

# Fin 510a, managerial accounting essay examples

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## Amazon. com vs. Industry Averages

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Since 2004, Amazon's online sales have far out-performed its top online retail competitors. By the end of 2012, the company reported \$61. 1 billion in total sales. Its nearest competitor in the online retail space, Staples, reported \$11. 8 billion in total sales in 2012 . With such a significant lead over its competitors in total sales, one could assume the company is having strong financial roots. However total sales is only one measure of financial strength. However, to have a deep insight into Amazon's financial position in the market, a financial analysis against industry averages should be conducted.

The following analysis will display profitability and solvency ratios to compare Amazon to industry averages. The comparison will reveal if Amazon is truly in a position of strength as its total sales imply. Table 1, below, compares Amazon's key ratios and returns against industry averages.

### **Note: the data for Industry averages is from Thomson Reuters Corporation,**

Retrieved February 17, 2014 from

Constraining our analysis for the fiscal year of 2012, the gross profit margin of the company improved by 2. 5% in comparison to the previous year and was reported to be 24. 8%. However, the profitability result was less than the industrial average of 31. 4%, which could primarily be attributed to high cost of sales which account for 75. 2% of total sales during 2012. Interestingly, the results seem optimistic for the company as over the years, the percentage of the cost of sales to the total sales has reduced significantly

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and if the trend continues, we can expect the gross margin to be in line with the industrial average.

However, the net profit margins of the company, indicates a completely different story as Amazon Inc. ended the year 2012 with the net loss of 0.1% that was 3.3% lower to the industrial average. This was primarily caused because of increasing percentage of Selling, Distribution Expenses to sales that during the year accounted for 15.92% in comparison to 14.28% during 2011. Thus, operating expenses can be blamed for declining net profit margins of the company.

Hence, although the company might soon get in line with industrial averages relating to gross profit but the major concern shall be the declining trend in Net income of the company.

In terms of liquidity, Amazon's 2012 current ratio was 1.12 which is very similar to the industry average of 1.11 which indicates that the company has strong liquidity roots and is capable of paying off its short term obligations, this might help them to borrow funds to finance its growth strategy.

Judging the efficiency ratios of the company, these accounts receivable turnover ratio in 2012 was 20.59 which is significantly higher than the 16.29 industry average. Amazon's nearest competitor in the online retail space, Staples, Inc., reported a 12.63 accounts receivable turnover ratio in 2012, 3.66 points lower than Amazon. This indicates a strong financial position against the industry. However, Amazon's ratio has trended down 5.98 points since 2010. This could be an area of concern for the company if the trend continues but should not be the main area of focus as they are still

performing better than their competitors.

The company's inventory turnover ratio slightly decreased from 2010 through 2012, to 8.34 and is 2.49 points below the industry average. This number reveals the largest disadvantage for Amazon over the industry averages of the three ratios analyzed. This trending decline coupled with their standing against the industry is a concern as low inventory turnover means high processing period, that indicates, that too much capital is tied in the inventory and the inventory levels are obsolete. Thus, the company's management should review its inventory monitoring process and compare them within the industry to uncover best practices they may be overlooking. Amazon's ratio of net sales to assets in 2012 was 2.11, 0.85 ahead of the industry average. Since 2010, the ratio has only changed by .02. During this same time, the company's total assets increased from 18.8 billion in 2010 to 32.6 billion in 2012 or 73.2%. By maintaining a relatively flat net sales to asset's ratio while total assets increased at remarkable rate shows that Amazon is doing a good job at moving its products.

Since 2010, the company's rate earned on total assets declined dramatically from 7.3% to 0.2% and is 4.1% below the industry average. Their decline can be attributed to their large increase in assets each year since 2010. The combination of their eroding rate earned on total assets and unfavorable comparison to the industry should raise a red flag to most companies as it is a measure to show profitability. As discussed earlier, the long-term focus of the company has been on growth not profit so the gradual decline in this ratio is not surprising. Conversely, management should begin to develop strategies to manage assets more efficiently to generate more positive

earnings. If the decline continues raising the funding necessary to continue its grown strategy could become difficult or come at a costly rate.

Amazon's rate earned on stockholders' equity reveals the largest percentage difference over the industry. In 2012 the company's rate earned on stockholder's equity was -0.5% compared to an industry average 8.6%, a difference of 9.1%. Thus, both the analyst and the investors of the company will not be happy with these results. Thus, if this trend in ROE continues it will become difficult for the company to obtain future funding at lower costs and this could largely affect its growth plans.

In the nutshell, our above analysis indicates that the investments in growth activities are driving the decision making for Amazon. The company doesn't appear to be too concerned that their financial stability is in a less favorable position than the industry average. They have their eyes on the future and will weather the storm to get there. Amazon's CFO said it best, " We're investing a lot because of the opportunities we see "

Ratio Comparison: Amazon Inc vs Industry Average

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