**Paper 4-Financial Analysis** **and Strategic Options and Actions**

1. Complete a five-year (most current full five years) financial analysis for your company and each of its major competitors.

 Present the information as ratios and trends (graphs and pie charts are very helpful for showing trends and relative comparisons).

Use the relevant metrics for your industry (e.g. if you are in the retail business and running brick-and-mortar store, then inventory turns, sales dollars per square foot of floor space, and sales per employee would be some appropriate measures).

Also use general measures such as ROE, Return on invested capital, Gross profit margin, and balance sheet information such as debt ratios, free cash flow, etc.

1. **What does the financial analysis tell you about your firm relative to the competition?** Whereis your company doing better than its competitors? Where does it need to improve?  What are the strategic implications for your company?

 **METRICS EXAMPLE**

|  |
| --- |
| **Financial Comparisons** |
| **Metric** | **Company 1** | **Company 2** |
| Profit Margin | **4.39%** | 1.45% |
| Return on Assets | **8.57%** | 6.22% |
| Return on Equity | 23.0% | **36.6%** |
| Debt to Equity | **0.71** | 2.11 |
| Return on Invested Capital | 18.6% | **21.7%** |
| Earnings Growth (3yr. avg.) | -1.7% | **+15.4%** |
| Inventory Turns | 8.3 | **15.0** |
| Sales/Square Foot | **$437** | 161 |
| Sales/Employee | $218,400 | **$277,328** |
| Net Income/Employee | $6,876 | **$7,243** |
| Free Cash Flow | **$7.4 bn** | $0.86 bn |
| Cash and short-term investments  | **12.8 bn** | 3.4 bn |
| Sales growth (3 year average) | **2.1%** | 1.2% |

**Company 2 -Good News**: Return on Equity, Return on Invested Capital, growth in earnings, inventory turns, and sales and profits per employee are better than the completion. **If we can continue to improve on these metrics we can continue to be better that competition.**

**Company 2-Bad News**: Profit Margins on sales, Return on Assets, debt-to-equity, sales per square foot, free cash flow, cash available, and annual sales growth are all less than competition. **These are areas that need to be improved to gain parity with the industry competitors.**

1. **Strategic Options and Actions**

Based on all the information that you have gathered about your company in this paper and the three previous (its general and competitive environments, financial analysis, industry life-cycle, Porter’s Five Forces analysis, competitors, threats and opportunities, value-chain analysis, resources, capabilities, strengths and weaknesses, life-cycle analysis, etc.), what are the strategic options for your company?

What strategy is best suited for your company (Cost leadership. Differentiation, Focus, Turnaround, or a combination and why)?

Based on the strategy that you recommend, what are the major actions that your company should to take to assure future profitability and growth?

Strategic Options and Actions should be a result of and flow from all the analysis and conclusions from the preceding steps:

1. **Mission and Goals** provide the framework for the developing the strategy as the strategy must be supportive of the mission and goals.
2. **External Environmental Analysis** provides a list of the **Opportunities and Threats** that are faced by the business that should be addressed by strategic actions.
3. **Competitive Analysis: Porter’s Five Forces** analysis including a review of the Complementors for the industry, should provide insights into what is necessary to be successful in the industry; reviewing the major competitors in the industry should provide insights into their strategies, their position, and their strengths and weaknesses. Do not attack strong competitors directly, find a way to win by focusing on their weaknesses and differentiating.
4. **Life-cycle Analysis** of the industry provides insights into the natural strategy and emphasis for the stage in the life-cycle.
5. **Value-chain Analysis** can be used to identify what support and primary activities are essential to success in a given industry, and how competitors are doing relative to your firm; and when used in conjunction with a **Resource Analysis** (tangible, intangible and organizational capabilities), can be used to identify **Strengths and Weaknesses** of a firm to form a basis for strategic actions. Strategy should be built on strengths and weaknesses need to be at least neutralized.
6. **Financial Analysis** is used to analyze key performance metrics in an industry relative to major competitors to identify **opportunities for improvement** and resultant strategic actions.
7. **Strategic Options** should be a result of reviewing the results of and consistent with the Environmental Analysis, Competitive Analysis, Life-cycle of the industry, Value-chain and resource analysis, and Financial Analysis and support the Mission and Goals of the organization.

C Vogus
Arkansas State University
Strategic Management