RUNNING HEAD: FAILURE OF THOMAS COOK

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Failure of Thomas Cook

***Liquidity/Solvency Ratios***

These ratios are used to see if a company will be able to pay off its short term debts in time or not. The assessment is made by comparing current assets and current liabilities. These ratios are important for people who have lent some money to company or those who intend to give loan to company in future.

*Current Ratio*

This ratio is used to assess short term debt paying ability of company. The formula is:

Current Assets/Current Liabilities

For 2018,

2113/4222

= 0.50

The ratio shows that there were only 50% of current assets to pay off current liabilities of the company. In other words, for every dollar of current liabilities, there is on $ 0.50 of current assets. A creditor will be concerned by seeing this situation because his money may not be returned on time. For the same time period, the ratio for booking holdings was 2.58 which meant that the company had $ 2.58 of current assets against each dollar of current liabilities. This shows a positive situation because company will be left with $ 1.58 even after paying all the short-term debts.

For 2017

2241/4325

= 0.52

In 2017, the situation of company was a bit better because it had $ 0.52 to pay against each dollar of current liabilities. There was a decrease in cash in hand with the company from the year 2017 to 2018. Company may not be able to generate enough cash from its operations which has badly affected its current assets. The ratio for Booking holdings for the same period was 1.88 which means that the company will have $ 1.88 of current assets against each dollar of current liabilities. Almost all the stakeholders will get a positive thought about the competitor because it will have excess cash available at any given point in time.

For 2016

2656/4630

= 0.57

The above figure shows that company had $ 0.57 for every $ 1 of current assets which means that company was not in a position to pay off its short term debts if they all become due at the same time. The problem with company is that it was not able to use the amount of cash available to it because some of these amounts were kept in restricted accounts. Some amount of money was also kept by insurance companies which cannot be used by Thomas Cook Company. A major competitor named booking holdings showed a figure of 2.46 for the same ratio over this period of time. This meant that the company had $ 2.46 of current assets for each dollar of current liabilities. There will be $ 1.46 left even after the payment to trade creditors. Investors and creditors will be satisfied with the performance of company. Equity holders will also be satisfied because they will see the possibility of some dividend paid to them at the end of year.

For 2015

2035/3702

= 0.55

This means that company has $ 0.55 of current liabilities against each dollar of current assets. This situation will be disturbing for the present and prospective creditors because there will be low probability of return of their loans. An analysis of a competitor revealed that it showed a ratio of 3.71 over the same period of time. This will attract more internal and external investment for the company in the form of debt and equity respectively. The employees will also be motivated because better financial performance may mean that their remunerations may be raised over a period of time.

***Profitability ratios***

Profitability ratios show the ability of company to use its resources efficiently so that operations generate profits. Profitability ratios are divided into margins and returns which are important for different stakeholders. The margins are calculated against sales which show how well company is controlling expenses. The returns are shown against assets and equity showing the efficiency with which company is using these resources.

*Gross Profit Margin*

= Gross profit / Net sales\*100

For 2018

1933/9584\*100

= 20.17 %

The company is earning 20 % gross profit on its sale which means that cost of service provision is higher for the company (Lesakova, 2007). This will hurt the investors because there will not be much money left for company to pay out dividends. Analysis of booking holdings as a competitor shows that it has a ratio of 98 % for this criteria and time period. The company is using the sales revenue very efficiently to earn the gross profit. The major difference between Thomas cook and its competitor is the cost of revenue generation. Thomas cook had not been able to control the costs of revenue generation whereas Booking holdings has been able to control these costs very efficiently.

For 2017

1993/9007\*100

= 22.13 %

The company is earning 22 % gross profit on its sale which means that cost of service provision is 78% for the company. This will hurt the investors because there will not be much money left for company to pay out dividends. The company has to analyse the composition of its costs of goods sold to see which items are causing the increase in costs. The competitor is able to generate 96% gross profit from sales for the same period of time. Thomas Cook has incurred 78 % of expenses in to generate revenues whereas the competitor has incurred only 4 % expenses.

For 2016

1822/7812\*100

= 23.32%

The company is able to earn a 23 % gross profit as compared to sales. The performance of company is improving when we go towards the past. The competitor has managed a 93% gross profit as compared to sales. This means that it has controlled the expenses incurred to generate these revenues.

For 2015

1772/7834\*100

= 22.62 %

There is no big change in this ratio for the company over the four year period which shows that it has not been able to control the cost of goods sold. For the same period, a competitor named Priceline group Inc. was able to earn 93% margin of gross profit over sales.

Various stakeholders like investors and employees will be affected by this set of ratios. The employees will feel that their efforts are not generating enough profits and investors will be worried about their returns. Some creditors will also argue that company has not been able to control its expenses so it will not be able to use loans appropriately. A comparison between the company and its competitor will reveal that debt servicing was the major cause of increase in costs for Thomas cook. The comparison by almost all stakeholders will yield a positive outlook for competitor and a negative outlook for Thomas cook.

