

Good essay about finance

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Financial Analysis: Caterpillar Inc

About the paper:

This paper is being commenced with the objective of conducting the financial analysis of Caterpillar Inc. The company which is one of the largest manufacturers of agricultural implements, trades on NYSE under the ticker symbol of 'CAT'. For the purpose of conducting the financial analysis, we have divided the paper in two parts:

Part 1: This will include common-size analysis of the company's financial statement.

- Income Statement(Horizontal Analysis): Refer to excel spreadsheet
- Balance Sheet(Vertical Analysis): Refer to excel spreadsheet

Part 2: This will include extensive ratio analysis of the financial statements under the following sections:

- Liquidity Ratios
- Profitability Ratios
- Solvency Ratios
- Efficiency Ratios
- Valuation Ratios

i)Liquidity Ratios

a) Current Ratio: Current Assets/ Current liabilities

2012: $42524/29755 = 1.43$

2013: $38335/27297 = 1.40$

b) Quick Ratio: Cash+ Accounts Receivables/ Current Liabilities

$$2012: (5490+18952)/24915= 0.98$$

$$2013: (6081+17176)/27297= 0.85$$

Profitability Ratios

a) Return on Assets: (Net Income+ Interest Expenses)/ Average Total Assets

$$2012: (5681+467)/(81446+89356/2)= 7.19\%$$

$$2013: (3789+465)/(89356+84896/2)= 4.88\%$$

b) Return on Common Shareholder Equity: Net Income/ Average Common Equity

$$2012: 5681/(4481+4273/2)= 129.79\%$$

$$2013: 3789/(4709+4481/2)= 82.45\%$$

c) Net profit Margin: Net Income/ Revenue

$$2012: 5681/65875= 8.62\%$$

$$2013: 3789/55656= 6.80\%$$

Efficiency Ratios

i) Accounts Receivable Turnover Ratio: Net Sales/ Average Accounts Receivable

$$2012: 65875/(10285+18952/2)= 4.50$$

$$2013: 55656/(18952+17176/2) = 3.08$$

- Days of Receivables: 365/ Accounts Receivable Turnover

$$2012: 365/4.50= 81.11 \text{ days}$$

$$2013: 365/2.86= 118.50 \text{ days}$$

ii) Inventory Turnover Ratio: Cost of Goods Sold/ Average Inventory

$$2012: 47852/(15547+14544/2)= 3.18$$

$$2013: 41454/(15547+12625/2)= 2.94$$

-Days of Inventory: $365/\text{Inventory Turnover Ratio}$

2012: $365/3.18 = 114.77$ days

2013: $365/2.94 = 124.14$ days

iii) Asset Turnover Ratio: $\text{Revenue}/\text{Average Total Assets}$

2012: $65875/(81446+89356/2) = 0.77$

2013: $55656/(89356+84896/2) = 0.63$

Solvency Ratios

i) Total Debt to Total Assets Ratio: $\text{Total Debt}/\text{Total Assets}$

2012: $71824/89356 = 0.80$

2013: $64085/84896 = 0.75$

ii) Time Interest Earned: $\text{Operating Earnings}/\text{Interest Expense}$

2012: $8573/467 = 18.35$

2013: $5628/465 = 12.10$

Valuation Ratios

a) Earnings per Share:

$(\text{Net Income} - \text{Preferred Dividends})/\text{Weighted average number of common shares outstanding}$

2012: $5681/670 = \$8.47$

2013: $3789/659 = \$5.74$

b) Price-Earnings Ratio: $\text{Stock Price}/\text{Earnings per Share}$

2012: $90.14/8.47 = 10.64$

2013: $86.26/5.7 = 8.54$

c) Payout Ratio: $(\text{Dividend per share} * \text{Number of outstanding shares})/\text{Net Income}$

2012: $(1.96 \times 670) / 5681 = 23.11\%$

2013: $(1.72 \times 659) / 3789 = 29.91\%$

In-depth analysis of the ratios:

Noted from the above calculations, we can infer that the year 2013 was indeed not appreciable for the company. Beginning with the liquidity analysis, we found that both the liquidity ratios indicated a declining trend leading to a conclusion that the liquidity roots did receive a setback this year.

However, what might upset the shareholders more is the declining profit margins both, bottom line and ROE multiple. While the bottom-line profit (net profit) declined from 8.62% to 6.80%, the ROE multiple decreased from 29.79% to 82.45%. Hence, if this trend continues, we might witness shareholders losing their confidence and the stock may see high sales pressures.

Similar trend was witnessed in the debt ratios and efficiency ratios. As for the debt ratios, although during 2013, lower assets were financed using the debt resources as the debt to total asset ratios declined from 0.80 to 0.75.

However, the major concern comes with declining interest coverage ratio from 18.35 to 12.10 that indicates that the company is losing on its capacity to pay off its interest payment obligations. Hence, not only the profitability and liquidity, but the solvency roots of the company has also gone weak during a year.

As for the efficiency ratios, as measures using the debt collection period, the debtors of the company went slow in making their payments as the collection period increased from 81 days to 118 days. In addition, the,

company also witnessed a fall in the inventory turnover ratio from 3.18 to 2.94 indicating that it takes more time for the company to process their inventory and capital is tied up in the inventory for a longer period of time. Hence, this proves that the management was also inefficient in using the company's asset base.

Overall, our analysis indicates that the management needs to consider their situation with utmost emergency and should try to revive their financial position.

Company's Accounting Cycle:

Referring to the financial statements of the company, we can infer that the company has followed all the steps of the accounting cycle by recognizing each financial transaction and their impact under varied financial statements.

In addition, all the business efficiencies seem to be created using the standard accounting practices that will foster a fair financial reporting which will be used by the millions of shareholders of the company. Furthermore, such business efficiencies are also created under the accounting standards; hence any discrepancy related to financial reporting could easily be unearthed by the financial analyst. Overall such business efficiencies will be beneficial for the shareholders and the company itself.

Works Cited

Accounting Cycle. 10 November 2014 .

Caterpillar Inc Balance Sheet. 11 November 2014 .