CASE STUDY: UNILEVER[1]

1. Introduction

Unilever is a British-Dutch company that operates in the market of consumer goods and sells its products in around 190 countries. Another remarkable fact is that they own more than 400 brands, what means an important diversification in both risk and the products they sell, among which there is food, personal care products and cleaning agents. In fact, twelve of these brands have sales of more than a billion euros.

The importance of this multinational is reflected too in the fact 2.5 billion people use Unilever products every day, being part of their daily life. They also are responsible for the employment of 161,000 people in the different countries they operate.

Finally, they believe in a sustainable business plan in which they reduce the environmental footprint and increase their positive social impact at the time they keep growing.

2. History

Unilever was officially formed in 1929 by the merger of a margarine Dutch company and a British soapmaker. The margarine company of Netherlands was also a merger between the first margarine factory called in the world and another factory of the same product and from the same city, Oss, in the Netherlands. The soapmaker company revolutionized the market because it helped to a more hygienic society and the manufacturing of the product was wrapped. The name of the company is a fusion between the Dutch firm called Margarine Unie and the British firm called Lever Brothers.

What Unilever did, was to expand its market locations to the American Latin and Africa. Moreover they widened the product areas to new sectors such as particular food and chemical products. During the 1980s, changes its strategy to redirect the business basically concentrating it to the core business. It implied the same investments to the different product

[1] Case written by Arnau López, Daniel Maruny, Marc Casas, Oriol Camprubí. Universitat Pompeu Fabra, 2018.

areas of the business. During the 1990s, the company maintained the same policy direction in order to have a more stable and consolidated market power. That is why the firm reduced about 37 areas that they were competing to concentrate all the resources in 13 areas. The four more important were Food, Personal Care, Home Care and Speciality Chemicals.
Initially at the 2000s, Unilever started adopting a social policy to promote sustainability in day-to-day activities and in the whole business.

Unilever have been involved in multiple acquisitions during its history. In 1943, it became the major shareholder of Frosted Food, which also is the owner of Birds Eye and the rights in the UK of freezing as a way to conserve the products, which was going to have a huge impact as a way to preserve foods in its natural form.
It also acquires Good Humor in the US, an ice-cream factory; Zwanenber that later on will be the basic unit of the meat sector of the firm.
In 1971 it acquires Lipton International, a tea company increasing its market share and becoming one of the biggest companies of the sector of tea. In 1973 it acquires Frigo, the main ice-cream company from Spain. in 1978, in order to have a bigger share in the US it acquires National Scratch, an organic chemical company. In 1984 the company did the first hostile takeover, the company was Brooke Bond from the tea sector, the biggest seller from the United Kingdom with the help of a TV advertisement of two chimps. In 1986 it acquires Naarden meaning a double of the market share of fragrances and food flavour. In the same year, the company acquires Chesebrough-Pond's that was the owner of the Vaseline company and Pond's. In 1989, it acquired Calvin Klein and Elizabeth Arden/Fabergé both of cosmetics but later sold. In 1993 it acquired the ice-cream company from United States Breyers. In 1996, it was acquired Helene Curtis in the hair sector. In 1997 ice-creams Kibon from Brazil is acquired. In 2000, it was acquired Bestfoods, considered the second acquisition with more capital in history. There were also obtained Slim-Fast Foods, Ben & Jerry's and the culinary French firm Amora-Amille. It also acquired during 2007, local food leader in Russia and drink brand from Indonesia called Buavita.

Even though the acquisition that the company had been done since its merger, during the 2000 century it began a process to reduced the number of brands that the company owned, in 2001 it was reduced from 1,600 to 900 brands. In 2002 87 more brands were sold.
In 2010, it increases the portfolio of brands of the firm by the acquisition of Alberto Culver that owns TRESemmé among others.

These would be the most important acquisitions of the company since its creation in 1929.

Mid 1800s	In the Netherlands, the Jurgen and Van den Bergh families start the butter-making business, later margarine.
Late 1800s	In England, Lever & Co starts producing soap
1890	Lever is converted into a limited company, following a big expansion.
1927	The above-mentioned dutch families and other companies for the Margarine Union.
1929	Unilever if formed due to the merge of Margarine Union and Lever Brothers.
1940s	Unilever starts working in the frozen food industry
1950s	Development of new mass markets for consumer goods (includes Africa and Asia).
1954-55	Launch of world-wide known personal care products such as Sunsilk shampoo or Dove.
1971	Acquisition of Lipton, the biggest tea business in the world.
1973	Acquisition of Frigo
1983	AXE is launched
1985	Launch of the first home use pregnancy test
1986	Expansion of the fragrances and food flavour industry.
1986	Acquisition of Pond, with its world-wide known brand Vaseline.
1990s	Expansion to eastern Europe
2000	Bestfoods joins Unilever, the second largest cash acquisition in history. Brands such as Knorr are included.
2001	Brand reform, from 1600 to 900 brands

***Figure** 1: Main events in the history of the company. Source: unilever.com*

3. Industry analysis and competitors

3.1. Sales in every industry related to Unilever

As we will explain later, Unilever has 4 divisions which are Beauty & Personal Care, Foods & Refreshment, Home Care and Water Purifier. These sectors are in constant growth because of the constant population and demand. The only exception is the Water Purifier Industry which is growing very fast because of the popularity of the home water purifiers.

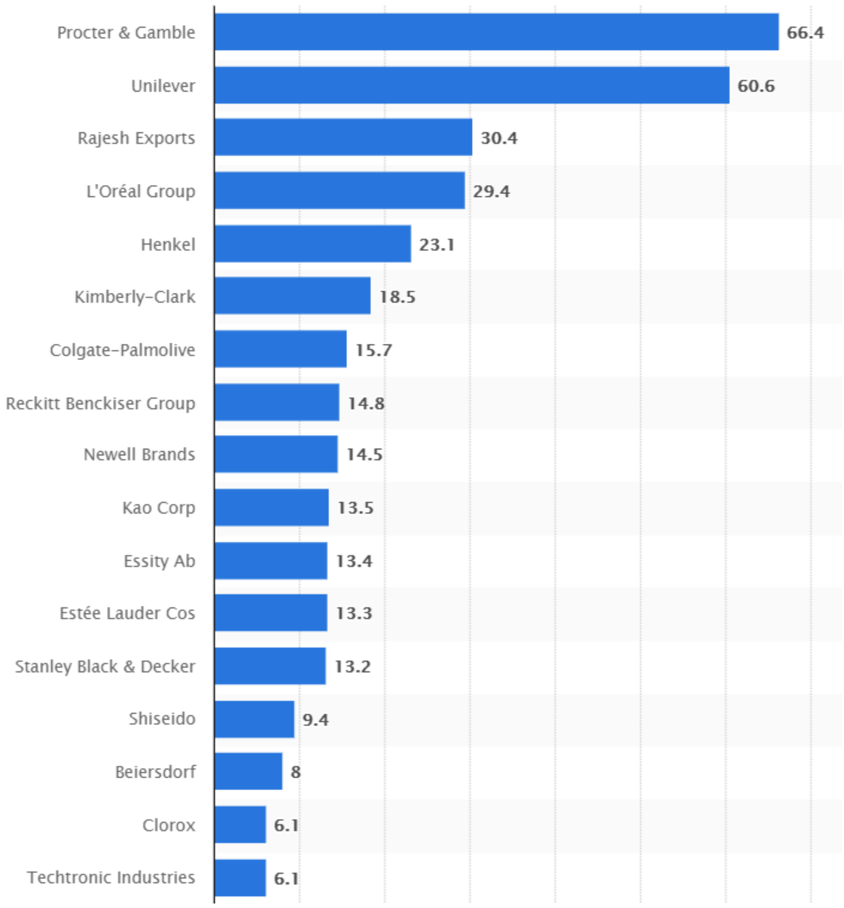

Figure 2: *Sales of the leading household/personal care companies worldwide in 2017 (in billion U.S. dollars). Source: statista.com*

As we can observe in the Figure 2, the multinationals Unilever and Procter & Gamble are leading the Home Care and Personal care markets. It is important to mention that L'Oréal Group does not participate in the Home Care industry so we must highlight that the french company has a huge market share in the Beauty Industry.

