

## **Financial Analysis of WHOLE FOOD MARKETS**

Whole Foods Market is the leading retailer of natural and organic foods and America's first national "Certified Organic" grocer. Company's mission is to promote the vitality and well-being of all individuals by supplying the highest quality, most wholesome foods available. Since the purity of food and the health of our bodies are directly related to the purity and health of our environment, WFM core mission is devoted to the promotion of organically grown foods, healthy eating, and the sustainability of our entire ecosystem.

WFM has one operating segment, natural and organic foods supermarkets. WFM is the largest retailer of natural and organic foods in the U.S. and the 12<sup>th</sup> largest food retailer overall based on 2012 sales rankings from Progressive Grocer. As of September 29, 2013, WFM operated 362 stores in the United States ("U.S."), Canada, and the United Kingdom ("U.K."), averaging over seven million customer visits each week. WFM stores average 38,000 square feet in size.

### **Purpose and Core Values**

"With great courage, integrity and love, we embrace our responsibility to co-create a world where each of us, our communities and our planet can flourish - all the while, celebrating the sheer love and joy of food."

### **Differentiated Product Offering**

WFM offers a broad and differentiated selection of high-quality natural and organic products with a strong emphasis on perishable foods. WFM product selection includes, but is not limited to: produce and floral, grocery, meat, seafood, bakery, prepared foods and catering, coffee, tea, beer, wine, cheese, nutritional supplements, vitamins, body care, and lifestyle products including books, pet products, and household products.

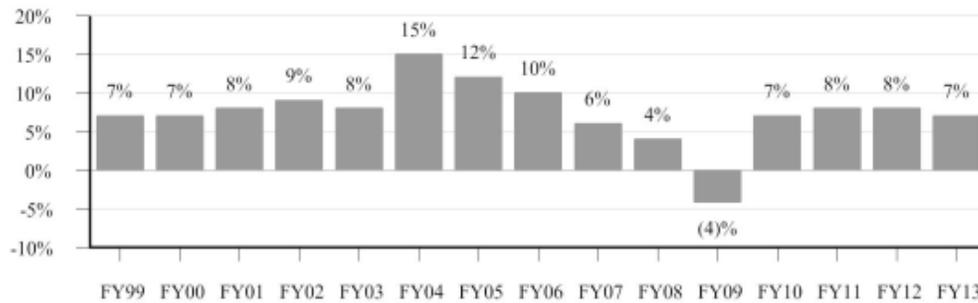
### **Quality Standards**

Maintaining high quality standards makes WFM branded produce exclusive and differentiated. To name a few Whole trade guarantees, whole body standards, MSC certified seafood, Eco scale rating system, enhanced standards for fresh produce and floral etc. It has recently introduced whole paws maintaining high quality standards of pet foods.

### **Growth Strategy**

WFM growth strategy is to expand primarily through new store openings, and while they may continue to pursue acquisitions of smaller chains that provide access to desirable geographic areas and experienced team members, such acquisitions are not expected to significantly impact their future store growth or financial results.

### Identical Store Sales Growth



### Marketing Strategy

WFM spend less on advertising and marketing than other supermarkets – approximately 0.4% of total sales in fiscal year 2013.

WFM allocates marketing budgets on various national and regional programs and on individual stores. It has marketers in every store dedicated to local events, community nonprofits and the best possible in-store experience. Dollars that would be spent on traditional media buys are instead typically spent on community nonprofit partnerships that help grow business and communities at the same time. They also connect and engage with customers through social media, e-newsletters, website and blog at [www.wholefoodsmarket.com](http://www.wholefoodsmarket.com).

### Social Responsibilities

WFM seek to be deeply responsible company in the communities where they do business around the world, providing ethically sourced, high-quality products and transparent information to the customers, reducing their impact on the environment, and actively participating in local communities. WFM goal is to contribute at least 5% of their after-tax profits annually to nonprofit organizations through Healthy eating educational programs, Whole planet foundation, Whole kids foundation etc.

