

Financial Analysis: A User Approach

Chapter 4

Quantitative Financial Analysis Using Financial Information

Quantitative Financial Analysis Using Financial Information

- A/K/A – Ratio Analysis

Ratio Analysis Is Always Comparative Analysis

- Time Series
- Cross Sectional
 - Competitors
 - Industry Averages
 - Market Averages
- Benchmarks and Rules of Thumb

Common Size Financial Statements

- Rescale Balance Sheet and Income Statement Accounts
 - Balance Sheet – Total Assets
 - Income Statement – Total Revenue

	6/27/08-\$	6/29/07-\$	6/27/08-%	6/29/07-%	WD
Assets					
Cash, CE, & S-TI	1,141	1,144	11.3%	12.1%	22.7%
Accounts Receivable	1,410	1,383	13.9%	14.6%	20.7%
Inventories	945	794	9.3%	8.4%	9.4%
Other Current Assets	776	480	7.7%	5.1%	3.2%
Total Current Assets	4,272	3,801	42.2%	40.1%	56.0%
Property & Equipment, net	2,464	2,278	24.3%	24.0%	34.2%
Goodwill & Other Intang.	2,463	2,488	24.3%	26.3%	4.0%
Other Assets	921	905	9.1%	9.6%	5.7%
Total Assets	10,120	9,472	100.0%	100.0%	100.0%
Liabilities					
Accounts Payable	1,652	1,301	16.3%	13.7%	24.2%
Accrued Expenses	1,275	1,018	12.6%	10.7%	7.3%
CP of LT Debt	360	330	3.6%	3.5%	0.6%
Total Current Liabilities	3,287	2,649	32.5%	28.0%	32.1%
Long-Term Debt	1,670	1,733	16.5%	18.3%	9.9%
Other LT Liabilities	577	353	5.7%	3.7%	2.7%
Total Liabilities	5,534	4,735	54.7%	50.0%	44.7%
Stockholders' Equity					
Common Stock	3,501	3,204	34.6%	33.8%	18.2%
Retained Earnings & AOCI	1,085	1,533	10.7%	16.2%	37.1%
Total Stockholders' Equity	4,586	4,737	45.3%	50.0%	55.3%
Total Liab. & SHE	10,120	9,472	100.0%	100.0%	100.0%

	6/27/08-\$	6/29/07-\$	6/27/08-%	6/29/07-%	WD
Sales Revenue	12,708	11,360	100.0%	100.0%	100.0%
Cost of Revenue	9,503	9,175	74.8%	80.8%	78.5%
Gross Profit	3,205	2,185	25.2%	19.2%	21.5%
Product Development	1,028	904	8.1%	8.0%	5.7%
SG&A	801	667	6.3%	5.9%	3.3%
Operating Income	1,376	614	10.8%	5.4%	12.5%
Other, net	47	53	0.4%	0.5%	0.3%
Income before Taxes	1,329	561	10.5%	4.9%	12.2%
Income Taxes	67	-352	0.5%	-3.1%	1.4%
Net Income	1,262	913	9.9%	8.0%	10.7%

Liquidity Ratios

Liquidity - Short-Term Debt Paying Ability

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Quick Ratio} = \frac{\text{Quick Assets}^*}{\text{Current Liabilities}}$$

* Quick Assets = Cash + Marketable Securities + Net Accounts Receivable

$$\text{Cash Ratio} = \frac{\text{Cash} + \text{Marketable Securities}}{\text{Current Liabilities}}$$

$$\text{Operating Cash Flow Ratio} = \frac{\text{Operating CF}}{\text{Current Liabilities}}$$

Item	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Current Assets	4,272	3,801	2,731
Current Liabilities	3,287	2,649	1,564
Quick Assets	1,141	1,144	1,107
Cash	990	988	1,104
Operating CF	2,538	943	1,399

Item	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Current Ratio	1.30	1.43	1.74
Quick Ratio	.35	.43	.71
Cash Ratio	.30	.37	.71
Operating CF Ratio	.77	.36	.89

Activity Ratios

A/K/A – Turnover Ratios

Inventory Turnover =	Cost of Goods Sold
	Average Inventory
Receivables Turnover =	Sales
	Average Accounts Receivable
Payables Turnover =	Sales
	Average Accounts Payable
Working Capital Turnover =	Sales
	Average Working Capital
Fixed Asset Turnover =	Sales
	Average Fixed Assets
Total Asset Turnover =	Sales
	Average Total Assets

