$

The breakeven EBIT using all preferred stock dividends is $450.7 million.The expected EBIT, or operating profit, for 2002 with the acquisition is $184.4 million, above the breakeven for debt/equity but not for preferred stock/equity.

Looking at this graphically, assume expected EBIT for 2002 is $184.4. Income statements for each alternative at this EBIT will look like:

	Debt	Common Equity	Preferred Stock
EBIT	$184.4	$184.4	$184.4
Interest	54.4	18.3	18.3
EBT	$130.0	$166.1	$166.1
Taxes (35%)	52.0	58.135	58.135
Net income	$ 78.0	$107.965	$107.965
No. of shares	102.65	150.15	102.65
EPS	$0.76	$0.71	$1.052
EPS to Common	$0.76	$0.71	$0.589*

*Net income of $107.965 minus new preferred dividends of $47.5 = $60.465 available to common shareholders. EPS = 60.465/102.65 = $0.589.

To plot these points on an EPS/EBIT graph you need two points. For the debt alternative, the first point is (184.4,0.76). A good second point is where EBIT exactly equals interest:

	Debt	Common Equity	Preferred Stock
EBIT	$54.5	$18.3	$18.3 + 47.5/(1-0.35) = 91.38
Interest	54.5	18.3	18.3
EBT	$ 0	$ 0	$73.08
Taxes	$ 0	0	25.58
Net income	$ 0	0	47.5
Preferred div.			47.5
EPS	$ 0	0	0

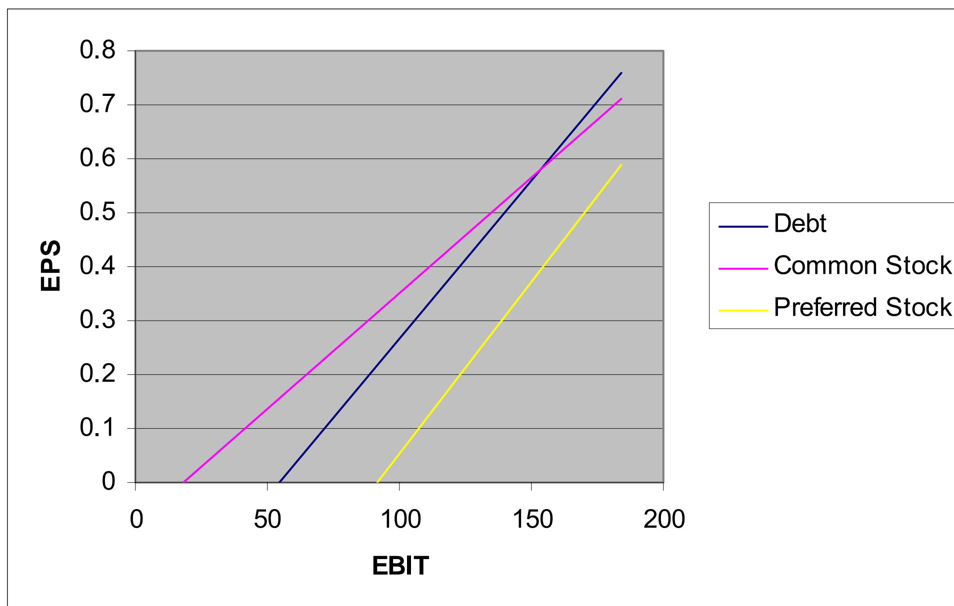
So, a second point is (54.5,0). In other words, the EBIT/EPS line intersects the X axis at the amount of interest expense, providing 0 EPS to common shareholders.

Now, this is an inaccurate way of looking at the debt alternative from the shareholders point of view. RDS will have a principal payment of $132 to make in the second year, so less income will be available to shareholders in year two of the term loan.

These numbers will change in 2003. Assume EBIT will be $170. (EBIT has been declining for RDA during the time period of the case.)

