

ACPA 7002

MSc International Innovation Management

Assignment 1: Financial Management &
Planning

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Business review of McLaren utilizing their published Financial Accounts.

**Abstract**

The purpose of this essay is to critically analyse the potential for a joint venture a joint venture to produce an electric vehicle with McLaren Holdings company, from a financial perspective. Highlighting Risks and trends found within the published accounts and from any other relevant sources.

Contents Page

	Page
1.0 Executive Summary	3
2.0 Introduction	3-5
3.0 Use and Limitation of ratios & McLaren Ration Analysis	6
3.1 Profitability Ratios	6-7
3.2 Liquidity Ratios	7
3.3 Activity Ratios	7-8
3..4 Leverage Ratios	9
3.5 Investor Ratios	10
4.0 Limitations of Ration Analysis	10
5.0 Summary of Findings	10-13
6.0 Conclusion and Recommendations	13
Appendices Ratios	

References

Bibliography

1.0 Executive Summary

A joint venture with McLaren is potentially high-risk venture based on the financial statements alone. However, depending on the investment required it is worthy of further investigation and analysis as it does provide opportunity, due to a strong Brand Value and history.

2.0 Introduction

McLaren Group is a British car manufacturer that was founded in 1981 after Ron Dennis acquired the McLaren Formula 1 team.

McLaren consists of:

McLaren Racing: Designs, builds, and operates race cars.

McLaren Automotive: Largest division set up in 2010 to design, build and assembles high performance supercars for retail.

McLaren Applied. Technology division, purpose to improve data advancements across multiple sectors.

Each subsidiary is a company, with different investors, directors and aims.

McLaren Automotive makes most money through a 4 family, product portfolio:

GT; Super Series, Motorsport, and Ultimate models.



(The Verge, 2016)

McLaren also makes money through winning F1 competitions and sponsorships – although the F1 business is largely supported by the revenues of the other two subsidiaries. See Yr. by Yr. profile attached: [McLaren – F1 Racing Team – Ricciardo, Norris \(formula1.com\)](https://www.formula1.com/en/latest/F1.RaceCalendar.McLaren.F1.Racing.Team.Ricciardo.Norris.html) (Formula1.com, 2022)

Sponsorship is another huge way to make money for F1 teams. In 2020, McLaren confirmed a multi-year partnership with Belarusian company Miory Steel. (Cattlin, 2021)

Luxury Car Market – Overview

The luxury car market was valued at around USD 440 billion in 2021. The market is projected to reach USD 600 billion in 2027, with a CAGR of approximately 5% during the forecast period (2022-2027). (Mordor Intelligence, 2022)

Factors influencing the sector include:

