Financial management argumentative essay

ASSIGN
BUSTER

In the same way that MarksSpencer has been subjected to a five forces analysis, Vodafone's operations will also have to be subjected to an analysis that puts Vodafone's performance against the backdrop of the wider industry which in this case is the telecommunications industry. The findings of the analysis in this respect present a brighter picture. To start with, barriers to entry in the telecommunications industry are very high. Massive capital expenditures will have to be taken into consideration by entrepreneurs planning to enter this industry.

As a result, Vodafone does not have to worry about an upstart every other day muscling in on Vodafone's territory. The company has had to invest millions in setting up its network worldwide and the reputation and the market share that the company enjoys is the product of years and years of gaining expertise and pouring money into it. Any new entrant who seeks to match the position and power of Vodafone will have to go through the same arduous process by which time Vodafone will have evolved to a higher plane of business operations altogether. Therefore, as far as the number of players is concerned, the telecommunications industry is pretty static.

But that does not mean that the threat to substitute products is minimal. That is by no means the case as the existing number of players in the industry is high enough that the consumers can go price shopping merrily knowing that there are enough choices. This has resulted in the fact that the industry is now caught in a desperate price war which is chipping away at its own profitability. The products offered in this industry, at their most basic level, can be categorized into two classes. One is voice and the other is value

added services. It is the voice category which has got caught in the price war.

All telecommunications companies basically attract new market share through voice as the use of value added services requires a somewhat advanced level of technical expertise. The means of attracting voice customers has become lowering prices. As a result, the industry is now caught in an endlessly repeating cycle of lowering prices the only means of stopping which seems to be expansion of value added services. Almost all the major players in this industry have made it their strategic focus to invest more on value added services and less on voice as a mean of ridding themselves of the price war. Of course, given enough time, value added services will also start to exhibit signs of a price war similar to that in voice, but that will take some time to happen and does not concern the investor in buying Vodafone’s shares at present. But the fact remains that at present the industry relies to a significant extent on voice and as a result of this trend, threat of substitute products is high.

Threat of competition is not very high for Vodafone as it is well poised to offer value added services through its highly developed internet operations. As mentioned before, the telecommunications industry is a very capital intensive industry. It takes enough to set up a voice network. To be able to integrate internet access into the bargain makes it a forbidding undertaking in terms of the resources required to invest. This means that Vodafone is in a much better position than most of its competitors to compete on the basis of value added services. As far as the threat of the bargaining power of buyers

is concerned, current reliance on voice products means that buyers have a lot of choice giving them high bargaining power.

However companies like Vodafone enjoying first mover advantages are steadily moving towards value added services and the level of education in the West is advanced enough that value added services will be continuing to enjoy greater and greater demand. In fact in this case, it is not clear whether the market is being pushed by the suppliers or whether it is being pulled by the consumers. At the very least, this is one industry where suppliers like Vodafone and consumers are collaborating on pushing forward the boundaries of the telecommunications industry. On the one hand the consumers want Vodafone to offer more and more services through the mobile network so that they do not have go looking for an internet cafe every time they are looking for some information online.

On the other hand, Vodafone wants consumers to purchase more and more of value added services because value added services are more profitable for the company. As a result, the long-term profitability of Vodafone looks solid. The bargaining power of buyers is not that high when value added services come into play and the bargaining power of suppliers is good enough. According to the above, as far as Porter’s five forces analysis of the two companies is concerned, the long-term profit potential of Vodafone looks more reliable than MarksSpencer’s. PEST analysis Industries are not immune to the political, economic, sociological and technological forces.

A major political disturbance of any sort will have a severely negative impact on all the industries. However it will not have that much of an impact on the

consumer goods industry relative to the telecommunications industry as the former industry deals in products that are related to the basic necessities of life. Therefore consumers will continue to set aide a certain portion of their income for the purchase of consumer goods. In fact, this portion set aside for the purchase of consumer goods is not disposable income the level of which takes a severe beating during politically and economically hard times. The level of disposable income comes into play when consumers are contemplating purchase of value added services. Therefore, economic projections of the UK and the rest of the world in which Vodafone has its operations will have to be taken into account when evaluating the long-term potential of the company.