	Debt	Common Equity	Preferred Stock
EBIT	$170.0	$170.0	$170.0
Interest	67.4	18.3	18.3
EBT	$102.6	$151.7	$151.7
Taxes (35%)	35.9	53.1	53.1
Net income	$ 66.7	$ 98.6	$ 98.6
Pref. div			47.5
NI to common			51.1
No. of shares	102.65	150.15	102.65
EPS	$0.65	$0.66	$0.50
Sinking fund	$132		
EPS to Common	$0	$0.66	$0.50

Because of the large principal repayment due in the second year, the debt alternative looks less attractive in the second year of the term loan.



6. Using a FRICT analysis framework, what alternative should RDA choose?

Flexibility: the ability to meet unforeseen financing requirements as they arise (either favorable, like a sudden acquisition opportunity, or unfavorable, like an unexpected environmental/safety hazard such as Exxon's oil tanker accident. Flexibility may involve liquidating assets or obtaining extra funds from the capital markets, or both. Flexibility can be measured by bond ratings (high rating is more flexible), coverage ratios and liquidity ratios (higher is more flexible), capitalization ratios (lower is more flexible), and identification of salable assets. Questions to ask:

- What are the company's future financing needs?
- Is the company a stable, low growth company?
- Do they anticipate making high dollar purchases, like acquiring another company?
- Are they unsure about their future?
- Are they a high quality company?

Historically, RDA has been a stable/moderate growth company. The future outlook is relatively good. However, the current acquisition is of the same size as RDA itself. Financing such an acquisition through debt may reduce RDA's future flexibility. RDA does not appear to need a great deal of flexibility. There is no indication that they are embarking on a program of acquisitions. In fact, the company appears to be downsizing its business. On the other hand, RDA could have to pass on future acquisitions or capital opportunities in the future if it takes on debt for this acquisition. RDA has a long, stable history. The company appears to be a reasonable candidate for debt financing.

Risk: the predictable variability in the firm's business (total risk, not just beta). Such variability may be due to macroeconomic factors or to industry or firm specific factors. To some extent, past experience may indicate the future range of variability in earnings before interest and taxes (EBIT) or Net Operating Income (NOI) and cash flow. High leverage tends to amplify these predictable business swings. The risk associated with any given financial structure can be assessed by EBIT-EPS analysis, break even analysis, the standard deviation of EBIT and beta. Questions to ask:

- What is the company's and the industry's risk of bankruptcy?
- Does the firm have tangible or intangible assets?
- Are they high growth or mature?
- Are cash flows stable or unpredictable?
- Does the firm make heavy capital expenditures?
- Is the firm profitable overall? How about when compared to other firms in the same industry?

RDA appears to be at low risk for bankruptcy. It is a mature, profitable company with stable cash flows. They have both tangible (production facilities) and intangible assets (customer lists, brand names). The firm has gone a long way in improving its profitability since the low point in the late 1990s. The firm again is a good candidate for debt financing. The expected EBIT is well above the breakeven point for the debt alternative. Atman's Z score indicates that

bankruptcy is unlikely. The overall economy is stable and the industry is not volatile. The firm has sufficient debt capacity to finance this acquisition with debt.

Income: this compares financial structures on the basis of value creation. Measures such as NPV (discounted cash flow value), projected ROE, EPS, and the cost of capital indicate the comparative vale effects of alternative financing structures. Question to ask:

- What financing strategy provides the highest income per shareholders, as measured by ROE and EPS?

The debt alternative provides more earnings per shareholder than the common equity alternative. However, the preferred stock alternative provides more income per shareholder than either debt or common equity. In general, debt is the better alternative. It is the only one that provides positive present value to the shareholders. Preferred stock is showing more income to shareholders in large part because of the terms of the loan.

Control: alternative financial structures may imply changes in control or different control constraints on the firm as indicated by the percentage distribution of share ownership, by the structure of debt covenants, and by how much dilution is caused by a new equity issue. Questions to ask:

- Will issuing equity cause a potential control problem?
- Is this a closely-held company, where management owns a large portion of the stock, and is unwilling to give up control?
- Or, are shareholders diverse, so a new equity issue is less likely to shift control?

RDA is a large, publicly traded company. The firm is not likely to be concerned about losing control through issuing equity. There are about 100 million shares outstanding. If additional common shares of $950 million are issued at $20 a share, then an additional 47.5 million shares will be issued. This represents a dilution of control of about one-third. Dilution can be avoided if the acquisition is financed through debt.