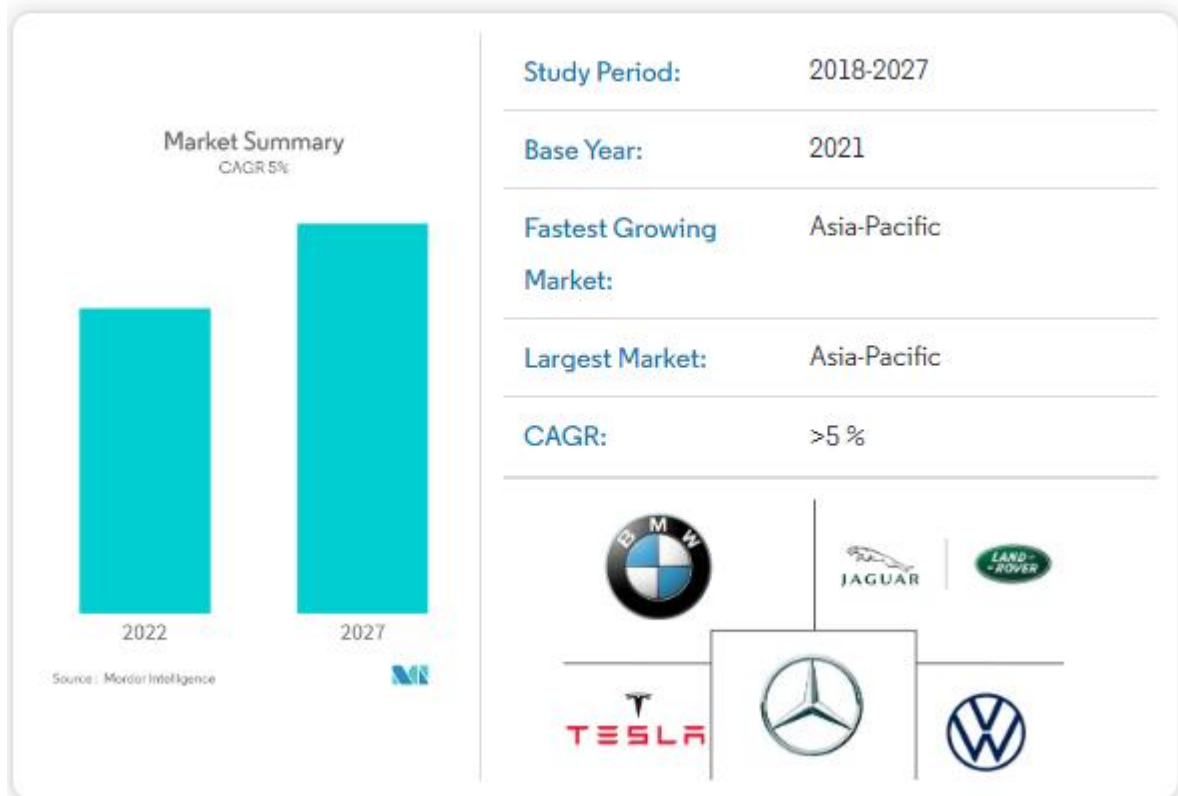
- Covid19 due to the impact upon sales and production. Significantly, 2020.
- A significant growth of tangible luxury offerings in vehicles, shifting consumer preferences from sedans to SUVs., and increasing disposable incomes of consumers have been propelling the demand for luxury cars worldwide.
- Import tariffs is expected to hinder the growth of the luxury car market. (E.g., Brexit & US -set to increase import duty for cars not build in US).
- Growing trend of electric luxury vehicles worldwide is fuelling the demand for luxury cars.
- Fuel prices caused by the war in the Ukraine with Russian and inflation are significant factors affecting the recovery of the car sector. (Engineeringyourfinances.com, 2022)
- Legislation – including emissions and safety, have the affect or increasing car production costs. (Engineeringyourfinances.com, 2022)

Luxury Car Market - Revenue Share (%), by Drive Type, 2019



Source: Mordor Intelligence

Market Snapshot



(Mordor Intelligence, 2022) **Luxury Car Competitors**

Brand
BENTLEY
BUGATTI
TOYOTA/LEXUS
MERCEDES-BENZ
BMW
ROLLS ROYCE
AUDI AG
LAMBORGINI
JAGUAR
PORCHE
TESLA
ASTON
MASERATI
ALPHA ROMEO
FERRARI
McLaren

(Passionbuz.com, 2022)

3.0 Use and Limitation of ratios and McLaren Ratio Analysis.

The purpose of Ratio analysis is to provide a significant insight into a company.

Ratio analysis is a popular technique of financial analysis. (corporatefinancialinstitute.com, 2022)
Financial statements are used to extract information that reflects Profitability; liquidity, efficiency; finance leverage and worth for investors.

Ratios are mathematical calculations that the company can use to evaluate its performance. (Fields, 2011). They help the company and investors to establish trends, showing improvement or decline.

3.1 Profitability ratios

Gross Profit:

(Gross Margin) shows the ratio of gross profit to sales expressed as a percentage.

The gross profit percentage is also a useful measure to compare the contribution that individual product sales make towards a company's overall fixed costs. (Marsh, 2012)

% GP

31.76	18.64	30.42
2021	2020	2019

The GP shows a decline in GP in 2020, justified by the impact of Covid 19 in the Annual Report with a recovery and improvement in YTD accounts in 2021. However, looking in more detail at the actual Turnover:

Sales

495,501	771,660	1,485,785
2021	2020	2019

It is clear to see the impact of Covid on sales and production, with sales in 2021 YTD sitting at a third (33.35%) of what they were in 2019. It is unlikely that this will significantly improve in the last quarter. This was impacted by a decision made in a 5 yr. business plan, created prior to Covid and that was applied despite Covid in Q1 2020 to allow for the intentional softening of sales volumes in the first quarter with the aim of bringing supply well below demand driving stock out of retailers. (Ref Pg3 AR statements 31 Dec 2020). Potentially, it could be said that this was a deliberate decision based on clearing older stock and models in preparation for creating a demand pre order system for the new hybrid models.

