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Financial Analysis Report

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Financial Analysis Report

**Executive Summary**

Edgewell Personal Care Company (EPC) is a global manufacturer of personal care products. The company operates in a highly competitive industry, both globally and in the United States. Some of the EPC Company major competitors include Procter Gamble, Colgate Palmolive, Church Dwight, and Fuling Global. Thus, these companies have to compete for customer acceptance as well as limited retail shelf space. The competition revolves around the brand perception, customer service, product performance, and price. The EPC Company main care products include wet shave blades, gels, lotions, electric shavers, and razors.

The EPC and P&G Company forecast and report their financial results on a "Non-GAAP" and GAAP standards. Thus, their financial reporting involves reconciling “Non-GAAP” results with GAAP measures. The financial result reconciliation involves measures which can be compared directly. Also, the financial comparison of EPC and P&G Companies will contain forward-looking and historical statements. Forward-looking statements will not be based on the historical facts but rather on estimating future results or events for each of the two companies. EPC and P&G Companies are subject to international operation risks such as currency fluctuations, global economic conditions and other global market conditions that would affect their operations adversely.

In this case, financial analysis and performance of EPC will be done relative to The Procter & Gamble Company as the major competitor. The latter company owns a Gillette brand, and it is emerging as the market leader in the wet shave segment. Schick-Wilkinson Sword is the main wet shave brand for the EPC. The global market coverage of the Gillette brand and Schick-Wilkinson is estimated to be 80%. Other product’s segments between the two companies include the feminine care, sun and skin care among other personal care products. This market is dynamic, and the competitive capacity depends on the ability to introduce new products, promotional programs, and advertisement. In the effort to expand the market in this product segment, The Procter & Gamble Company and other global personal care companies have impacted trends in the care market. It is due to market growth and trends that the two companies have different financial performance, although operating in the same industry. However, the competition impact between EPC and The Procter & Gamble Company can be demonstrated more clearly through a financial ratio analysis.

Financial ratio analysis involves weighing the performance of the company by financial statement values. Financial ratios are categorized depending on what they measure, such as growth, liquidity, profitability, and capital structure. All these financial ratios combined will provide a comprehensive financial report between EPC and The Procter & Gamble Company.

**Income Statement Comparison**

The income statement summarizes the results of the operations for the two companies for the years 2015 and 2016. Income statement comprises of net sales, gross margin, expenses and net income. The primary factors driving the difference in the operations include the overall market growth which affects the net sales. Similarly, change in the sale volume is affected by the competitor’s activity and customer base expansion which drives the prices as well as unit volume.

|  |
| --- |
| **Edgewell Personal Care Company** |
| **Income Statement for the Years 2015 and 2016 (In Millions)** |
|  |  | **2015** |  | **2016** |
| **Sales/Revenue** |  | **2,420** |  | **2,360** |
|  COGS excluding D&A | 1,140 |  | 1,100 |  |
| Depreciation & Amortization Expense | 90.0 |  | 100 |  |
| Cost of Goods Inc. D&A |  | 1230 |  | 1,200 |
| **Gross Income** |  | **1,190** |  | **1,160** |
|  SG&A Expense |  | (872.1) |  | (809.5) |
| Unusual Expense |  | (662.7) |  | (67.6) |
| EBIT after Unusual Expense (Gross Income-Expenses) |  | (346.8) |  | 284.8 |
| Non-Operating Income/Expense | (12.1) |  | 6.9 |  |
|  Interest Expense | (99.8) |  | (71.8) |  |
|  Pretax Income |  | (458.7) |  | 219.9 |
| Income Tax |  | 162.6 |  | 41.2 |
| **Net Income (Loss)** |  | **(296.1)** |  | **178.7** |

Table 1 *EPC Company’s Income Statement* (Reuters Fundamentals (New York Stock Exchange)

The EPC Company had net sales of $2,360 in 2016 which is a decrease of 1.1% from 2015 fiscal year. However, if the income statement excludes the effect of currency fluctuations, the net sales for the year 2016 can be considered as increased by 1.4% compared to the fiscal year 2015. On the other hand, the 2016 fiscal year gross incomet is $1,160 mln compared to the prior year $1,190.0 mln. The decline in gross profit was as a result of lower net sales and also high production costs.

**Profitability Financial Ratios**

**Contribution Margin Ratio**

The CM ratio measures the impact of changes in sales to profit. Also, it is used as the standard tool in budgeting to estimate the decrease in profits in case of sales decline. It expresses contribution margin in terms of sales.

**EPC Contribution Margin Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **Contribution Margin** | 2.42 | 2.36 |
| **Sales** | 1.19 | 1.16 |
| **CM Ratio** | 2.03 | 2.03 |

Table 2 *EPC Contribution Margin Ratio*

**P&G Contribution Margin Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **Contribution Margin** | 13,441 |  11,049 |
| **Sales** | 65,299 |  70,749 |
| **CM Ratio** | 0.210 |  0.160 |

Table 3 *P&G Contribution Margin Ratio*

For a company that is performing better, the CM ratio should be relatively high. The EPC Company has maintained a constant Contribution Margin Ratio for the years 2015 and 2016. Since the CM ratio is bigger than 1, it shows the ability of the EPC company to cover administration overhead and fixed costs.