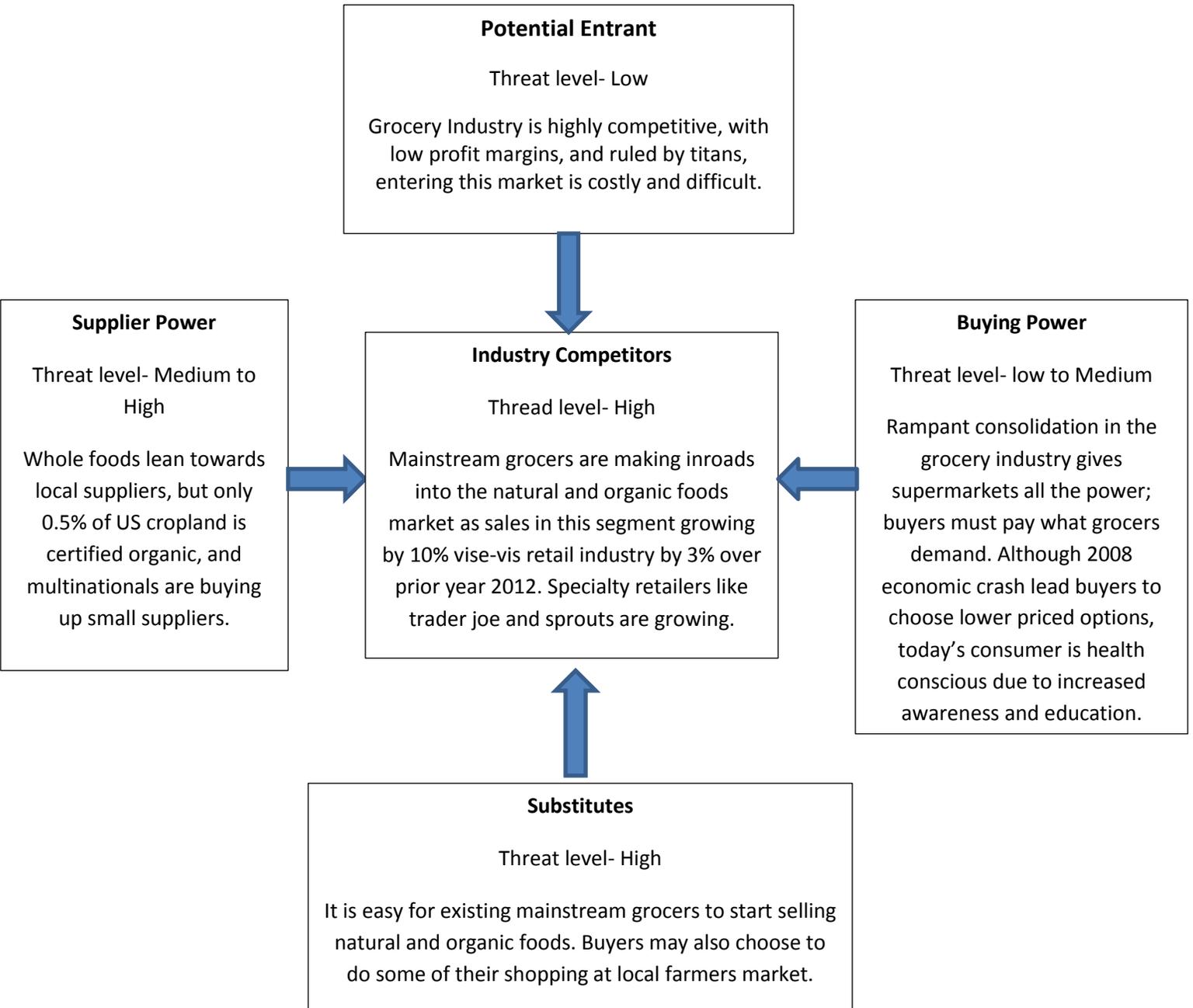
### Competitive Analysis:

Organic Food Retailers	Traditional Grocers	Super Centers & Clubs
The Fresh Market	Kroger	Walmart
Trader Joe	Safeway	Target
Sprouts	Super Value	Costco

WFM is the largest grocery chain of organic and natural foods in the United States, WFM competes within specialized segments of the 544billion sales of overall grocery industry. It faces competition from Farmers markets, large super markets, and other traditional grocers. However WFM enjoys competitive position due to its early start, scale & expansion- as it has close partnership with over 2000 organic suppliers worldwide, mission-driven brand superiority, and premium shopping experience.

# Industry Analysis

## PORTERS FIVE FORCE ANALYSIS



## **TIME SERIES ANALYSIS (Evaluation of over time company ratios)**

### **Profitability Ratio:**

Return on asset, Gross profit margin and Net profit margins have consistently increased past 3 years, quality of Income is satisfactory as cash flow from operating activity by net income is greater than 1 all 3 years as net income is growing in line with cash flow. Net income as percentage of cash flow is increasing indicating efficient working capital management. Fixed asset turnover ratio is increasing consistently in past 3 years. For each dollar spent on PPE, WFM earns about 5.6\$ in sales revenue in 2013. SG&A expenses have consistently reduced past three years.