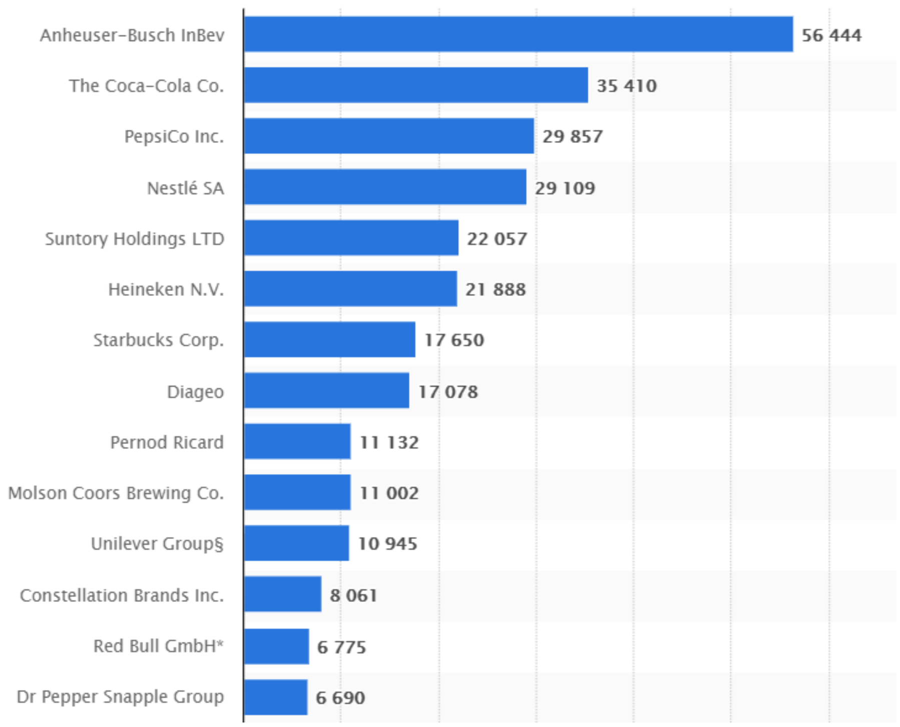

***Figure 3**: Leading beverage companies worldwide in 2017, based on sales (in million U.S. dollars). Source: Statista.com*

The Beverage market is leaded by far by the world's largest beer producer Anheuser-Busch InBev. They are followed by the huge rivals The Coca-Cola Company and PepsiCo Inc. In this market, Unilever has the potential to expand further on it because as we can see, Unilever is ranked as the eleventh beverage producer in terms of sales.

Rank	Company	Food Sales ($ millions)	Year Ending
1	Nestlé	72,245	Dec. 14
2	PepsiCo, Inc.	66,683	Dec. 14
3	JBS	52,580	Dec. 14
4	Anheuser-Busch InBev	47,063	Dec. 14
5	The Coca-Cola Company	45,998	Dec. 14
6	Archer Daniels Midland Company	43,232	Jun. 14
7	Tyson	37,580	Sep. 14
8	Mondelez International	34,244	Dec. 14
9	Cargill	33,700	May 14
10	Mars	33,000	Dec. 14
11	Unilever	29,070	Dec. 14
12	Danone	28,545	Dec. 14
13	Kraft Heinz	28,000	Dec. 14

Figure 4: *The World's Top 100 Food and Beverage Companies of 2015. Source: www.foodengineeringmag.com*

In the Food industry, the swiss multinational Nestlé is leading with a huge market share. Unilever is placed eleventh and as we said in the Beverage market has still potential to expand even though this Industry is very tough and competitive.

The Global Water Purifier industry is currently valued at 10800 million US$ and is expected to reach 15000 million US$ in 2025. This market is still very new so companies are positioning themselves in the global market. Stand Out companies like Aquasana, Brita, PUR, Unilever Pureit and Philips.

3.2 Main Competitors

The main competitors of Unilever are other Fast-Moving Consumer Goods (FMCG) companies with a similar structure and size. For example, the American consumer goods multinational *Procter & Gamble*, the largest food company in the world *Nestlé*, the British *Reckitt Benckiser Group* which produces hygiene, health and home products, the global manufacturer *Mars*, the New York company *Colgate-Palmolive*, *Johnson & Johnson* the consumer goods and pharmaceutical American multinational, the *Kraft Heinz Company* which is a recent merger and the german chemical and consumer goods *Henkel*. All of them work internationally but try to understand consumers' demands in every country they operate.

3.3 Global FMCG companies total sales ranking

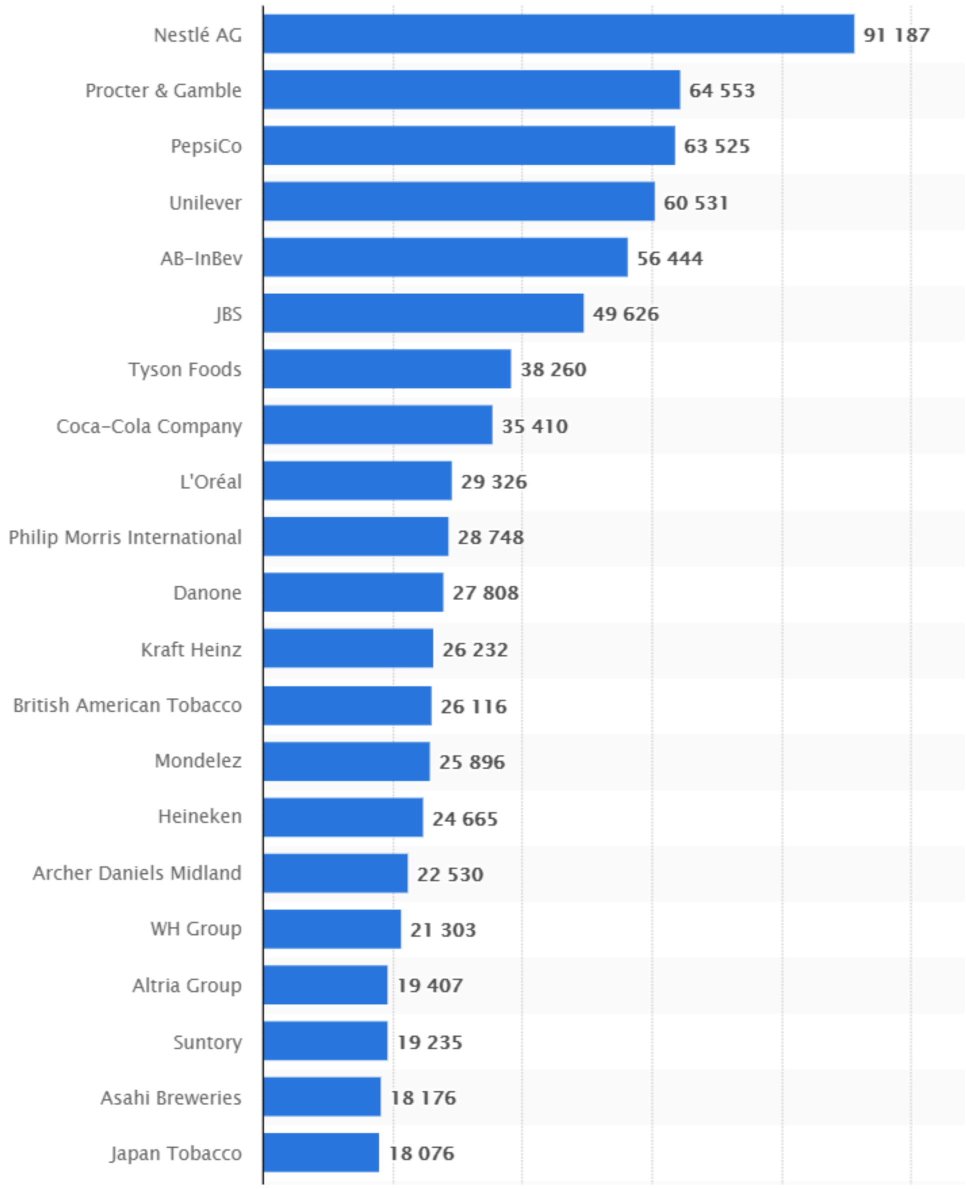

Figure 5: *Top 50 FMCG companies worldwide in 2017, based on net sales (in million U.S. dollars).*