**Operating Margin Ratio**

 OM ratio is a profitability ratio that expresses operating income in terms of total revenue. In other words, operating margin ratio demonstrates the proportion of revenue available to cover non-operating cost. OM ratio is calculated as operating income divided by net sales (total revenue).

**EPC Operating Margin Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **Operating Income** | (12.10) | 6.90 |
| **Net Sales** |  242.00  | 236.00 |
| **OM Ratio** | -0.05 | 0.03 |

Table 4 *EPC Operating Margin Ratio*

**P&G Operating Margin Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **Operating Income** | 13,441 | 11,049 |
| **Net Sales** | 65,299  | 70,749 |
| **OM Ratio** | 0.200 | 0.200 |

Table 5 *P&G Operating Margin Ratio*

OM ratio shows the ability of the companies to support their operations. Thus, P&G Company has a higher OM ratio and is considered to be more stable in covering operating expenses compared to EPC Company. The P&G operating margin ratio of 20% means that for every $1 of income there is a balance of 20 cents after covering expenses.

**Return on Equity**

Return on shareholders’ equity ratio shows the amount of net income generated by the companies using shareholders’ equity or funds invested. Thus, companies with a higher return on equity are more efficient in generating net income from the shareholders' funds. Return on shareholders’ equity ratio will be calculated as net income divided by shareholders' common equity.

**EPC Return on Equity**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Income | **(296.100)** | **178.700** |
| Common Equity | 1,864.100 | 1,829 |
| ROE | -0.160 | 0.100 |

Table 6 *EPC Return on Shareholders’ Equity*

**P&G Return on Shareholders’ Equity**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Income | 7,036,000.00 | 10,508,000.00 |
| Common Equity | 62,419,000.00 | 57,341,000.00 |
| ROE | 0.11 | 0.18 |

Table 7 *P&G Return on Shareholders’ Equity*

Based on the above return on shareholders’ equity for the years 2015 and 2015, P&G Company has a higher ratio compared to EPC. The higher ratio indicates that P&G is more capable of generating net income using shareholders’ equity compared to EPC.

**Liquidity Financial Ratios**

**Current Ratio**

It is a liquidity ratio that measures the ability of the company to pay its long-term and short-term debts using current assets (Kirkham, 2012). In most cases, the current ratio is used by the investors and creditors in assessing the ability of the company to pay its current liabilities.

**EPC Current Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Current Asset | 1452.00 | 1636.60 |
| Current Liability | 868.20 | 1600.80 |
| Current Ratio |  1.47 | 1.00 |

Table 8 *EPC Company Current Ratio*

**P&G Company Current Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Current Asset | 74475.00 | 61232.00 |
| Current Liability | 29790.00 | 30770.00 |
| Current Ratio | 2.50 | 1.99 |

Table 9 *P&G Company Current Ratio*

Since current ratio demonstrates the financial stability of the company, P&G Company is in a better financial position compared to the EPC. The high current ratio of P&G resulted from the Beauty Brands assets and liability which were held for sale on the closing date. In this case, the company recorded the Beauty Brand transaction for assets and liability. Thus, they were reported on the Consolidated Balance Sheets. The firm will be considered to be healthy and perform well when the liquidity ratio is ranging between 1 and 3. Thus, P&G Company is more liquid compared to EPC.

**Acid-Test Ratio**

The ratio will measure the capacity of the two firms to settle their current liabilities using the quick assets. In this case, quick assets include all assets that can be converted into cash within or less than 90 days. According to the balance sheet elements of EPC and P&G Company, quick assets include account receivables, short-term investments, and cash equivalents.

Acid-Test Ratio = Quick Assets/Current Liabilities

Quick assets = Current Assets-Inventories

**P&G Company Acid-Test Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Current Assets | 74475.0 | 61232.0 |
| Inventories | 29790.0 | 0.0 |
| Quick Assets | 44685.0 | 61540.0 |
| Current Liabilities | 29790.0 | 30770.0 |
| Acid-Test Ratio | 1.5 | 2.0 |

Table 10 *P&G Acid-Test Ratio*

**EPC Acid-Test Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Current Assets | 1452.0 | 1636.6 |
| Inventories | 673.0 | 24308.0 |
| Quick Assets | 778.0 | 36924.0 |
| Current Liabilities | 868.2 | 1600.8 |
| Acid-Test Ratio | 0.9 | 1.2 |

Table 11 *EPC Company Acid-Test Ratio*

Based on the above Acid-Test ratio for fiscal year 2015, P&G ratio is bigger than 1. It

means that the company is in a position to pay current liabilities without disposing long-term assets (Pervan and Kuvek, 2013). However, the Acid-Test ratio for EPC is less than 1 which means that company has to sell long-term assets to settle current liabilities. P&G Company’s Acid-Test ratio for the year 2016 is higher compared to the EPC Acid-Test ratio. The latter company has invested more in the inventories, thus a low level of quick assets.

