Ratio analysis sainsburys vs morrisons finance essay

When considered as a whole, the grocery market in the UK has steadily growing in size, being about 4 bigger today than it has been a year ago; August 2012 update: 12 weeks ending July 8, 2012 growth rate slows from 4. 2% to 2. 1% due mostly to a drop in price inflation: 6. 2% to 3.
8%. Morrison's is growing more slowly then Sainsbury's; the company is on track to add approx. 20 new stores in 2012 with most of those locations featuring a larger selection of produce. The UK grocery market was worth £163. 2 billion in 2012, an increase of 3. 8% on 2011, IGD forecast that the UK grocery market value will be worth £192. 6bn in 2017, an 18. 0% increase on 2012. The grocery market's share accounts for 54. 3p in every £1 of UK retail spending.

What is the size of the UK grocery market Source: IGD UK channel forecasts 2012

1. 2 The Companies

1. 2. 1 Sainsbury's

J Sainsbury plc. is the parent company of Sainsbury's Supermarkets Ltd, commonly known as Sainsbury's, the third largest chain of supermarkets in the United Kingdom with a share of the UK supermarket sector of 16. 5%. The group also has interests in property and banking. It was founded in 1869 and today operates over 1, 000 supermarkets and convenience stores and employs around 150, 000 colleagues. It is listed on the London Stock Exchange and is a constituent of the FTSE 100 Index.

1. 2. 2 Morrison’s

The supermarket, which generated sales of £18. 1 billion in the year, said it had not done enough to communicate its promotions and suffered because it still lacked a meaningful presence in the two fastest growing sectors of the market. Morrison’s is the UK’s fourth largest food retailer with over 400 stores. The super market is mainly food and grocery – weekly shop. Morrison’s employs 129, 000 staff at 498 stores. Their reports show that like-for-like sales dropped 2. 1% in the year, while the average of 11. 4 million customers in its stores each week was down on the prior year.

2. Gearing Ratio Analysis

2. 1 Gearing Ratios

Gearing Ratios (%)

Company/Year

2012

2011

Sainsbury

31. 73

30. 13

Morrison

22. 86

16. 25

Source : Appendix 1

Sainsbury’s

A gearing between 25% – 50% is generally considered nominal for an established business. It implies that Sainsbury is happy to finance its activities using borrowing. Sainsbury focuses more on investment in revenue growth rather than profit as the company increased sales revenue and non-current assets but suffered a loss in 2012.

Morrison’s

The business is considered “ low gearing” as its gearing is less than 25%. The business is growing through reinvestment of profits and minimizing risk. However, in 2012, there is an increase in gearing from 16. 25% in 2011 to 22. 86% and this is mainly because the business increased long-term borrowings by £548m and reduced retained earnings and shared capital.

2. 2 Interest Cover Ratio

Interest Cover Ratio

Company/Year

2012

2011

Sainsbury

6. 04

7. 40

Morrsion

20. 59

20. 62

Source : Appendix 2

Sainsbury's

The ratio indicates that the borrowing capital is used effectively to generate profits and that the business is able to meet its short-term interest obligations from its earnings. Sainsbury is growing, making worthwhile investments to continue to expand.

Morrison's

The ratio suggests that Morrison is generating enough income to cover its interest obligations and is thus financially stable. However, such a high ratio also suggests that Morrison is neglecting opportunities to magnify profits through leverage.

3. LIQUIDITY RATIO ANALYSIS

3. 1 CURRENT RATIO

COMPANY/YEAR

2011

2012

SAINSBURY

. 580

. 647

MORRISON

. 545

. 574

Source : Appendix 3

Sainsbury’s

Sainsbury’s current assets are considerably less than the current liabilities in both the years as Sainsbury has invested a lot in fixed assets as well as in subsidiaries and joint ventures. Sainsbury is obliged to pay a lot of money as a part of tax and also in generating its assets so the liability is therefore more than the assets. For every 1pound liability they have only 64. 7 pence worth of asset to cover it.