Operating Profit:

Operating profit shows how well the management team are at keeping costs to a minimum whilst generating revenue. The operating profit ratio below is prior to Depreciation and Amortization.

%

2021	2020	2019
4.80	-6.49	13.76

The operating profit ratio show more positivity in 2019. A decline in 2020 and a fair recovery in 2021. When reviewing the AR 31 Dec2020. We can clearly identify the impact of Covid with McLaren showing safety and support to their employees as a primary value. (Ref: Pg3 Impact of Covid19 1st Lockdown). Closing Production and Furloughing employees in inline with Government Guidance.

In Q1 2020 Capital expenditure was reduced by £83M compared to previous year, with expenditure focused only on programs that delivered return in the year. (Ref Pg4 AR statements 31 Dec 2020).

Other savings were made in Staff costs, marketing, events, motorsport, travel, racing costs, IT, and facilities management.

Reducing Marketing and presence in motorsport in the competitive sector of luxury cars is a high-risk strategy that can have long lasting impact upon sales.

The group has completed a resizing and restructuring program at the end of July 2020 saving £14.7M

Net Profit:

The net profit has been calculated after interest and tax. The net profit is showing a significant loss in 2021, although there has been some recovery since 2020.

	2021	2020	2019
%	-13.90	-83.09	-2.30

Return on Assets

The return on asset ratio provides insight into the efficient use of company's assets.

Fixed & current assets	2021	2020	2019
%	-5	-38	-2

Cashflow was significantly impacted by Covid 19. With T/O declining due to reduced W/sale volumes. Impairment charges on projects no longer being pursued, have also impacted. Investment cashflow is being managed through cancelling programs in favor of those that product ROI in the year. In addition, a short-term loan has been realized from the National Bank of Bahrain and £300M of convertible shares have been issued.

Post Balance sheet events (22nd Jan 2021) show a change in the Groups Chief Financial Officer and in April 2021 a Sale and Leaseback transaction with Global Net Lease for £170M (A 20 yr. lease). Showing McClaren making use of assets to improve their cashflow situation.

Return on Equity

The purpose of the return on equity ratio is to show the rate of return by equity investors in the company. (Marsh, 2012)

Shareholder Equity - (Note - Cumulative compulsory convertible preference shares of £0.01 - have been deducted)	2021	2020	2019
%	-26.63	-207.72	-5.08

Currently due to a loss-making status there are no dividends for shareholders in McLaren. Currently the group is still privately owned. But during 2020 has issued convertible loan note and warrants. These warrants have given investors voting and dividend rights on an 'as-converted' basis. According to the AR 31 Dec 2020. The investors cumulatively held 21.05% in the subsidiary on a diluted basis. Providing investors with considerable influence.

McLaren has lost total control of McLaren racing, which is now a joint venture. Which is now subject to equity method accounting (Ref: Pg55 AR 31 Dec 2020). (McLaren Group Ltd, 2020)

3.2 Liquidity Ratios

The liquidity ratio indicates a company's ability to repay its debts as they fall due. It is usually expressed as a single figure. A figure that is greater than 'one' would indicate that the company is liquid. A ratio of less than 'one' would indicate that the company might struggle to pay debts when they are due. (Marsh, 2012)

Quick Ratios/Acid	2021	2020	2019
Current Assets	576,993	517,215	604,663
less stock	163,880	112,773	151,656
over Current Liabilities	314,070	613,600	747,523
	1.32	0.66	0.61

Based on Marsh summation that a ratio of more than one would signify the company is liquid, could not be stated in 2020 or 2019. However, the Directors report admits the pressure on liquidity placed on McLaren by the pandemic has only been averted by the injection of £300m through subscription to convertible preference shares by existing shareholders in Q1 2020 (McLaren Group Ltd, 2020). In addition the group has also had to seek short term liquidity by way of a secured loan from the National Bank of Bahrain. (McLaren Group Ltd, 2020) and through selling a stake in McLaren Racing.

Whilst the group states they have a 3-phase plan. They are subject to multiple risks including foreign exchange, Credit Risk and Liquidity risk.

This is supported in the Independent auditors reports – which states: 'The Covid-19 Pandemic has had a significant impact on the group and the global automotive industry more broadly' This pandemic has resulted in significant operational and financial disruption which has put pressure on the liquidity of the group' Meaning the group will require additional funding to meet their liabilities over the next 12 months. (McLaren Group Ltd, 2020)

Suggesting they are not a sound investment risk currently.