**Efficiency Financial Ratios**

**Accounts Receivable Turnover**

It is an efficiency ratio and measures the number of times a company can convert its accounts receivable into cash. In other words, it shows the frequency in which a company can collect an average account receivable during the financial year.

**EPC Accounts Receivable Turnover**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Credit Sales | 2,421,200.000 | 2,362,000 |
| Av Acc. Receivables | 279,800.000 | 260,700 |
| Acc. Rec. Turnover | 8.650 | 9.060 |

Table 12 *EPC Accounts Receivable Turnover*

**P&G Accounts Receivable Turnover**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Credit Sales | 76,279.000 | 65,299.000 |
| Av Acc. Receivables | 4,861.000 | 4,373.000 |
| Acc. Rec. Turnover | 15.690 | 14.930 |

Table 13 *P&G Accounts Receivable Turnover*

Based on the above accounts receivable turnover analysis, P&G Company is likely to collect credit sales more frequently compared to EPC Company.

**Days Sales in Accounts Receivable**

The days sales in accounts receivable demonstrate the efficiency of the company in collecting cash from their customers. Alternatively, they are the number of days a company takes in converting sales into cash. The ratio is obtained by dividing the accounts receivable with total credit sales and then multiplying it by 365 days.

**EPC Days Sales in Accounts Receivable**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Credit Sales | 2,421,200 | 2,362,000 |
| Av Acc. Receivables | 279,800 | 260,700 |
| Days Sales | 42  | 41  |

Table 14 *EPC Days Sales in Accounts Receivable*

**P&G Days Sales in Accounts Receivable**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Net Credit Sales | 76,279 | 65,299 |
| Av Acc. Receivables | 4,861 | 4,373 |
| Days Sales | 24  | 25  |

Table 15 *P&G Days Sales in Accounts Receivable*

P&G Company’s ability to collect cash from the customers within 24 and 25 days for the years 2015 and 2016 is more favorable compared to EPC.

**Inventory Turnover and Days Outstanding Ratio**

Inventory turnover ratio measures the frequency in which a company sell its inventory within a financial period. The frequency depends on the volume of purchases and sales made by the company. Thus, to improve turnover the company has to make a larger amount of sales. It is calculated by dividing the cost of sales and average inventory. On the other hand, inventory days outstanding ratio measures the number of days that a company would take to sell its entire inventory. It is calculated by dividing ending inventory with the cost of sales and multiplying it by 365 days.

**EPC Inventory Turnover and Days Outstanding Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Cost of Goods Sold | 1,230 | 1,200 |
| Average Inventory | 33,280 | 30,920  |
| Inventory Turnover | 27 | 26 |
| Days Outstanding  | 14 | 14 |

Table 16 *EPC Inventory Turnover and Days Outstanding Ratio*

**P&G Inventory Turnover and Days Outstanding Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| Cost of Goods Sold | 32,909,000.0  | 37,056,000.0  |
| Average Inventory | 4,979,000.0 | 4,716,000.0 |
| Inventory Turnover  | 6.6 | 7.9 |
| Days Outstanding | 56.0 | 47.0 |

Table 17 *P&G Inventory Turnover and Days Outstanding Ratio*

**Market Value Ratio**

**Price/Earnings Multiple**

 P/E ratio of a company compares the market value of a stock to its earnings. In other words, the ratio compares the market and earning per share. Thus, a high P/E ratio is a sign of positive performance of a company in future. Similarly, a low P/E ratio indicates that a company is currently performing poorly. The ratio is calculated as market price per share divided by earning price per share.

**EPC Price/Earnings Multiple**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **MPS** | 89.01 | 89.26 |
| **EPS** | 2.80 | 3.90 |
| **P/E Ratio** | 31.79 | 22.89 |

Table 18 *EPC Company Price/Earnings Ratio*

**P&G Company Price/Earnings Ratio**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016** |
| **MPS** | 39.20 | 41.20 |
| **EPS** | 2.44 | 3.69 |
| **P/E Ratio** | 16.06 | 11.17 |

Table 19 *P&G Company Price/Earnings Ratio*

**Conclusion**

**EPC Strengths**

The P/E ratio of the EPC demonstrates one of its strengths. High P/E ratio has been associated with the stronger portfolio with more than 65 brands. Also, it embraces innovation that drives their brand leadership on the global market.

**EPC Weaknesses**

The results of profitability ratios show the major weaknesses of the EPC Company. For instance, in the net profit margin, EPC Company is not able to generate revenue that can cover the operating costs. Similarly, Acid-Test and current ratio indicated that EPC Company could not effectively use total assets or quick assets to settle current liabilities.

**EPC Opportunities to Improve**

Although most of the EPC financial results are not favorable, there is an opportunity of performing better in future. For instance, before closing the year 2016 financial statements, the Company had completely acquired Bulldog Skincare Holdings. The acquired company dealt with grooming and skincare products for men. Also, the acquired firm had a net worth of $34 million at the time of acquisition. The acquisition is expected to expand Edgewell’s portfolio into global markets where it can leverage its international geographic operations. The post-acquisition period of Bulldog appeared in the Edgewell Company’s results of the quarter ended April 31, 2017. All the assets acquired were included in the Edgewell Company Sun and Skin Care segment.

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