Source:statista.com

Nowadays, Unilever is the fourth FMCG company based on their net sales of 2017 by making 60531 millions of U.S. dollars. The only companies that surpass Unilever in the FMCG market are Nestlé, Procter & Gamble and PepsiCo respectively. We must consider that this ranking made by www.statista.com only contains the data of the companies that have published it. Companies like Oetker or Mars are not included.

3.4 SWOT Analysis of the FMCG industry

Strengths

Economies of scale: Every FMCG company can take profit of economies of scale.

No Seasonality: The FMCG Industry has constant sales because they produce products every day products.

Strong Brands: Presence of well known brands in this sector.

Weaknesses

Differentiation in the FMCG market is difficult because producers can only compete in availability, range of products and prices. Their products can be easily substituted, specially in emerging markets like Asia or Africa where they use traditional alternatives.

Dependance of retailers: FMCG companies don't usually sell their own products, so they depend on retailers.

Counterfeit consumer goods: Goods of inferior quality sold without the brand's owner authorization under another's name.

High advertising costs: Increase in Advertising spending may affect margins.

Opportunities

Improving economic conditions: getting out of the recession leads to higher consume.

Digital strategy: Going digital will lead to more sales for FMCG companies because people is increasingly buying online.

Innovation: Products can be improved or invented in the healthcare market.

International laws: The European Parliament and the European Commission are trying to protect big food companies from some retail practices. The manager of Unilever Germany has publically supported it.

Population Growth: Nowadays, population is constantly growing so the demand for FMCG grows.

Threats

Highly competitive: Unilever competes with other huge companies like P&G and Nestlé and local companies that try to dominate every market.

Retailer's products: Increasing popularity in retailer's own brands.

Political situation: Non stable political situation in some emerging countries.

4. Present situation of the company

4.1. Products and services offered

The products they sell can be classified in four divisions:

- Beauty & Personal Care: *Axe, Clear, Dove, Rexona...*
- Foods & Refreshment: *Breyers, Cornetto, Heartbrand (Frigo), Hellmann's, Knorr, Magnum, Ben&Jerry's, Cornetto...*
- Home Care: *Cif, Domestos, Comfort, Skip…*
- Water Purifier: *Unilever Pureit* and *Truliva*

GROUP	2017	2016	2015
Turnover growth	1.9%	-1%	10%
Underlying sales growth	3.1%	3.7%	4.1%
Operating margin	16.5%	14.8%	14.1%
Free Cash Flow	5.4 billion €	4.8 billion €	4.8 billion €

***Figure 6**: Group financial performance. Source: Unilever.com*

BY CATEGORIES	2017	2016	2015
PERSONAL CARE			
Turnover	20.7 billion €	20.2 billion €	20.1 billion €
Turnover growth	2.6%	0.5%	13.2%
Underlying sales growth	2.9%	4.2%	4.1%
Operating margin	19.8%	18.4%	18.1%
HOME CARE			
Turnover	10.6 billion €	10 billion €	10.2 billion €
Turnover growth	5.6%	-1.5%	10.9%

Underlying sales growth	4.4%	4.9%	5.9%
Operating margin	10.8%	9.5%	7.3%
FOODS			
Turnover	12.5 billion €	12.5 billion €	12.9 billion €
Turnover growth	-0.1%	-3.1%	4.5%
Underlying sales growth	1%	2.1%	1.5%
Operating margin	18.2%	17.4%	17.8%
REFRESHMENT			
Turnover	9.9 billion €	10 billion €	10.1 billion €
Turnover growth	-0.8%	-1.1%	10.3%
Underlying sales growth	4.9%	3.5%	5.4%
Operating margin	13.5%	9.7%	8.3%

***Figure 7**: Financial performance divided by categories. Source: Unilever.com*

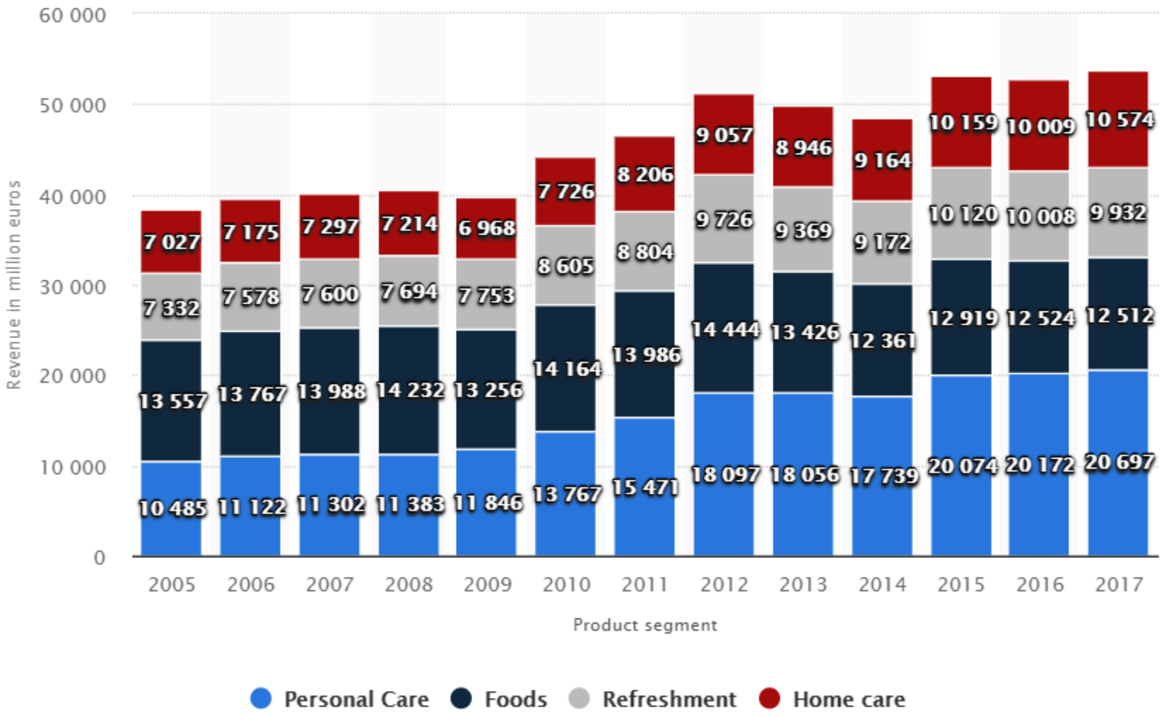

Figure 8*: Global revenue of the Unilever Group from 2005 to 2017, by product segment (in million euros). Source:statista.com,*

As we can observe in the previous graph, Unilever has increased their revenue over the past 12 years in a 40%. The sectors that made possible this huge increase were the personal care industry that doubled their revenue, the refreshment sector that expanded a 35% and the home care industry that boosted a 50%. In the other hand, the food sector decreased an 8%, which is not a big deal compared to the gains in the other industries.

