Analyze the financial aspects of creative using financial theories essay

1. ObjectivesThe objective of this project is to analyze the financial aspects of Creative using financial theories.

The financial theories will be applied to find out the problems and/or weaknesses the company faces in their financial statement. Lastly, recommendations will be introduced from the data collected. 2. Method of InvestigationBy using the financial report of Creative, doing a face-to-face interview with the store manager and researching for other support materials from secondary research such as related websites, articles and brochures, the strengths and weaknesses of Creative are being identified. From the strengths and weaknesses identified, recommendations will be made, so as to assist Creative in maintaining as being the global leader for product innovation in the audio and PDE market. 3.

Market Research3. 1 Market SegmentationCreative Technology is able to gain competitive advantages over her competitors as she is widely recognized as a global leader for product innovation in the audio and PDE market. Currently, Creative is trying to expand into the personal digital entertainment (PDE) market. The potential costumers Creative will be targeting at are known as “ mouse potatoes”. The “ mouse potatoes” include the gaming and music enthusiasts who are dedicated to interactive entertainment and willing to spend money to get the latest ‘ technotainment’. 3.

2 Market ProfileCreative Technologies was founded in 1981 with the vision that multimedia will revolutionize the way people interacted with their personal computers. Creative made her name with the launch of Sound

Blaster sound cards, multimedia revolution and portable audio players. As being globally recognized as a leader in digital entertainment products and product innovation in the audio and PDE, Creative aims to find a perfect balance between form and function so as to provide her consumers with products that is a sensory feast for both the eyes and the ears. 3. 3 Marketing MixProduct: Creative Technologies have a great number of products which are separated into 20 different product lines, with an average of 5 different types of items in each line and about 8 varieties to choose from.

Her main product lines will be the Sound Blaster cards, Portable media players, MP3 players and PC peripherals. All the products are designed in a user-friendly way and include warranties and instruction manuals on how to operate the device. Then, customer support and product software updates are also provided. Price: The general pricing approach used by Creative is competition-based pricing. Then, the price-adjustment strategies used are namely promotional pricing and psychological pricing. Place: There are currently 3 CREATIVE stores.

Creative’s main store is located at International Business Park. It is the largest store out of all 3 as it serves as a research centre and a customer service centre. Next, are the two branches located at the city area; Plaza Singapura and Marina Square. The colors black and white are chosen to display the splendor and sophistication of the stores.

On average, each store has an average of about 400 to 500 customers per day on weekdays and 1000 customers per day on weekends. Promotions:

Creative has many types of advertising methods. Publishing advertisement on the newspaper and magazines and journalist appraisal are done for new products. Also, brochures are given out on road shows and from their retail outlets for new and current products. Sales promotions are carried out a few times per year to generate short term sales. To build rapport with her consumers, Creative emails consumers who are on their mailing list the latest products and promotions available.

4. Financial Analysis4. 1 Common Size and Comparative Income StatementHorizontal AnalysisBalance SheetIn comparison for the total current assets of year 2005 to 2006, there was a decrease in total amount of current assets from 2006 to 2005. However, in percentage, it has a higher percentage of 76% as compared to 2005 which only have 73%.

In 2006, the amount of cash received had increased more than 2005 of which $100million were from the compensation from Apple settlement (refer to appendix financial report 06 pg 2 ; article 3), thus it increased the percentage of cash and cash equivalents for that year as the actual amount and percentage of the other assets had dropped. As compared to the 2005, Creative had lesser cash but more accounts receivable whereas in 2006, they received more cash and lesser account receivable in their total current assets, thus this shows that there were more company indebted to Creative in 2005 than in 2006. Also, even though there was a decrease in the actual amount for account receivable in 2006, it still has a slightly higher percentage in the total assets as compare to the 2005. The decrease in actual amount for account receivable in 2006 might be due to the company giving cash incentive or discounts to companies that purchase stock on credit from them.

Using cash incentive, it would attract debtors to return their debts in cash on time which in turn would help to decrease the amount of bad debts in the company. Inventory for 2006 had also decreased significantly in term of the actual amount and overall percentage of the total assets. The decrease in inventory was in line with management's intention to maintain a lower inventory balance; this could be due to several factors such as excess and obsolescence of inventory which includes the write-down of flash memory inventory and low demand from the market that leads Creative to decrease in their inventory (refer to appendixes financial report 06 pg 2). Furthermore, though there was a drop in property and equipment in the actual amount, the percentage for 2006 has an increase as compared to 2005; reason was most probably because the other factor of assets had decreased in percentage for 2006. In 2006, the actual amount for total assets had decrease. This might be caused by the significant drop of fixed assets and inventory.

