Sun microsystems report essay

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Introduction Sun Microsystems is a leading supplier of computer related products, including servers, workstations, storage devices, and network switches.

In the 2001 annual report, a letter to stockholders from the President and CEO Scott G. McNealy offered a remark saying that the fiscal year was ended with a significant revenue growth of 16% and that was a good indication of gaining market share. Also, that the employees were responsible for bringing the costs down and new products to the market. However, no earnings were cited and the information of income statement and additional analysis of other factors, consolidated balance sheet were available at the summaries. This report from Sun Microsystems to the shareholders will present all the information, in regard to the annual percentage change in net income per common share-diluted for 1998-1999, 1999-2000, and 2000-2001.

In addition, this report will compute the net income/revenue (sales) for those years, and will explain the major reason for the change reviewed for 2000-2001, using the ratio of the major income statement accounts to the net revenues (sales), cost of sales, research and development, selling, general, and administrative expense, and provision for income tax. In addition, using the data above, this report will show the return on stockholders' equity for 2000 and 2001, the profit margin, and the return on assets (investments) through net income/total assets and net income/sales x sales/total assets. It will also show the return on equity through return on assets/(1 – debt/assets), explaining the main contributing factor to change in return on stockholders' equity between 2000 and 2001, in terms of Du Pont system of analysis. In other moment, this report will indicate the price/earnings (P/E)

ratio for each year, based on the average stock price of each year (11 ? , 16 ? , 28 ? , 9 ? respectively), answering why the P/E has changed from 2000 to 2001. It will indicate the ratio price to book value for each year, and if there is any dramatic shift in the ratios worthy of note.

After that, this report will do an evaluation of financial statement analysis tools and a recommendation of business alternatives that can be made using the financial statement analysis. Annual Percentage Rate Change per common share-diluted, net income/revenue (sales) and main reason for changes in 2001. The annual percentage rate change per common share-diluted is calculated in to steps. First, it is necessary to calculate the change per common share-diluted for every two years (1998-1999, 1999-2000, 2000-2001). Then, get the result of that and divide by the first year taken.

The results will be as follow: 1998-1999 = 291% 999-2000 = 77% 2000-2001 = -51% The net income/revenue (sales) for each year is calculated taken the net expenses less the total costs and expenses of the relevant year. The results for the four years are: 1998 = $1, 114 1999 = $1, 520 2000 = $2, 393 2001 = $1, 312 Considering the major income statement accounts for 2000 and 2001, which have the following data, the major reason for the change in the net income/revenue (sales) was the increase in cost of sales in 2001. These costs were $7, 549 in 2000 and $10, 041 in 2001. The ratio was increased from 5.

92% to 13. 11%, an increase of 7. 19%. Year 2000 major income statement accounts cost of sales = $7, 549 research and development= $1, 630 selling, general and administration = $4, 072 provision for income tax =

$917 total = $14, 168 Ratio of major income statement accounts / net revenue (sales) from year 2000 = $14, 168 / $2, 393= 5.

92060= 5. 92% Year 2001 major income statement accounts cost of sales = $10, 041 research & development= $2, 016 selling, general and administration = $4, 544 provision for income tax = $603 total = $17, 204 Ratio of major income statement accounts / net revenue (sales) from year 2001 = $17, 204 / $1, 312 = 13. 1280487 = 13. 11% Return on Stockholders' Equity for 2000 and 2001, Ratios, and Main Contributing Factor to the Change in Return on Stockholders' Equity between 2000 and 2001, according to the terms of Du Pont System of Analysis. Using the Du Pont System of Analysis, which is net income divided by the stockholders' equity, the percentage of return on stockholders' equity for 2000 is 67%, and for 2001 is 33%.

Analyzing the ratios, some of the results found are: Profit Margin = Net Income/Sales 2000 = 11% 2001 = 5%, Return on Assets (investment) = Net income/Total Assets 2000 = 13% 001 = 5%, Net income/Sales x Sales/Total Assets 2000 = 11% x 1. 1% = 12. 1% 2001 = 5% x 1% = 5%, Return on Equity = Return on Assets/ (1-Debt/Assets)2000 = 0. 13 / 1-0. 483 = 26% 2001 = 0.

50 / 1-0. 417 = 11% The DuPont system of analysis looks at the return on assets (investment) = Profit margin x Asset turnover. Sun Microsystems return on stockholders' equity shows a decrease from 26% in 2000 to 11% in 2001. Sales increased over the previous year, the company incurred more debt in line items, such as operating cost of sales, R&D, increasing total

expenses on assets. Earnings at Sun Microsystems are down, and the company is carrying a higher debt and producing lower stockholder returns than the previous year. Leadership in the organization has delivered market share, at the expense of shareholders' equity.

