Student 5: Low Achieved

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Executive Summary

This report is prepared for Mi-Cha who is thinking about investing $10,000 shares in The Warehouse Group (WHS). This report is based on the 2013 annual report. 1

Mi-Cha wants a long-term investment as she does not plan to retire for another 25 years and the main purpose of the investment is to have a significant amount of money for when she retires, to accompany her Kiwisaver fund. This report will give Mi-Cha an interpretation of WHS's annual report and look into the viability of investing long term in the company.

For the reason I give in my report below, I will be recommending that Mi-Cha buy $10,000 worth of shares in The Warehouse Group.

Profitability

The Warehouse Group is made of four businesses: The Warehouse, Warehouse Stationery and two new additions in 2013, Noel Leeming and Torpedo7. These new stores have already had a positive effect on profitability. The Warehouse, which is the core of the Group, is a retail store known as "the house of bargains" and "home of essentials". They sell everything from clothing to furniture to outdoor equipment and the main market for The Warehouse is New Zealand. The Warehouse is not only increasing the number of stores it has but is also refitting older stores to make them appealing to customers and also make them profitable.

Revenue has increased from 2012 to 2013. The Warehouse reported a revenue of $2.24 billion compared to 2012 when the revenue was $1.73 billion, a 29.3% improvement. The rise of the revenue can be attributed to one of The Warehouse's main goals which is "focusing on delivering great products at the right price". This is because they have increased the amount of stock in their stores and have now added big name brands such as Sony, Acer and Kambrook. The Warehouse also stated that the improved quality of their merchandise has resulted in a lower return rate of products from 20% to 5%. Also, another important focus for The Warehouse is online sales which have risen over the past couple of years. The company estimates that online sales will triple in the next five years. The Warehouse has also launched a new website called Red Alert which is a daily deals site.

Another important factor that would have had an effect on the revenue is the mark-up percentage. In 2012 the company added an average of 36 cents to each $1 of cost price. In 2013 the mark-up decreased to 34 cents. In my opinion The Warehouse's main customer targets are the lower to middle socio-economic group of people so in order to keep sales high, they must get their pricing right. 2

All of these factors have contributed to the rise of revenue in 2013.

Some of the major expenses WHS Group faces are employee wages, rents and occupancy, and other operating expenses. Although these expenses affected profit, The Warehouse believes that all the expenses are helping the company head in the right direction and in doing so will help profitability in the future.

We can see this in the first major expense, staff wages, which increased from $288.33 million in 2012 to $355.63 million in 2013. Some wages will probably have been put up but also the company sent most of their customer service staff on 'love your customer' courses. That is why staff expenses increased.

The lease and occupancy costs also increased by … *[detail omitted from this exemplar]*

Cash management and liquidity

WHS Group stated that their opening cash position was $16.29 million and finished the year at $22.76 million, a big increase that shows that WHS has managed their cash well. Buying Noel Leeming and Torpedo7 will have had a big effect on the cash increasing throughout the year. I wanted to make sure this improvement in cash was not coming from a massive loan, so I looked at the borrowing and interest rate to see if the loan had risen … *[some detail omitted from this* 2

exemplar] Although the borrowing was raised, it did not change the fact that more cash was coming into the business through customers.
I then looked at the working capital ratio to see if WHS Group can pay their debts for the next accounting period. In 2012 the ratio was 1.42:1 and in 2013 it was 1.40:1. This drop can be explained by the Group using cash to invest in their expansion. However the drop is something that you would not want repeated in the following year as it could mean that The Warehouse cannot pay its immediate debts.
The student has briefly discussed cash flows from operating, financing and investing activities. Reference has been made in the operating activities section to the payment of dividends, and loan repayment was erroneously referred to in the investing activities section.

Market analysis
WHS has paid dividends on ordinary shares to shareholders since 1994 so they have a very good history of loyalty to shareholders. The dividend for 2013 was announced at 5.5 cents per share, a drop of one cent from 2012. However, this should not concern shareholders as retained earnings increased from $76.43 million in 2012 to $153.23 million in 2013, an increase of $76.79 million. The WHS Group wanted a larger retained earnings so it chose not to pay out as much in dividends. So shareholders and those like Mi-Cha looking to invest shouldn't worry because the reduction in dividends planned as an investment in the future. 2
In May the share price reached a high of $4.39 per share showing there is a lot of confidence in the company and meaning shareholders believe the company is on the right track and making wise moves in the market.
The Warehouse Group is the biggest operating retailer in New Zealand which is also reflected in its share price. This tells us that in the New Zealand market WHS is going very strong compared to its opposition and is continuing to grow. This is rather pleasing for shareholders because gaining more of the New Zealand market will lead to more dividends. 2

Conclusion
I would advise Mi-Cha to invest long term in The Warehouse Group. The company keeps expanding in a small and well planned out way to increase future profits. Mi-Cha has the time to wait out the expansion because she does not intend to retire for 25 years. 3

All sources cited and a bibliography provided.