### **Working Capital Efficiency:**

WFM has strived consistently in the betterment of its working capital management by reducing the day's receivable to 5 days, day's inventory outstanding about 17 days and increasing days payable outstanding to about 12 days in the past three years. And its accounts receivable has de grown by 4.6% in the year 2013 indicating their efforts to collect all the receivables in time ensuring shorter cash conversion cycle.

### **Short term liquidity risk:**

Test of liquidity helps us understand company's capability in meeting its current liabilities. WFM has maintained current ratio more than 1 in all the past three years however in 2012 it was 2.15 it has reduced to 1.8 in 2013 indicating that WFM has tried not to block too much funds in current assets. WFM has maintained about 1.1\$ cash and near cash assets for every 1\$ current liability indicating their strength in meetings its short term obligations. WFM has maintained about 0.9 Operating cash flow over average current liability in past 3 years, and its operating cash flow over capital expenditure is over 1 in all three years. Free cash flow has been growing significantly year on year .

### **Long term solvency risk:**

WFM has debt to equity ratio less than 0.5 reducing risk on equity owners returns. However, it appears as if WFM has stopped taking advantage of interest tax shield by keeping interest expense to zero past 2 years and its long term liabilities are mostly in the form of deferred lease payments. Long term debt to total asset is negligible as it is less than 0.11 in all the three years.

### **Other Ratios:**

Sales growth is oscillating in past three years from 12% in 2011, 15.7% in 2012 and 10.4% in 2010 however grocery and super market industry revenue has de grown by -0.4%.Which very clearly indicate that WFM has surpassed industry expectations. Sales per square foot has increased from 854\$ in 2011 to 937\$ in 2013.

## COMPARISON WITH KROGER

Kroger is one of the main competitors for WFM.

WFM has maintained positive net working capital of \$892M whereas Kroger -\$1875M in the year 2013. WFM current and quick ratios are more than 1 indicating that WFM's ability to service its short term debt is much higher than Kroger as its current assets are way more than its liabilities.

WFM has ROA of 10.17% and Kroger 6.74% in 2013, Net profit margin and gross profit margins of WFM is greater than Kroger however WFM has higher SG&A expenses due to its increased direct store expenses.

Cash conversion cycle of Kroger is much shorter i.e. only 7 days visa-vise 11 days for WFM due to its increased day's payable and increased efficiency. This very clearly shows areas of improvements for WFM.

Efficiency of Inventory management is essential for grocery industry which majorly deals with products of shorter gestation period. Whole foods turns over its inventory 21 times keeping its days inventory outstanding to 17 days where as Kroger turns over its inventory 14 times and its days inventory is 25 days, this unravels the fact that WFM manages its inventory efficiently reducing storage and obsolescence cost.

Kroger is highly levered its debt equity ratio is 4.4 in 2013 although it puts higher risk on equity holders returns it takes complete advantage of interest tax shield therefore enhancing its diluted EPS to 2.9\$, whereas WFM maintains 0.4 debt equity ratio and its EPS being 1.47\$. However, WFM has not disappointed its investor by paying 1.4\$ dividend per share as against Kroger only 0.63\$ in 2013.

Kroger has 2640 stores in 2013 and its revenue per store is \$37.2M, WFM has 632 stores and its revenue per store is \$35.7M. However, looking at the growth prospects of WFM signing 94 new stores in 2013 and consistent increase in per square foot sales past 3 years, elucidates that WFM has stronger opportunities of surpassing its per store revenue against Kroger.

Kroger is a big company with total asset being \$29B compared to WFM only \$5B and having multiple segments of operations such as retail food and drug store, multi department stores, jewelry stores and convenience stores and fuel business unlike WFM which specializes in natural and organic food store segments, yet is more promising as its sales growth rate in 2013 is 10.41% as against Kroger only 1.82%. and its future projecting sales growth are also in double digit. WFM market cap is 18B as against 23B of Kroger is evidential that WFM is giving tougher competition to Kroger in spite of operating only in specialty segment stores.

## CONCLUSION

Grocery industry revenue growth is expected to recover from -0.4% to 0.2% in coming years its way below the expected US GDP growth rate of 2.2% therefore we can say that grocery and super market industry is in decline phase of its life cycle. It may pose heavy challenge on WFM to maintain its top line and bottom line growth rate to its past record of 25% CAGR return to its investors since 1992.

