



---

## FINANCIAL MANAGEMENT FOR THE HOTEL INDUSTRY

---



BMIH5007

Teacher Name : Dale Clarke

Student name : Mohammed Robyat Khan ( 2013063)

## Executive Summary

This report has been prepared for Jurys Inn to analyse the financial efficiency from the ratio analysis. It has also prepared trend analysis and has shown the ratio trends through column charts for the period 2019-2020. In the first part, there is an introductory part that makes the basis of the report. Then comes the calculation part, which is named 'Financial Analysis' where specific explanations were given for the ratios calculated. The ratios are-profitability, liquidity and gearing ratios.

After the calculations, a trend analysis has been prepared to find out whether the ratios are having upward or downward trends. It was found that most of the ratios are going to the favorable position, only except debtor ratios and creditor ratios.

The next two parts show the need for ratio analysis and the benefits and concerns regarding this analysis for the hotel industry. After all the discussions and analysis have been performed, this study concluded that, the company is having significant growth in its performance and is supposed to have a positive trend further. If the management can resolve the debtor and creditor payment issues, it will see further attainments in the future.

## Table of Contents

|                                                                                       |    |
|---------------------------------------------------------------------------------------|----|
| Executive Summary .....                                                               | 1  |
| Introduction .....                                                                    | 3  |
| Financial Analysis .....                                                              | 4  |
| Profitability Ratios .....                                                            | 4  |
| Asset Turnover Ratios .....                                                           | 5  |
| Liquidity Ratios .....                                                                | 5  |
| Gearing Ratios.....                                                                   | 6  |
| Financial Analysis Trend .....                                                        | 8  |
| Profitability .....                                                                   | 8  |
| Following table shows the results and the comment regarding appropriate ratios: ..... | 8  |
| Liquidity .....                                                                       | 9  |
| Gearing .....                                                                         | 9  |
| Knowledge Obtained from Ratio Analysis .....                                          | 11 |
| Benefits and Limitations of Ratio Analysis .....                                      | 12 |
| Conclusion .....                                                                      | 14 |
| Bibliography .....                                                                    | 15 |

## Introduction

Through ratio analysis, the information from the financial statements of a company is analysed and compared. The data from the statements are generally used to determine the financial health or performance of a company (Tian & Yu, 2017). To compare the performance with peer companies in the industry, to see if there remains a trend in the company's profitability, liquidity and solvency, ratio analysis is used (Zorn et Al., 2018). This study has been done to analyse the financial soundness of Jury inn. It is a company managing a hotel portfolio in two different areas- the UK and Northern Ireland. Being an operator in the hospitality industry, they face fierce competition with other mid-range hotels. So, this study measures their profitability and the ability to meet short and long-term liabilities for 2019 and 2020 and also analyse the trend found from the calculation. Additionally, it also has discussed the importance and limitation of ratio analysis in the hotel industry.

## Financial Analysis

### Profitability Ratios



Figure 01: Profitability Ratios

Sources: Author's Creation adapted from Husain & Sunardi, 2020

The profitability ratios of Jurys Inn for 2019 and 2020 are calculated below:

| Profitability Ratios |                                                             |                                       |                                       |
|----------------------|-------------------------------------------------------------|---------------------------------------|---------------------------------------|
| Name                 | Formula                                                     | 2019                                  | 2020                                  |
| Gross Profit Margin  | Gross Profit/Sales                                          | $= (5050/5500) \times 100$<br>=91.82% | $= (5150/6000) \times 100$<br>=85.83% |
| Net Profit Margin    | Net Profit/Sales                                            | $= (4008/5500) \times 100$<br>=72.87% | $= (4073/5500) \times 100$<br>=67.88% |
| ROCE                 | Profit Before interest/Total Asset less Current Liabilities | $= (4028/6226) \times 100$<br>=64.70% | $= (4091/6274) \times 100$<br>=65.21% |

Table 01: Profitability Ratios

Source: Author's Calculation

Above ratios are all above the benchmark ratios (20%-40%). So, it can be said that Jurys Inn is earning good profits and the management is capable to generate revenues.

## Asset Turnover Ratios

These ratios show how efficiently a hotel can incur sales/ revenues from assets (Patin et. Al., 2020). Following are the calculations for Jurys Inn:

| Asset Turnover Ratios    |                                                      |                           |                           |
|--------------------------|------------------------------------------------------|---------------------------|---------------------------|
| Name                     | Formula                                              | 2019                      | 2020                      |
| Total Assets Turnover    | Sales Turnover/Total Assets less Current Liabilities | =5500/6226<br>=0.88 times | =6000/6274<br>=0.96 times |
| Fixed Assets Turnover    | Sales Turnover/Fixed Assets                          | =5500/4500<br>=1.22 times | =6000/4650<br>=1.29 times |
| Working Capital Turnover | Sales Turnover/Net Current Assets                    | =5500/1726<br>=3.19 times | =6000/1624<br>=3.69 times |

Table 02: Asset Turnover Ratios

Source: Author's Calculation

As the fixed asset turnover is more than the industry benchmark (1), and working capital turnover is higher than the benchmark (1.5- 2), the company has generated good enough sales concerning assets.