***Working capital efficiency ratio***

The inventory turnover ratio is calculated to see the number of times a company is able to convert its inventory to sales. This is an important aspect because inventory handling creates certain costs which have to be paid by company.

Cost of Goods Sold / Average inventory

For 2018

= 7651/43

178

The company has performed well in selling its inventory quickly. This may give a positive outlook to the investors about the efficiency of company’s operations. Competitors will also be interested in this ratio because they will need to do better than the company regarding same figure. There is no inventories mentioned in the balance sheet of competitor which can be justified by the fact that business is rendering services rather than goods which means that there will be minimal amount of inventories required by the business.

For 2017

= 7014/42.5

165.03

The company has improved its rotation of inventory in 2017 as compared to 2016 as shown by increased turnover of inventory.

For 2016

= 5990/37.5

159.73

As compared to the year 2015, inventory turnover has decreased for the company in 2016 as compared to 2015. There is a decline in cost of goods sold and increase in average inventory which has resulted in a decrease in turnover ratio.

For 2015

6062/33

=183.69

The highest inventory turnover ratio for company is calculated in the year 2015. The cost of goods sold is high which has caused an increase in inventory turnover. Converted to days, this will mean that company is converting inventory to sales after every two days of operations.

***Long term financial Structure***

This part of ratios includes the analysis of capital structure of the company. There are two major sources of capital for the company namely debt and equity. The debt to equity ratio shows the percentage of debt taken up by company as compared to equity issued. The formula is given as follows:

Total liabilities/ Total equity

For 2018

6278/291

=21.57

For 2017

6335/280

= 22.625

For 2016

6564/391

16.79

For 2015

5590/368

= 15.19

The company debt has increased as compared to equity from the year 2015 to 2018. This means that company has taken huge amount of loan over the period under consideration. This shows the lack of confidence of people in the operations of company. The investors would have noticed a decline in liquidity of company which decreased its ability to pay any kind of dividends to them. Investors also say the decline in profitability which signalled that there will be no increase in the share price of the company. These factors contributed to the fact that company had no other option than to take some debt from financial institutions. The loan was actually received by the German subsidiary of the company (Weiss & Donahue, 2019). This means that the company prepared and showed a consolidated set of financial statements (Chrepa, et al., 2019). The equity holders will be very disappointed because creditors have the first right on whatever the company earns. For the year 2018, the competitor had the ratio of debt to equity at 1.26 which meant that 126 % business was financed by debt. In a business including airline and related services, this ratio is not a very bad figure. This is also true because the company was able to keep the costs of revenue generation very low. The taking of loan has not affected the ability of competitor to generate reasonable amount of profit over time.

*Investor Perspective*

The major aspect of investors is a ratio related to the shares of a company. We can see that the earnings per share is very low over the period of four years for the company. This will affect both the present and perspective shareholders because both will try and quit their investment from this company. The current shareholders will see all the ratios and analyse the situation of company. The liquidity, profitability and investor relations depict a negative situation for company whereas there is some hope in the operations of company as we saw in the efficiency ratios. The earning per share for Booking holdings was $ 47.78 for the year 2018.

One of the major stakeholders who lost a lot of business was the hotel industry. This is because there were huge amount of bills pending with Thomas Cook regarding payment to hotels. These bills were supposed to be paid by the end of summer. Failure to pay off these bills will mean that there will be many jobs lost in hotels (Taylor, 2019).

***Task two***

The authorities could have taken a lesson from the failure of Monarch airlines. A repatriation scheme should have been in place for passengers who went aboard from the UK on any airline that has a chance of going bankrupt. This scheme should be practical and should save the passengers who are away from their homes irrespective of how and from whom the ticket was purchased. The biggest requirement of this scheme was indicated by the level of debt taken up by company over the four-year period under consideration. Almost all ratios show that there was a need of such safety measures for passengers. The company itself could have been saved if a committee was formed to look after the operations in 2016.

The Civil Aviation Authority had to play a much active role in this scenario. The company had huge costs incurred for the generation of revenue. The auditors and officials from CAA should have investigated the break up of these costs so that they could come up with some solution. One option is the cut off of some routes which were not profitable for the company. In order to retrieve the confidence of stakeholders, an in-depth analysis of expenses was required. The government refused to put in 200 million pounds to help the company. This amount could have helped the company to improve its liquidity and eventually coming out of all troubles.