3.3 Activity Ratios

Days Outstanding or Debtor Days

Debtors' days is an indication of how good a company is at collecting debts from its customers and how much trade credit it allows. The fewer days the better. (Marsh, 2012)

Days Sales Outstanding:

2021	2020	2019
#DIV/0!	70	50

Debtors' days are showing an increase from 2019 to 2020. However, this has not exceeded 90 days which is a common threshold for business. Trade debtors has decreased from 2019 £201,872 to 2020 £149,012. The ratio is also impacted by the drop in Turnover in 2020.

Inventory Turnover

Average Inventory

(2021,2020+2019) div 3

2021	2020	2019
2.37	4.40	7.24

Days Payable outstanding

Inventory Turnover average has decreased, showing improved management, of stock by 2021.

Days payable outstanding:

2020	2019
72.73	90.98

Trade creditors have decreased from 101,638 in 2019 to 613,398. It should also be noted that McLaren operates a Trade Finance facility that is used to support McLaren retailers. The total available facility is up to US\$220,000k. The value of this was £156,061k in 2019 and has reduced to £63,713k. It could be suggested this decrease comes from the deliberate softening of sales volumes undertaken in Q1 2020, with the aim of driving stock out of retailers. (See Note 17 AR 31 Dec 2020). (McLaren Group Ltd, 2020)

There is also a Trade Credit Insurance Facility that covers 95% of the Trade Finance Balance. (McLaren Group Ltd, 2020)

When considering McLaren's creditors, the total value falling due within 1-year totals at 613,600. (McLaren Group Ltd, 2020)

3.4 Leverage Ratios

Leverage ratios indicate the level of debt incurred by a business entity against several other accounts in its balance sheet. (corporatefinancialinstitute.com, 2022)

Stockholder equity has increased significantly by 2019 from 258,192 to 671,192. Decreasing the long-term debt in favor of shareholder equity. The purpose of which might be to improve an external investor outlook, through improved solvency.

Debts/Equity Ratio

Long term debt - see note
Stockholders' Equity
%

2021	2020	2019
503,686	751,934	780,539
671,192	308,661	258,192
75.04	243.61	302.31

Note: Long term debt: senior secured notes; obligations under finance leases; Derivative financial liabilities; Provision for liabilities deferred; Deferred capital funding. See notes: 18,19,21,23,24,25,

(McLaren Group Ltd, 2020)

Interest Coverage

This ratio examines financial durability.

Interest Coverage

EBITDA
Interest Charge
%

2021	2020	2019
23,785	-50,076	204,484
	-425,600	-71,827
#DIV/0!	11.77	-284.69

The interest coverage ratio has worsened significantly in 2020 due to the pandemic and limitations on trading. This can be seen in the interest EBITDA figure -50,076. Which 2021 became 23,785. Whilst we cannot see the % figure in 2021. The outlook is set to be improved due to the decrease in liabilities.

3.5 Investor Ratios

This is the amount of earnings attributable to each equity share. For example, if a company has paid up capital of 100,000 ordinary shares of €5 and makes a net profit after tax of €50,000 then the earnings per share will equal fifty cents per share. Simply divide the net profit after tax by the number of shares. (Marsh, 2012)

Earnings per ordinary share.

	2020	2019
	0.072	0.004

Currently, McLaren does not make a profit after tax. Dividends must be authorized by shareholders and as at the published AR 31 Dec. 2020. No dividends had been issued.

4.0 Limitations of ratio analysis include:

Historical Information: – Published accounts are not real time information, as they are the past. They therefore do not represent future company performance.

Inflationary effects: - Financial statements are released periodically and, therefore due to the time difference between release dates, if inflation occurs in between periods, then real prices are not reflected in the financial statements. The numbers across different time periods are not comparable until they are adjusted for inflation. (corporatefinancialinstitute.com, 2022)

Changes in Accounting Policy: Should the company change accounting policies and procedures; this could significantly affect financial reporting. Changes generally, can be found in the notes. (corporatefinancialinstitute.com, 2022) This may occur with executive changes such as those that have occurred at McLaren (Paul Walsh to Executive Chairman and the appointment of Kate Ferry as Chief Financial Officer in Jan 2022). (McLaren Group Ltd, 2020)

Operational Changes A company may change its operational structure.

(corporatefinancialinstitute.com, 2022) This could include anything from product changes to supply chain. Comparisons should be made from before and after. McLaren is leaning towards hybrid models and has made efforts to ease older stock in Retailer showrooms.