## Liquidity Ratios

These ratios measure the ability to pay off short-term debts (Madushanka & Jathurika, 2018). The most commonly used ratios are- current, quick and cash ratios.

### Current Ratio and Quick Ratio

The calculations for 2019 and 2020 are shown below:

| Current & Quick Ratios |                                           |                       |                       |
|------------------------|-------------------------------------------|-----------------------|-----------------------|
| Name                   | Formula                                   | 2019                  | 2020                  |
| Current Ratio          | Current Assets/Current Liabilities        | =3065/1339<br>=2.29:1 | =3240/1616<br>=2:1    |
| Quick Ratio            | Current Assets- Stock/Current Liabilities | =1615/1339<br>=1.21:1 | =1820/1616<br>=1.13:1 |

Table 03: Current and Quick Ratios

Source: Author's Calculation

From the summary table, it is clear that the company is having a higher or equal ratio than the benchmark ratio. It indicates that it is capable of satisfying the current bills.

### Debtor Days & Creditor Days

The calculations for 2019 and 2020 are as follows:

| Debtor & Creditor Days |                               |                                         |                                         |
|------------------------|-------------------------------|-----------------------------------------|-----------------------------------------|
| Name                   | Formula                       | 2019                                    | 2020                                    |
| Debtors Days           | Debtors*365/Credit Sales      | $= (1600 \times 365) / 5500$<br>=106.18 | $= (1800 \times 365) / 6000$<br>=109.50 |
| Creditor Days          | Creditors*365/Credit Purchase | $= (800 \times 365) / 450$<br>=648.89   | $= (870 \times 365) / 850$<br>=373.59   |

Table 04: Debtor and Creditor Days Ratio

Source: Author's Calculation

The benchmark for these ratios is 35-40 days. But the ratios are much higher than that. It means that they are slow to pay or receive cash from creditors and debtors. It leaves some scope for change in operations.

### Gearing Ratios

Gearing means the amount of debt used as a percentage of equity capital. This ratio shows the level of financial risk a company may face. Though there are many gearing ratios in effect, for the hotel industry, the following ratios are most appropriate:

#### Debt Ratio

The calculations for Jurys Inn for 2019 and 2020 are shown below:

| Debtor & Creditor Days |                         |                          |                          |
|------------------------|-------------------------|--------------------------|--------------------------|
| Name                   | Formula                 | 2019                     | 2020                     |
| Debt Ratio             | Total Debt/Total Assets | $= 150 / 7565$<br>=1.98% | $= 145 / 7890$<br>=1.84% |

Table 05: Debt Ratio

Source: Author's Calculation

## Interest Coverage Ratio

The calculations for 2019 and 2020 are shown below:

| Debtor & Creditor Days |                                                        |                    |                     |
|------------------------|--------------------------------------------------------|--------------------|---------------------|
| Name                   | Formula                                                | 2019               | 2020                |
| Interest Cover         | Profit Before Interest & Tax/Periodic Interest Charges | =4028/20<br>=201.4 | =4091/18<br>=227.28 |

Table 06: Interest Cover Ratio

Source: Author's Calculation

The above ratios show that, Jurys is performing well as the debt ratio is lower than 35% and the interest cover ratio is higher than 1.5.

## Financial Analysis Trend

After calculating the ratios, trend analysis has been prepared to get an insight into how the hotel is performing and how it may perform later (Sagala, 2019). For this, a summary table along with the trend chart is shown here.

### Profitability

The following table shows the results and the comment regarding appropriate ratios:

| Profitability Ratios     |        |        |       |         |           |
|--------------------------|--------|--------|-------|---------|-----------|
|                          | 2019   | 2020   |       | Comment | Benchmark |
| Gross Profit Margin      | 91.82% | 85.83% | %     | Good    | >40%      |
| Net Profit Margin        | 72.87% | 67.88% | %     | Good    |           |
| ROCE                     | 64.70% | 65.21% | %     | Good    | >20%      |
| Total Assets Turnover    | 0.88   | 0.96   | times | Good    |           |
| Fixed Assets Turnover    | 1.22   | 1.29   | times | Good    | >1        |
| Working Capital Turnover | 3.19   | 3.69   | times | Good    | >2        |

Table 07: Profitability Ratio Summary

Source: Author's Calculation

In the case of gross profit margin, around 92% and 86% of sales resulted in gross profit for the years 2019 and 2020 consecutively. Additionally, Jurys Inn has earned a 72.87% margin in 2019 and a 67.88% net profit margin in 2020. It is also applicable for ROCE too. So, overall, this hotel has efficiency in managing its profits.

