**AMAZON PLC**

**MANAGEMENT REPORT ON THE FINANCIAL HEALTH OF AMAZON PLC**

The following key ratios were computed to determine the financial health status of Amazon PLC. The financial statements for 2021 and 2022 were analysed to determine the below results:

**LIQUIDITY RATIO:**

The liquidity ratio measures the ability of the company to meet its current obligations from its liquid assets. The following measures were used to determine the liquidity level of Amazon PLC:

* **Current Ratio:** The current ratio is a liquidity ratio calculated as current assets divided by current liabilities. The Company’s current ratio slightly deteriorated from 1.14x to 0.94x on the back of a significant decline in marketable securities by 73% following a decline in the fair value of these financial instruments as the value of these securities were based on prices that would be received to sell the asset in an orderly transaction between market participants at the measurement date.
* **Quick Ratio:** Quick ratio measures the ability of the company to settle its current liabilities using its highly liquid assets (cash and cash equivalents, account receivables, and marketable securities). Amazon's quick ratio slightly decreased from 0.91x to 0.72x on the back of a decrease in quick/highly liquid assets and a slight increase in current liabilities because of a decrease in the fair value of marketable securities which reduced by 73%.
* **Cash ratio:** This metric measures the ability of the firm to meet its current obligation from its available cash and cash equivalents. Amazon’s cash ratio shows an improvement from 0.25x recorded in 2021 to 0.35x in 2022 on the back of an increase in cash and cash equivalents which increased by 49% from 2021 to 2022.
* **Defensive Interval ratio (days):** This measures the number of days the company's current assets would be able to cover its annual daily operating expenses. It further measures the days the company can continue its working without the requirement of using its non-current assets or outside financial resources. Amazon’s defensive interval ratio declined from 133 days to 107 days on the back of a moderate decline in the company’s assets by 9% and an increase in the annual operating expenses. Following the decline, we advise that the company look into improving its current assets and subsequently manage operating expenses.
* **Inventory Days:** The inventory days indicate the number of days the company would be able to convert its inventory to sales. Amazon Inventory days showed a little decrease from 43.74 days in 2021 to 43.48 days. However, this indicates the ability of the company to convert its inventory to sales is relatively static due to little or no change in the company's inventory and a moderate increase in sales from 2021 to 2021.
* **Payable Days:** This metric analyses how well the company is managing its accounts payables and other suppliers. The company’s payable days declined by 5% from 105 days to 100 days. This indicates the company is not utilizing its cash position as the payable days also declined from 2020 to 2021. However, considering the industry in which the company operates, there is a possibility the company operates a short-term credit arrangement with its suppliers, hence, the decline in payable days.
* **Receivable days:** Amazon’s receivable days increased from 26 days in 2021 to 30 days in 2022. This indicates that the company is not efficiently managing its debtors. However, considering the industry in which the company operates, 7-30 days receivable days is fairly good. Nevertheless, the company should introduce initiatives to combat the yearly increase in receivables days such as offering discounts, shortening payment deadlines, etc.
* **Net Trading Cycle:** The company recorded a negative NTC which is considered favorable as the company operations are being financed by the vendors. Considering the industry in which the company operates, a negative NTP is favourable as it indicates that they can take advantage of the suppliers’ credit and turn their inventory quickly.
* **Working Capital/Working Capital as a Percentage of Sales:** Amazon recorded a negative working capital in 2022 from a positive $19.3 billion as a result of reduced current assets and subsequently increase in current liabilities. However, a negative WC necessarily means the company is operating inefficiently as the decline leads to generating extra cash for the business. It is important to note that the decline in current assets is attributed to a significant decline in marketable securities. It is important to company identify viable securities in which the company can invest. This would help improve current assets as other factors affecting working capital are moderately mild but should be effectively managed to prevent reoccurring negative positions.

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 has become a source of cash instead of being a cost for the company. 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 RATIOS:** An analysis was done on the profitability level of Amazon PLC. The following metrics were analysed:

* **Gross Margin:** The company recorded a slight increase in gross margin from 42% in 2021 to 44% in 2022 as a result of a moderate increase in sales and a corresponding decline in cost of sales. Amazon needs to introduce measures to improve sales and effectively manage the cost of sales.
* **EBITDA Margin/EBITDA/EBIT/EBIT:** EBITDA is referred to as Earnings before interest, tax, depreciation, and amortization. The analysis of the company's financials shows the decline in the company’s EBITDA as a result of an increase in operating expenses and cost of sales and a moderate increase in sales. The company should establish actions to effectively manage its growing expenses and subsequently Improve its sales to match up its expenses and improve earnings.
* **Net Margin:** Amazon PLC recorded a negative margin of -1% in 2022 from a positive 7% in 2021 which is about 108% de. This is majorly attributed to a significant increase in operating expenses by 13% without a corresponding increase in sales to match the effect. It is, however, notable to note the effect of other income(expenses) which significantly impacted the reported net income.
* 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:** Analysis of debt management is important in determining thesolvency of the business.

