

Fedex vs. ups

Economics, Financial Markets



THE BATTLE FOR VALUE, 2004: FEDEX CORP. VS. UNITED PARCEL SERVICE, INC. Executive Summary: As the U. S. package delivery business segment matured, International segment became the battle ground for the two package delivery giants – FedEx and UPS. FedEx is considered to be the innovative, entrepreneurial, inventor of customer logistical management, and an operational leader. UPS, on the other hand, is considered to be big, bureaucratic, and industry follower, although UPS is shedding this negative image with newer innovations. FedEx Corp. started in 1971, by the end of 2003; it had nearly \$15. billion in assets, net income of \$830 million on revenues of about \$22. 5 billion and shipped more than 5. 4 million packages daily. UPS, Inc. founded in 1907, by the end of 2003; it had \$28. 9 billion in assets, net income of \$2. 9 billion on revenues of \$33. 4 billion, and with excellent (AAA) bond rating. The struggle to deliver value and dominate the package delivery market between FedEx and UPS has reached titanic proportions and clearly evident from their respective expenditures. Between 1992 and 2003, capital expenditures for FedEx and UPS rose at an annualized rate of 34. 64% and 36. 78%, respectively.

Currently both companies are matching each other's investments in capital almost exactly. Placing ourselves in the center of the battle of giants and using the data provided in the Exhibits 1 through 11, we try to answer the following questions in this case analysis. 1: Who is creating more value and how? 2: Who is destroying the value? FedEx's growth strategy is " Produce superior financial returns for shareholders by providing high value added supply chain, transportation, business and related information services

through focused operating companies competing collectively, and managed collaboratively under FedEx brand”.

UPS’s growth strategy is “ Serve the evaluation distribution, logistics and commerce needs of customers with excellence and value in all services. With strong financials and broad employee ownership provide long-term competitive returns to the shareholders”. FedEx’s financial ratios are improving while UPS has far better ratios in liquidity, leverage, and profitability. UPS has consistently paid and increased dividends while FedEx just started paying dividends in 2003. FedEx’s EPS comp. annual growth rate (CAGR) 1992 -2003 is 27. 54% compared to UPS’s 13. 9%. However, since going public 1999, UPS has better EPS Compounded Annual growth rate (CAGR) compared to FedEx- 34. 30% vs. 6. 98%. UPS has far better Cum. Total market returns than FedEx – 705. 95% vs. 528. 02%. UPS has far better EVA(2003) compared to FedEx - \$1, 195 million vs. \$170 million. MVA(2003) for UPS also far better than FedEx - \$11, 816 million vs. \$69, 315 million. By looking at the calculations above we can clearly say that both UPS and FedEx created value, but UPS has created more value for shareholders than FedEx.

Case Analysis Detail:

We start with analyzing both companies using the data provided in the book in the exhibits 1 through 11. We start the Economic profit analysis of both FedEx and UPS by review and analyzing the Return on Net Assets (RONA). A Return on Net Assets Ratio determines whether the institution is financially better off than in previous years by measuring total economic return. A decline in this ratio may be appropriate and even warranted if it reflects a

strategy to better fulfill the institution's mission. An improving trend in this ratio indicates that the institution is increasing its net assets and is likely to be able to set aside financial resources [pic] to strengthen its future financial flexibility. Looking at the graph generated from data presented in Exhibits 9 & 10, shows from 1992 to 1994 the ratio for FedEx is improving while it is decreasing for UPS, although it is still well below UPS figures. A quick look at Exhibit 4, we did not find any competitive developments to support the movement of the ratio for both companies. To get more insight into this movement for FedEx and UPS we check the Activity Analysis specifically the Asset turn over ratios for both companies.

Review the Fixed asset turnover and Total asset turnover for FedEx and UPS for the period 1992-1994, it is observed that UPS is utilizing its assets better during this period – see graph below. [pic] Although by itself this ratio number can be misleading, since companies with lower margins can have higher asset turnover ratios. In order to understand the real impact of asset turnover ratio we need to combine with margin ratio and then determine if it's pricing strategy by UPS that is generating this high ratio or in fact UPS is much more efficient in using its assets than FedEx.