It is relevant to underline that operating margin has improved in all sectors during the last years.

4.2. Customers and Distribution Channels

"We are committed to building trust through responsible practices and through transparent communication". As Unilever explains in their website, they goal is to promote customers' loyalty so their image and their advertising is very important for them.

Unilever's Beauty & Personal Care, Home Care and Food brands sell their products in supermarkets and grocery stores. In the other hand, Truliva and Pure it sell their water purifiers online.

4.3. Key success factors

Firstly, Unilever has more than 6000 scientists, engineers, chefs and technicians working in Unilever's R&D trying to improve their products and inventing new ones.

Another key factor is their diversification, they have a large range of product which allows them to reduce risks. Also, their investment in marketing and advertising is a key factor, Unilever won the award of the Most Awarded Advertiser at the 60th Cannes International Festival of Creativity. In addition, Unilever's CEO, Paul Polman, is very concerned about the climate change and other social issues which give Unilever a fantastic image. Furthermore, he has received several awards and accolades for his responsible business and he is Chair of the International Chamber of Commerce (ICC), which guarantee an excellent management of the company.

5. Main problem or challenges the company is facing now

As we said in the SWOT, one of the biggest challenges Unilever is facing are the cheaper supermarket "own label" offering. As the company says "Successful customer relationships are vital to our business and continued growth.[...] our retail customers frequently compete with us through private label offerings". Although, Unilever tries to maintain good relationships with their customers, they've been accused several times of abusing of their dominant position in the market. For instance, Unilever has a conflict with Kaufland, one of their biggest retailers in Germany. Almost 500 of their products are not sold in their stores because they accuse Unilever of abusing of their dominant position to increase prices enhancing their margin. Another example is when in 2016, Unilever tried to increasing their prices by a 10% in UK because of the pound decrease after the Brexit decision but Tesco refused it.

Another challenge the company faced recently was the Kraft Heinz takeover bid over Unilever of 143 billions of US$, which was not successful.

Recently, Paul Polman announced that he will retire from the company and Alan Hope, President of the Beauty & Personal Care division, will become the new CEO of Unilever in January of 2019. His retirement was a consequence of his propose of moving the Unilever's headquarters from London to Rotterdam, in order to defend against takeover bids, like the Kraft Heinz one, because Netherlands' law against takeovers is stricter but this measure was not accepted by one of the big groups that own Unilever.

6. Questions

1. Prepare a qualitative analysis of Unilever, identifying its strengths and weaknesses.
2. Analyse the Balance sheet and Income Statement of Unilever and identify its strengths and weaknesses.
3. Analyse other relevant topics: working capital, growth, dividends and value creation.
4. Construct a cause and effect diagram.
5. Make recommendations to improve Unilever’s performance.
6. Demonstrate the recommendations.

1. Prepare a qualitative analysis of Unilever, identifying its strengths and weaknesses.

	+ Strengths	- Weaknesses
WHO	-Full attendance by the committee members at board meetings during 2017. -Transparency in the appointment of the executives and important personnel. -Unilever Future Leaders Programme: consist on preparing qualified students for some specific tasks the firm needs (related to training level). -Diversified Board of Directors in regards of nationality, gender and experience. The company follows the same structure in all the sections to promote a proper atmosphere. -Marijn Dekkers, the Chairman, has experience in jobs of responsibility acquired in other companies like Bayer or Thermo Fisher Scientific Inc. -Through a programme called C4G they pretend to develop an owner's mindset, that means to give workers more power, improve the collaboration between them and a system of incentives.	-There is not young people in the decision-taking positions. If we talk about non-executive directors, the younger is Youngme Moon and she is 53 years old. In regards of the executive part, three of them share the minimum age, 48 years.
WHAT	- Variety of products and brands. -Big geographic diversification, they sell their products in more than 190 countries.	-The growing tendency of the white-label products during the crisis time may reduce the sells of some products they offer.

	-The most part of their brands are well-known and have good reputation. -As they are a big multinational, they have power to negotiate with trade debtors, trade creditors, banks and employees. -The industry of consumer goods is not one of the most affected by the economic recession. -Thanks to its diversification, losses in one of its brands, can be compensated with gains in another brand.	-Although their high investment in innovation, its goods can be imitated easily. - Fines due to the abuse of a dominant position in the italian single wrapped ice-creams. The fine was about €60 but it also has other costs like reputational costs. - Investors opposition for the announcement of the possible unification of the dual listed in the Stock Exchange of London and the Euronext of Amsterdam. The headquarters are going to be in Rotterdam.
HOW	- One of the biggest aspects that it tries to potentiate is the sustainable living. The key areas that they are promoting are: the improvement of Health and Wellbeing, the reducement of the Environment Impact and Enhancing Livelihoods, called the Unilever Sustainable Living Plan (USLP). -Corporate Social Responsibility: invest in poor communities in developing countries. - Innovation: they invest about €1 billion in R&D each year. - Portfolio bigger than 20,000 patents and applications of them. - Dual-listed company to diversify risk: the 2 companies are Unilever plc.listed	-They had received lots of critics because of a Dove ad, one of the brands owned by the firm, in which a black woman changed her skin for a clearer one, and was accused to be racist. -Lack of control of the selling process, they depend on shops and supermarket chains.

	in the London Stock Exchange in the FTSE 100 index and Unilever N.V. listed in Euronext Amsterdam in the AEX index. -Adaptation of the products in the different markets ("multi-local multinational"). -Takes advantage of economies of scale.	

2. Analyse the Balance sheet and Income Statement of Unilever and identify its strengths and weaknesses.

	Strengths	**Weaknesses**
Liquidity	- The Z score is in a good position, with a value of 1.44, much better than the previous two years and this means that the company has a very low probability of default. - The company is operating with negative working capital, however it is a positive in the industry because the cash collection and inventories days are much faster than the payments to suppliers, so it can be financed and use this natural financing to growth. - The level of cash and cash equivalents is a little bit higher than the average industry which is positive but it has decreased from the previous year.	- The ratio current assets/current liabilities is below the one of competitors even they have improved it slightly in the last years. - The competitors have a higher percentage of cash compared to current liabilities, and this can be seen in the ratios of treasury and the acid test (cash/ current liabilities). - They can only return ⅓ of the current liabilities with the money they have in cash and accounts receivable, while this ratio in the competitors is around ½. - The company is running a working capital deficit, however it

		may not be a big problems because also the industry is operating with working capital deficit. Nevertheless, it is positive if it can be improved.
Debts	- Low financial expenses, similar to competitors (around 1% of sales).	- The repayment capacity is lower than the competitors, they need around 3 years to pay all debts with the operating cash flow they generate while the other two companies need around 2 years. - It can be bad because it is increasing over time but is not so worrying. The ratio liability/assets has increased and it is higher than the competitors, so the company is less strong to external shocks compared to the competitors. - The debt quality that is current liabilities over total liabilities is stable over the time but is higher than the competitors, in which this percentage is around 30% while in the company is higher than 50%, meaning that more than half of the debts have to be paid before one year.
Asset management	- In this aspect the company works very well as the sales volume over both current or non-current assets is much higher than the competitors, so they take	

	advantage of the assets they have.	
Terms	- The company has managed to reduce inventories days (stocks/daily cost of sales) in the last years. - Clients pay in 23 days, it has increased a little in comparison with the other years but is still less than the competitors; and they pay the suppliers in 98 days what is good because they have this money 75 days.	- The company could pay the suppliers some days later because the competitors take more time to do that.
Sales	- Unilever sales have slightly increased the last year while P&G has decreased sales and Nestlé has maintained the same ones of the previous year. So this means that nowadays in this industry is difficult to increase sales a lot. The industry has been stable during the last 5 years.	- The fact that the industry has been stabilize during the last years can be a negative aspect because it means that it is difficult to improve the capacity of growth since sales does not allow it.
Expenses	- The cost of debt is similar to the competitors. - Financial expenses are around 1% of the sales, like the other ones.	- The competitors can operate with lower costs of goods sold, however it is not a big problem because the competitors incur higher other operating costs leaving with a similar EBIT.
Profit	- Last year's profit was the highest from the last 5 years, so it means that the company is improving its	- Competitors have higher profits in average than the company.