Timing: asks questions about whether the current capital market environment is the right moment to implement any alternative financial structure, and what the implications of future financings will be if the proposed structure is adopted. The current market environment can be assessed by examining the Treasury yield curve, the trend in the movement of interest rates, the existence of any "windows" in the market for new issues of securities (in other words, is it a hot market to issue equity), and P/E multiple trends. Questions to ask:

- Are stock prices and interest rates high or low?
- What do you expect the stock market prices and interest rates to be in the future
- What signal issuing either debt or equity will send.

RDA's stock price has been declining. Management may be concerned that issuing equity might send a negative signal to the market. However, the market to book ratio is high ($20 market price vs. $4 book value per share, a market to book ratio of 5 times.) The proposed interest rate is reasonable – just above the risk free rate. RDA's credit rating must be good to be able to obtain such a low interest rate. If the acquisition is made using debt, it is more likely that the share price will increase, assuming the current P/E ratio is maintained. Financing the acquisition

with debt signals the market that management is confident about the proposed acquisition and that it will be a success.

Other: anything else that doesn't fit into the above categories. For example, is management unusually risk averse and unwilling to take on debt? There may be other specialized considerations. A sole owner of a closely-held company might worry significantly about the effect of various financing tactics on the liquidity of the investment in the event that he or she decides to sell out.

TN Exhibit 1 - READERS DIGEST ASSN - Financial Statement Analysis

Balance Sheet	2002	% Chg	2001	% Chg	2000	% Chg	1999	% Chg
Current Assets	863.7	12.082	770.6	-0.246	772.5	-32.621	1,146.50	17.88
Current Liabilities	980.8	14.113	859.5	-4.965	904.4	-8.304	986.3	-2.914
Other Assets	1,839.00	103.317	904.5	-8.294	986.3	74.876	564	-4.633
Total Liabilities	2,230.80	83.017	1,218.90	-2.838	1,254.50	-5.606	1,329.00	1.808
Shareholders Equity	471.9	3.441	456.2	-9.538	504.3	32.189	381.5	47.525
Income Statement								
Sales	2,368.60	-5.941	2,518.20	-1.39	2,553.70	0.849	2,532.20	-3.854
Cost of Goods	911.8	-0.284	914.4	1.465	901.2	-2.022	919.8	-2.44
Net Income	91.2	-30.961	132.1	-23.993	173.8	14.417	151.9	748.603
Statement of changes								
Operating cash flows	132.5	693.413	16.7	-90.452	174.9	-21.393	222.5	136.954
Investing Cash Flows	-772.9	-1,312.98	-54.7	88.738	-485.7	523.822	114.6	71.557
Financing cash flows	715.5	1,887.50	36	186.331	-41.7	-14.56	-36.4	64.557
Dividends	21.3	-2.74	21.9	-3.097	22.6	-45.542	41.5	-57.261
Capital Expenditures	25.9	-61.63	67.5	-48.669	131.5	111.755	62.1	70.604

Balance Sheet	1998	% Chg	1997	% Chg	1996	% Chg	1995	% Chg
Current Assets	972.6	5.055	925.8	-23.113	1,204.10	-0.905	1,215.10	1.491
Current Liabilities	1,015.90	0.276	1,013.10	-8.976	1,113.00	3.815	1,072.10	3.094
Other Assets	591.4	-17.632	718	2.571	700	-5.863	743.6	-12.734
Total Liabilities	1,305.40	0.586	1,297.80	-8.939	1,425.20	8.142	1,317.90	4.73
Shareholders Equity	258.6	-25.26	346	-27.751	478.9	-25.265	640.8	-18.987
Income Statement								
Sales	2,633.70	-7.231	2,839.00	-8.363	3,098.10	0.965	3,068.50	9.339
Cost of Goods	942.8	-3.796	980	-4.947	1,031.00	-10.317	1,149.60	10.754
Net Income	17.9	-86.592	133.5	65.633	80.6	-69.47	264	7.192
Statement of changes								
Operating cash flows	93.9	-3.494	97.3	-18.372	119.2	-50.416	240.4	-23.711
Investing Cash Flows	66.8	306.173	-32.4	-122.594	143.4	-34.069	217.5	1,129.68
Financing cash flows	-102.7	58.269	-246.1	-14.359	-215.2	51.124	-440.3	-44.265
Dividends	97.1	-49.767	193.3	1.683	190.1	8.319	175.5	11.277
Capital Expenditures	36.4	-72.775	133.7	-47.341	253.9	30.54	194.5	-39.07

