Tescos performance based on financial ratios commerce essay

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This research proposal studies on the factors which Tesco in their current profitability and meet it short-term financial obligation. Tesco also look strong for the employee's motivation and the company competitive exists. Tesco was founded in year 1919 by Jack Cohen and the first Tesco name appeared in year 1929 (Tesco, 2010). Nowadays, the Britian leading retailer is Tesco and also United Kingdom based international supermarket chain (TESCO, 2010 and Tesco House, n. d.). They operating over 4, 800 stores globally and employing over 472, 094 people (Checksure, n. d.). At the beginning, they specializing in food, now move into areas like clothes, consumer electronics, consumer financial services, selling and renting DVDs, compact discs and music downloads, internet service and consumer telecoms (Tesco House, n. d.). They have 588 supermarkets and 257 are superstores. Besides that, they operates in 13 countries such as Republic of Ireland, Hungary Czech Republic, Slovakia, Turkey and Poland in Europe, China, Japan, Malaysia, South Korea, Thailand, India, and the U. S. (Tesco, 2010).

The key towards Tesco success was related to their financial position which consists of generate a return on its resource, able to meet its short-term financial obligations and the efficiency ratios.

Usually, the financial ratios analysis is including profitability, liquidity and investment ratios. It's normally used to analysis company performance which analyzes the success, failure and progress of company business. (Woods, 1999). In addition, it can also calculate for a company to be compared with other companies and own companies own past figures (Jiao and Bhalotra, 2007).

Profitability ratios determine that the company's able to generate a return on its resource (missouribusiness. net, n. d.). Besides that, profitability shows proportion is advantageous business, measuring the overall performance was investigated, the profits of the company, can be used to test how your company operation, compares the current performance and the record of the past (Jiao and Bhalotra, 2007). It including gross profit, net profit margin, return on assets, and return on equity.

The gross profit margin is indicates how well the company be able to generate a return at the gross profit level (Missouribusiness. net., n. d.). The gross profit margin considers the firm's cost of goods sold, but does not include other costs (Netmba. com, n. d.). The formula for calculate the gross profit margin which is gross profit margin equal sales minus cost of goods sold divide by sales and multiply 100 percent.

The formula calculates for net profit margin is net profit divide total sales also can call net sales and multiply 100 percent. However, this ratio ability provides a significant investment, indicate its sales business ability covers the smallest fixed cost and remains an acceptable profit (Missouribusiness. net, n. d).

Formula calculation for return on assets is net incomes before taxes divide by total assets and multiply by 100 percent. This ratio display the effectively of the firm's assets able being used to generate profits (Netmba. com, n. d.). In addition, low return on assets (ROA) indicates inefficient management, adverse when a high ROA which mean efficient in management (Barry, n. d.). Otherwise, this ratio in public company normally report return on assets to

their shareholders, cause to tell them how well when using its assets to produce income.

The return on equity (ROE) also knows as return on investment (ROI). The calculation compete for ROE which is return on equity equal net profit before taxes divide by shareholder equity multiply by 100 percent. These ratios usually indicate how well the company is utilizing its equity in investment and normally will higher than return on assets. According to proficient, if those companies hope their business growth in future, therefore, their ratio needs at least 10 to 14 percent in ROI (Barry, n. d.). This is a good figure to compare beside competitors or an industry average. For example, if the ratio is lower which mean that they meager management performance. In other words, a high return on investment indicates that management is doing well.

Liquidity ratios is show how quick the company able to convert assets to cash, and pay off interest (Carter, 2010). Furthermore, the low levels of liquidity ratio can demonstrate poor management for grown up company (Netmba. com, n. d.). Besides that, it’s providing with useful limit for business managers to help them regulate their borrowing and spending (Barry, n. d.). The main liquidity ratios are the current ratio and quick ratio.

Current ratio is also called the working capital ratio (Missouribusiness. net, n. d.). It is the number of times a company’s current assets exceed its current liabilities, which is an indication of the solvency of that business (Auerbach, n. d.). The formula to compute the current ratio which is total Current Assets divide total Current Liabilities. A general rule of thumb for current ratio should be at least 2: 1 (Missouribusiness. net, n. d.). A lower current ratio

determines that the company may not be ability to pay its invoices on time, while a higher ratio means that company has money in cash or safe investment that could be put to better use in business (Barry, n. d.).

The quick ratio is also called the acid test ratio (Missouribusiness. net, n. d.). It indicates the extent to which company could pay current liabilities without relying on the sale of inventory (Missouribusiness. net, n. d.). A general rule of thumb states that the ratio should be 1 to 1 or 1: 1 (Missouribusiness. net, n. d.). If it is higher, the company may be keeping too much cash on hand or have a poor collection program for accounts receivable (Barry, n. d.). If it is lower, it may indicate that the company relies too heavily on inventory to meet its obligations. The formula for compete quick ratio is current assets minus inventory and divide current liabilities.

4. 0 Significance of study:

Basically, this study is seen vital as in it helps Tesco to do their financial performance more effectively. Regarding on that, it more related to the financial ratio analysis whether in term of profitability, liquidity and investment ratios that Tesco would take in for their effective management. Furthermore, this study also could acts as references for other retails that going to develop in the future as well to enhance competitive advantages.