For the asset turnover ratios, it is also doing quite well. In 2019, total asset turnover was 0.88 times, which means, Jurys has generated \$0.88 in sales for every \$1 in total assets less current liabilities. In 2020, it was even better at 0.96 times.

All the profit margin ratios are showing downward trends, which means that, they might be lower in later years. But All the asset turnover ratios are on an upward trend. So, in terms of that, Jurys inn may perform better in using the asset in the future.

## Liquidity

Here goes the summary table:

| Liquidity Ratios |        |        |      |          |           |
|------------------|--------|--------|------|----------|-----------|
|                  | 2019   | 2020   |      | Comment  | Benchmark |
| Current Ratio    | 2.29:1 | 2.00:1 |      | Good     | >1.5      |
| Quick Ratio      | 1.21:1 | 1.13:1 |      | Good     | >1        |
| Debtor Days      | 106.18 | 109.50 | days | Not Good | >30-35    |
| Creditor Days    | 648.89 | 373.59 | days | Not Good | >30       |

Table 08: Liquidity Ratio Summary

Source: Author's Calculation

It shows whether the company has enough liquid assets to pay off the debts or payables within a short-term period. But it is in an alarming situation regarding the payment to creditors. It should change the payment policy readily to keep a good relationship with the lenders.

The company has a substantial amount of liquid assets to pay off short-term debts but the chart is showing a downward trend, which is slightly alarming. Additionally, the low trend in debtor and creditor days is good as the company needs to reach the benchmark of 35-40 days from the present value.

## Gearing

The summary table:

| Gearing Ratios |       |        |         |           |
|----------------|-------|--------|---------|-----------|
|                | 2019  | 2020   | Comment | Benchmark |
| Debt Ratio     | 1.98% | 1.84%  | Good    | <35%      |
| Interest Cover | 201.4 | 227.28 | Good    | >1.5      |

Table 09: Gearing Ratio Summary

Source: Author's Calculation

Jurys Inn is performing well in managing the debts. It has a very low amount of debt in terms of assets and it also pays the interests in time. In 2019 the ratio was only 1.985 and in 2020 it even lowered. So, to see it more clearly, here goes the comparison:

The debt proportion may be even lower than before in the previous year. So the hotel has a very low chance to have bankruptcy risk. Also, it has a good possibility to continue having good trends in the future.

## Knowledge Obtained from Ratio Analysis

Financial ratios help the businesses to evaluate the performance of the company and help to compare it with other similar companies (Correa-Mejía & Lopera-Castaño, 2020). For the hotel industry, it is much more relatable as this industry operates in a highly competitive market. Being in a service company, the hotel management needs to focus on the changing trends in the social, economic, political and behavioral changes in the country (Park & Min, 2020). Ratio analysis is a good way to provide sufficient insight into where the company is going and how it is doing at present. Looking at the financial statements only cannot be a solution to derive information about the profitability and solvency of the hotel. Due to the need for physical assets, hotels need to invest heavily in several tangible assets, such as land, buildings, etc. To obtain these assets, most often hotels have to take debts. In some cases, many hotels become heavily burdened with debts and fail to repay those due to low levels of assets. So apart from solvency ratios, profitability ratios are also important for hotels.

Here are the reasons for which understanding the financial ratios and their fluctuations is essential for Hotel management (Abidin et Al., 2021):

- Measuring the ability of the hotel to fulfill the obligation of providing services to the customers.
- Establishing a well-developed link and relationship between different stakeholders, such as- lenders and creditors
- Preparing strategies and financial planning
- Forecasting sales, costs, liabilities etc. and preparing budget accordingly
- Imposing financial control over the hotel that can ensure profitability and solvency
- Assessing the management competency by reviewing the summary of the analysis

Therefore, to analyse the information seen in the financial statements, the understanding ratio is important for hotel management.

## Benefits and Limitations of Ratio Analysis

Ratio analysis helps to visualize and extract necessary information from financial statements and also helps to compare with the peer companies (Fahlevi & Mukhibad, 2018). As for the hotel industry, ratio analysis acts as an important tool to analyse the current situation and performance of a hotel. Still, it is not free from limitations, as trend analysis from ratio analysis can be proven wrong because of several aspects. Following are the benefits of ratio analysis for hotel management:

### **i. Financial Planning**

Through ratio analysis, companies can easily find out the revenue drivers, cost drivers and trends in costs and other features. From the analysis, the probable future amount needed for continuing business may also be forecasted. So, a hotel can easily try to act accordingly based on the forecast.