Morrison’s

Morrison current ratio is smaller than the current ratio of Sainsbury which indicates that Sainsbury is doing slightly better than Morrison in the market. Morrison current liabilities is more than the current assets due to more of borrowing that involves short term loans, investment in fixed assets and payment of tax. For every 1pound liability they have only 57. 4 worth of asset to cover it.

3. 2 ACID TEST RATIO

COMPANY/YEAR	2011	2012
SAINSBURY	. 304	. 348
MORRISON	. 239	. 247

Source : Appendix 4

Sainsbury’s

The acid test ratio is very less as Sainsbury, being a retail store, is highly dependent on sale of inventory. As acid test ratio of Sainsbury is . 348 that is less than 1 it means that Sainsbury cannot pay their current liabilities.

Morrison’s

Like Sainsbury’s, Morrison also being highly dependent on inventories, acid ratio is expected to be less. Morrison’s acid ratio is . 247, which is less than 1, meaning Morrison cannot pay their current liabilities. It would be only able to generate 24. 7 % cash of its current liabilities.

Both the companies fails in extinguishing its current liabilities but this is not due to their market position or growth but just due to the nature of the business (retail).

4. PROFITABILITY RATIO ANALYSIS

4. 1 Return on Capital Employed (ROCE)

Return on Capital Employed

Co./Year

2012

2011

Sainsbury's

10. 11 %

11. 06 %

Morrison's

13. 83 %

13. 70 %

(Source : Appendix 5)

Sainsbury's

ROCE growth in 2012 was lower than last year partly due to the cumulative effect of Sainsbury's accelerated investment in space growth since 2009 (Sainsbury's, 2011). This initially shrank profits whilst increasing the value of capital employed.

Morrison's

Morrison's delivered improved returns to its shareholders. For every £1 capital invested in the business, the annual return is 13. 83 pence in 2012 and was 13. 70 pence in 2011. This profitability ratio of Morrison is moderately higher than Sainsbury’s, hence Morrison’s is able to gain more profit on average capital employed.

4. 2 Return on Equity (ROE)

Return on Equity

Co./Year

2012

2011

Sainsbury’s

10. 62 %

11. 79 %

Morrison’s

12. 78 %

11. 66 %

(Source : Appendix 6)

Sainsbury’s

Sainsbury’s Return on Equity in 2012 has decreased by 1. 17 % compared to 2011 due to decline in shareholder funds. In 2011, they performed slightly better than Morrison’s as they had better reserves and share capital and the Profit after Tax (PAT) was significantly lower than Morrison’s.

Morrison's

Morrison's ROE has significantly improved over d last few years and continue to reach high values. In 2012, they showed a 1. 12% increase in ROE compared to 2011 and had a 12. 78 % shareholder equity. The shareholders invested a lot which resulted in higher returns.

4. 3 Gross Profit Margin

Gross Profit Margin

Co./Year

2012

2011

Sainsbury's

5. 43 %

5. 49 %

Morrison's

6. 89 %

6. 96 %

(Source : Appendix 7)

Sainsbury's

A moderate decline in the ratio between 2011 and 2012 explains the fact that the gross profit was lower in relation to sales revenue. This means that cost of sales was higher relative to sales revenue within the period.

Morrison’s

Morrison’s Gross Profit Margin is higher than Sainsbury’s as they had a lower sales revenue and moderate gross profit compared to the latter. In 2012, 6. 89 % of the net sales are available to pay off all the operating expenses.

4. 4 Net/Operating Profit Margin

Net/Operating Profit Margin

Co./Year

2012

2011

Sainsbury’s

3. 74 %

4. 07 %

Morrison’s

5. 48 %

5. 38 %

(Source : Appendix 8)

Sainsbury’s

Sainsbury accounted to lower Net Profit Margin than Morrison’s because of falling sales and rising costs. The market has a lot of competition where small groceries and convenience stores capture quite a bit of total UK food retail.

Morrison’s

Morrison’s performed fairly well and showed significant increase in the operating profits from Sainsbury’s over the past year. It accounted 5. 48 % Net Profit Margin in the current financial year (Sales Revenue: £17663m). It is a result of superior execution and induction of higher margin products in their sales mix.