Seasonal effects: Some organizations are subject to seasonal factors that can create misleading information and impact the ratios. (corporatefinancialinstitute.com, 2022) McLaren isn't subject to seasonality, however it is subject to world events such as pandemics, plus other PESTLE factors.

Manipulation of financial statements: Ratio analysis is based upon information reported by the company. There is the potential for a company to manipulate information to report better results than its actual performance. (corporatefinancialinstitute.com, 2022) There is a possibility this may occur with McLaren, when they wish to appear in a more positive financial state, to gain investment. Analysis and interpretation of the 'The auditor's report, AR 31 Dec 2021', is recommended.

Any ratio analysis and reporting require due diligence before reaching conclusions.

5.0 Summary of Findings

McLaren Ratio summary and other influencing factors.

Financial strategy underpins a company's mission and goals. It ensures financial resources are available to achieve the objectives laid out in a corporate strategy. (Marsh, 2012)

According to McLaren's Annual Report they are in the process of delivering a three-phase plan to strengthen their balance sheet. They continue to deliver luxury cars at premium pricing levels to their target consumer. Changes in their executive board and actions to sell off shares in McLaren

Racing (joint venture-MSP Sport) (McLaren Group Ltd, 2020) suggest they are in a process of raising finance. The Group also entered a Sales & Leaseback transaction with Global Net Lease to sell the McLaren Technology Centre and McLaren Production Centre for proceeds of £170M entering a 20-year lease. Capital expenditure has been reduced and stock reduction plans have been achieved and actions have been taken to improve liquidity. EBITDA had also improved in the last quarter of 2020. (McLaren Group Ltd, 2020) Hybrid and lightweight carbon fibre models, are the focus of production, with the AR stating they will achieve an electric model by the end of 2030.

McLaren Models

McLaren Super Series Models

- 2022 McLaren 720S Spider (Starts at \$318,000)
- 2022 McLaren 720S (Starts at \$305,000)
- 2022 McLaren 765LT (Starts at \$368,000)
- 2022 McLaren 765LT (Starts at \$382,500)

McLaren Hybrid Models

- 2022 McLaren Artura (\$225,000)

McLaren GT

- 2022 McLaren GT (Starts at \$215,000)

McLaren Ultimate Series Models

- 2022 McLaren Elva (Starts at \$1,700,000)
-
- 2022 McLaren Speedtail (Starts at \$2,250,000)

McLaren Customer Race Cars

- 2022 McLaren 720S GT3
- 2022 McLaren 720S GT3X
- 2022 McLaren 570S GT4

(Supercars.net, 2022)

To date they have one hybrid model in the Artura and have no products within the electric car sector.

Competitors include Ferrari, Porsche, and Tesla. Tesla are advance in the production of electric vehicle technology and are an IPO.

Ferrari launched on the IPO in October 2015 and whilst their initial launch price dipped due to excessive hype, they started off financially in a better financial position than McLaren when reviewing the Annual Data.

Ferrari

Annual Data Millions of US \$ except per share data		2019-12-31	2018-12-31	2017-12-31	2016-12-31	2015-12-31	2014-12-31
Revenue		\$4,218.609	\$4,039.399	\$3,862.111	\$3,436.086	\$3,169.491	\$3,670.624
Cost Of Goods Sold		\$2,021.947	\$1,916.651	\$1,865.967	\$1,748.085	\$1,664.274	\$2,001.025
Gross Profit		\$2,196.662	\$2,122.749	\$1,996.144	\$1,688.001	\$1,505.217	\$1,669.599
Research And Development Expenses		\$783.116	\$759.428	\$742.742	\$679.049	\$623.581	\$718.659
SG&A Expenses		\$384.361	\$386.59	\$371.942	\$326.715	\$376.01	\$398.76
Other Operating Income Or Expenses		\$-1.645	\$-0.626	\$-5.007	\$-23.72	\$-12.253	\$-34.655
Operating Expenses		\$3,191.069	\$3,063.294	\$2,985.658	\$2,777.568	\$2,676.118	\$3,153.099
Operating Income		\$1,027.54	\$976.105	\$876.453	\$658.518	\$493.373	\$517.525
Total Non-Operating Income/Expense		\$-47.132	\$-27.828	\$-33.073	\$-30.685	\$-11.272	\$11.647
Pre-Tax Income		\$980.408	\$948.277	\$843.38	\$627.833	\$482.101	\$529.172
Income Taxes		\$197.855	\$19.27	\$235.961	\$185.505	\$160.025	\$177.02
Income After Taxes		\$782.553	\$929.007	\$607.419	\$442.328	\$322.076	\$352.152
Other Income		-	-	-	-	-	-
Income From Continuous Operations		\$782.553	\$929.007	\$607.419	\$442.328	\$322.076	\$352.152
Income From Discontinued Operations		-	-	-	-	-	-
Net Income		\$779.316	\$926.705	\$605.155	\$441.27	\$319.591	\$347.31
EBITDA		\$1,421.719	\$1,317.116	\$1,171.016	\$932.642	\$798.464	\$901.525
EBIT		\$1,027.54	\$976.105	\$876.453	\$658.518	\$493.373	\$517.525
Basic Shares Outstanding		187	189	189	189	189	189
Shares Outstanding		188	189	190	189	189	189
Basic EPS		\$4.17	\$4.91	\$3.20	\$2.33	\$1.69	\$1.83
EPS - Earnings Per Share		\$4.16	\$4.89	\$3.19	\$2.33	\$1.69	\$1.83