### **ii. Measuring Operational and Financial Efficiency**

Through degree of operating leverage, financial leverage, debt ratio, ROE etc., a hotel can easily measure its operational efficiency (Pavone et. Al., 2021). For example, if Jurys Inn finds out that, they are taking more debts, whereas their assets cannot cover up all the payments, then they might become cautious to not use as much debt as before.

### **iii. Cost Control**

Ratios help to find out the most costly sources and help to compare the cost level with other companies. So, the hotel can start to reduce costs, if they find out that the cost is much higher.

### **iv. Liquidity Indicator**

To assess the short-term debt paying capability, current, quick and cash ratios help much. It shows whether the hotel holds the capability to use readily available assets to meet up short-term liabilities.

#### **v. Overall Profitability Indicator**

The hotel management is always concerned to learn about the capability to raise profit from the day-to-day business. After calculating all the ratios together, they can easily conclude whether the hotel is running profitably or not. This too leads to financial strategies.

Following are the limitations of ratio analysis that must not be ignored before conducting analysis (Li, 2019):

- As financial statements are released periodically, they do not consider inflation most often. This may incur the wrong result.
- Ratio analysis are done on historical data and so, they may not represent the accurate projection for the future.
- In case the hotel changes its accounting policy or adopts different operational management, then the ratio before and after the changes may not provide a correct comparison.
- Sometimes, companies manipulate financial statements. In such cases, ratios may not provide accurate results.

## Conclusion

This study has been prepared to calculate the ratio analysis and to find out the trend from them. After analyzing the data of 2019 and 2020 of Jury Inn, different profitability, liquidity and gearing ratios have been calculated. In terms of profitability, Jurys Inn is performing well and is generating a significant amount of profit from the revenue. Moreover, it can use the assets to generate revenues. After that, in terms of liquidity ratios, it is also in a good position in terms of paying short-term loans. But, it has to work more precisely to reduce the debtor and creditor days as those are way higher than the industry benchmark. This company is managing the debt and interest payment well as the gearing ratios are all showing a good ratio. So, it can be concluded that, Jurys Inn's management is performing well in every term except payment to creditors and receiving from debtors. So, if this issue is solved, the hotel is expected to perform better in near future.

## Bibliography

- Abidin, J.Z., Abdullah, N.A.H. and Khaw, K.L.H 2021. BANKRUPTCY PREDICTION: SMES IN THE HOSPITALITY INDUSTRY. *International Journal of Banking and Finance*, 16(2), pp.51-80.
- Correa-Mejía, D.A. and Lopera-Castaño, M 2020. Financial ratios as a powerful instrument to predict insolvency; a study using boosting algorithms in Colombian firms. *Estudios Gerenciales*, 36(155), pp.229-238.
- Fahlevi, E.D. and Mukhibad, H., 2018. Use Of Financial Ratios And Good Corporate Governance To Predict Financial Distress. *Jurnal Reviu Akuntansi dan Keuangan*, 8(2), pp.147-158.
- Husain, T. and Sunardi, N 2020. Firm's Value Prediction Based on Profitability Ratios and Dividend Policy. *Finance & Economics Review*, 2(2), pp.13-26.
- Li, J 2019, December. Research on Limitations of Financial Statement Analysis. In *5th International Conference on Economics, Management, Law and Education (EMLE 2019)* (pp. 378-382). Atlantis Press.
- Madushanka, K.H.I. and Jathurika, M 2018. The impact of liquidity ratios on profitability. *International Research Journal of Advanced Engineering and Science*, 3(4), pp.157-161.
- Park, J. and Min, H 2020. Turnover intention in the hospitality industry: A meta-analysis. *International Journal of Hospitality Management*, 90, p.102599.
- Patin, J.C., Rahman, M. and Mustafa, M 2020. Impact of total asset turnover ratios on equity returns: dynamic panel data analyses. *Journal of Accounting, Business and Management (JABM)*, 27(1), pp.19-29.
- Pavone, P., Migliaccio, G. and Simonetti, B 2021. Investigating financial statements in hospitality: a quantitative approach. *Quality & Quantity*, pp.1-25.
- Sagala, D.A.P.H 2019, October. Effect of Current Ratio, Debt To Equity Ratio, Net Profit Margin, and Total Asset Turnover on Earning Per Share. In *International Conference on Global Education* (pp. 1507-1521).
- Tian, S. and Yu, Y 2017. Financial ratios and bankruptcy predictions: An international evidence. *International Review of Economics & Finance*, 51, pp.510-526.

Zorn, A., Esteves, M., Baur, I. and Lips, M 2018. Financial ratios as indicators of economic sustainability: A quantitative analysis for Swiss dairy farms. *Sustainability*, 10(8), p.2942.