Looking at the numbers for this period for both companies using Exhibits 2&3, we observed that UPS has far better Net profit margins compared [pic] to FedEx's, that points to high asset turnover due to its pricing strategy. As we see in the above graph, UPS Asset ratios are declining while FedEx assets ratios are improving and correspondingly FedEx-RONA is also improving though lacking behind UPS's RONA ratio even though FedEx has greatly

improved their asset turnover ratios, the Net Profit margins are still well below UPS (see Net Profit Margin graph above). Does this mean UPS is creating more value than FedEx as shown by RONA graph?

We need more concrete data to answer this question. Although RONA has a strong virtue of usage, as compared to traditional methods for measuring company success, is that it also considers the assets a company uses to achieve its output. However, RONA can't alone be used to determine who is creating value to destroying value, because managers might bypass value-creating activities because they would reduce RONA (a risk if RONA is greater than WACC), or they might undertake value-destroying activities because they would increase RONA (if RONA is less than WACC).

Moreover, since RONA does not explicitly measures capital charges, we need to analyze Economic Value Added to determine who is creating or destroying value. Ultimately maximizing EVA should rather be seen as the key financial success than maximizing RONA. [pic] Above graph shows from 1992 to 1994 both companies were destroying Economic value, UPS less than FedEx. 1995 UPS created \$217 million value while FedEx was still in the negative territory. This is when UPS launched “ guaranteed 8 A. M. overnight delivery” (Exhibit 4 - Timeline of Competitive Developments).

This was frontal attack on FedEx who has “ offers 10 A. M. delivery” (Exhibit 4 - Timeline of Competitive Developments). UPS EVA dropped to negative \$138 million due to the strike by its union workers which cost UPS \$700 million revenues. Interesting to see from the graph is that FedEx could not capitalize on this opportunity as its EVA was down by \$215 million. In fact

the graph shows, FedEx destroyed EVA from 1992 till 2002 and the only year it was able to create EVA was in 2003 by the amount of \$170 million compared to UPS of \$1,195 million.

In year 2003, UPS EVA was whopping 703% more than FedEx. Reviewing numbers and graph, in the tech bubble of 2000-2002, UPS still maintain positive EVA while FedEx delivered negative EVA. Looking at the above graph and correlating it against the Exhibit 4, the positive EVA of FedEx can be lined up with Kinko's Purchase in year 2003. [pic] Analyzing the cumulative Economic Value Added (EVA-Cum) graph, from year 1992 to 2003, FedEx destroyed \$2.2 billion (\$2,252 Million) economic value while UPS has created \$4.328 billion (\$4,328 million) in economic value. This answers the questions put forward in the executive summary. But we will go further and analyze the Market Value Added (MVA) for each company to support our argument that UPS created more value than FedEx. [pic] Since going public in 1999, UPS has created close to \$70 billion in Market Value Added (MVA) as compared FedEx's \$11 billion MVA. This shows UPS has created substantial values for the shareholders far better than FedEx.

Since FedEx's MVA is not negative, it shows they did not destroyed value for the shareholders but UPS created more value for the shareholders. This is amazing achievement for UPS that is considered big and bureaucratic while FedEx is considered the innovative. What is the key to UPS's success even being heavily unionized? The Key is efficiency. Business week wrote " Every route is timed down to the traffic light. Each Vehicle was engineered to exacting specifications. And the drivers endure a daily routine calibrated

