Report

Liquidity

Amazon's current ratio increased from 1.04 in 2017 to 1.10 in 2019. With the ratio above 1.0, Amazon demonstrates its capacity to pay short-term obligations, which has improved over the last three years. yet, when the quick ratio is consistently less than 1.0 for a few years in a row, it signals that Amazon may have problems completing its short-term obligations without depending on inventory sales; yet, it has increased from 0.76 to 0.86 from 2017 to 2019. These demonstrate that, while Amazon can satisfy short-term obligations, it does so through inventories. This conclusion is also consistent with its cash ratio, which is likewise less than 1.0, indicating that it may be difficult to pay short-term obligations using cash on hand.

The cash ratio was 0.35 in 2017 and 0.41 in 2019, which is low compared to the desired ratio of 1.0. Amazon's defensive interval is likewise considered short, with a 50-day optimal time.

As the quick ratio demonstrates, Amazon has a limited capacity to meet operational expenditures without depending on inventory sales and a limited ability to cover expenses with cash. This might be because Amazon is putting money into expanding and growing its facilities.

Given Amazon's reliance on inventory, it is encouraging that the company has decreased its inventory days from 52 days in 2017 to 45 days in 2019, implying faster inventory turnover and more effective inventory management. The net trading cycle has increased from 2017 to 2019, however the most successful year was 2018, with a net trading period of 29 days, compared to 32 in 2019 and 33 in 2017. Amazon, on the other hand, can turn inventory and accounts receivables into cash faster with a minor improvement. The drop in net trading cycle in 2018 might be attributed to Amazon being more efficient since receivable days and payable days were the lowest. Amazon's receivable days have remained consistent, indicating efficient practises; nonetheless, payment days have fallen from 113 in 2017 to 104 in 2019, but remain quite high.

The most substantial rise has been in working capital as a percentage of revenue, which has increased by 133% between 2017 and 2019. This demonstrates that Amazon effectively manages their operating capital.

According to this research, Amazon has a somewhat steady and balanced approach to liquidity management, but the deficiencies are visible in the inability to meet costs with cash. As a result, cautious cash management is advised.

The Current ratio is greater than 1 indicating the short-term asset’s ability to meet short term liabilities. Quick and Cash ratios above 0.5 which also indicates that the company can meet more than 50% of its short-term liabilities with its cash in hand. The decline in current ratio was mainly to be attributed to a reduction of marketable securities (following the sale of the company’s stake in Rivian).

As an online marketplace where thousands of vendors are hosted on site, Amazon’s payable days is typically higher than other companies as it is part of its 90-day credit policy. As a result of Amazon’s nature of business, its payable balances are higher than its inventories and receivables where it holds inventory on behalf of its vendors. Therefore, working capital is negative and so is the trading cycle. On a year over year basis the number has worsened, but can be supported with the argument that Amazon has started its own fulfilment services and is a fast growing company.

Operating with a negative Trading Cycle became a source of cash for the company, instead of being a cost for it. However, it can be observed that the Trading Cycle days have reduced over the years indicating that the number of days that they can hold on to the cash has reduced.

Profitability

Over the years, Amazon has been able to enhance its gross margin, EBITDA margin, and EBIT margin. The gross profit margin has improved by 10% over the last three years, which is encouraging for prospective investors. A gross margin of more over 50% is regarded good, however Amazon's is just 41% as of 2019, which may be deemed low. The EBITDA margin has also grown 47.8% from 8.7% to 12.9%, indicating that Amazon has improved operational efficiency and profitability, as greater margins imply lower operating expenditures compared to total value. This is emphasised further by a rise in EBIT margins, which have steadily improved from 2.14% in 2017 to 4.98% in 2019. However, because the EBIT margin is less than 5%, it is still seen as inadequate. From 2017 to 2018, the net margin climbed by 141%. However, net margins have stayed reasonably consistent and are still deemed poor because they are less than 5%. However, with the changes, it demonstrates that Amazon has improved profitability by boosting revenue.

It is notable that Amazon’s Technology & content and Sales & marketing have seen sharp increases, indicating the heavy spend on AWS and Prime Video content. While the e-commerce segment is seen to be normalizing post the Covid-19 boom, sales reflect the increasing global inflation levels.