However, Vodafone has the distinctive advantage of having invested in a wide variety of business operations. Therefore even in economically hard times when businesses are not investing that much in telecommunications, they will be investing in other areas of technology for example. One of these areas might be making their online operations more secure. In this respect as well, Vodafone has expertise which will help it weather the economic storm should one emerge. The point to make in the analysis is that Vodafone has a wide portfolio of business ventures and this diversification will make sure that even if one technological sector takes a beating as a result of an economic downturn, the company will tide through riding on other of its ventures.

Analysis of financial statements While PEST and Porter’s five forces analysis is critical prior to arriving at an investment decision, the process will be left half undone unless a rigorous analysis of the financial statements of the two

companies is conducted as well. In this case analyst reports such as those from Goldman Sachs and Lehmann Brothers will have to be taken into account. The important part of the analysis is to review the financial statements for the last few years and then, assuming that percentages of changes will maintain as before and also taking into account the data from the analyst reports in order to assess how revenues and costs will change in the future, to project the balance sheet and the income statement and the statement of cash flows for at least three years into the future. The investor will have to grasp an idea of how revenues have been changing in the last few years.

Then he might reasonably proceed assuming that if the revenues have been growing consistently for a certain fixed percentage for the last five years, then they will continue to do so in the next three years. Of course that is simplifying things a bit as there are any number of external and internal environmental factors which will directly impact profitability. These factors the investors can bring into his analysis by means of the analyst reports. These reports specialize in the past and the projected performance of the company on which it is focusing and also on how the internal structure of the company has changed if it has. In the case where the industry has been growing consistently for the last five years but it is expected to slow down, the investor will have to scale down on his optimistic projections.

Thus the investor will have to blend information from both internal and external reports concerning Vodafone and MarksSpencer in order to project what the revenues of the two companies will be in the next three years. Costs will also have to be projected. It is reasonable to assume that costs as

a percentage of revenues will continue to be the same as they were before unless according to the analysts reports, one or the other of the two companies are downsizing and letting a lot of their people go. In such a scenario, expenses arising from wages and salaries will have to be adjusted accordingly.

Significant investments in plant and equipment will also have to show up in the balance sheet projections. Items such as accounts receivable and inventory will have to be projected based on common-sized statements indicating past performance. Once again analyst reports might indicate that the company’s credit policies have changed. Accounts receivables as a percentage of sales therefore will have to be adjusted accordingly.

Once three-year projections for the income statement and the balance sheet have been made, yearly projections for the statement of cash flows can be derived from those two statements. This will indicate whether the company will have enough cash in hand to pay off the short term liabilities. What should be taken into particular consideration is whether analyst reports have one of the companies downsizing. In that case, all projections for the future will have to be adjusted down rather than up as this will have a negative impact on employee morale thus affecting their productivity negatively.

Once projections of all three financial statements have been successfully completed, ratio analysis is the unavoidable next step. Liquidity ratios, efficiency ratios and profitability ratios will have to be projected. However the ratios taken on their own will not accomplish much. They will have to be compared against industry benchmarks and thus they will indicate whether

the company is performing above industry average or not. Conclusion Most important in arriving at a solid investment decision is to decide whether the shares have been underperforming or over-performing. Shares which are underperforming are the best buy.

Therefore what the investor will have to do is to conduct all the prior analyses and based on the findings, decide whether Vodafone shares or MarksSpencer shares are underperforming more. Based on the prior analysis, it appears that Vodafone shares have been significantly underperforming given their profitable expansions worldwide as indicated by the falling price-earnings ratios. Therefore the investor should invest in Vodafone. BIBLIOGRAPHYBrigham, Eugene F. , and Michael C.

Ehrhardt. Financial Management: Theory & Practice. South western college pub. 2007.