5. 0 Literature Review:

Part A

5. 1 Profitability ratios

Profitability ratios are an indication of company’s overall efficiency and performances. According to the calculation of annual report, the Tesco gross

profit margin from year 2009 (7. 76%) to 2010 (8. 10%) increases 0. 34 percent. During year 2010, Tesco net profit margin increasing 0. 14 percent from 3. 97 percent to 4. 11 percent (Tesco, 2010). It indicates Tesco every year able to grown their revenues (Wearden, 2010). This is because they believe that having a good profitability the companies now can operate well in worldwide markets. Besides that, the profitability also provided information for investor to let the investors to know how well they company is going to evolution (Beginnermoneyinvesting. com, n. d.). Not only Tesco using this ratios and Carrefour S. A also use this ratio method. Because the Carrefour believe that improve in the profitability, it will efficient to the businesses running. Therefore, Tesco and Carrefour believed that using past data as a benchmark to make a conclusion as to why the profitability is increasing and decreasing, so that the company can go well (Mysmp. com, n. d.). For example, during the fiscal year in 2008, the Tesco had a better sales growth rate, so that they company moving up from number four to number three in the ranking in the world. When hold on more of retaining, its profits would cope with future external market challenges (Fresh & Easy Buzz, 2010).

5. 2 Investment Ratios

Return on equity also known as return on investment (ROI). This ratio widely use by company because it ability to indications how efficiently the money invested in a company is providing a return to those investors (finpipe. com). In addition, the investor will through by ROE to get information what they need to make a sound decision (Winters, 2002). The investors normally will look for positive ROE, before making any kind of investment and also use to

compare different investment options by an investment advisor (Dogra, n. d.). During 2010, Tesco ROE is 12. 04 if compare to 2009 (11. 98%) it increase around 0. 06 percent. Besides that, Carrefour also emphasis on ROE, because investor is their money income if their ROE is not well that will influence their business and will affect them to expand in international business in worldwide. Therefore, the equity also look more to the operational and profitability ratios which to determine future profits that will accrue to the shareholder and the shareholders compare the profitability of different projects by looking into their return on investment ratios (Dogra, n. d. and finpipe. com, n. d.). According to Shannon report (2010), Tesco CEO Terry Leahy announcement that the 145 store Fresh & Easy should become profitable in fiscal 2013. Because of this announcement it causes the return on equity growth. In addition, a sharp improvement in Asia markets like Thailand and Korea able to helped drive sales growth.

Return on Assets is evaluate to use get a feel for how well a company using their assets to generate income (money-zine. com, n. d.). During year 2010, Tesco ROA increase around 0. 5 percent from 6. 4 percent to 6. 9 percent, because of the amortization charge on intangible assets arising acquisition. It also causes the group trading profits increase. In addition, they release cash from property through a sequence of joint ventures and other sale and leaseback transaction. Therefore, these transactions so far is completed which with pension funds, property companies and other investors would have delivered aggregate proceeds of £2. 2bn (Tesco, 2010).

5. 3 Liquidity ratios

Liquidity ratios are determined of a company ability to meet its debts (Winters, 2002). Liquidity ratios have current ratio and quick ratio. Current ratio is help company to see their able to pay their current debts without going against future earnings. In year 2009, Tesco current ratio 2009 is 0. 77: 1 and year 2010 is 0. 74: 1. However, we can realize that current ratio from 2010 is decrease. This is because they always have new markets to invest in. The Tesco CEO Terry Leahy increase in borrowing ratios when spearheaded £6. 6 billion of spending on expansion, including the £958 million takeover of South Korea's Homever supermarket chain. Although, Tesco's facing debt is high but they feel it still very healthy balance sheet (Bloomberg, 2009).

Quick ratio is show of the company's ability to make the payments on current obligation. Quick ratio for Tesco in year 2009 is 0. 61: 1 and year 2010 is 0. 56: 1. It shows that year 2010 ratio is decrease. This is because during that period they facing financial crisis. Although their ratio is decrease but they still can pay the debts because of they repaid their debt more early and use that was earning little interest to buy back higher interest-bearing corporate bonds (Tesco, 2010).

Part B

5. 4 Competition

Besides that, competition in the worlds market is more important because it enables help the company assess intelligently the business environment in which the firm operates. This is because if without competition, the company

unable to improve as in no competitive advantage. The competition enables the management to identify the company's weak points which to helps the firm to concentrate on the areas it needs to improve. The Main competitors of the Tesco are Carrefour S. A., J Sainsbury plc, Wm Morrison Supermarkets PLC and so on (Datamonitor, 2004). These are the main competitors in business strategies and the value markets. In other words, it also can help the company to know what kinds of actions are required to development with the competitive position in the industry (Articlesbase. com, n. d).

5. 5 Motivation

Employees are considered the important asset of a company. Based on that, the key of business success is general relying on employees. Employees are considered the important asset of a company. Based on that, the key of business success is general relying on employees. Tesco mission is work as a team, trust and respect each other, listen, support and say thank you, and share knowledge and experience to customers. Above all they want their employees everyone at Tesco can enjoy their work. Besides that, the Tesco believe that " if you treat people well they will give great service" so they customer able to enjoy their shopping trip. Tesco know their employees can work better when they are given the space to make decisions and take responsibility. They also encourage their employees to learn from their mistakes and challenge conventional thinking (Tesco, 2010).

6. 0 Methodology:

Theoretical framework for this study is:

Gross Profit Margin (IV)

DB

Total Assets Turnover (IV)

Net Profit Margin

(IV)

Return on Assets (IV)

Stock Turnover Period (IV)

Tesco Performance

(DV)

Quick

Ratio (IV)

Return on Equity (IV)

Current

Ratio (IV)

In this case, the Tesco performance is dependent and financial ratios are independent. Generally, secondary data collection is going to be done in order to help achieve the objectives in this study. It can through by annual report to do a comparatives which how well the Tesco performance in current year and previous year. In addition, they can highlight the variances

in past budget, so that they can improve in following year through by these problems.

(Words count: 2061)

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