

FINANCIAL STATEMENT ANALYSIS & VALUATION

EASTON

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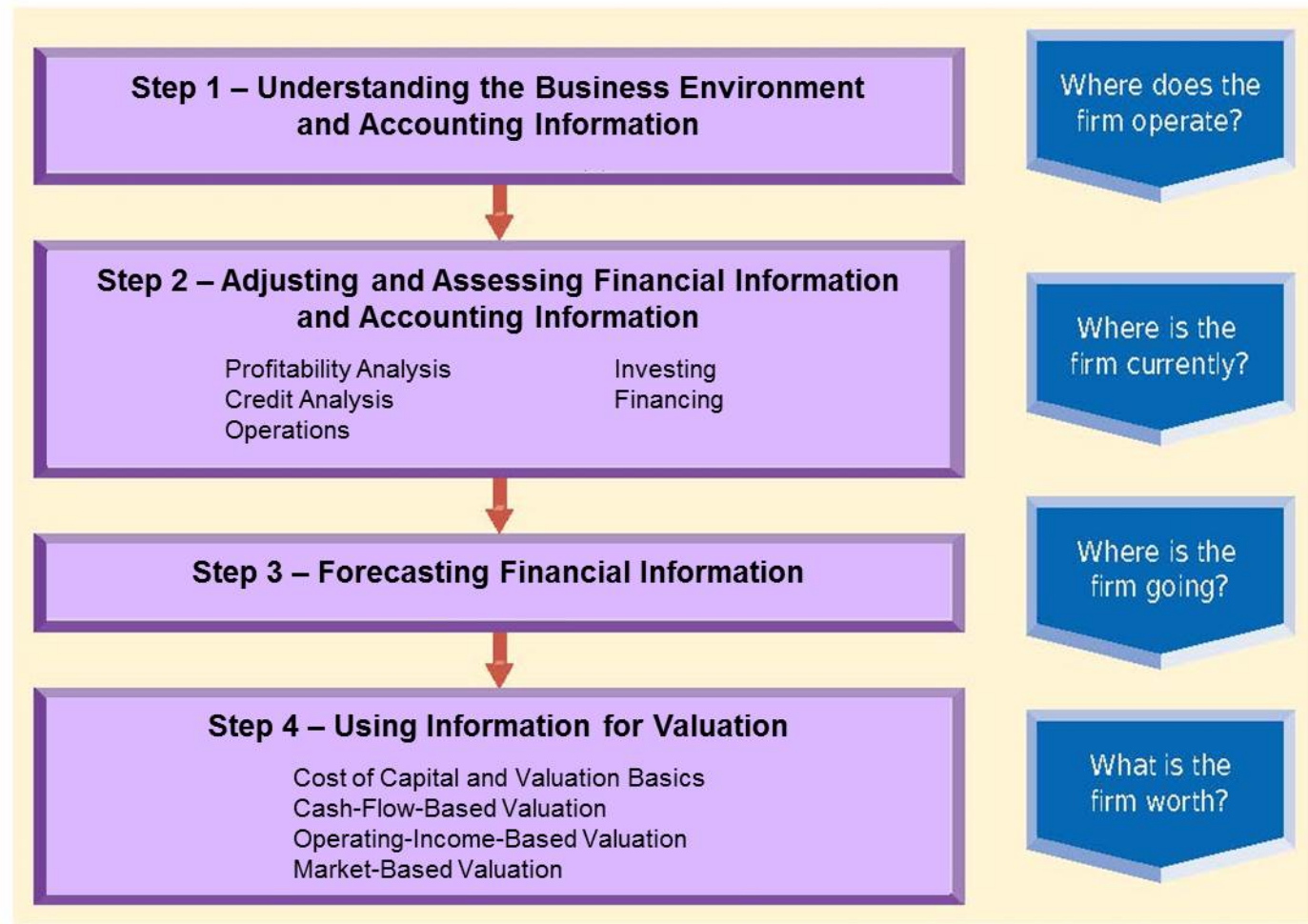