Item	6/28/08 - STX	6/29/07 - STX	6/30/06 - STX
Inventory	945	794	891
Accounts Receivable	1,410	1,383	1,445
Accounts Payable	1,652	1,301	1,692
Current Assets	4,272	3,801	4,333
Current Liabilities	3,287	2,649	3,337
Net Fixed Assets	2,464	2,278	2,106
Total Assets	10,120	9,472	9,544
Sales	12,708	11,360	-
Cost of Goods Sold	9,503	9,175	-

Item	6/28/08 - STX	6/29/07 - STX	6/28/08 - WDC
Inventory Turnover =	10.93	10.89	17.72
Receivables Turnover =	9.10	8.03	9.46
Payables Turnover =	8.61	7.59	7.83
Working Capital Turnover =	11.89	10.58	7.82
Fixed Asset Turnover =	5.36	5.18	6.70
Total Asset Turnover =	1.30	1.19	2.08

Average Days Inventory in Stock =	365
	Inventory Turnover
Average Days Receivables Outstanding =	365
	Receivables Turnover
Average Days Payables Outstanding =	365
	Payables Turnover
Length of Operating Cycle =	Avg Days Inventory + Avg Days Receivables Outstanding

	6/28/08 - STX	6/29/07 - STX	6/28/08 - WDC
Average Days Inventory in Stock	33.4	33.5	20.6
Average Days Receivables Outstanding	40.1	45.4	38.6
Average Days Payables Outstanding	42.4	48.1	46.6
Length of Operating Cycle	73.5	78.9	59.2

Leverage/Solvency

- Leverage – the use of debt (instead of equity) to finance assets
- Solvency – long-term debt paying ability

Debt to Equity =	Total Liabilities
	Total Stockholders' Equity
Debt Ratio =	Total Liabilities
	Total Assets
Times Interest Earned =	Net Income + Interest Expense + Income Tax Expense
	Interest Expense
Long-Term Debt to Equity =	Total Long-Term Liabilities
	Total Stockholders' Equity
Debt to Market Equity =	Total Liabilities
	Total Market Value of Equity

Item	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Total Liabilities	5,534	4,735	2,179
Total Stockholders' Equity	4,586	4,737	2,696
Total Assets	10,120	9,472	4,875
Net Income	1,262	913	867
Interest Expense	126	141	52
Income Tax Expense	67	(352)	114
Long-Term Liabilities	2,021	1,868	615
Market Value of Equity	9,350	11,480	7,680

Ratio	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Debt to Equity =	1.21	1.00	0.81
Debt Ratio =	0.55	0.50	0.45
Times Interest Earned =	11.55	4.98	19.87
Long-Term Debt to Equity =	0.44	0.39	0.23
Debt to Market Equity =	0.59	0.41	0.28
Debt to Equity =	1.21	1.00	0.81

Profitability Ratios

Gross Margin =	Gross Profit (Sales-COGS)
	Sales
Return on Sales =	Net Income
	Sales
Return on Assets =	Net Income
	Average Total Assets
Pretax Return on Assets =	Net Income + Interest Expense + Income Tax Expense
	Average Total Assets
Return on Total Equity =	Net Income
	Average Stockholders' Equity
Dividend Payout =	Common Dividends
	Net Income

Item	6/28/08 - STX	6/29/07 - STX	6/30/06 - STX
Sales	12,708	11,360	
Cost of Sales	9,503	9,175	
Net Income	1,262	913	
Total Assets	10,120	9,472	9,544
Interest Expense	126	141	
Income Tax Expense	67	-352	
Stockholders' Equity	4,586	4,737	5,212
Common Dividends	216	212	

Ratio	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Gross Margin =	25.2%	19.2%	21.5%
Return on Sales =	9.9%	8.0%	10.7%
Return on Assets =	12.9%	9.6%	22.3%
Pretax Return on Assets =	14.9%	7.4%	26.6%
Return on Total Equity =	27.1%	18.4%	39.3%
Dividend Payout =	17.1%	23.2%	0.0%

Dupont Model

- A Decomposition of Return on Equity into Multiple Elements
- Recall $ROE = \text{Net Income} / \text{Average Stockholders' Equity}$

ROE =	Return on Assets			X	Solvency
ROE =	Profitability	X	Activity	X	Solvency
ROE =	Net Income	X	Sales	X	Avg. Tot. Assets
	Sales		Avg. Tot. Assets		Avg. Stkhldrs. Equity