	efficiency. - The percentage of net operating profit over sales is higher than the previous 2 years, and is more or less the same as the competitor ones. - Net Profit/EBT, the ratio that shows which part of the EBT is remaining after taxes is increasing over time, what is a great notice.	
Return	- The return on assets and the return on equity is much bigger than the competitor companies. This difference can be seen in this second ratio (net income/equity) that almost double the ratio of the best competitor in this aspect. - The financial leverage is positive because the return on assets is greater than the average interest rates, in this case the ROI is 15% and the average interest rate is 2.7%.	
Self-financing	- The result plus amortization and depreciation minus dividends (self-financing) has increased in the last three years, specially in the last one. - The ratio self-financing/ increase in assets is high so the company' growths in a conservative way, in fact, self-financing is bigger than	- The pay-out, that is dividend/equity, is around 0.60 and it has to be reduced to have high self-financing level. Despite this, is not far from competitors and as we have seen, they are in a healthy self-financing position, so is not as bad as it could seem.

	the increase in assets the last year (1.61). - Dividend profitability is high compared to the competitors (0.27) and has increased the last years, has to be high to satisfy shareholders' interests.	
Growth	- Company is growing at a balanced way. Although the situation is not ideal, as debt has increased, profits have increased more and the Higgins formula shows us that the growth is balanced.	

3. Analyse other relevant topics: working capital, growth, dividends and value creation.

First of all, to compute the ratio we have chosen to compare Unilever with two of its main competitors: Procter & Gamble (based in the USA) and Nestle (based in Switzerland). As this company is very specialised, it is difficult to find an industry which fits it well, so it is better to compare with other companies with similar structures and operations.

To compute ratio we have used Unilever Group Consolidated accounts, which includes information from the main mother companies Unilever Nv and Unilever Plc and also information from the hundreds of subsidiaries, partnerships, associates and joint-ventures. The general accounts provide a broader view of the whole company. Our sources for the accounts are unilever.com (for the consolidated accounts) and database Amadeus (for the Unilever PLC accounts, which is the biggest mother company).

Balanced growth

For a company it is important to grow, but it is more important that the growth is balanced and sustainable, to avoid dying from success.

To compute it, we use the following data:

- ➔ Increase sales=1.02
- ➔ Increase assets=1.05
- ➔ Increase debt=1.13
- ➔ Increase profit=1.17

This can be illustrated as: SADP

In this case, growth is not well-balanced but the company has increased profits. For a growth to be balanced, increases in Assets and Debt should be lower than the increase in sales. So, the situation is not ideal because debt has increased too much but given that the increase in profits is even higher, we can't say that this is a weakness.

The fact profits have increased more than sales can be explained because of a reduction in costs, as the ratio net income/sales has increased 2% the last year. For example the percentage of cost of goods sold has decreased, and the same has happened with the one of taxes.

The increase in debt is bigger than the increase in assets because the company has decided to reduce the level of equity, and what is the same, to finance their assets even with more debt (75% of them are financed with debt).

We use the Higgin model to calculate the capacity to grow (Higgins, R., 1977), the formula estimates the annual percentage of growth in sales a company may have assuming there is no increase in equity or grants to finance growth. These are the ratios in 2016:

- ➔ M= Net profit/Sales = 0.11
- ➔ D= Dividends/Net Profit = 0.65
- ➔ L= Debt/Equity = 2.33
- ➔ A= Assets/Sales = 1.06

$$\frac{\square(1-\square)\square(1+\square)}{\square-\square(1-\square)\square(1+\square)}=\frac{0.11(1-0.65)\square(1+2.33)}{1.06-0.11(1-0.65)\square(1+2.33)}=0.138$$

The annual sustainable growth rate would be 13.8%. If we compare it with the growth in 2017, which is around 1%, we see that there is still room for improvements and that the company is growing at a sustainable level.

Forecasting insolvency

There are some techniques to do predictions about the future solvency of a company, one of them is the Z-score formula, a multidimensional indicator useful to separate companies in a good financial position from others that can have risk to bankruptcy. For the analysis of our company, we will use a formula proposed in a UPF study:

Z= -3.9 +1.28(current assets/current liabilities) +6.1(Equity/Assets) +6.5(Net profit/ assets) +4.8(Net profit/Equity)

Replacing the ratios for the ones of Unilever:

Z= -3.9 +1.28(0.73) +6.1(0.25) +6.5(0.11) +4.8(0.45) = 1.434

If the value of the formula is greater than zero, as this case, it means is highly probable that Unilever enjoys good economic and financial health. However, we can see the ratios that have more weight are the ones the company has to improve, specially the net profit/assets for example by reducing costs and increasing the net profit. Equity/Assets also could be improved but if the cost of debt is lower than the profits it generates can be good to have debt, and in addition, the competitors ratios are similar to the one of Unilever, so even it is risky, can be a good strategy to have debt above what is considered normal. If we compare it with previous years it can be seen that the ratio had a decreasing trend between 2013 and 2016, and in this last year it has recovered a lot becoming similar to the first year analyzed.

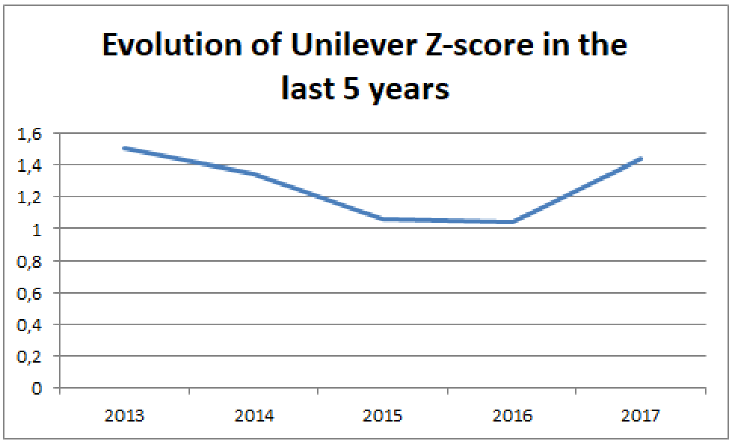

Figure 9: *Evolution of Unilever Z-score. Source: Own calculations.*

Value creation

Profitability

To analyze well the profitability ratio (Profitability= Net result/Equity) is useful to break it down into the product of the following three ratios:

Profitability = Margin · Turnover · Leverage

If we compute profitability in this way we can check which of the ratios we need to improve. In the case of Unilever, the profitability ratio is:

- Margin = net result/total sales = 0.12
- Turnover = total sales/total assets = 0.92
- Leverage = total assets/equity = 4.04

Profitability (ROE) = 0.12 · 0.92 · 4.04 = 0.45

As both turnover and leverage ratios are so high, the best way to increase profitability would be to increase the margin by reducing costs maintaining the same volume of sales. It would be risky to increase more the leverage ratio even the debt is profitable, and in regards of the turnover one is in a very good position and maybe is difficult to improve more the efficiency of the assets.

EVA (Economic Value Added) may be defined as what is left once we have deducted the total amount of expenses from total income. The main difference with the net profit is that it takes into account the opportunity cost for shareholders besides the cost of debt.