(macro trends.net, 2022)

Risk

Risk of entering a joint venture with McLaren is very real in terms of their liquidity. Foreign exchange offers a very real risk in terms of current Global volatility and are exposed to the US dollar and Euro. (McLaren Group Ltd, 2020)

IPO

However, McLaren are also rumoured to be looking to list on the IPO. (There is rarely smoke without fire). The adjustment in their board and methods they are using to improve their liquidity, through external investment (joint venture) and fresh equity injection, after the pandemic may support this theory, despite their being no mention of this in their AR 31 Dec 2020.

The rumours suggest that McLaren intends to go through a reverse takeover, by dealing with a (SPAC) Special purpose acquisitions company. This would allow them to go public without the same level of scrutiny and investment of time and money, that would be required for a conventional IPO (ig.com, 2021)

Competitors who have seen significant growth once listed include Tesla (Advanced in Electric car Technology) and Ferrari, although there is always a danger of loss due to the initial hype and PR that surrounds a listing. Ferrari were impacted by this. Plunging 41% in its first 4 months of trading. (Forbes.com, 2019) This has become a common factor with other company's suffering the same hype and drops after trading e.g., Facebook. (Forbes.com, 2019)

However, Ferrari are now trading strongly and investing in the production of electric vehicles. (Bloomberg.com, 2022)

Market Value

There are a lot of internal (e.g., financial strength, product quality, resources) and external factors (e.g., PESTLE, Supply chain, competition) that establish the value of a business. Brand value is subject to sensitivity of trends, USP's and conscious consumerism.

The economic value of a business is used by buyers and sellers to determine the price they are prepared to buy or sell a business for. Before a valuation can be undertaken it is necessary to understand the reasons for the valuation. (Marsh, 2012)

The book values

This is based on the value of an owner's equity as recorded in the accounts. This may be a starting point but, unfortunately, accounting records may not reflect the true value of assets and liabilities. (Marsh, 2012)

The tangible book values

This method simply values tangible assets and places no value on goodwill or other intangibles. Book values are adjusted by removing intangibles. (Marsh, 2012)

The economic book values

This method takes account of all assets including goodwill and values them at the market rate. (Marsh, 2012)

Based on revenue excluding FX (published financial statements, October 2021) IG.com suggest McLaren could be looking at a valuation of around £560 million. (Ig.com, 2022) Should they list on the IPO.

7.0 Conclusion and Recommendation

When considering a joint venture opportunity with McLaren, it is recommended the organisation consider their own business objectives, strategic position, financial position, business process and cultural alignment, as a joint venture with McLaren is not without risk.

Considering the financial risk stated in their AR 31, Dec 2021. (McLaren Group Ltd, 2020) it would be recommended for this organisation to complete a more in-depth analysis of the P & L. with cooperation from McLaren financial executive. If they are serious about the partnership.

As McLaren have yet to engage with electric vehicles there is a definitive opportunity to engage with a strong brand and improve Brand value for both businesses.

Should McLaren list on the IPO there is potential for PR and hype to cause a high then low in share price based on trends that have occurred with other companies.

Recommendations would include proceed to investigate further and act within the best interests of this organisations business objectives and finances. Consideration to other potential partners may be worthy of comparison regarding ROI.

Appendices Ratios



McClaren
Ratios.xlsx

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