

# Performance evaluation of sainsbury's analysis



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Task-3 Sainsbury's plc has been operating in the UK market since 1869. Annual report'09 suggests that the company is currently serving 18 million customers each week with strength of 150, 000 staff. It floated itself in 1973 under London Stock Exchange in 1973 as the biggest floatation at the time. To understand any strategy for any company, it is important to know what the key strengths, weaknesses, opportunities and threats are for the company. Sainsbury's, historically has been renowned for its fair pricing. Furthermore, when the economic recession started, they introduced a new pricing strategy named ' good, better, best' pricing structure to meet the customers' needs of matching their budget. This strategy turned out to be strength and also a competitive advantage. Sainsbury's own vast numbers of its own branded product which are mostly known as ' Sainsbury's basic' products, attracting large number of customers who do not want to spend a lot. Significant presence in the UK market is also strength of the company. They currently own 16% of the whole UK market having 18 million customer turn up each week.

Poor IT infrastructure is indeed, Sainsbury's one of the weaknesses. The company had to compensate each of the 10, 000 customers with ? 10 voucher who could not browse their online store for two days due to faulty IT system. Expansion through acquiring is a big opportunity for the company. It recently acquired 24 new stores from Co-operative in the fiscal year 2009 and planning to acquire more 50 new stores in the convenience store segment. High amount of competition amongst the rivals is the biggest threat for Sainsbury's.

Although they are practising 'good, better, best' price design but some low pricing super markets, like Aldi, Lidl, are threatening to lose customers.

Liquidity: To measure the liquidity of any company, the first two tools that come first are the current ratio and the acid-test ratio or quick ratio. Martin et al. (2005) described that the current ratio of a company measures its liquidity by its liquid asset relative to its short term debt. On the other hand, the quick ratio is calculated similarly but the amount of inventory is excluded from the current assets first.

For retail based conglomerate it is very important to control the inventory to keep the profitability up. The current ratio and the quick ratio for the years 2009, 2008 and 2007 are 0.54, 0.61, 0.70 and 0.30, 0.34, 0.51 respectively (Appendix-2). These figures indicate that the company is able to pay its each pound of short term liability by the mentioned pound amount of current assets and the trend has been decreased in liquidity in the recent year. The total amount of working capital for the years 2009, 2008 and 2007 have been throughout negative.

This means that the company's current liabilities are exceeding the amount of current assets. According to the Chief Finance Officer in the annual report of 2009, a new short term financing was organized through two revolving credit facilities. The first one is due in May 2011 of £163m and the other one is due in February 2012. Company's strategy to maintain the working capital is to do by cash trade and also by improving stock days. The stock turnovers (days) for Sainsbury's (Appendix-2) for 2009, 2008 and 2007 are 14.07, 14.76 and 13.48. Profitability:

The revenue for Sainsbury's has constantly increased in the last five years which led the company to manipulate on the increasing the profit margin and other profitability measures. Company's revenue jumped to ? 1. 89b in 2009 from ? 1. 72b in 2007 which is an increase of 9. 9%. However, the gross profit decreased by 11. 6% and operating profit increased by 29. 42% in the same period of time. The reason was that the revenue did not increase in proportion to the cost of sales. Gross margin is the amount left from the revenue after deducting the direct cost of sales. Sainsbury's Gross Margin (Appendix-2) was 5. 8, 5. 62 and 6. 83 accordingly in the year 2009, 2008 and 2007. The operating profit is the amount left after subtracting the indirect cost or the overhead and operating margin is the measure that indicates how much the operating profit is of the total revenue.

In 2009, the operating profit was 3. 56% which was slightly above than the previous year. After deducting all the expenses, the left amount is the net profit and the proportion of net profit in respect to total revenue is the net profit margin. Sainsbury's net profit margin for the years 2009, 2008 and 2007 were 1. 3%, 1. 84% and 1. 89% respectively. The management thinks that the tough market condition and the other competitors with very cheap pricing have pushed them to squeeze their profit margin ratio. The graph below shows the Return on Capital Employed as well. The ROCE gives the idea about how much return a company is making on its used capital. (investorwords. com) The ROCE for the company was 9. 46%, 7. 10% and 7. 59% for the years 2009, 2008 and 2007 respectively. The year 2009 proved to be a little bit more in context of return on capital employed.

Now, if these figures are compared with the market leader, it will be clearer about the company's profitable position. In the years 2009, 2008 and 2007 TESCO, who is the market leader for the market Sainsbury's are operating, also performed very well. TESCO's revenue also took a steep upward curd in between 2007 and 2009. Their revenue increased by 29. 4% to ? 54327m in 2009 from ? 42641m in 2007. TESCO's ROCE was 11. 44%, 14. 02 and 15. 90% in the mentioned years. The gross margin and operating margins were, 7. 76%, 7. 67% ; 8. 12% and 5. 9%, 5. 9% ; 6. 2% for the above mentioned years respectively.