Mainly, the drop in investments as actual amount and percentage in the year 2006 was also due to SigmaTel's initial public offering that causes Creative's ownership percentage in the company to reduce even though Creative did not dispose any of its shareholdings during the initial public offering (refer to appendix financial report 06 pg 14). The total current liabilities in 2006 had an increase of 2% in percentage as compared to 2005; however, the actual amount of the current liabilities has decreased. This might be that the company has started to pay off much of their liabilities such as the accounts payable, accrued liabilities, income taxes payable and current portion of long term obligations and others. In 2006, the total liabilities had decreased, thus causing the long term obligation percentage in total liabilities to increase to 25% which is higher as compared to 2005. There was a large increase in share capital in 2006 that caused both the actual amount and percentage to increase greatly too. The drastic increase of the share capital may due to overcoming the negative effect that Creative faced in the year 2006 due to the adverse market conditions for MP3 digital audio players during the year.

The MP3 market continued to be adversely affected by the aggressive pricing practices and intense competition, exerting severe pressure on gross margins (refer to appendix financial report 06 pg 2 & article 5). Other reserves were incurred that year too. However, there was no deferred share compensation and additional paid-in capital paid that year and other shareholder's equity items such as the unrealized holding gains on investments, retained earnings had decreased in term of the actual amount and percentage. This leads to the reason of the decreased in total shareholder's equity, which include the decrease in total current liabilities, these were the effects that lead to the decreased in total liabilities and shareholder's equity. Income StatementThere was a slight decrease in the total amount of sales in the year 2006 as compared to year 2005, even though there was an increase in cost of goods sold which took up 85% as a total sale in the year 2006 as compared to year 2005 which only 77% as a total sale.

The increase of cost of goods sold was due to the steep and aggressive pricing of the MP3 audio player market however it pulled down the gross profit margin. The decrease in gross profit was primarily attributable to a substantial write-down of flash memory inventory in the third quarter of fiscal year 2006 due to a steep drop in the flash memory prices. The drop in flash memory prices had caused market uncertainty that resulted in lower sales and reductions in the selling prices of digital audio players, which negatively impacted gross profit (refer to appendix financial report 06 pg 2). Thus, the increased of cost of goods sold and decreased in sales, caused a decrease in gross profit in that year. As compared to the year 2005, more sales and lower gross profit were made, which lead to a higher gross profit marginIn the year 2006, though operating expenses were about the same as the year 2005 as sales made for the both year were quite close, however, due to the low gross profit, the year 2006 incurred a heavy operating loss as compare to the year 2005 where their gross profit earned was much higher than the year 2006 of amount and percentage. Which reflected that in the year 2006, there were a lot of goods and products produced and sold more than the year 2005, however, they were sold at a much lower price causing a lost in operating income.

This cause was due to the MP3 market in the year 2006 where there were aggressive price practice and intense competition in the marketing, exerting severe pressure on gross margins. In the end, a heavy net loss was incurred at the end of the year. As the more the products sold, more operating expenses were need, however, due to the low amount and percentage of gross profit for the year 2006 could not cover up after deducting operating expense. The drop in gain from investments, net for the year 2006 was due to the decrease in investment too, the lesser the investment the lesser investment gain. Overall, a net loss in 2006 was incurred much heavier than the net income of year 2005 was due to the low gross profit margin earned in the year 2006 as cost of goods sold for that year has a very high percentage.

4. 2 Comparative Common SizeHorizontal AnalysisBalance SheetThere was an increase in 14% of cash and cash equivalents in year 2006 as compared to year 2005. However, account receivable had decreased up to 18% in year 2006 as compared to year 2005. This shows that Creative had made an effort in the year 2006 to collects more cash and decrease their amount of accounts receivable of people who are in debt to them.

This may be that in year 2005, Creative has made most of the companies who were in debt in the year 2005 to pay up to them in the year 2006 and the company may have give cash discounts to companies that purchase stock from them who can pay up on time which will help to decrease the amount of bad debts in the company. Inventory in year 2006 had a decreased of 41%, as the decrease in inventory was in line with management's intention to maintain a lower inventory balance (refer to appendixes financial report 06 pg 16). This also shows that Creative has start to reduced or clear their stock left in the inventory, which may due to the write-down of the flash memory card and steep competitive MP3 audio player stocks. Creative may have started to pay off a lot of their advance debts, thus other assets and prepaid increased by 23% as compare to year 2005.

Resulting a dropped of 20% in the total current which was largely due to the decrease of inventory and accounts receivable. In the year 2006, their property and equipment, net, investments and other non-current assets has decreases. There was a drop of investments in the year 2006 due to SigmaTel's initial public offering that caused Creative's ownership percentage in the company to reduce even though Creative did not dispose any of its shareholdings during the initial public offering (refer to appendix financial report 06 pg 14). This thus caused the total assets to decrease to 23% as compared to year 2005.

