

# Financial Statement Analysis Paper

## Example 1: Dell Computer

Dell Inc.	Current Year		Prior Year		3 Years Ago	
	\$	Percent	\$	Percent	\$	Percent
<b>Income Statement</b>						
Revenue	61,494	100.0%	52,902	100.0%	61,101	100.0%
Cost of Goods Sold	49,128	79.9%	42,789	80.9%	49,375	80.8%
Gross Profit	12,366	20.1%	10,113	19.1%	11,726	19.2%
R&D	661	1.1%	624	1.2%	663	1.1%
Selling General & Administrative	7,302	11.9%	6,465	12.2%	7,102	11.6%
Non Recurring	0	0.0%	0	0.0%	0	0.0%
Others	0	0.0%	0	0.0%	0	0.0%
Operating Income	4,403	7.2%	3,024	5.7%	3,961	6.5%
Depreciation Expense	970	1.6%	852	1.6%	769	1.3%
Other Income/Expense	116	0.2%	12	0.0%	47	0.1%
EBIT	3,549	5.8%	2,184	4.1%	3,417	5.6%
Interest Expense	199	0.3%	160	0.3%	93	0.2%
Tax Expense	715	1.2%	591	1.1%	846	1.4%
Income from Cont Operations	2,635	4.3%	1,433	2.7%	2,478	4.1%
Net Income	2,635	4.3%	1,433	2.7%	2,478	4.1%
<b>Balance Sheet</b>						
Cash	13,913	36.0%	10,635	31.6%	8,352	31.5%
Short Term Investments	452	1.2%	373	1.1%	740	2.8%
Accounts Receivable	10,136	26.3%	8,543	25.4%	6,443	24.3%
Inventory	1,301	3.4%	1,051	3.1%	867	3.3%
Other Current Assets	3,219	8.3%	3,643	10.8%	3,749	14.1%
Total Current Assets	29,021	75.2%	24,245	72.0%	20,151	76.0%
Long Term Investments	1,503	3.9%	1,113	3.3%	954	3.6%
PP&E Net	1,953	5.1%	2,181	6.5%	2,277	8.6%
Goodwill	4,365	11.3%	4,074	12.1%	1,737	6.6%
Intangibles	1,495	3.9%	1,694	5.0%	724	2.7%
Other Assets	262	0.7%	345	1.0%	657	2.5%
Total Assets	38,599	100.0%	33,652	100.0%	26,500	100.0%

Accounts Payable	15,474	40.1%	15,257	45.3%	12,045	45.5%
Short/Current L.T. Debt	851	2.2%	663	2.0%	113	0.4%
Other Current Liabilities	3,158	8.2%	3,040	9.0%	2,701	10.2%
Total Current Liabilities	19,483	50.5%	18,960	56.3%	14,859	56.1%
Long Term Debt	5,146	13.3%	3,417	10.2%	1,898	7.2%
Other Liabilities	6,204	16.1%	5,634	16.7%	5,472	20.6%
Minority Interest	0	0.0%	0	0.0%	0	0.0%
Total Liabilities	30,833	79.9%	28,011	83.2%	22,229	83.9%
Preferred Stock	0		0		0	0.0%
Common Stock	11,797		11,472		11,189	42.2%
Additional Paid In Capital	0		0		0	0.0%
Retained Earnings	24,744		22,110		20,677	78.0%
Treasury Stock (-)	28,704		27,904		-27,904	-105.3%
Other Equity	-71		-37		309	1.2%
Total Stockholders' Equity	7,766	20.1%	5,641	16.8%	4,271	16.1%

<b>RATIO ANALYSIS</b>					
<b>Growth Ratios</b>					
Sales Growth	16.2%		-13.4%		-0.1%
Income Growth	83.9%		-42.2%		-15.9%
Asset Growth	14.7%		27.0%		-3.8%
<b>Activity Ratios</b>					
Receivable Turnover	6.6		7.1		8.6
Inventory Turnover	41.8		44.6		48.2
Fixed Asset Turnover	31.5		24.3		26.8
<b>Profit Ratios</b>					
Profit Margin	4.3%		2.7%		4.1%
Return on Assets	7.3%		4.8%		9.2%
Return on Equity	39.3%		28.9%		61.9%
<b>Liquidity Ratios</b>					
Current Ratio	1.49		1.28		1.36
Quick Ratio	1.42		1.22		1.30
<b>Solvency Ratios</b>					
Debt to Total Assets	0.80		0.83		0.84
Times Interest Earned (Accrual)	17.83		13.65		36.74