The below graph shows the similar information which was done for Sainsbury's for the same period of time above. Debt-Equity: This section represents how the company's finance has been done. The section can be very interesting toward the investors who are willing to invest in Sainsbury's plc. These tools will measure whether the money we investing are safe or at very high risk position. Debt ratio illustrates the total amount of liability, both current and non-current, in contrast with the amount of the total asset a company posses. (Arnold 2005) This shows that if company's ability to pay off its debt covered by the amount of asset they have.

On the other hand, the gearing ratio shows how the company's finance is funded, whether it is doing business by its own money or by lending it from outside. If the fund is mostly borrowed that means the company is highly geared and if anything goes wrong whether the company be able to fund its projects to run or not. It is a tool to measure the risk in long term period. As for Sainsbury's, from 2007 to 2009 the debt ratio was 56. 38%, 51. 21% and

54. 58% respectively. It illustrates that the company owns debts which are the abovementioned percentage of their total asset.

On the other hand, the gearing ratio for the company is 38. 49%, 33. 87% and 36. 56% in the years 2009, 2008 and 2007 accordingly. These percentages illustrates that the long term liabilities for the company is the mentioned percentage of their total amount of equity. This number increased in the latest financial year as acquired 24 new stores from co-operatives. Now, as a nature of business the company has to go for acquisitions each year as they are trying to grip more of the market shares and it is important for them to maintain a good balance between debt and the equity.

Investors also may not be interested in company where the gearing is very high, which illustrates risky investment for the investors. If we take a glimpse at TESCO, their debt ratio is 72. 41% and the gearing ratio is 53. 61% for the year 2009. The number illustrates that the company is highly geared, however, the business nature suggests that to expand and acquire it will need long term capital and it can also be seen that TESCO are well able to pay off their debts on due time as they have heavy cash flow everyday.

The strategy can be found at the statement of Chief Finance Officer in the annual report of 2009 where he stated, " The Group's financing requirements are managed by pre-funding cash flow requirements and maturing debt obligations, maintaining a diversity of funding sources with an appropriate mix of fixed, floating and inflation-linked borrowings and by spreading debt repayments over a range of maturities". Management Efficiency: The

efficiency of any company's management can be drawn by the portion which they earn as return on asset or return on equity.

The return on asset for Sainsbury's is 2.87%, 3.34% and 2.9% in the years 2009, 2008 and 2007. It has been calculated by dividing the income after tax by the total amount of asset. The returns on equity for Sainsbury's are 6.6%, 6.67% and 7.47% in the years 2009, 2008 and 2007. Dividends: Dividends are the amount of profit which is distributed among the shareholders of a company after a certain period of time, usually twice a year. Sainsbury's paid £218m, £178m and £140m in dividends in 2009, 2008 and 2007 respectively.

The number of shares outstanding is 436 million and the paid dividend per share was 13.2p where the earnings per share was 22.1p in 2009. The payout ratio was 59.73% which is calculated by dividing the dividend per share by EPS. Now this ratio has been consistently very high from 2007 till 2009. The payout ratio was 63.33% in 2007 and 61.22% in 2008. Sainsbury's plc is maintaining a long term policy regarding the dividend cover. As per that the company is going to maintain a dividend cover in between 1.5 to 1.75.

Accordingly the company's dividend cover in 2009, 2008 and 2007 was 1.7, 1.63 and 1.51 accordingly. Company's 'Employee Share Ownership Plan' trust owns 9.65 million shares at a face value of 283/7 pence. There is another policy obtained by the company called DRIP-Dividend reinvestment policy, under which the ordinary shareholder's can re-invest their amount of dividends to buy new shares from the market through a special

arrangement. 32, 562 shareholders participated in it in 2009. Other factors: There are some other factors which can influence the company to obtain or to re-organise their financial strategies.

To continue smooth operation and to sustain business for long term Sainsbury's always keep the risks in mind and tests them on a regular basis. Act of terrorism risk, business strategy risk, economic and market risk, environmental and sustainability risk, financial strategy and treasury risk, fraud, IT system and infrastructure risk are stated as very important ones for the company. Task-4 In a tough market and economic condition, companies have to always keep on changing their strategies depending on the demand and appropriate moves.

The market is highly competitive and it is very tough to make a large profit margin where huge information about the market is prevailing already. \* International expansion: to achieve the 50% increase in the revenue within the next three years, Sainsbury's should look for opportunities abroad. The market leader TESCO has gone international long back and currently operating in several countries.