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Financial Analysis of Air New Zealand

***Executive Summary***

This report is written to show the financial and non-financial factors affecting the performance of Air New Zealand, which is listed at the ASX. It operates a global network that provides passenger and cargo services over 19 countries and accommodates approximately 17 million passengers per year. The major competitive advantage for the company lies in the Pacific rim where the airline caters Australia, New Zealand and Asia. There are 3400 flights on average per week for the company reaching various domestic and international destinations. The company earned a revenue of $ 5.5 billion in 2018 financial year (Airnewzealand, 2019). This report is prepared from the perspective of an outside investor. Financial analysis helps stakeholders to decide whether a particular company is worth of taking certain decisions or not (Feng & Wang, 2000). In this report, financial analysis will help a probable shareholder to decide whether or not he should invest in the company. Financial ratios have been considered a unique outcome of accounting in the United States (Horrigon, 1965).

***Analysis***

Current ratio has been one of the oldest ratios in the financial analysis of any company and is calculated to see short term liquidity of a company (Horrigon, 1968). It is calculated by dividing current assets by current liabilities. For the year 2018, this ratio was 0.83, whereas, in 2017, it was 0.78. The major difference between these two years was seen in derivative financial assets which raised considerably from 2017 to 2018. Gross profit margin is helpful in examining gross profit as a percentage of sales (Lesakova, 2007). For the year 2018, the gross profit margin was 23.55%, whereas the same figure in 2017 was 24.82 %. Net profit margin for the year 2018 was 7.11% whereas, in 2017, this figure was 7.47%. Debt to equity ratio for the company in 2018 was 2.605, whereas the same figure in 2017 was 2.61. All ratios regarding earnings per share have improved from the year 2017 to 2018. The return on equity for company in 2018 was 17.5% whereas the same figure was 19.23% in the year 2017. There is a considerable role of internal variables in determining performance of airlines when economic variables are controlled (Jenatabadi & Ismail, 2012)

***Interpretation***

Since this report is written from the perspective of a person who wants to invest in this company as a shareholder, he will see the returns that the company is paying to its existing shareholders. Shareholders form the equity section of the balance sheet and return on equity has dropped from 19.23% to 17.5%. This means that net income as a percentage of equity has decreased from 2017 to 2018. Analysis reveals that the company has seen an increase in both net income and shareholder's equity, but there has been more increase in equity as compared to net profit. This may mean that the company has introduced additional capital, but it has not been able to utilize this capital to generate enough additional net income. Another implication of this happening will be that net income will now be distributed over a larger number of shareholders and income per share will be lower. The profit margins will also be important for the shareholder because they will show the ability of a company to pay out to its shareholders. There has been a slight decrease in gross profit margin as well as net profit margin from the year 2017 to 2018 showing that there has been a decrease in gross and net profits as a percentage of sales. This means that the company did not manage its direct and indirect expenses efficiently enough in 2018 as compared to 2017. There has been a considerable decrease in dividends paid to shareholders by the company from 2017 to 2018, which is also a point of concern for a shareholder. An investor will also be interested in the liquidity aspect of the company, which is primarily measured by the current ratio. Current ratio shows the ability of the company to pay its short-term debts if they all become due together. We see that the company will not be in a position to pay its short-term loans if they all become due together. Investor will see it as a negative sign because company may not have enough assets to pay out its shareholders. Debt to equity ratio is another measure which shareholder will assess in this scenario because it shows the ratio between debt acquired by company and equity issued by company. There are respective pros and cons for debt and equity financing and investors in the form of shareholders are particularly interested in the source of company financing. In case of debt, company does not have to share the ownership but on the other hand, it has to pay interest on this form of financing (M.P.Narayanan, 1988). Equity has no direct costs associated with it, but it needs that company share a significant level of ownership with shareholders. The debt to equity ratio for company is alarming for both 2017 and 2018. The ratios show that company has taken two times debt as compared to its equity in these two years. Another point to be noted is that creditors' interest has a priority upon shareholder’s payments so a company will pay interest before announcing any dividends for shareholders.

As far as the non- financial variables are concerned, GDP has a significant impact on airline’s performance (Ramanathan, 2001). With a change in various economic variables, companies make changes to their policies and procedures to adapt. We can take an example where interest rate variation will affect this company because a huge amount of loans has been obtained. These economic indicators generally affect the internal factors of the company, so a probable shareholder does not have to worry about these aspects.

***Conclusion***

The major concern from the perspective of a shareholder will be the debt to equity ratio for this company. Based on this aspect and a slight decrease in all other ratios, a prospective shareholder should not invest in this company. Although the current performance of this company will be very attractive from the viewpoint of a layman in-depth analysis reveals that there are many problems in financial performance of the company. This company will be suitable for an investor that wants to lend his money to it and earn interest on his amount.

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