To calculate EVA we need the following data (in thousand euros):

- Net operating profit after taxes: 7,201,332
- Assets: 58,199,874
- Weighted average cost of capital: 0.02

EVA = 7,201,332-(58,199,874 · 0.02)=6,037,334

A positive EVA, as in this case, means the company has created wealth worth 2% plus 6,037,334 th €. This 2% is the cost of debt plus the opportunity cost of the shareholders to invest in another place.

<u>Analysis of working capital</u>

	2017	2016	2015	2014	2013
Working Capital (real) (million euros)= Current assets – Current liabilities	-6,204	-6,662	-7,346	-7,278	-5,225
Operating Working Capital (million euros)	-1,924.3	-2,435.4	-2647.1	-1,444.8	-1,228.8

= Operating current assets – Operating current liabilities					
Operating CA = Inventory + Clients + Other operating CA + Minimum cash required	11,501.7	11,435.6	11,140.9	11,161.2	10,506.2
Operating CL = Suppliers + Other operating CL + Accruals	13,426	13,871	13,788	12,606	11,735
Working Capital Deficit (million euros)	-4,279.7	-4,226.6	-4,698.9	-5,833.2	-3,996.2

Figure 10*: Evolution of working capita. Source: Own calculations.*

To analyze the company's liquidity situation we use the working capital, to assess whether the company is performing good or not.

During all the years the company is running a deficit when regarding the working capital, since the difference between the real working capital and the working capital needed is negative, this means that the company will have to find another sources of financing because the operating activities are run inefficiently. To solve this situation the company could try to delay the payments of current liabilities or to try to be paid earlier, in order words an improvement of the collection and payment terms.

Even though the company has increased the number of operating current assets, the number of operating liabilities has increased proportionally so that the working capital needed has moved approximately from 2,000 million to 2,500 million, however we can appreciate a decreasing trend of the working capital needed but also of the real working capital so that the deficit has decreased.

When comparing with the competitors we can appreciate that even the top performs have problems to achieve a better management of the working capital since Procter & Gamble and Nestlé are both running working capital deficits.

This means that the industry can improve its performance of the efficiency of working capital but we can also conclude that this type of industry can operate with deficit working capital.

Furthermore it is clear that the industry is operating with negative working capital because the collection of cash is much and the inventories days are much lower than the payment terms, so that this means that the company and also the industry uses the fast cash cycle to be directly financed thanks to the fact of paying to suppliers much more later.

Dividends

To analyze if it is a good option for investors to put their money in this company, we have take a look on some important ratios:

- Price earnings ratio:
  Market value of the share/earnings per share = 42.59/2.16 = 19.72
  It is a good ratio for investors satisfied with a lower profitability with low risk, it is around 5% of profitability. It is important to remark that earnings per share have increased in comparison with the last years, so it is expected them to grow even more.

- Dividends/Net profit = 3,916,000/6,496,070 =0.60
  The company returns a 60% of the net profit to shareholders with dividends, this is a high amount, but allows the company to invest an important part of the benefits again.
- Dividends/Equity = 3,916,000/14,409,423 =0.27
  This ratio is so high, even more if we compare it with the competitors, that are doubled for Unilever in this case. The company has the capacity to return almost ⅓ of the equity in dividends.

To maintain shareholders happy is important the last ratio (Dividends/Equity) to be high, this means the company is generating profit from the equity and is returning part of it to the shareholders, in this case 0.27 is a very good notice. For the company it is also important the second ratio (Dividends/Net Profit) to be low, this can be achieved by increasing net profit, and allows the firm to grow with its own resources, what is important to not to increase the debt, that is high enough.

4. Construct a cause and effect diagram.

The Cause and effect diagram helps us in order to present the main problems the company is facing and what effects they produce, making easier to found measures to solve these problems.

Figure 11: *Cause and effect diagram. Source: Own*

5. Recommendations

When analyzing the company we have found the main problems the company has faced in 2017 are an excess of short-term liabilities, which is a problem of liquidity; and low repayment capacity. As we have seen before, high debt is not a huge problem for the company because of the profitability of this debt, but it is possible to improve it a bit.

Increase in capital

It is easy to see that the company has a high debt, about the 75% of assets are financed by debt, and even if this debt is profitable it would be advisable to increase assets with an increase of equity, in this way the ratio liabilities/assets will decrease and the company will keep taking profit of its high return on assets. Reduce the ratio of indebtedness to 0.7 would be advisable.

- Indebtedness= Liabilities/Assets =0.7
- 43,791,577/(58,199,874+x) = 0.7

- Where x is the amount that have to increase equity and assets.
- x=4,359,521.7

This increase in equity would be used to acquire assets directed to investments in growing the core and evolving markets specially related to personal and home care, the company started in 2017 these operations, which should be continued but equity-financed.

The total amount of assets now is 62,559,395.7.

If we assume the company will keep achieving the same return on assets, this increase in assets will cause an increase on the EBIT.

- ROA= EBIT/Assets = 0.15
- (8,870,977+x)/62,559,395.7=0.15
- Where x is the increase in EBIT
- X=512,932.355

This means that sales are expected to grow and that as operating expenses are high they can be reduced, which is positive for the firm, since EBIT increases.

We consider that as the firm has a competitive advantage on the asset turnover, the increase in assets maintains the same level of return. As the EBIT has increased, Sales and COGS have had to increase proportionally too, so the new amounts are 56,901,614.3 for sales and 32,358,764.1 for COGS.

Debt restructuration

If we analyze the debt quality, Unilever has reduced the ratio current liabilities/total liabilities by a 5% in the last 5 years, but is still a problem because has been 0.53 in 2017. If we look to the competitors, we find that 0.4 could be an appropriate value for this ratio.

As we have said that the amount of debt is not problem, the company should transform debt from short to long-term.

- Current liabilities/Total liabilities =0.4
- 23,212,803-x/43,791,577=0.4
- Where x is the amount to be transformed to long-term liabilities
- x=5,696,172.2

From this equation we get that the company should transform 5,696,172.2 thousand € of short-term liabilities to long-term ones, so the amount short-term liabilities happens to be 17,515,630.8 thousand €. The liabilities that are transformed to long-term are loans.

Improve working capital management

As the company has a deficit in the working capital which can be reduced with the acquisition of assets and the reduction of current liabilities.

Suppose that the previous increase in assets is divided in the same way that are distributed, 30% approximately to current assets and 70% to noncurrent assets.

So that, the new amount of current assets is: 1,307,856.51 + 17,008,527= 18,316,383.51.

The new amount of current liabilities is: 17,516,657.8. The liabilities that are transformed to long-term are loans.

So the new working capital is: 18,316,383.51 - 17,516,657.8= 799,725.71

To maintain the same proportions as the balance sheet:

Current assets	18,316,383.51
Stocks	4,273,053.6
Debtors	3,708,894.6
Other current assets	6,757,783.3
Cash	3,577,863.5

Current liabilities	17,516,657.8
Loans	2,021,149.8
Creditors	8,229,932
Other current liabilities	7,266,675

Figure 12*: Improve working capital managemen. Source: Own calculations.*

The working capital needed is:

- Operating current assets= 4,273,053.6 + 3,708,894.6 + 6,757,783.3 + 0.1 x 17,516,657.8= 16,491,397.2
- Operating current liabilities= 8,229,932 + 7,266,675 = 15,596,607
- The working capital needed is= 16,491,397.2 - 15,596,607 = 994,790.2

- Working capital real - working capital needed= 799,725.71 - 994,790.2= -195,064.49

As we can appreciate the reductions in loans improve the working capital management because the deficit is considerably reduced.

The change in the deficit of working capital is: [-195,064.49 - (-4,279,000.7)]/ -4,279,000.7 = -0.95 x 100= -95%. The deficit of working capital has been reduced a 95%.