The role of auditors and management has not been very positive during the whole scenario because no issue has been highlighted by either party over the four-year period. An active role by the auditors would mean that there would have been questions regarding financial performance. We see that there is a decline for company is almost all aspects of the financial ratios. The auditors and management should have responded to the concerns raised by the stakeholders. These concerns were shown in the form of various things. The inability of the company to raise equity was one sign that public is showing distrust in the company. The auditors should have investigated the causes of decline in company’s financial performance. The debt to equity ratio also puts forward many questions. Why was the company allowed to take so much loan that only increased the costs of handling the company? Some of the cash shown in the balance sheet was not available for the company to use. The auditors should have questioned this happening so that they can improve the situation. The company should have implemented a low cost policy throughout the operations so that it could save money. Shutting down some routes is one option available to the company. There are airlines which are no fringe low cost providers. The company could have followed their model. There was an option for company to operate from point to point rather than from a central hub. This would have meant that the company could save certain amount of money in terms of fuel and maintenance. The company should have aimed at earning no or lowest profits by keeping the costs lower.

The company had no cash in hand, going into liquidation with only 1 million pounds in cash and 31 million in the bank. The company would have run out of cash within a short span of time. There were very low amounts of assets which forced the company to go into liquidation rather than administration. There were almost no amounts to pay for the administration. The only asset which could attract other companies are airport slots of company. The repatriation costs have been put at 100 million pounds by the UK customers of the company. 60% of the repayments will be covered by Air travel trust funds. The company will not be able to pay all the refunds of bookings. Some of these will be paid by credit card issuers.

The authority that looks after financial aspects will investigate the collapse and in particular the auditors. Price water house Coopers was the auditor for company from 2008 to 2017. The company did not follow certain accounting principles and in particular, to show historical goodwill as a current item.

***Task three***

The company was following the physical model in this era of online business. There have been many difficulties faced by companies when they try and run the traditional business models. With the passage of time successful business models have collapsed due to pressure from competitors and other forces. The concept of innovation in business models has emerged over a period of time. Business model innovation is not clearly defined as yet. There are also various elements of the process which are not very clear and are subject to trial and error methods. So far, the research of topic has been restricted to the business to customer part of the chain (Schneider, et al., 2013).

A company like Thomas Cook should have analysed the business environment in a great detail. There were a large number of shops which were used to book for customers. A much better option would have been online booking through website and social media platforms. This would have saved much cost for the company. The same platforms could have been used for marketing purposes. This business model could have been used side by side with physical location model. The revenue generation could have been used as a criterion to see if a physical location is feasible or not. The company caused a loss of a large number of jobs which could have been reduced by switching to online system. All the members of supply chain could have been taken on board with the new improved business model. Customers would be able to book their hotels and other accessories directly online along with ticket from airline. In fact, a whole package could have been offered by company so that customers would stay with them. This was also necessary because competition has been very tough in the airline industry. The companies find it hard to differentiate their offerings. The only way to remain competitive in this industry is to remain ahead of the competitors. Cost efficiency is one of the ways to be successful. In the traditional business model, cost saving was not possible because there were certain fixed and variable costs associated with physical shops for booking. In the online business model, there is only one time cost of developing an online platform. Customer retention is also important in this business because customers will be able to find some alternate very easily. Thomas Cook failed to retain its customers because it was not able to satisfy any of its stake holders by its financial performance (Jenatabadi & Ismail, 2012). All the internal and external stakeholders suffered due to company performance. The online business model would have helped the company in terms of liquidity. The savings in terms of expenses would have been available in terms of cash and cash equivalents. Similarly, there are many expenses which could be avoided by adopting the online business model.

The analysis also reveals that there were no specific goals pursued by the company either in the short run or in the long run. If there were any such goals, management did not check their pursuance properly. Financial results were enough to show that company was not performing properly as compared to a competitor but there were no corrective measures taken up by management. In 2012, the company was first threatened by the presence of huge amount of debt (travelweekly, 2019). A former employee of the company put a bid of 400 million pounds to acquire the company and escape it from the huge amount of loan. The deal was rejected without any explanation. Lack of proper goals from management also resulted in a taking over of The Co-Operative Travel in 2011 which initially set the business on a wrong path.

The role of board of directors was also questionable. It had not performed the duty of looking after the interests of shareholders in a proper way. The board could not put the knowledgeable people at the right places during the whole scenario. These people knew the problems and could have brought some positive changes.

Like all other businesses, travel and tourism has gone through the changes in customer habits. There are digital options available to customers which will mean that they will go for personalised packages offered by cost effective airlines. This created a considerable decline in the business for Thomas Cook but due to major financial issues and lack of market knowledge, company was not able to change itself. Company took some bad decisions and there was not attempt to restructure it into a lean company. Brexit also had some impact on the company as many people cancelled their trips out of uncertainty. Changes in weather conditions in some major destinations also meant that company had to change its business very quickly which it failed to do (Rasch, 2019).

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