In evaluating the industry, the environmental factors such as market size, demographic trends, regulatory factors, technology, supplier channel, consumer changing tastes and preferences are favorable for the natural/ organic food industry than the overall grocery industry as increased customer awareness and want of health & wellness benefits coupled with an affluent customer base willing to pay a premium price. Therefore WFM is just about 3% of overall food retail market, it is well positioned to capitalize on these attractive industry fundamentals for natural and organic foods. However, stiff competition and consumer demand for lower prices will pose a higher challenge going forward as many competitors have started imitating whole foods success model in organic foods segment.

Overall, WFM is a good buy basis strong product differentiation, corporate governance, transparency in operation, expected future sales growth, as their core mission is devoted to the promotion of foods, healthy eating, and sustainability of our entire ecosystems bringing health, balance and wealth to their investors.

### **Note:**

Both Companies reports its results of operations on a 52- or 53-week, fiscal year ending on the last Sunday in September by Whole foods, on Saturday nearest to January 31<sup>st</sup> by Kroger. Fiscal years 2013 and 2011 were 52-week years and fiscal year 2012 was a 53-week year, with an additional week falling in the fourth fiscal quarter.

Both WFM and Kroger values inventories lower of cost or market method using LIFO for approximately 96% and 92% of its inventories respectively. Therefore, no conversion from LIFO to FIFO being made.

Kroger Company's non-controlling interest is not taken into consideration for calculating Net Income.

## WHOLE FOODS MARKET

RATIOS	2013	2012	2011
<b>Cash liquidity and cash sources&amp; uses</b>			
NetWorking Capital	892	1,126	574
Current ratio	1.82	2.15	1.65
OCFCL	0.98	0.99	0.93
OCFCX	1.88	2.01	2.07
Free cashflow	472	463	390
Quick Ratio	1.11	1.45	0.94
<b>Profitability Ratios</b>			
ROA	10.17%	9.72%	8.35%
Net Profit Margin	4.27%	3.98%	3.39%
Asset T/O	2.38	2.44	2.44
Gross Profit Margin	35.84%	35.52%	34.99%
SG&A	28.51%	28.68%	29.09%
<b>Efficiency Ratio</b>			
A/R T/O	67.10	62.90	65.64
Days receivable outstanding	5.44	5.80	5.56
Inventory T/O	21.04	21.22	19.91
Days inventory outstanding	17.35	17.20	18.33
PPE T/O	5.59	5.58	5.21
Accounts Payable T/O	33.72	31.32	29.27
Days payable outstanding	10.83	11.65	12.47
cash conversion cycle	11.97	11.35	11.42
<b>Leverage Ratios</b>			
debt/equity	0.43	0.39	0.43
Times Interest earned	0.00	0.00	137.00
Long term debt/ total asset	0.10	0.10	0.10
<b>Growth &amp; Other Important Ratio</b>			
Sales Growth	10.41%	15.74%	12.24%
Inventory Growth	10.70%	10.98%	4.33%
Fixed asset growth	10.72%	9.81%	5.89%
A/R growth	-4.57%	12.57%	31.58%
operation cash flow/NI	1.83	1.97	2.20
sales per square foot	937.37	918.29	854.44

## KROGER

RATIOS	2013	2012	2011
<b>Cash liquidity and cash sources&amp; uses</b>			
Net Working Capital	-1,875	-3,102	-1,780
Current ratio	0.82	0.72	0.80
OCFCL	0.31	0.28	0.31
OCFCX	1.47	1.42	1.36
Free cashflow	1075	843	700
Quick Ratio	0.23	0.20	0.21
<b>Profitability Ratios</b>			
ROA	6.74%	7.47%	3.86%
Net Profit Margin	1.54%	1.55%	0.67%
Asset T/O	3.65	4.02	3.84
Gross Profit Margin	20.57%	20.59%	20.92%
SG&A	15.45%	15.37%	17.00%
<b>Efficiency Ratio</b>			
A/R T/O	90.79	96.62	100.63
Days receivable outstanding	4.02	3.78	3.63
Inventory T/O	14.47	14.96	14.16
Days inventory outstanding	25.22	24.40	25.77
PPE T/O	6.20	6.59	6.31
Accounts Payable T/O	16.80	17.42	16.72
Days payable outstanding	21.73	20.95	21.83
cash conversion cycle	7.51	7.23	7.57
<b>Leverage Ratios</b>			
debt/equity	4.44	4.85	4.90
Times Interest earned	6.15	5.98	2.94
Long term debt/ total asset	0.51	0.49	0.50
<b>Growth Ratio</b>			
Sales Growth	1.82%	7.03%	10.02%
Inventory Growth	9.81%	0.63%	2.98%
Fixed asset growth	13.77%	2.65%	2.24%
A/R growth	6.18%	10.75%	12.31%

**References:**

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