Repayment capacity

In regards of the repayment capacity Unilever has decreased a lot the ratio cash flow/loans in the last 5 years, from 0.59 in 2013 to 0.29 in 2017 and it is much lower than both competitors.

One of the possible solutions to this problem is to increase cash flow by reducing costs, for example, or to reduce loans. If we analyze the cash flow, we can see that one of the bigger costs the company has compared to the competitors is the high cost of goods sold (COGS) that is 57% of sales for the 50% of the competitors. We can see in the profit and loss account that the trend of the percentage of COGS over sales is diminishing, what is good news and means that the company is doing it well, even it can improve more. So it would be good if the company could reduce this cost to be the 50% of its sales:

- The new sales we get with the increase in assets are: 56,901,614.3
- 56,901,614.3 · 0.5 = 28,450,807.2 thousand euros

This is the new amount of COGS, that will cause an increase in the EBIT and in the net profit. This measure, jointly with the increase in equity and assets will benefit the net profit of the company by 4,455,889,300€, so the increase in equity advised in the first measure could be done through this increase in the net result, as the increase proposed in equity, 4,359,521,700€, is less than the extra amount of benefits. This way, it wouldn’t be necessary to ask for more capital to the shareholders (or ask for the money and then return it to the shareholders when the net profit is achieved).

6. Demonstration of the recommendations

	2017	Increase in capital	Debt restructuration	Improve WC management
Non-current assets	41,191,347	44,243,012.2	44,243,012.2	44,243,012.2
Current Assets	17,008,527	18,316,383.51	18,316,383.51	18,316,383.51
Stocks	3.967.942	4,273,053.6	4,273,053.6	4,273,053.6
Clients	3.444.066	3,708,894.6	3,708,894.6	3,708,894.6
Cash	3.322.391	3,577,863.5	3,577,863.5	3,577,863.5
Other current assets	9.597.644	6,757,783.3	6,757,783.3	6,757,783.3
Total Assets	58,199,874	62,559,395.7	62,559,395.7	62,559,395.7

	2017	Increase in capital	Debt restructuration	Improve WC management
Equity	14.409.423	18,768,944.7	18,768,944.7	18,768,944.7
Non-current Liabilities	20.578.774	26,274,919.2	26,274,919.2	26,274,919.2
Current Liabilities	23.212.803	17,516,657.8	17,516,657.8	17,516,657.8
Suppliers	8,229,932	8,229,932	8,229,932	8,229,932
Loans	7,717,322	2,021,149.8	2,021,149.8	2,021,149.8
Other current	7,266,675	7,266,675	7,266,675	7,266,675

liabilities				
Equity+Liabilities	58,199,874	62,559,395.7	62,559,395.7	62,559,395.7

Figure 13: *Demonstration of the recommendations on the balance shee. Source: Own calculations.*

	2017	**Increase EBIT due to an increase on assets**	**Reduction COGS**
Sales	53,797,057	56,901,614.3	56,901,614.3
COGS	30,593,267	32,358,764.1	28,450,807.2
EBIT	8,870,977	9,382,909.4	13,290,866.3
Net profit	6,496,070	7,008,002.4	10,915,959.3

Figure 14: *Demonstration of the recommendations on the income statement. Source: Own calculations*.

	2017	**Value after measures**
Debt (Debt/Assets)	0.75	0.70
Debt Quality (CL/Total liabilities)	0.53	0.40
Repayment capacity	0.29	0.5
Current Assets/Current Liabilities	0.73	1.05
ROE	0.45	0.58

Figure 13: *Demonstration of the recommendations on the value of the ratios. Source: Own calculations.*

Appendix:

All values in millions of €	2017	2016	2015	2014
A) CASH FLOWS FROM OPERATING ACTIVITIES				
1)Operating profit	**8,857**	**7,801**	**7,515**	**7,980**
2) Adjustments	**2,415**	**2,027**	**1,863**	**1,849**
(+) Amortization, depreciation and impairment	**1,538**	**1,464**	**1,370**	**1,432**
(-) Financial income	**-157**	**-115**	**-144**	**-177**
(+) Financial expenses	**1034**	**678**	**637**	**594**
3) Changes in current capital	**-68**	**51**	**720**	**8**
(+/-) Inventory	**-104**	**190**	**-129**	**-47**
(+/-) Debtors and other accounts receivable	**-506**	**142**	**2**	**82**
(+/-) Creditors and other accounts payable	**542**	**-281**	**847**	**-27**
4) Other cash flows from operating activities	**-3,912**	**-2,832**	**-2,768**	**-4,294**
(-) Interest Payment	**-1034**	**-678**	**-637**	**-594**
(+) Interest revenue	**157**	**115**	**144**	**177**

(+/-) Other adjustments (pensions, provisions…)	-871	-18	-254	-1,566
(-) Income tax payment / (+)Income tax revenue	-2,164	-2,251	-2,021	-2,311
5) Cash flows from operating activities (1+2+3+4)	7,292	7,047	7,330	5,543
B) CASH FLOW FROM INVESTING ACTIVITIES				
6) Payment for investments (-)	-7,029	-3,975	-4,287	-2,647
7) Divestments costs (+)	1,150	787	748	2306
8) Cash flows from investing activities (6+7)	-5,879	-3,188	-3,539	-341
C) CASH FLOW FROM FINANCING ACTIVITIES				
9)Collections and payments on equity instruments	-5,666	-257	-276	-1,351
10)Collections and payments for financial liability instruments (and loans)	8,619	1,265	1,154	-129
11)Dividend payments	-4,386	-4,081	-3,910	-3,710
12) Cash flows from financing activities (9+10+11)	-1,433	-3,073	-3,032	-5,190
E) INCREASE / DECREASE IN CASH AND CASH EQUIVALENTS (5+8+12)	-20	786	759	12
Cash and cash equivalents at the beginning of the year	3,198	2,128	1,910	2,044
Effects of foreign exchange rate changes	-9	284	-541	-146
Cash and cash equivalents at the end of the year (Part of the difference is due to the effect of foreign exchange rates)	3,169	3,198	2,128	1,910

Figure 12: Cash flow statement (data in millions euros). Source: Unilever.com

	2017	2016	2015	2014	2013
DEBT AND CAPITALIZATION					
Debt = Liability / Assets	0.75	0.69	0.68	0.70	0.66
Debt Quality = Current Liabilities / Total Liabilities	0.53	0.53	0.56	0.58	0.58
Repayment Capacity = Cash flow /Loans	0.29	0.42	0.5	0.42	0.59
Cost of debt = Financial Expenses / Loans	0.02	0.04	0.05	0.05	0.05
Financial Expenses = Financial Expenses / Sales	0.01	0.011	0.012	0.012	0.01
LIQUIDITY					
Liquidity = Current Assets / Current Liabilities	0.73	0.68	0.63	0.63	0.70
Treasury = Debtors + Cash / Current Liabilities	0.29	0.33	0.26	0.25	0.30
Acid Test = Cash / Current Liabilities	0.14	0.16	0.11	0.11	0.13
Z (UPF) = -3,9 + 1,28 CA/CL+ 6,1 E/A+ 6,5 NI/A+ 4,8 NI/E	1.44	1.04	1.06	1.34	1.50
Working Capital (real) (million euros)= Current assets – Current liabilities	-6,204	-6,662	-7,346	-7,278	-5,225
Operating Working Capital (million euros)= Operating current assets – Operating current liabilities	-1,924,3	-2,435.4	-2647.1	-1,444.8	-1,228.8
Operating CA = Inventory + Clients + Other operating CA + Minimum cash required	11,501.7	11,435.6	11,140.9	11,161.2	10,506.2
Operating CL = Suppliers + Other operating CL + Accruals	13,426	13,871	13,788	12,606	11,735
Working Capital Deficit (euros)	-4,279.979	-4,226.6	-4,698.9	-5,833.2	-3,996.2
ASSETS MANAGEMENT					
Non-current assets turnover = Sales / Non-current assets	1.31	1.26	1.38	1.37	1.54
Current assets turnover = Sales / Current assets	3.16	3.80	4.20	3.92	4.11