Item	6/28/08 - STX	6/29/07 - STX	6/30/06 - STX
Net Income	1,262	913	
Sales	12,708	11,360	
Total Assets	10,120	9,472	9,544
Total Stockholders' Equity	4,586	4,737	5,212

Ratio	6/28/08 - STX	6/29/07 - STX	6/27/08-WDC
Profitability =	9.9%	8.0%	10.7%
Activity =	1.30	1.19	2.08
Return on Assets =	12.9%	9.6%	22.3%
Solvency =	2.10	1.91	1.76
Return on Equity =	27.1%	18.4%	39.3%

SEAGATE TECHNOLOGY
CONSOLIDATED BALANCE SHEETS
(In millions, except share and per share data)

	June 27, 2008	June 29, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 990	\$ 988
Short-term investments	151	156
Accounts receivable, net	1,410	1,383
Inventories	945	794
Deferred income taxes	274	196
Other current assets	502	284
Total current assets	4,272	3,801
Property, equipment and leasehold improvements, net	2,464	2,278
Goodwill	2,352	2,300
Other intangible assets, net	111	188
Deferred income taxes	616	574
Other assets, net	305	331
Total Assets	<u>\$ 10,120</u>	<u>\$ 9,472</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 1,652	\$ 1,301
Accrued employee compensation	440	157
Accrued restructuring	80	21
Accrued expenses	519	532
Accrued warranty	226	233
Accrued income taxes	10	75
Current portion of long-term debt	360	330
Total current liabilities	3,287	2,649
Accrued restructuring	7	21
Accrued warranty	219	197
Other non-current liabilities	351	135
Long-term debt, less current portion	1,670	1,733
Total Liabilities	5,534	4,735
Commitments and contingencies (See Notes 8 and 9)		
Shareholders' equity:		
Preferred shares, \$0.00001 par value per share—100 million authorized; no shares issued or outstanding	—	—
Common shares, \$0.00001 par value per share—1,250 million authorized; 485,127,434 issued and outstanding at June 27, 2008 and 534,981,463 issued and outstanding at June 29, 2007	—	—
Additional paid-in capital	3,501	3,204
Accumulated other comprehensive income (loss)	(16)	(4)
Retained earnings	1,101	1,537
Total Shareholders' Equity	4,586	4,737
Total Liabilities and Shareholders' Equity	<u>\$ 10,120</u>	<u>\$ 9,472</u>

See notes to consolidated financial statements.

SEAGATE TECHNOLOGY
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except per share data)

	Fiscal Year Ended		
	June 27, 2008	June 29, 2007	June 30, 2006
Revenue	\$ 12,708	\$ 11,360	\$ 9,206
Cost of revenue	9,503	9,175	7,069
Product development	1,028	904	805
Marketing and administrative	659	589	447
Amortization of intangibles	54	49	7
Restructuring and other	88	29	4
Total operating expenses	<u>11,332</u>	<u>10,746</u>	<u>8,332</u>
Income from operations	1,376	614	874
Interest income	57	73	69
Interest expense	(126)	(141)	(41)
Other, net	22	15	22
Other income (expense), net	<u>(47)</u>	<u>(53)</u>	<u>50</u>
Income before income taxes	1,329	561	924
Provision for (benefit from) income taxes	67	(352)	84
Net income	<u>\$ 1,262</u>	<u>\$ 913</u>	<u>\$ 840</u>
Net income per share:			
Basic	\$ 2.46	\$ 1.64	\$ 1.70
Diluted	2.36	1.56	1.60
Number of shares used in per share calculations:			
Basic	512	558	495
Diluted	538	587	524
Cash dividends declared per share	\$ 0.42	\$ 0.38	\$ 0.32

See notes to consolidated financial statements.