There was a decrease in accounts payable, accrued liabilities, income taxes, current portion of long term obligations and others, which resulted to a 19% decrease in their total current liabilities. The significant decrease in liabilities factors such as the accounts payable had a decrease of 31%, the current portion of long term obligation of 36% and others and the other types of liabilities that were affected was due to having cash used in operating activities to offset these liabilities (refer to appendix financial report 06 pg 16). While the decrease of income taxes payable was due to the different tax jurisdictions in different countries, and when converted to USD, the income taxes were lower due to the translation of monetary denominated in currencies in the US dollar (refer to appendixes article 6). There was a significant increase of 3502% share capital in year 2006; $290, 188 of share capitals was pump into the company which was probably due to offset the loss in net income for the year. The decrease of 70% of unrealized holdings gains on investments was also due to the decrease in investments for that year. Low investments will lead to lesser unrealized holdings gains on investments.

Retained earnings has also a significant decrease of 86% as since there was a decrease in their net income for year 2006, thus retained earnings has decreased too. Overall, the total liabilities and shareholder's equity had a decrease of 23% as compared to the year 2005. Income StatementIncome in fiscal year 2006 was a net loss of $118, 747, 000, causing percentage of net income to decrease by 20, 195%. The decrease was firstly due to the sales in fiscal year 2006.

The sales decreased by 8% even though there was an increase of 1% in the cost of goods sold. This was because there were more goods sales but low net sales due to a steep drop in the prices of flash memory cards during the second half of the fiscal year which contributed to the reductions in the selling prices of digital audio players (refer to appendix financial report 06 pg 2). Next, the operating loss has a decrease of 112% in 2006 as compared to 2005 even though the operating expenses were lower. This was due to the decrease in the gross profit of 40% in 2006 as there was a steep drop in the flash memory prices, resulting in lower sales and reduction in the selling prices of digital audio players even though most cost of goods were sold (refer to appendix financial report 06 pg 2). There was a drastic decrease of 43% in their other charges was due to a $37.

3 million charge which comprised a $31. 4 million impairment charge relating to the goodwill and other intangible assets of 3Dlabs (refer to appendix financial report 06 pg 5). Even though gross profit was low but

operating expense remains the same amount in order to continue its operation on selling of goods as they are considered as fixed expense, it resulted in the operating income to be a loss. Then, gains from investments were 75% lower as Creative made lesser strategic equity investments in companies that can provide with technologies or products which believes that it could help Creative to gain competitive advantages in the market it competes in.(refer to appendix financial report 06 pg 12). Interest expense was 156% lower in fiscal year 2006 as compared to fiscal year 2005 due to the five-year $175.

0 million syndicated term loan, of which $100. 0 million was drawn-down in December 2004 and the remaining $75. 0 million in February 2005. Even though there was an increase of 75% in interest income due to the increase in cash and cash equivalents of the company. Overall, there was still net loss income due to high cost of goods sold, which lead to a decrease in gross profit where it could not cover up the rest of the operating expenses and thus even the other interest income, gain from investments, net, total add up could not also cover up the loss.

4. 3 Trend AnalysisTrends at Creative indicated that the cost of goods sold was increasing faster than sales, which was slowing down the increase in gross margin. Even though there was a slip in gross margin percentage on 2003 due to the low sales rate, the trend pick up on the next year, pushing the gross margin to the peak. However, on 2005, the gross margin dropped by 2% and by 2006, the trend dropped to only 63%, the lowest percentage over the 5 years.

Even though gross margin was the lowest during 2006, the cost of goods sold is 177%, the highest of the 5 years. The drop in the contribution margin in year 2006 was due to a steep drop in the prices of flash memory cards during the second half of the fiscal year, and contributed to reductions in the selling prices of digital audio players (refer to appendix financial report 06 pg 2 ; article 6). For the operating income, it decreased slightly in year 2003. As the operating expense for that year had dropped, the decrease of operating expense for that year was due to a slight decrease in gross profit.

At 2004, there was a significant increase in sales and cost of goods sold, thus pushed the operating income to 158%, the peak of the 5 years. However, in 2005, there was a sharp drop of the operating income, with 244% of loss made. This was because even though the sales increases, the cost of goods sold also increased and it was more than the sales, causing the gross profit to decreased. Also, there was an addition charge of $65, 225 of other charges and overall operating expense was higher than the previous years. In year 2005, the operation loss was the highest, with a decrease of 518% as there were lesser sales even though there were more costs of goods sold.

The operating expense was still considerably high, thus because of low sale, high cost of goods sold and operating expenses, it caused the gross profit to be the least as compared to the 4 years. Over the 5 years, net profit had increased sharply from the year 2002 to 2004, from 100% to 119% in the year 2003 and 681% in the year 2004. However, there was a significant drop in net income in the year 2005 to 3% and in 2006; it dropped to the worst amount of -599% which was the worst net loss among the 5 years. The significant drop in the year 2006 was partly due to the low sales, high cost of goods sold and thus incurring low gross profit earn. After offsetting the rest of the operating expense and adding of other incomes, they still could not incur a positive net income.