Part One – Introduction

This report aims to examine two actual companies and show the interpretation of their financial figures. The financial statements will be analysed using ratio and trend analysis in respect of profitability, financial position, liquidity and efficiency. Ratios will be used to compare and evaluate the financial position of one company, for a given accounting period, to the financial position of another company for the same period.

Unfortunately, ratio analysis suffers number of limitations. Some of those limitations are different accounting policies, lack of standard definitions, inflation, etc. (Melville, 2014)

Different accounting policies, means different companies might use different methods to calculate depreciation and valuation of inventories. For instance, if we compare two companies which use two different ways to evaluate their inventories and depreciation, the comparison would not be accurate. It will be misleading. (Peavler, 2014)

The second limitation stated above is absence of standard definitions. Some accounting ratios could be defined in more than one method. This makes it problematic to link ratios considered by different accountants.

Another limitation is inflation. It is crucial to ratio analysis because if the inflation rate has changed during the period within the companies are compared the figures will not be adequately comparable.

These limitations can lead to misinterpretation of the company's financial position. It is important that users of financial information should be aware of those problems when making decisions upon the information gained from ratio analysis. After all, wrong interpretation is in help for wrong decisions. (ratio-analysis.org, 2014)

The following report is written on the comparison of financial performance of BT Group plc and Vodafone Group plc. Two companies connecting people all over the world. The main aim of the report is to compare the financial performance of BT and one of its great competitors – Vodafone in the year ended on 31 March 2014. The main source of data used is the published annual reports of BT and Vodafone (see Appendix 2).

Liquidity ratios

i. Current ratio and Quick ratio

Although the calculations for the two ratios are different (see Appendix 1), the BT ratios match exactly with each other for 2013 and 2014. Same is for Vodafone. The current ratio gives us an idea of the company's ability to pay its upcoming bills with its short-terms assets (cash). (Melville, 2014) The higher the ratio, the more favourable it is for the company. There is not a considerably change in the BT's ratios from 2013 to 2014. This is another sign of steady management control.

Vodafone's ratio figures have risen from 0.8:1 to 1.0:1. It means that in 2014, there is £1 pound available on liquid assets to correct £1 pound of liability.

The reason for the lack of change between the current and the quick ratios is because of the very small amount of company's inventory possessions.

Use of resources ratios

i. Asset turnover

This ratio can tell us more about the generated sales form the company's assets. The figure for BT in 2014 is 1.1 times. It has not nearly changed from 2013. The asset turnover figure tells us that each pound invested in assets makes £1.1 of sales. Although the company is not improving fast in this aspect, it is still developing in a positive way.

Vodafone unfortunately, has lower level of asset turnover. There is no change between the two years. However, this shows stability in terms of management control. The meaning of the figures is that the company makes £0.3 p from every pound invested in assets.

ii. Trade receivables collection period

This ratio shows the period which it takes for the company to collect the money owed by its customers. The lower the number, the better for the company and the quicker it will collects money owed by customers.

BT has not change significantly the ratio through the two years. In 2014, it took 58 days on average to collect its money from customers for products and services.

Vodafone, on the other hand, is in worse situation than BT. It needs 84.6 days to collects its money from customers. Moreover, the figure has risen from 2013 with 7.7 days, which is not favourable for the company.

$$Return\ on\ total\ assets = \frac{Profit\ from\ operations}{Total\ assets} \times 100$$

2014

$$= \frac{(3{,}913)}{121{,}840} \times 100 = \mathbf{(3.2)\ \%}$$

2013

$$= \frac{(2{,}202)}{138{,}324} \times 100 = \mathbf{(1.6)\ \%}$$

$Earnings\ per\ share =$ [b]$\mathbf{42.1\ p}$ ← 2014

[b]**(15.7) p** ← 2013

Financial Position

$$Interest\ cover = \frac{Profit\ from\ operations}{Finance\ costs}$$

2014

$$= \frac{(3{,}913)}{1{,}554} = \mathbf{(2.5)\ times}$$

2013

$$= \frac{(2{,}202)}{1{,}596} = \mathbf{(1.4)\ times}$$

[b] Earnings per share are not calculated but given in the companies' financial statements.