TN Exhibit 2

READERS DIGEST ASSN ANNUAL RATIO REPORT

TICKER: RDA

LIQUIDITY	June-02	June-01	June-00	June-99	June-98	June-97	June-96	June-95
Current Ratio	0.881	0.897	0.854	1.162	0.957	0.914	1.082	1.133
Quick Ratio	0.422	0.396	0.370	0.743	0.491	0.492	0.619	0.657
Working Capital Per Share	(1.177)	(0.866)	(1.282)	1.488	(0.404)	(0.821)	0.846	1.321
Cash Flow Per Share	1.277	1.840	2.151	1.582	0.598	1.695	1.202	2.853
ACTIVITY								
Inventory Turnover	5.742	6.487	8.375	7.155	5.714	5.266	5.247	6.461
Receivables Turnover	7.752	8.530	8.439	7.273	6.562	6.770	7.661	7.776
Total Asset Turnover	1.082	1.467	1.472	1.547	1.642	1.600	1.604	1.531
Average Collection Period (Days)	46.440	42.202	42.658	49.496	54.860	53.176	46.991	46.298
Days to Sell Inventory	62.698	55.492	42.983	50.313	63.004	68.363	68.613	55.723
Operating Cycle (Days)	109.138	97.694	85.641	99.809	117.864	121.539	115.604	102.020
PERFORMANCE								
Sales/Net Property, Plant & Equip	14.090	15.719	16.757	17.063	9.228	9.018	11.847	11.958
Sales/Stockholder Equity	5.019	5.520	5.064	6.637	10.184	8.205	6.469	4.789
PROFITABILITY								
Operating Margin Before Depr (%)	9.301	12.080	11.932	8.321	5.559	9.669	12.688	14.228
Operating Margin After Depr (%)	7.785	9.824	10.072	6.595	3.805	8.024	11.113	12.772
Pretax Profit Margin (%)	5.936	7.458	10.330	8.360	1.576	7.404	4.445	13.769
Net Profit Margin (%)	3.850	5.246	6.806	5.000	0.680	4.702	2.602	8.604
Return on Assets (%)	3.326	7.808	9.808	7.325	1.061	8.042	4.165	13.412
Return on Equity (%)	20.289	30.604	36.278	35.526	7.224	41.677	17.618	42.925
Return on Investment (%)	6.970	28.672	34.206	32.844	6.419	38.208	16.559	40.996
Return on Average Assets (%)	4.107	7.618	9.944	7.653	1.035	7.452	4.106	13.109
Return on Average Equity (%)	20.655	28.973	41.657	43.021	6.069	34.458	14.933	38.235
Return on Average Investment (%)	10.297	27.236	38.948	39.150	5.491	32.052	14.165	36.474
LEVERAGE								
Interest Coverage Before Tax	8.559	11.262	48.107	38.140	5.415	31.029	58.375	129.030
Interest Coverage After Tax	5.903	8.219	32.036	23.211	2.904	20.071	34.583	81.000
Long-Term Debt/Common Equity (%)	184.608	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Long-Term Debt/Shrhldr Equity(%)	173.342	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Total Debt/Invested Capital (%)	73.703	35.138	17.728	0.000	0.000	8.786	0.000	0.000
Total Debt/Total Assets (%)	35.176	9.570	5.083	0.000	0.000	1.849	0.000	0.000
Total Assets/Common Equity	6.100	3.919	3.699	4.850	6.806	5.182	4.230	3.200
DIVIDENDS								
Dividend Payout (%)	22.247	15.749	12.348	32.083	577.108	145.234	238.083	66.311
Dividend Yield (%)	1.068	0.696	0.503	0.943	3.318	6.261	4.118	3.513

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