SEAGATE TECHNOLOGY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

	Fiscal Year Ended		
	June 27, 2008	June 29, 2007	June 30, 2006
OPERATING ACTIVITIES			
Net income	\$ 1,262	\$ 913	\$ 840
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization	844	851	612
Stock-based compensation	113	128	90
Deferred income taxes	10	(365)	23
Allowance for doubtful accounts receivable, net of recoveries	(3)	40	—
Redemption charges on 8% Senior Notes due 2009	—	19	—
In-process research and development	4	4	—
Tax benefit from stock options	(6)	—	(44)
Non-cash portion of restructuring and other	2	19	—
Other non-cash operating activities, net	(12)	17	12
Changes in operating assets and liabilities:			
Accounts receivable	(67)	34	(190)
Inventories	(151)	106	(113)
Accounts payable	351	(391)	91
Accrued expenses, employee compensation and warranty	154	(465)	120
Accrued income taxes	13	8	54
Other assets and liabilities	24	25	(38)
Net cash provided by operating activities	<u>2,538</u>	<u>943</u>	<u>1,457</u>
INVESTING ACTIVITIES			
Acquisition of property, equipment and leasehold improvements	(930)	(906)	(1,008)
Proceeds from sale of fixed assets	29	55	—
Purchases of short-term investments	(486)	(322)	(3,220)
Maturities and sales of short-term investments	460	997	3,528
Net cash and cash equivalents acquired from Maxtor	—	—	297
Acquisitions, net of cash and cash equivalents acquired	(78)	(178)	(28)
Other investing activities, net	14	(48)	(130)
Net cash used in investing activities	<u>(991)</u>	<u>(402)</u>	<u>(561)</u>
FINANCING ACTIVITIES			
Net proceeds from issuance of long-term debt	—	1,477	—
Repayment of long-term debt	(34)	(5)	(340)
Redemption of 8% Senior Notes due 2009	—	(400)	—
Redemption premium on 8% Senior Notes due 2009	—	(16)	—
Proceeds from exercise of employee stock options and employee stock purchase plan	178	219	118
Dividends to shareholders	(216)	(212)	(155)
Tax benefit from stock options	6	—	44
Repurchases of common shares	(1,479)	(1,526)	(399)
Net cash used in financing activities	<u>(1,545)</u>	<u>(463)</u>	<u>(732)</u>
Increase in cash and cash equivalents	2	78	164
Cash and cash equivalents at the beginning of the period	988	910	746
Cash and cash equivalents at the end of the period	<u>\$ 990</u>	<u>\$ 988</u>	<u>\$ 910</u>
Supplemental Disclosure of Cash Flow Information			
Cash paid for interest	\$ 121	\$ 88	\$ 38
Cash paid for income taxes, net of refunds	34	38	15

See notes to consolidated financial statements.

SEAGATE TECHNOLOGY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For Fiscal Years Ended June 27, 2008, June 29, 2007 and June 30, 2006
(In millions)

	Number of Common Shares	Par Value of Shares	Additional Paid-in Capital	Deferred Stock Compensation	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
Balance at July 1, 2005	477	\$ —	\$ 632	\$ (3)	\$ (9)	\$ 1,921	\$ 2,541
Comprehensive income, net of tax:							
Change in unrealized gain (loss) on marketable securities, net					(2)		(2)
Change in unrealized gain (loss) on cash flow hedges, net					4		4
Net income						840	840
Comprehensive income							842
Issuance of common shares related to employee stock options and employee stock purchase plan	18		118				118
Issuance of common shares, assumption of options and nonvested shares in connection with the acquisition of Maxtor	98		1,956				1,956
Substantial premium on convertible debt assumed			175				175
Dividends to shareholders			(155)				(155)
Tax benefit from stock options			44				44
Repurchases of common shares	(17)					(399)	(399)
Stock-based compensation			88	2			90
Balance at June 30, 2006	576	—	2,858	(1)	(7)	2,362	5,212
Comprehensive income, net of tax:							
Change in unrealized gain (loss) on marketable securities, net					7		7
Change in unrealized gain (loss) on cash flow hedges, net					(4)		(4)
Net income						913	913
Comprehensive income							916
Issuance of common shares related to employee stock options and employee stock purchase plan	21		219				219
Dividends to shareholders						(212)	(212)
Repurchases of common shares	(24)					(576)	(576)
Payments made under prepaid forward agreements						(950)	(950)
Shares received under prepaid forward agreements	(38)						
Stock-based compensation			127	1			128
Balance at June 29, 2007	535	—	3,204	—	(4)	1,537	4,737
Cumulative effect adjustment to adopt recognition and measurement provisions of FASB Interpretation No. 48 (See Note 4)							
						(3)	(3)
Comprehensive income, net of tax:							
Change in unrealized gain (loss) on cash flow hedges, net					(9)		(9)
Change in unrealized gain (loss) on auction rate securities, net					(3)		(3)
Net income						1,262	1,262
Comprehensive income							1,250
Issuance of common shares related to employee stock options and employee stock purchase plan	15		178				178
Dividends to shareholders						(216)	(216)
Tax benefit from stock options			6				6
Repurchases of common shares	(65)					(1,479)	(1,479)
Stock-based compensation			113				113
Balance at June 27, 2008	485	\$ —	\$ 3,501	\$ —	\$ (16)	\$ 1,101	\$ 4,586

See notes to consolidated financial statements.