* **Debt to Equity:** The company recorded 0.46x in 2022 from 0.35x recorded in 2021. This is however considered good as it indicates the company is lowly leveraged as the company is not majorly financed by Debt. The recorded debt to equity is favorable to investors as their interest is safeguarded. Furthermore, this indicates that Amazon is an attractive investment for potential investors.
* **Debt to Total Assets:** Amazon PLC recorded a slight increase in Debt to Total Assets from 12% in 2021 to 15% in 2022.This record shows the proportion of debt in the company’s assets is relatively mild and is considered very attractive to existing and potential investors.
* **Long-term debt to Capital:** This measure recorded a mild increase from 26% in 2021 to 31% in 2022 on the back of additional debt received by the company. However, the mild increase is fairly good as it indicates the company is not at risk of insolvency as it is lowly leveraged. Nevertheless, the company needs to take necessary precautions to ensure the debt intake is properly managed to avoid high leverage in the future.
* **Times Interest earned:** The number of times the company has to pay its interest from its income declined from 13.57x in 2021 to 5.17x in 2022 due to low operating income due to high operating expenses caused by the high inflation rate affecting the economy. The company should create initiatives to manage operating expenses and further improve sales.
* **Debt Coverage:** Amazon PLC's debt coverage declined from 7.32x in 2022 to 3.38x on the back low operating income. Despite the significant decline, the record in 2022 is fairly good as it shows the ability of Amazon PLC to cover its annual net debt payments from its operating profit. Nevertheless, the company should come up with strategies to improve operating profit and manage its debt profile.
* **Free Cash Flow to Equity/FCFE per share:** There was an increase in the FCFE recorded in 2022 from $2.3 billion recorded in 2021. This is favorable to existing investors as it boosts their confidence in the firm.

Following the analysis of the above ratios, It is however notable to state that the debt management initiatives of Amazon PLC are fairly good and it signifies the company is healthy and attractive to existing and potential investors.

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 Utilization:** This is a significant measure in financial analysis to signify the ability of the company to generate sales from the utilization of its assets. The below analysis was carried out:

* **Asset/ Fixed Asset Turnover:** the ability of the company to generate sales from the utilization of its assets slightly declined from 1.12x to 1.11x on the back of a moderate increase in assets and sales. Other assets moderately increased except the marketable securities which are based on the forces of the market beyond the control of the company. Fixed assets turnover also declined on the back of little investment in PPE or other assets to improve sales.
* **Inventory Turnover/Return on Asset:** There was little increase in inventory turnover from 14.39x in 2021 to 14. 94x. On the flip side, the company recorded a negative return on assets on the back of negative net income due to negative other income(expenses) or high operational expenses. The company should create initiatives to properly manage its assets to improve returns.

Following the above analysis, signifies the company is not properly utilizing its assets in generating enough sales and return. The company should invest in viable assets to improve sales/ return and subsequently create strategies to significantly increase sales.

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 Ratio:** An analysis of the following ratio was done to provide information on how the company is faring in the stock market. The return on assets, equity, and capital employed recorded a decline in 2022 majorly attributed to low/negative return recorded in the year. The negative return is a result of rising operational and other expenses and relatively moderate sales. Furthermore, the company needs to properly utilize its capital/financial resources to generate funds. It is worth noting that there was a record of increased assets, and financial resources from both capital providers (equity and debt) during the course of the year.

A negative EPS was also recorded in the course of the year which is significantly attributed to negative return in 2022. This is however not attractive to existing and potential investors as they are not receiving the value of their investment in the company. Furthermore, Amazon PLC recorded a decline in EV/EBITDA value and Enterprise Value which is majorly attributed to a decline in the stock price from year-end 2021 to 2022 from $166.7 to $84. However, it is important to note the performance of the company in the stock market is determined by the market participants. Notwithstanding, the company should properly manage other factors affecting the enterprise value such as cash reserves and Net debt.

ROE, ROA and ROCE all are within the health territory, however, have declined 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