Morrison’s seems to be more profitable than Sainsbury’s across all available profitability measures.

5. 0 Efficiency Ratios

(Source of Data, Apendix 9, Financial Reports of Sainsbury’s and Morrison’s)

5. 1 Fixed Assets Turnover

This ratio shows how efficiently the company is using fixed assets to generate sales. Low ratios indicate the company is capital intensive or that company requires a lot of fixed assets to generate a given amount of sales. (Gildersleeve, R. (1999) p. 136).

Efficiency Ratios

Year/Comp.

Sainsbury’s

Morrison’s

2011

2. 40 times

2. 18 times

2012

2. 39 times

2. 22 times

Sainsbury’s

In 2012 Sainsbury’s shows an increase in Sales Revenue for approx 1, 100 £m, which made its ratio slightly lower comparing to 2011. The ratio remained fairly similar because the value of fixed assets at net book value increased as well. The reason for the increase in fixed assets could be explained by Sainsbury’s tendency for opening new stores. The financial report states that they opened 19 new supermarkets, 28 extensions, and 73 convenience stores, which are only to begin operating and contributing to sales.

Morrison’s

On the other hand Morrison’s managed to improve their ratio by obtaining similar value of their fixed assets from 2011 to 2012, and using them more efficiently to score an increase in sales revenue of 1, 100£m. Generally looking at the industry the Average ratios for Retail – Food companies are between 4-5 (Wal-Mart Stores USA – 5. 00), (Gildersleeve, R. (1999) p. 136), so Sainsbury’s should aim to increase the use of their fixed assets in order to increase the sales.

5. 2 Average Inventories Turnover

Shows how many days company had to stock goods for sale before they were sold. In the retail-food industry this period should be kept fairly low because of the nature of the business. Lower ratio indicates that company will spend less funds towards stocking items before putting it on sale and getting profit from it.

Average Inventories Turnover

Year /Comp.

Sainsbury

Morrison

2011

14. 86 Days

15. 19 Days

2012

15. 85 Days

16. 85 Days

Sainsbury's

Sainsbury's shows growth in the average of inventories held over the course of year by almost 100 £m. As costs of sales have increased from 2011-2012, this ratio shows a slight growth in number of days goods are kept in stock. The increase of inventory in stock could be explained by Sainsbury's growth of sales in 2012. Higher demand forces company to have more items in stock in order to satisfy the needs of the customers.

Morrison's

Morrison's shows even higher growth in average days the goods are stocked. Morrison's also note the increase in cost of sales, even more than Sainsbury's. The financial reports of Morrison's state a few reasons, among which increasingly higher prices of fuel on the market.

5. 3 Profit Per Employee

Profit Per Employee

Year/ Comp.

Sainsbury

Morrison

2011

5, 572. 78 £ per emp.

6, 617. 50 £ per emp.

2012

5, 256. 58 £ per emp.

7, 217. 60 £ per emp.

Sainsbury's

It is notable that company's profit has been reduced from 2011-2012 for 2. 8 m£, which is 3. 4%, even though its sales have risen for 6. 8%. This could be explained by the number of reasons, but one of them that is important for this ratio is that they have also increased the number of employees. This has negatively influenced their Profit per Employee ratio, leaving it behind the industry average and Morrison's.

Morrison's

Unlike Sainsbury's, Morrison's notes the increase in profit and reduction of number of employees. This is the most desirable situation for a company. Their profit was higher for 8 % in 2012 than in 2011.

5. 4 Average Trade Debtor Collection Period

It indicates the period of time which is needed for company to collect trade debts. This ratio reveals a great deal about a company's credit policy and the efficiency which it can collect money from its customers. (Fight, A. (2006) p. 57)).

Average Trade Debtor Collection Period

Year/Comp.

Sainsbury

Morrison

2011

1. 61Days

4. 79 Days

2012

1. 90 Days

4. 34 Days

Sainsbury's

Sainsbury's shows an increase in the average time that they needed to collect the trade dept. Even though their costs of sales remained fairly similar, there was a substantial increase in the amount of trade debt. Even though this negatively influenced the ratio, Sainsbury's has made trades from which they expect to receive money in near future. Furthermore their ratio shows efficiency at collecting debts, comparing both to the industry and Morrison's.