Industry Measures	Jan-11		Jan-10		Jan-09	
Product Revenue	\$ 50,002.0	81.31%	\$ 43,697	82.60%	\$ 52,337	85.66%
Services Revenue	\$ 11,492.0	18.69%	\$ 9,205	17.40%	\$ 8,764	14.34%
Total Revenue	\$ 61,494.0	100.00%	\$ 52,902	100.00%	\$ 61,101	100.00%

Revenues come from the sale of Dell's products and services. Revenues increased a combined 16% from January 2010 to January 2011 primarily because of the recovery in the economy. The health of the economy is critical for the company because its products are not primary products; so during a recession, people will rather save money for food than buy a computer. This explains the big decline in revenues for the 2009 fiscal year (a 13.4% drop compared to the previous year). The increase in 2010 is also due to a change in business strategy. Dell is growing its enterprise solutions and services business which changed the revenue stream of the company. Services revenue has weighted more on total revenues year after year. It went from 14.3% of revenues in January 2009 to 18.7% of revenues in January 2011. Also, services revenue has been profitable with a 25% growth in 2010 and 5% growth in 2009. (Part 2, Item 7, Form 10-K, Dell Inc., January 2011)

Cost of goods and services have been relatively stable as a percentage of revenue for the past three years. Other expenses such as selling and administrative expenses, R&D expenses, depreciation expenses and more have also been relatively constant in the last three years. However, the company did have higher costs on a dollar basis. This increase in amortization of intangible assets and other cost is due to the increase in intangible assets from the Perot Systems in Fiscal 2010. Also, the company had a migration to contract manufacturers and closures of certain manufacturing facilities that caused an increase in severance and facility action costs. Even with all these value increases, the company has done a good job keeping their costs stable

as a percentage of revenues. Dell is well managed and knows how to control their costs. The company is on top of every detail and there are no surprise costs to harm the company. (Part 2, Item 7, Form 10-K, Dell Inc. 2011)

The net income performance of the company has been excellent for fiscal 2011 with an 84% increase from the previous year. This big increase in net income resulted in a 1.6% growth in profit margin and a 2.5% growth in ROA (return on asset). Higher revenues and good cost control are responsible for these growths. Another reason for the growth in net income is the change in the business operation of the company. Its service operations are expanding and have a lower cost than manufacturing the products. Fiscal 2010 had a decrease in net income of 42.2% mainly due to the drop in revenue and the acquisition of Perot Systems. Dell is planning to keep expanding specially on the services aspect of their business, which will help the company on the long run. (Part 2, Item 7, Form 10-K, Dell Inc. 2011)

Current assets accounts increased \$4,776 billion from the previous year, from representing 72% of total assets in fiscal 2010 to 75.2% in fiscal 2011 (a 3.2% growth). The cash and cash equivalent account is mostly responsible for this change as the account rose by more than \$3 billion or 4.4% of total assets. The company recognizes all highly liquid investments, including credit card receivables due from banks, with original maturities of three months or less at date of purchase. This rise is explained by an increase in revenues so cash provided by operations, and mainly by a decrease in cash used in investing activities. Cash used for investing activities totaled \$1.165 billion in fiscal 2011, a \$2,644 billion drop from fiscal 2010. The decrease is primarily due to the lack of material importance for the acquisitions in fiscal 2011 compared to the acquisition of Perot Systems in fiscal 2010. This also reflects lower proceeds

from sales of investments and property (partly offset by lower capital expenditures). (Part 2, Item 8 & 9, Form 10-K, Dell Inc. 2011)