Solvency/debt management

The solvency/ debt management ratios provide insight into Amazons ability to manage its debt. The debt/equity ratio has decreased over the 3 years from 0.89 to 0.38, the decrease in debt to equity demonstrates that Amazon has reduced its dependence on debt to support its activities during the last three years. Amazon's debt-to-total-assets ratio has likewise declined over time, from 0.19 in 2017 to 0.10 in 2019. The smaller this percentage, the lesser the financial risk. The decrease of this ratio has reduced Amazon's financial risk, resulting in beneficial results.

Furthermore, Amazon's long-term debt to capital ratio has decreased over time, indicating a reduction in long-term debt compared to capital. The fall from 0.47 in 2017 to 0.27 in 2019 is a respectable 20% decrease. Amazon demonstrated its rising capacity to cover its debt by increasing the Times interest earned from 5.88 to 8.95 in 2019. The higher this ratio, the greater the capacity to satisfy interest commitments using operating income. In 2018, Amazon had the highest debt coverage, with a debt coverage of 5.92.

However, it was lowered to 3.43 in 2019. Amazon such as like to maintain a high debt coverage since it demonstrates a strong ability to satisfy debt commitments. Debt ratios are declining, but TIE ratios and debt coverage are improving, indicating a better financial condition. The FCFE per share has climbed from $31.98 in 2017 to 69.29% in 2019. This is a good indicator for investors, as it shows the continuous growth of Amazon. This demonstrates the company's ability to create cash flow for distribution to shareholders, as well as Amazon's enhanced cash flow creation.

Amazon’s long-term liabilities have been increasing over the years as the company has increased its Financial lease commitments to facilitate the number of new fulfilment centres opened over the last year. Although the long-term debt remain rather steady, financial lease commitments have dramatically increased which has increased the debt service burden as well. However, the company has adequate levels of interest coverage and free cash flow indicating its financial health. However, the increase in the debt level would also mean that the company’s borrowing capacity in future is strained where it might have to pay higher interests to secure more debt.

Asset utilisation

Amazon's high asset turnover demonstrates Amazon's capacity to generate income from its assets while also demonstrating effective asset utilisation. However, asset turnover has declined over time, falling from 135 in 2017 to 124 in 2019. A decline in total asset turnover is also observed in fixed asset turnover, which has reduced from 2.50 in 2017 to 2.18, indicating a decrease in asset efficiency. However, the turnover of fixed assets has remained steady. Amazon's inventory turnover has increased from 6.98 in 2017 to 8.08 in 2019, showing that the company is selling more items and managing its inventory more effectively. The return on assets for Amazon has increased from 0.02 in 2017 to 0.05 in 2019. This demonstrates that amazon is more effectively generating profits from their assets. This indicates that Amazon is making greater revenues from their assets.

Amazon has a large portion of goodwill in its asset base, where the Fixed asset turnover is almost three times higher than the total asset turnover. The goodwill and intangibles are manly as a result of acquisitions in addition to the increased R&D spending on AWS which we will have to closely watch for future profitability.

Investor/market ratios

Amazon's price to equity ratio is low, and it has been declining from 2017 to 2019. This suggests that the market regards Amazon's earnings positively. Another encouraging sign for investors is that Amazon's profits per share have constantly climbed over the years, rising from $6.15 in 2017 to $22.99 in 2018, or a 274% growth. The company's price to book value (PBV) ratio is quite low and has been declining, indicating a potentially appealing pricing that is consistent with the price to equity ratios. As a result, the enterprise value to EBITDA ratio is very low, indicating undervaluation, and the fact that it is declining signals a more favourable valuation. Amazon's return on equity and return on capital employed have both increased, showing that the company is doing well. Overall, the market values the firms' profits positively, as seen by low P/E and declining PBV ratios.

Finally, Amazon is in a very good financial position, as seen by improvements in liquidity, debt management, and profitability. Amazon's sales climbed by $48 billion in 2019 to $281 billion, indicating growth. There is space for improvement in cash management and asset utilisation. One factor that might deter individuals from investing in Amazon is that they do not pay dividends and have never done so since they reinvest the income in expansion. With a continuous degree of growth and profitability as evidenced throughout the ratios, investing in Amazon would be profitable if you were to hold the shares for an extended period of time.

ROE, ROA and ROCE all are within the health territory, however, have declined slightly compared to previous year. Furthermore, given Amazon’s valuations, one would expect the ratios to be better as there are many other smaller companies with better returns than Amazon, however, it is notable that these valuations are backed by Amazon’s expansion.