Morrison's

Morrison's have significantly higher average debt collection period. Even though they have managed to slightly decrease their Trade receivables from 2011-2012, their costs of sales increased by approx 1, 000£m which has not made it possible for this ratio to improve further.

6. INVESTMENT RATIO ANALYSIS

FORMULAS

* Eearning Per Shares = profit available to shareholders/ no. of shares ranked for dividend

* Dividend Yield= dividend per share/ market price * 100%

*Dividend cover = Preference Dividend/Ordinary Dividend

SAINSBURY'S MORRISON'S

2011 2012 2011 2012

(%) (%)

EARNING PER SHARE

33. 8

31. 5

23. 43

26. 03

DIVIDEND YIELD

15. 10

16. 1

9. 60

10. 70

DIVIDEND COVER

1. 75

1. 75

2. 40

2. 39

6. 1 EARNING PER SHARE YEAR

Sainsbury's

In 2011 Sainsbury's experienced a sharp increase in earnings per share going up by 33. 8%. And in 2012 the Sainsbury went down with 31. 5% having a loss of 2. 3%. It is important that assets are revaluated in order to keep the real value of assets on balance sheet. Earnings per share in 2011 increased by 2. 3% to 33. 8 p, reflecting the improvement in the operating profit and the effect of the additional shares, more importantly due to the property profits.

Morrison's

Morrison's earnings per share compared to Sainsbury's are lower. This is driven by smaller profit and the fact that Morrison's is a smaller sized supermarket chain. The earning per share has 23. 43% at 2011 mainly caused by the higher profits on business disposals that the company went through last year, so the return to shareholders was a lower rate per share.

6. 2 DIVIDEND YIELD YEAR

Sainsbury's

The dividend yield had a slightly decreased since the dividend per share only increased by 15. 10% from 2011 year. This was a decision from the company and it reflects the reduction in the earning per share already mentioned and the fall in the dividend cover by 1. 75% in 2011.

Morrison's

Morrison dividend yield is much less in 2011 it was 9. 6% and in 2012 the dividend went up to 10. 70%.

6. 3 DIVIDEND COVER YEAR

Sainsbury's

Dividend cover of Sainsbury's says that earnings available for dividend cover is 1. 75% in 2011 and also in 2012 so there was not change in the divided cover over the past two years. In terms of dividend cover, Sainsbury's has its policy based on their calculations to maintain the dividend cover between 1. 50 – 1. 75 times. The reason behind it is that if the dividend cover is too low, there is a possibility that the company will not be able to pay out the investors.

Morrison's

In Morrison's divided cover, it showers that in 2011 it has 2. 40% whereas in 2012 it has 2. 39%, which is still more than Sainsbury. For the year 2011 Morrison's dividend cover is 2. 4 times, claim that it is in line with the European food retail sector average (Morrison's, 2011).

7. Future Perspectives and Strategies

Both Sainsbury's and Morrison's have their business strategies for future outlined in their financial statements. Morrison's financial strategy continues to deliver improved margins whilst positioning long term growth. They wish to increase their customer appeal and growth of sales, which is meant to be converted into profitable growth.

They have realized the potential in online retail, so they will finally enter the online groceries market to challenge Tesco, Asda and Sainsbury's, making it the last of the major supermarket groups to have an internet presence, but only after reporting its first fall in profits for six years. C: UsersUSERDesktopfinancial management1. JPG

Sainsbury's based their business strategy on meeting consumer needs, taking into the account the on-going inflation over the past four years. The economic downturn has changed how and what consumers buy, and these changes appear to be lasting. In 2012 they have launched their Live Well for Less campaign based on awarding loyalty and providing the best quality possible for optimal price. Through Nectar loyalty scheme they have a wealth of data about their customers' behaviour. C: UsersUSERDesktopfinancial management2. JPG

Source of the table: Morrison's financial statement 2012.