In order to grow sales, additional debt and risk were incurred and inventory on hand reduced profits. Price/Earnings Ratio and the Change Reason in the levels of 2000 and 2001 The P/E Ratio is calculated by the stock price divided by the net income per common stock dilution. Based on that, the results are the following for the four years: 1998 11. 25/0. 4= 46.

88 1999 16. 75/0. 31= 54. 03 2000 28.

50/0. 55= 51. 82 2001 9. 50/0.

27= 35. 19 " The price-earnings ratio (or P/E ratio, as it is commonly called), is influenced by the earnings and the sales growth of the firm, the risk (or volatility in performance), the debt-equity structure of the firm, the dividend payment policy, the quality of management, and a number of other factors" (Block & Hirt, 2005). From 2000-2001 Sun Microsystems experienced a drop in net income from $1, 854 to $927. The decrease in net income caused the net income per common share to drop from $0. 5 to $0. 27.

An increase in the shares used in the calculation of net income per common share also contributed to the decrease in net income per common share. These changes would cause the P/E ratio to decrease because the current value of common stock was not as valuable in 2001 as it was in 2000. Ratio of Price to Book Value and Shifts in the Ratios The Ratio of Price to Book

Value is calculated getting the average stock prices for each of the four years divided by the book values per share. Based on that, the ratio for each year is: 1998 $11. 5/$1.

18 = 9. 53 1999 $16. 75/$1. 55 = 10. 81 2000 $28.

50/$2. 29 = 12. 45 2001 $9. 50/$3. 26 = 2.

91 Between 2000 and 2001, there was a dramatic shift in the ratio of price to book value ratio. " Stockholders' equity minus the preferred stock component represents the net worth, or book value, of the firm… If you take everything that the firm owns and subtract the debt and preferred stock obligation, the remainder belongs to the common stockholder and represents net worth" (Block & Hirt, 2005). Sun Microsystems' was able to increase the total of stockholders' equity by increasing total assets. The company also increased total debt, but the increase of total assets was a great deal larger. This change in the book value caused the ratio of price to book value drop significantly. Evaluation of Financial Statement Analysis Tools and Business Alternatives Financial Statement Analysis Tools are made with some assumptions of accounting and various components from the financial statements of a business.

These tools are used in conjunction to evaluate the financial performance of a business. The relative success of a business is evaluated y the financial ratios. Other aspects that can influence the success is the impact of inflation and disinflation on financial operations and timing of the recognition of sales as revenue, the treatment of inventory write-offs, the presence of extraordinary gains and losses, among others. Normally, radio analysis

allows the analyst to compare a performance of a business to the others in its industry.

The ratios are divided in four main groups to best help on the evaluation. Profitability ratios measure the ability of a business to earn an adequate return on sales, assets, and stockholders' equity. The asset utilization ratio measures how quickly the business turns over the accounts receivable, inventory, and longer-term assets. Liquidity ratio measures the ability to pay off short term obligations. Last, the Debt Utilization ratio indicates the overall debt position of the firm comparing to the business' asset base and earning power. To understand how the return on assets and equity are derived, analysts will use the Du Pont System of analysis, by breaking down return on assets and after that, showing how this return becomes return on equity.

Based on the numbers calculated above, Sun Microsystems has experienced significant fluctuations in performance. The net income between 1999 and 2000 had a big growth, leading up to a big decline between 2000 and 2001. The income statements have shown increased revenues in 2001. This is explained by the change on cost of sales, influencing negatively also the stockholders' equity. The support for losses came from return on assets and return on equity, where this return on stockholders' investments are small for revenue generated and the stock prices declined accordingly.

Those stocks were not as highly valued in the market in 2001. The difference between the net worth per share, and what the company was able to sell shares were decreased. Changes in the industry as a whole or changes in the habit of consumers could contribute for the changes in the stock values. Sun

Microsystems needs to seek for alternatives to save the company from keep having decreases on stockholders' equity. Some of these alternatives could be getting outsource of some employees to save some money, allowing more focus and emphasis on development of products to help increase revenue.

One negative consequence of this action could be the lost of moral of actual mployees, which were too responsible for winning the fight against costs over the last four years. This can be solved by implementing a good human resources strategy to keep the motivation up. Another good alternative could be bringing a consulting firm to identify possible problems with the respective solutions. This will increase a little the cost, but in a short period, this action would be compensated by the results. Through a new vision and focusing better in the appropriate market segment will bring new forces and energy to the company and the growth will change the route that Sun Microsystems starts in 2001. Conclusion Sun Microsystems needs to implement new plans and alternatives quickly to save the company from declining and losing its space into the market.

Looking carefully at the financial statement analysis, an analyst can identify its strengths and needs and make sure the company will keep growing and developing in the right direction. References Block, Stanley B. & Hirt, Geoffrey A. (2005). Foundations of Financial Management.

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