MODULE 1

Framework for Analysis and Valuation

Financial Statement Analysis & Valuation

4-Step Process



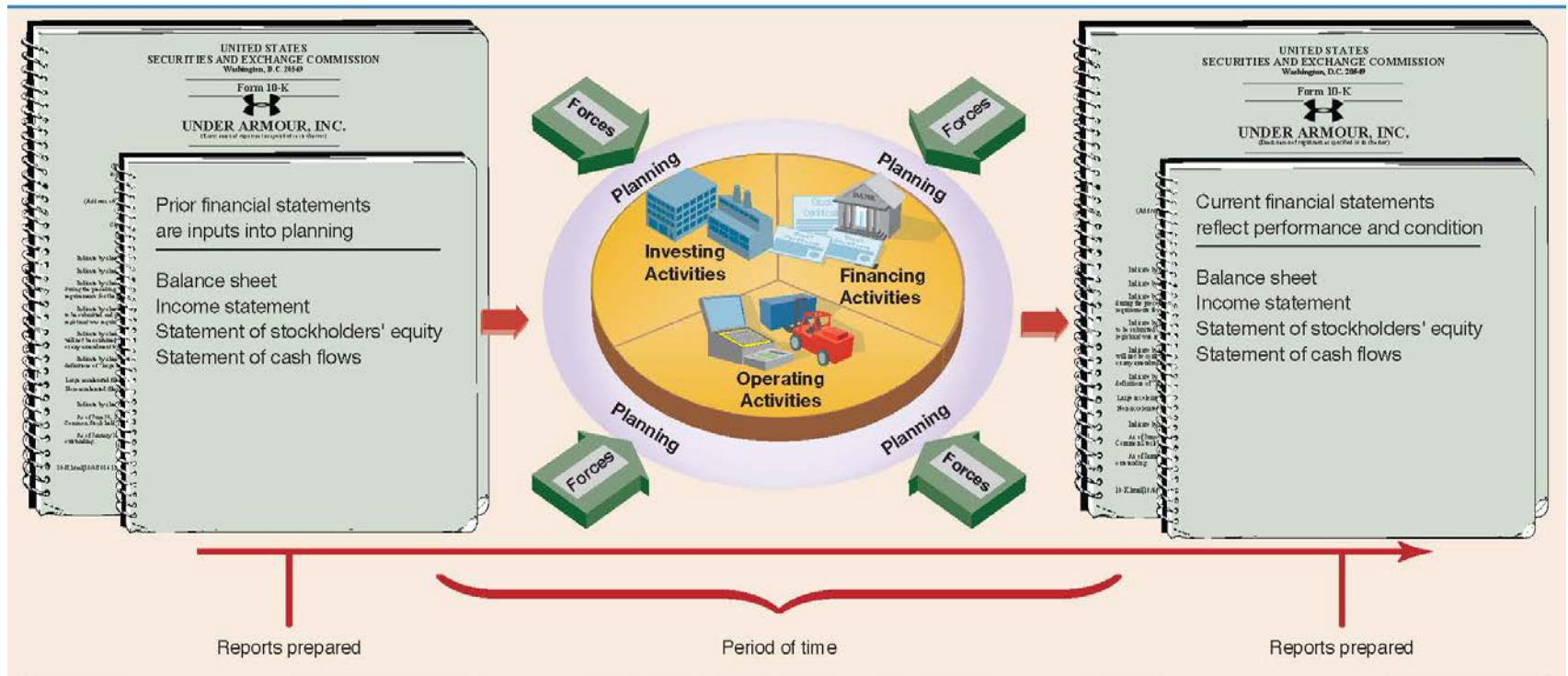
Learning Objective 1

Explain and assess the
four main business activities.

Four Types of Activities

- Companies
 - *Plan* business activities,
 - *Finance* those activities,
 - *Invest* in those activities,
 - Then engage in *operating* activities

Business Activities and Financial Statements



Learning Objective 2

Identify and discuss
the users and suppliers of
financial statement information.

Demand for Financial Accounting Information

- **Managers and employees**: current and future financial health.
- **Investment analysts** and information intermediaries: predicting companies' future performance.
- **Creditors** and suppliers: to help determine loan terms, loan amounts, interest rates, and required collateral.
- **Stockholders** and directors: to assess the profitability and risks of companies and other information useful in their investment decisions
- **Customers** and strategic partners: to assess a company's ability to provide products or services and to assess the company's staying power and reliability.
- **Regulators** and tax agencies: for antitrust assessments, public protection, setting prices, import-export analyses, and setting tax policies.
- **Voters** and their representatives: economic, social, taxation, and other initiatives, and to monitor government spending.