Source: Sainsbury's Financial Statement 2012

8 Conclusions

Financial statements suggest that Morrison's financial performance was very good. They had a profitable year (profit of £58m) while Sainsbury's performance was not good compared to 2011 (loss of £42m). Morrison's financial performance was strong, and they continued to invest in long term growth of the business, and to deliver increasing returns to shareholders.

Even after having steady increase in sales revenue and gross profit, Sainsbury suffered loss compared to previous year mainly because their interest and tax expenses increased while profit from joint ventures reduced. Though Sainsbury's acquisition of non-current assets was underfinanced with long term sources of finance, they still managed to generate more sales and cover the debt payable easily.

Alternatively, Morrison's financial management was excellent as they covered all their non-current assets with long term sources of finance. High interest cover ratio indicates that there is no sort of pressure on the company and is very profitable.

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Appendix 1

Gearing Ratio = Long Term Loans + Value of Preference Shares

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Share Capital + Reserves + Long term Loans + Minority Interest

Sainsbury’s

2012

2011

2617 + 0

538 + 5091 + 2617 + 0

2339 + 0

535 + 4889 + 2339 + 0

= 31. 73 %

= 30. 13 %

Morrison’s

2012

2011

1600 + 0

253 + 5144 + 1600 + 0

1052 + 0

266 + 5154 + 1052 + 0

= 22. 86 %

= 16. 25 %

Appendix 2

Interest Cover Ratio = Profit before interest and tax

Interest payable

Sainsbury

2012

2011

834

138

859

116

= 6. 04

= 7. 40

Morrison

2012

2011

968

47

887

43

= 20. 59

= 20. 62

Appendix 3

Current ratio = current assets / current liabilities

Sainsbury's

2011

2012

Current assets = 1708

Current liabilities = 2942

Current ratio = 1708/2942

= . 580

Current assets = 2032

Current liabilities = 3136

Current ratio = 2032/3136

= . 647

Morrison's

2011

2012

current assets = 1138

current liabilities = 2086

current ratio = 1138/2086

= . 545

Current assets = 1322

current liabilities = 2303

current ratio = 1322/2303

= . 574

Appendix 4

Acid test ratio = liquid asset / current liabilities

Liquid asset = current asset – inventories

2011

2012

Current assets = 1708

inventories = 812

liquid asset = 1708 – 812

= 896

current liabilities = 2942

acid test ratio = 896 / 2942

= . 304

Current assets = 2032

inventories = 938

liquid asset = 2032 – 938

= 1094

current liabilities = 3136

acid test ratio = 1094 / 3136

= . 348

Sainsbury's

Morrison's

2011

2012

current assets = 1138

inventories = 638

liquid asset = 1138 – 638

= 500

current liabilities = 2086

acid test ratio = 500 / 2086

= . 239

current assets = 1322

inventories = 759

liquid asset = 1322 – 759

= 569

current liabilities = 2703

acid test ratio = 569 / 2703

= . 247

Appendix 5

Return on Capital Employed (ROCE)

ROCE =

For Sainsbury's

2012

2011

834 X 100

538 + 5091 + 2617 + 0

859 X 100

535 + 4889 + 2339 + 0

= 10. 11 %

= 11. 06 %

For Morrison's

2012

2011

968 X 100

253 + 5144 + 1600 + 0

887 X 100

266 + 5154 + 1643 + 0

= 13. 83 %

= 13. 70 %

Appendix 6

Return on Equity (ROE) = Profit after Tax X 100

Share Capital + Reserves

For Sainsbury's

2012

2011

598 X 100

538 + 5091

640 X 100

535 + 4889

= 10. 62 %

= 11. 79 %

For Morrison's

2012

2011

690 X 100

253 + 5144

632 X 100

266 + 5154

= 12. 78 %

= 11. 66 %

Appendix 7

Gross Profit Margin = Gross Profit X 100

Sales Revenue

For Sainsbury's

2012

2011

1211 X 100

22294

1160 X 100

21102

= 5. 43 %

= 5. 49 %

For Morrison's

2012

2011

1217 X 100

17663

1148 X 100

16479

= 6. 89 %

= 6. 96 %