Research paper on netflix financial ratios

Business, Company

Executive summary

Netflix is a one of the leading company in the entertainment industry. In 1997, Reed Hastings founded the company which began its operations by 1998 of renting and selling DVDs by mail. The company has grown to become leading online rental movie provider with a subscription base of over 10milllion. The company competitors include Blockbuster, Movie Gallery and Redbox among others. The company has included digital streaming to boost its revenue and market share so as to cope with the increasing competition. To sustain the large demand of online streaming movies the company has partnered with Samsung, LG electronics, CBS, Starz entertainment among others. The company follows GAAPs in preparing its accounting records and presents them according to IFRS. This means that its annual financial records reflect a true and fair view of company's financial position. The company financial ratios are all within the industry range, and all of which reflect firm's ability to succeed in long run.

Liquidity ratios

This ratio gauges the effectiveness of a company to pay current liabilities as they fall due. The importance of keeping good liquidity level is that suppliers would trust the organization and would be willing to supply goods on credit.

Current ratio

Current ratio tests company's liquidity. The ratio aims at establishing the company's capability in paying current liabilities from the available current assets . generally, a company is at a good position to pay current liabilities if the current ratio is almost one is to one (magoon, 28).

Current ratio = Current AssetsCurrent liabilities

2012= 2240. 79/1675. 93= 1. 3

2011= 1830. 86/1225. 06= 1. 5

2010= 640. 97/388. 58= 1. 6

Though the ratio has been falling since 2010 the company is able to pay its current liabilities from its current assets for the last three years. The ratio is within the industry average which is around 0. 8 for the three years considered.

Capital structure analysis ratios (indebtedness)

Debt to equity ratio

Debt to equity ratio = Total LIabilitiesTotal Equity

This is a leverage ratio which attempts to compare company's liabilities to the entire company's equity. It gives the composition of company's capital. A ratio higher than 0. 5 indicates the company has relied more on external financing than internal financing (bull, 2008).

Efficiency ratio

Asset turnover ratio

The ratio shows overreliance on external financing (Coyle, 2000). The industry average also shows that company's main competitors have their ratios above 2. 5 for the three years considered.

Asset turnover ratio

Asset turnover ratio = revenueAverage Total Assets

This ratio gauges the profitability of a company in respect to the assets it owns. Therefore, it checks the efficiency of management in using the

available assets to generate revenue. It is sometimes called return on investment.

2010 = 2162. 68982. 07 = 2. 2

2011 = 3204. 583069. 20 = 1. 04

2012= 3609. 28/ 3967. 8= 0. 91

This ratio shows that the efficiency of the company fell gradually over the last three years. However, this may not be unique because industrial average ratios depict the same scenario.

Profitability ratios

This ratios show how the company's ability to generate returns for the shareholders. (Bragg , 2002).

The above table has shown that net profit margin fell over the last three years. This shows that the management has not been able to control the company's expenditure so as to maintain high profit levels. The return on assets has decreased sharply over the last three years this shows that the management was unable to increase its effectiveness in utilization of assets. Lastly, the return on capital also fell drastically as well this shows that the return to shareholders fell. Therefore, it can generally be said that the profitability of the company fell over the last three years.

An analysis of its cash flow statement

The analysis of cash from operating activities shows a sharp decline in net cash flow from operating activities. Cash from operations was as follows: year 2012 was 22. 77 year 2011 was 22. 77 while in year 2010 was 317. 71. This indicates decreasing capabilities of company to raise revenue.

The money obtained from operating activities in year 2011 and 2012 was not enough to finance capital expenditure for the both years. The free cash flow was below one dollar in year 2011 and 2012. This shows that the company is unable to change the down turn in short run, so as to be able to maintain or grow its long term business and dividends.

Company stock price for the last three years

The stock prices increased in the year 2011 following high profits of year ending 2010. However, the fall in profit in the year ending 2011 led to a fall in stock prices thereafter.

The company stock price since 1st January, 2013

The chart shows that the company stock prices have been increasing gradually for the last few weeks (NFLX Basic Chart, 2013).

Dividend policy and history of dividend payments

The company has not been paying dividends over the last three years. The company adopted plough back profit policy so as to lower its debt equity ratio (Netflix, 2013).

Capital structure

The company has relied more on external financing than internal financing. This is proved by the debt equity ratio which is considerably high. Therefore, it is likeable that the company may face solvency problems in future. The attempt by management to plough back profit is the only way which can help to minimize the probability of solvency problems.

Recommendation s

The company profits fell drastically in the last two years. This has led to fall of share market price therefore, it is better for an investor to continue holding stocks of the company now than selling them at a loss. It is likely that the price will increase over time. However, the company policy to fail to pay dividends may make the company share price to rise at as low rate. Therefore, it is not recommendable for an investor who has short time interest on the company to purchase its stocks.

It is however, recommendable for investors with long term interests to invest in the company. This is because the share price has started to grow gradually. It seems that the market share of the company is likely to continue growing because the company revenues did not fall over the last few years despite the declining profitability and increasing competition. The company adoption of digital video streaming is key to its prosperity in the competitive market and will be key to generating returns for investors.

References

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