Supply of Financial Accounting Information

- The quantity and quality of accounting information that companies supply are determined by managers' assessment of the **benefits and costs of disclosure**.
 - **Form 10-K**: the audited annual report that includes the four financial statements with explanatory notes and the management's discussion and analysis (MD&A) of financial results.
 - **Form 10-Q**: the unaudited quarterly report that includes summary versions of the four financial statements and limited additional disclosures.

Benefits of Disclosure

- The benefits of supplying accounting information extend to a company's capital, labor, input, and output markets.
 - **Cost of capital** (as reflected in lower interest rates or higher stock prices),
 - **Recruiting efforts** in labor markets, and
 - the ability to establish superior **Supplier-customer relations** in the input and output markets

Costs of Disclosure

- Preparation and dissemination of financial information,
- Competitive disadvantages,
- Litigation potential, and
- Political costs.

SEC's Regulation Fair Disclosure (FD)

- Goal is to curb the practice of selective disclosure by public companies.
- Reg FD reads as follows:

“Whenever an issuer discloses any material nonpublic information regarding that issuer, the issuer shall make public disclosure of that information . . . simultaneously, in the case of an intentional disclosure; and . . . promptly, in the case of a non-intentional disclosure.”

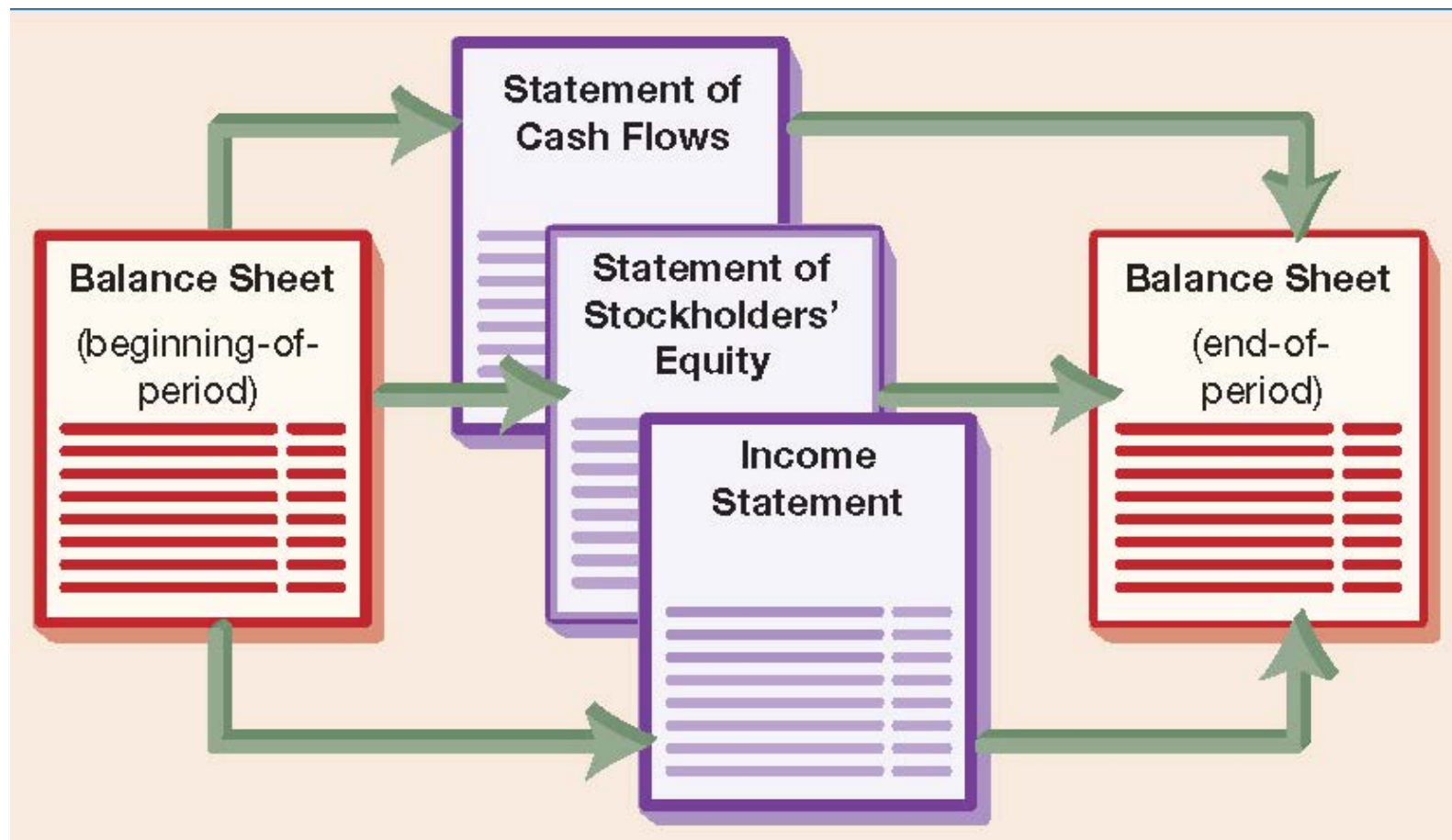
International Accounting Standards