DEADLINES					
Inventories days = Stocks / Daily cost of sales	47.3	51.7	51.4	53.6	49.1
Days receivable (days) = Clients / Daily Sales	23.4	23.1	20	21.3	20.9
Days payables (days) = Suppliers / Daily cost of sales	98.2	103.7	98.3	98.2	87.3
SALES					
Sales growth = Last year's sales / Previous year sales	1.02	0.99	1.1	0.98	0.96
PROFITABILITY, SELF-FINANCING AND GROWTH					
Return on assets = EBIT / Assets	0.15	0.14	0.15	0.17	0.17
Return on equity = Net Income / Equity	0.45	0.33	0.33	0.39	0.36
Cash flow / Sales	0.13	0.13	0.13	0.10	0.13
Cash flow / Assets	0.12	0.12	0.14	0.11	0.14
Dividends / Net profit	0.60	0.65	0.65	0.58	0.57
Dividends / Net equity	0.27	0.21	0.21	0.22	0.20

Figure 13: Unilever's main ratios. Source: Own calculation with the data from BS and P&L.

	2017 Procter & Gamble	**2017 Nestlé**	**2017 Unilever**
DEBT AND CAPITALIZATION			
Debt = Liability / Assets	0.537	0.795	0.75
Debt Quality = Current Liabilities / Total Liabilities	0.467	0.348	0.53
Repayment Capacity = Cash flow /Loans **Cash flow consider economic cash flow (net profit + depreciation)/ ST and LT debt**	0.577	0.407	0.29
Cost of debt = Financial Expenses / Loans	0.015	0.029	0.02

Financial Expenses = Financial Expenses / Sales	0.007	0.008	0.01
LIQUIDITY			
Liquidity = Current Assets / Current Liabilities	0.877	0.893	0.73
Treasury = Debtors + Cash / Current Liabilities Només hem considerat accounts receivables i cash and cash equivalents	0.501	0.565	0.29
Acid Test = Cash / Current Liabilities	0.184	0.220	0.14
Z (UPF) = -3,9 + 1,28 CA/CL+ 6,1 E/A+ 6,5 NI/A+ 4,8 NI/E	2.2	1.13	1.44
Working Capital (real) (thousand euros)= Current assets – Current liabilities	-3,716,000	-3,864,000	-6,204 ,276
Operating Working Capital (th euros)= Operating current assets – Operating current liabilities	-2,296,000	1,684,000. 4	-1,924,3
Operating CA = Inventory + Clients + Other operating CA + Minimum cash required The minimum cash required is using 10% of the current liabilities	14,378,00 0	27,202,00 0.4	11,501.7
Operating CL = Suppliers + Other operating CL + Accruals	16,674,00 0	25,518,00 0	13,426
Working Capital Deficit (thousand euros)	-1,422,000	- 5,548,000. 4	-4,279.7
ASSETS MANAGEMENT			
Non-current assets turnover = Sales / Non-current assets	0.693	0.914	1.31
Current assets turnover = Sales / Current assets	2.455	2.789	3.16
DEADLINES			
Inventories days = Stocks / Daily cost of sales	51.875	73.625	47.3
Days receivable (days) = Clients / Daily Sales **Clients només hem considerat Accounts receivable**	25.774	50.50	23.4
Days payables (days) = Suppliers / Daily cost of sales	108.058	153.34	98.2

Suppliers només hem considerat Accounts payable			
SALES			
Sales growth = Last year's sales / Previous year sales	0.996	1.003	1.02
PROFITABILITY, SELF-FINANCING AND GROWTH			
Return on assets = EBIT / Assets	0.116	0.077	0.15
Return on equity = Net Income / Equity	0.276	0.12	0.45
Cash flow / Sales	0.28	0.12	0.13
Cash flow / Assets	0.151	0.08	0.12
Dividends / Net profit	0.470	0.945	0.60
Dividends / Net equity	0.130	0.11	0.27

***Figure 14**: Unilever's and competitors' main ratios. Source: Own calculation with the data from BS and P&L.*

	ROE =	**EBIT/Sales**	**Sales/Assets**	**(Assets/Equity) x (EBT/EBIT)**	**Net Profit/EBT**
Procter & Gamble 2017	0.28	0.21	0.54	2.05	1.16
Nestlé 2017	0.12	0.11	0.69	1.95	0.79
2017	0.45	0.16	0.92	3.72	0.8
2016	0.33	0.15	0.95	3.14	0.74
2015	0.33	0.14	1.04	3.07	0.73
2014	0.39	0.16	1.02	3.20	0.72
2013	0.36	0.15	1.12	2.84	0.74

Figure 15: Breakdown of profitability. Source: Own calculation with the data from BS and P&L.

Bibliographical references:

● AMADEUS database: for the financial statements.

● AMAT, O. (2014) English version adapted from the book ‘Análisis integral de empresas’.

● Unilever.com: for information related to financial statements, notes and official data, for history information too.

● statista.com

● investopedia.com

● forbes.com

● reuters.com

● Articles on Unilever:

- KISSINGER, Daniel. “Unilever's SWOT Analysis & Recommendations.” *Panmore Institute,* 21 Feb. 2017, panmore.com/unilever-swot-analysis-recommendations.
- RYAN, Carol “Unilever Has a First-World Problem to Fix.”*Breakingviews.com*, 2018, www.breakingviews.com/considered-view/unilever-has-a-first-world-problem-to-fix/.
- WHEATLEY, Malcolm. “The 3 Biggest Risks Facing Unilever.” *The Motley Fool*, The Motley Fool, 21 Nov. 2012, www.fool.com/investing/international/2012/11/21/the-3-biggest-risks-facing-unilever.aspx.
- “Tropezó El CEO De Unilever, y Renunció.” *Revista Mercado*, www.mercado.com.ar/notas/8028184.

● Articles on FMCG markets:

- MCGRATH, Maggie. “World's Largest Food And Beverage Companies 2018: Anheuser-Busch, Nestle And Pepsi Top The List.” *Forbes*, Forbes Magazine, 6 June 2018, www.forbes.com/sites/maggiemcgrath/2018/06/06/worldslargest-food-and-beverage-companies-2018-anheuser-busch-nestle-and-pepsi-top-the-list/#2c69aed11b08.

- NAIR, Geeta. “Over a Dozen Brands to Compete for Water Purifiers Market Share.” *The Financial Express*, हिन्दी, 28 June 2018, www.financialexpress.com/market/over-a-dozen-brands-to-compete-for-water-purifiers-market-share/1224481/.
- TAYLOR, Kate. “These 10 Companies Control Everything You Buy.” *The Independent*, Independent Digital News and Media, 4 Apr. 2017, www.independent.co.uk/life-style/companies-control-everything-you-buy-kelloggs-nestle-unilever-a7666731.html.
- “Water Purifier Market 2018 Global Trend, Segmentation and Opportunities Forecast To 2023.” *MarketWatch*, MarketWatch, 18 June 2018, www.marketwatch.com/press-release/water-purifier-market-2018-global-trend-segmentation-and-opportunities-forecast-to-2023-2018-06-18.
- “Unilever Reclama Protección Contra Las Artimañas (a Veces Sucias) Del Retail.” *Marketing Directo*, 22 Nov. 2018, www.marketingdirecto.com/anunciantes-general/anunciantes/unilever-reclama-proteccion-contra-artimanas-veces-sucias-retail.
- “The World's Top 100 Food and Beverage Companies of 2015.” *Food Engineering RSS*, Food Engineering, www.foodengineeringmag.com/top-100-food-&-beverage-companies-2015.