In general, the company had a good fiscal year. It improved its ability to generate profit. All three of the main profitability's ratio (profit margin, return on assets and return on equity) have increased from the previous year; it means that the company is using its resources more efficiently. Contingencies such as lawsuits and federal, state and local regulations are reasonably possible because they are not in Dell's control and can occur at any time; the company believes that they will have a material adverse effect on its financial condition or results of operations if some of them occur. Also, the company received an unqualified opinion by its auditor, PricewaterhouseCoopers LLP, who is responsible to obtain reasonable assurance about whether the financial statement are free of material misstatement and verify the internal control of Dell over financial reporting. (Part 2, Item 8, Form 10-K, Dell Inc. 2011)

The property, plant and equipment (PPE) account is not very heavy in the company's balance sheet. It only represents 5.1% of Dell's total assets. The company uses lease and cash to acquire PPE. As of January 2011, Dell had approximately 18.1 million square feet of office, manufacturing, and warehouse space worldwide, with 8.3 million of these square feet located in the U.S. Also, 68% of these square feet are owned by Dell and the rest of the 32% are leased. Depreciation is provided using the straight-line method over the estimated economic lives of the assets, which range from ten to thirty years for buildings and two to five years for all other assets. Leasehold improvements are amortized over the shorter of five years or the lease term. During Fiscal 2011, the company closed a manufacturing plant in Winston-Salem (North Carolina), consolidated space on their Austin (Texas) campus that allowed them to close one building, and sold their fulfillment center in Nashville (Tennessee). Currently, a business center

in Coimbatore, India and a data center in Washington are under construction. The company has also announced the sale of its manufacturing facility in Lodz, Poland. All these activities during fiscal 2011 resulted to a drop of 1.4% in PPE. The fixed asset turnover ratio is 31.5 times, compared to 24.3times in the previous year. This big jump shows that the company is using its fixed assets more efficiently to generate revenue and it's a positive aspect for the future. The company is increasing revenues by offering various services that require less fixed assets. It's a change in their business operations and a shift of their revenue stream. (Part 1 & 2, Item 2 & 8, Form 10-K, Dell Inc. 2011)

Another strong aspect of the company's operations is its liquidity. As current assets increased and current liabilities decreased, both current ratio and quick ratio increased from 1.28 and 1.22 in fiscal 2010 to 1.49 and 1.42 respectively. On a dollar standpoint current liabilities stayed relatively stable. However, due the increase in total assets, current liabilities decreased 5.8% as percentage of total assets. These changes help Dell become more liquid and this is definitely an advantage. (Part 2, Item 8, Form 10-K, Dell Inc. 2011)

The Company generally borrows on a long-term basis and is exposed to the impact of interest rate changes and foreign currency fluctuations. The fair value of its debt obligations at January 28, 2011 totaled \$5.1 billion, compared with \$3.4 billion at January 29, 2010. The net increase in fiscal 2011 was primarily due to net issuances of approximately \$1.5 billion. No debt is maturing in fiscal 2012. This gives the company a little room to breathe and not issue any commercial paper or long-term debt to refinance maturing debts. The Company uses derivative instruments such as forward contracts and purchased options to hedge certain foreign currency exposures, and interest rate swaps to manage the exposure of its debt portfolio to interest rate risk. As stated in its 10-K document: *"Dell's objective is to offset gains and losses resulting from*

*these exposures with gains and losses on the derivative contracts used to hedge the exposures, thereby reducing volatility of earnings and protecting fair values of assets and liabilities. Dell assesses hedge effectiveness both at the onset of the hedge and at regular intervals throughout the life of the derivative and recognizes any ineffective portion of the hedge, as well as amounts not included in the assessment of effectiveness, in earnings as a component of interest and other, net.*” (Part 2, Item 8, Note 5, Form 10-K, Dell Inc. 2011)

The company’s stockholder’s equity went up \$2 billion. This increase is due to an increase in retained earning. As net income increased more than the stockholder’s equity, ROE (return on equity) went from 28.9% in fiscal 2010 to 39.3% in fiscal 2011. During this fiscal year, Dell also bought back \$800 million of shares which increased its level of treasury stock. Dell doesn’t pay dividends so the stockholders can make profit in the market with stock price variations. (Part 2, Item 8, Form 10-K, Dell Inc. 2011)