

Chapter 6

Financial Strategy

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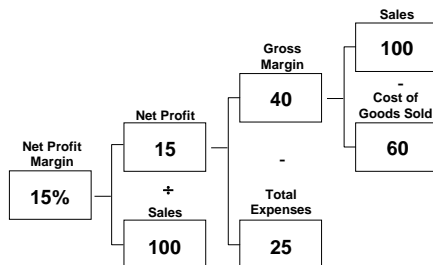
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The Strategic Profit Model: An Overview

$$\text{Profit Margin} \times \text{Asset turnover} = \text{Return on assets}$$
$$\frac{\text{Net profit}}{\text{Net sales (crossed out)}} \times \frac{\text{Net sales (crossed out)}}{\text{Total assets}} = \frac{\text{Net profit}}{\text{Total assets}}$$

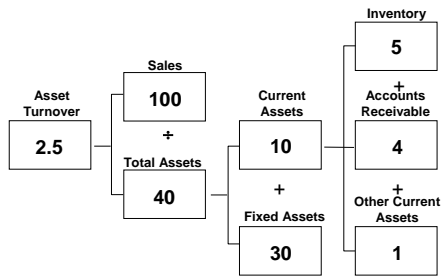
PPT 6-2

The Strategic Profit Model: Margin Management



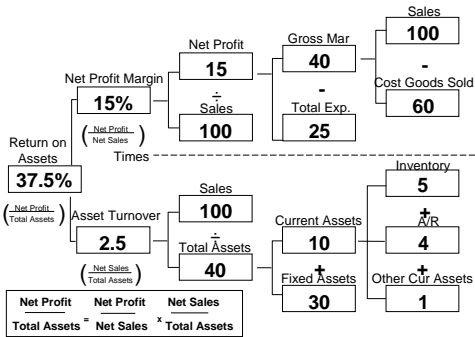
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The Strategic Profit Model: Asset Management



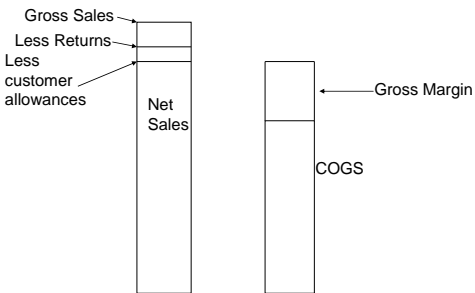
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The Strategic Profit Model: Return on Assets



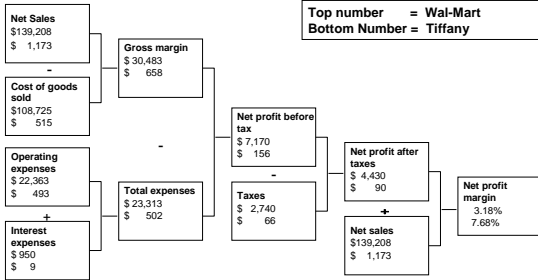
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Components of Gross Margin



PPT 6-6

Profit Margin Models for Wal-Mart Stores, Inc., and Tiffany & Co. (\$ in millions)



PPT 6-7

Gross Margin for Wal-Mart and Tiffany

<u>Gross Margin</u>	=	<u>Gross Margin %</u>
<u>Net Sales</u>		
Wal-Mart: \$ 48,250	=	21.95%
\$219,812		
Tiffany: \$ 944	=	58.75%
\$1,607		

Why does Tiffany's have higher margins than Wal-Mart?

Does the higher margins mean the Tiffany's is more profitable?

PPT 6-8

Total Expenditures / Net Sales Ratios for Wal-Mart and Tiffany

<u>Total Expenses</u>	=	<u>Total Expenses/Net sales ratio</u>
<u>Net Sales</u>		
Wal-Mart: \$ 37,499	=	17.06%
\$219,812		
Tiffany: \$ 653	=	40.65%
\$1,607		

Why does Tiffany's have higher expenses than Wal-Mart?

PPT 6-9

Types of Retail Operating Expenses

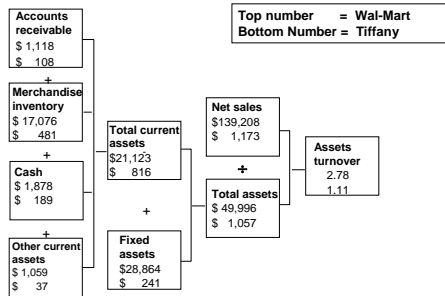
- Selling expenses = Sales staff salaries + Commissions + Benefits

- General expenses = Rent + Utilities + Miscellaneous expenses

- Administrative expenses = Salaries of all employees other than salespeople + Operations of buying offices + Other administrative expenses

PPT 6-10

Asset Turnover Model for Wal-Mart Stores, Inc. and Tiffany & Co. and Subsidiaries (\$ in millions)



PPT 6-11

Inventory Analysis

Inventory
Total assets

Wal-Mart: $\frac{\$22,614}{\$83,451} = 27.10\%$

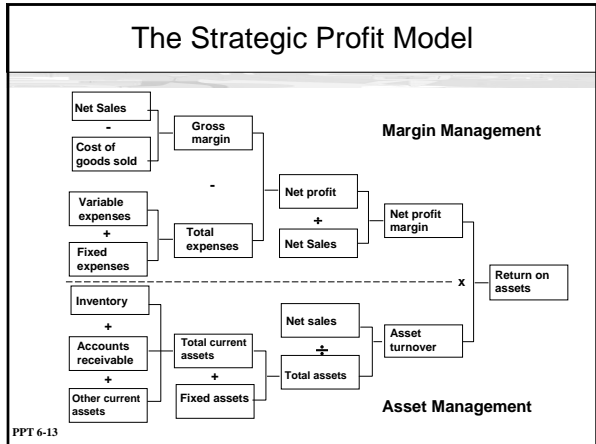
Tiffany: $\frac{\$ 612}{\$1,630} = 37.53\%$

Net sales = **Inventory turnover**
Avg. inventory

Wal-Mart: $\frac{\$219,812}{\$28,974} = 7.59$

Tiffany: $\frac{\$1,607}{\$1,484} = 1.08$

PPT 6-12



Return on Assets

Return on assets = Net profit margin X Asset turnover

= $\frac{\text{Net profit}}{\text{Net sales}} \times \frac{\text{Net sales}}{\text{Total assets}}$

= $\frac{\text{Net profit}}{\text{Total assets}}$

Wal-Mart:	<u>\$ 6,854</u>	=	8.21%	
	\$83,451			
Tiffany:	<u>\$ 175</u>	=	10.74%	
	\$1,630			

PPT 6-14

Productivity Measures

Returns on Investments

vs.

Absolute Profits

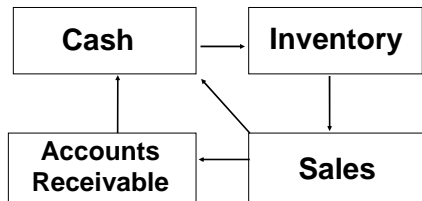
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**Activity-Based Costing Profitability Statement
for Pepperidge Farm and
Private-Label Cookies at Safeway**

	Pepperidge	Private-Label cookies
Retail price per case	\$ 31.20	\$ 27.00
Cost per case	<u>24.00</u>	<u>18.00</u>
Gross margin	7.20	9.00
Other "relevant" costs	<u>1.50</u>	<u>5.00</u>
Contribution margin	5.70	4.00

PPT 6-16

A Simplified Cash Flow Diagram



PPT 6-17
