# Proctor and gamble leverage ratios

Business, Company

Proctor and Gamble is one of the American multinational companies which manufactures and sells a broad variety of consumer goods and is a Fortune 500 company. Its total assets worth's about $ 143, 992 millions during 2008. P& G net earning during 2008 is $ 12075 millions. Protector and Gamble leverage ratios are strong. Long –term debts and total debt is about 35% of its equity. This means that company is very cautious in borrowing. A wise financial management is to trade on leveraging. Normally, a debt –equity ratio is allowed up to 1.

Thus, a company can avail loan up to 100% of its equity to fund its expansion, diversification or working capital. Expansion, diversification and acquisition helps to improve the profitability The P& G should think of expanding or acquiring new business to improve its profitability and to increase its market share. Since, P&G is having strong debt –equity ratio, it can further trade on leverage by borrowing more funds to fund its expansion, diversification or acquisition. Further, P&G debt-equity ratio is less than the industry average. It connotes that the other players in the industry are availing more debts for their growth.

Further, P&G is having a strong interest coverage ratio. It can service up to 12 times of its present interest charges as it is having surplus net profit after servicing interest charges. By leveraging, P&G can also improve the earning per share to its existing shareholders as there is no divestment of existing share holding or issue of fresh capital and thereby expanding the present shareholders network. Larger the shareholding, lesser will be the earnings per share. It is to be noted that if a company resorts to high debt that need not necessarily result in bad financial results.

A prudent CEO of the company may go for borrowingmoneyat 4% and earns about 10% with that of borrowed funds. Since, P&G is having strong debt – equity ratio, I strongly felt that P&G can further trade on leverage by borrowing more funds to fund its expansion, diversification or acquisition. This ratio signifies total debts owed by the company as compared to its equity. If the long term debt is on decreasing for one or more financial years, it is a good sign that company financials are strong. When repayment of long term debt is made from internal accruals, the cash will be increasing and the balance sheet will be ranked as vibrant.

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P&G total debts to equity ratio demonstrate that the company is gradually paying off its long term debts and it is good sign that the company financials are vibrant. As mentioned earlier, P&G should think of improving its profitability by resorting to expansion, diversification and acquisition by borrowing long term loan as it is still within the industry average. Times Interest Earned: Many financial analysts employ the Times interest earned or Interest –Coverage –Ratio to assess a company's capability to service its debt. This ratio is arrived from comparing operating income i. e.

income before taxes and interest, with that of actual interest expenses incurred. For instance, the Interest Coverage Ratio will be four if the operative income were quadruplicate the interest expenses. This yardstick is used to gauge a company's capability to meet its debt commitments. This is always indicated as a ratio and depicts how many times a business can meet its interest commitments on a pretax basis. If a company is having a

negative interest coverage ratio , it indicate that company may be in the verge of bankruptcy as any interest default or principal default may compel creditors to file liquidation process.

P& G interest coverage ratio is roughly around 12% in the last three financial years. This means that P&G is having greater disposable income after meeting its interest commitments. Thus, P&G should deploy its surplus funds in to other projects or fund its expansion to earn greater returns. Further, P&G should also try to avail loans at a lower cost of capital than at its current interest rates not only to cater its debt commitments but also to earn greater returns and to increase the shareholders value.

The industry average for interest coverage ratio is 76% whereas P&G interest coverage ratio is hovering around 12% in the last three financial years. This implies that P&G competitors are earning more pre-tax profits than that of P&G. Thus, P&G should analyze why it lagging behind its competitors in earning pre-tax profits . It has to study its competitor's strategy and to try to peruse the same to increase its profitability so that it can increase its interest coverage ratio to the industry average level.

Bench marking will thus helpful for P&G to find out its pitfall and to analyze its performance and to improve its profitability by diversifying and expanding its operations. This financial indicator is used to know the percentage of loan used tofinancethe company assets. In P&G , debt comprises of 57% of its total assets during 2008. Further, P&G has started to repay loan from the internal accruals in the last three financial years. This indicates that P&G is generating sufficient internal accruals to pay off or reduce its debt obligations and is also with in the industry average.