down to the minute. We can analyze UPS's efficiency by analyzing the ratios and comparing them against FedEx's financial and analytical ratios. Using exhibits 2 and 3, graphing the data, comparison shows UPS activity ratios are weakening and FedEx is doing great job in improving. [pic] The Average days outstanding for UPS have increased from approximately 25 in 1992 to over 50 in 2003. FedEx on the other hand, has done better job to manage the average days outstanding. Average Days outstanding by itself doesn't mean much and it must be analyzed with other activity ratios to conclude result. pic] The working capital turnover comparison shows except for 1993 FedEx has done better compared to UPS. The WC_Turnover for FedEx was 41.25 in 2003 compared to 7.72 for UPS, indicated FedEx is generated far more sales compared to cash it uses to fund these sales as compared to UPS. [pic] FedEx's fixed and total asset turnover ratio is better than UPS. This indicates FedEx is using its asset better than UPS to generate sales. Although by itself this ratio number can be misleading, since companies with lower margins can have higher asset turnover ratios.

In order to understand the real impact of asset turnover ratio we need to combine with margin ratio and then determine if it's pricing strategy by FedEx that is generating this high ratio or in fact FedEx is much more efficient in using its assets than UPS. Looking at the numbers for 2003 for both companies, FedEx with 3.69% Net profit margins compared to UPS's 8.65% seems to have high asset turnover due to its pricing strategy. The above graph shows that activity financial ratios of FedEx are improving while they are weakening for UPS.

Next we analyze Liquidity Ratios of both companies to see which company has the ability to pay its obligations in timely manner with minimal cost. [pic] The Current Ratio of UPS is better and improving than FedEx. The anomaly in 1999 for UPS was due to the public offering of its securities. The graph shows both companies can service their short-term debt, its UPS that has more efficient operating cycle than FedEx. The graph shows FedEx's CR is improving but still behind its top competitor UPS. [pic] UPS has better cash ratio and thus can service its short term debt more comfortably than FedEx.

This also indicates that UPS has less debt than FedEx too. The anomaly in 1999 is due to public offering of UPS securities. The graph shows UPS Cash ratio offer better safety of margin than FedEx when it needs to service its debt. Although FedEx's Cash Ratio is improving but it is still behind UPS. Reviewing the Cash flow from operations ratio and Defensive interval shows that UPS has better liquidity ratios than FedEx and can handle short term cash requirement more efficiently, though FedEx's ratios are improving.

The above graphs show UPS has better liquidity ratios than FedEx. Now we review the Long-Term Debt and Solvency analysis of both companies. The below graph shows FedEx is more leveraged than UPS, though FedEx's leverage position is improving. Graph shows UPS's leverage was high in 2001 and 2002, we can find the answer in Exhibit 4 – Timeline of Competitive Development – UPS acquired all-cargo air service in Latin America 2000 and acquired Mail Boxes Etc. retail franchise in 2001. While in 2003 FedEx acquired Kinko's which could explained higher leverage compared to UPS. [pic] The Capital Expenditure Ratio shows, both companies actually almost

matching each other's Capital expense. Exhibit 4 –Timeline of Competitive Developments shows the details of the major Capital expenses by both companies in competition to gain competitive advantage. Both companies made acquisitions to grow in different fields. [pic] The above graphs shows UPS is consistently leveraged low while FedEx is improving. Next we analyze the profitability analysis for both companies. Data from Exhibit 2 & 3 shows, FedEx's profitability is worse UPS.

PS beat FedEx in almost all profitability ratios by handsome margin. It is evident from 2003 numbers for Net Profit Margins 3. 69% and 8. 65% for FedEx and UPS respectively. The following graph shows the comparison of profitability of both companies. [pic] Finally, we review the growth analysis of both companies. Exhibit 2 & 3, provides the picture that shows FedEx growth is higher than UPS. [pic] The below graphs summarizes and compares both companies EPS, Dividend payout, Stock price, and PE ratios. [pic]

UPS's stock price shows since going public, it has delivered better value to its shareholders than FedEx. [pic] The above graph shows, UPS has consistently paid and increased dividends to its shareholders, while FedEx started dividend payout in 2003. [pic] UPS has a higher EPS growth than FedEx implies that FedEx has been unable to translate net income growth into high EPS growth. Hence, our analysis conclude that both UPS and FedEx created value for their shareholders, but UPS created more value than FedEx in the long run.