- Companies in more than 120 countries, including the European Union, the United Kingdom, Canada, and Japan use International Financial Reporting Standards (IFRS) for their financial reports.
- International Accounting Standards Board (IASB) oversees the development of IFRS.
- The IASB and the Financial Accounting Standards Board (FASB) work together cooperatively, often undertaking joint projects.
- Consequently, IFRS and U.S. GAAP (generally accepted accounting principles) are generally more alike than different for most transactions.

Learning Objective 3

Describe and examine
the four financial statements.

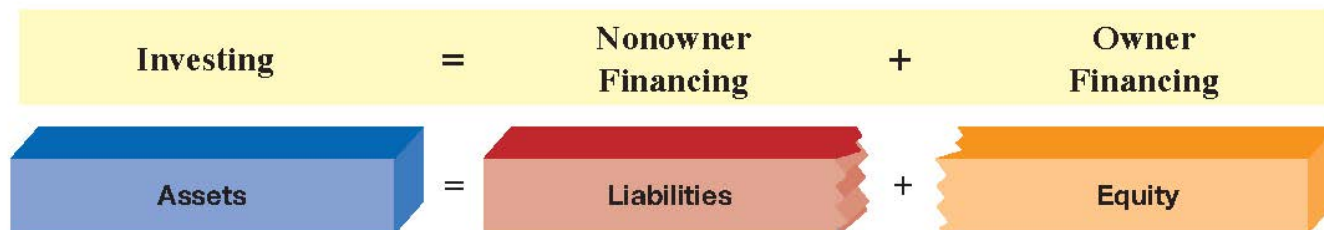
Financial Statement Links Across Time



Balance Sheet

- Reports a company's financial position at a point in time.
 - **Resources** (assets), namely what the company owns
 - **Sources** of asset financing
 - From stockholders—**owner financing**, or
 - From banks or other creditors and suppliers—**nonowner financing**

Accounting equation



The accounting equation works for all companies at all points in time.

Under Armour Balance Sheet

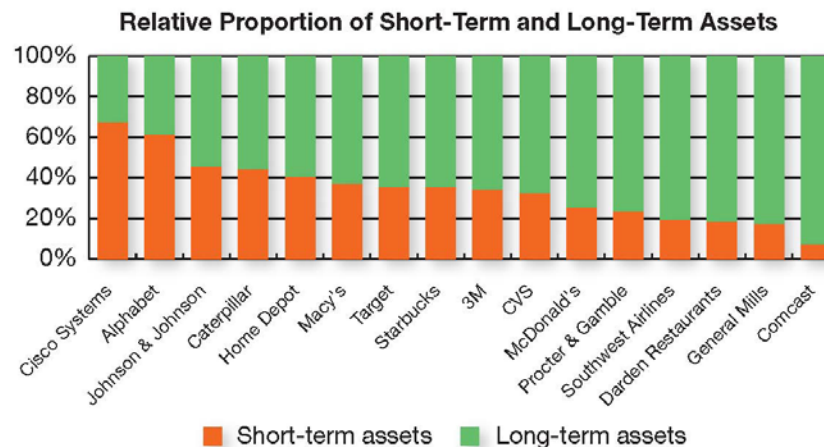
UNDER ARMOUR Consolidated Balance Sheet* December 31, 2015		Report amounts at a point in time
Assets		Investing
Short-term assets	\$1,498.8	
Long-term assets	1,370.1	
Total assets	<u>\$2,868.9</u>	Total resources
Liabilities		Financing
Short-term liabilities	\$ 478.8	
Long-term liabilities	721.9	
Total liabilities	<u>1,200.7</u>	Nonowner financing
Stockholders' Equity		
Contributed capital	636.7	
Retained earnings	1,076.5	
Other equity	(45.0)	
Total stockholders' equity†	<u>1,668.2</u>	Owner financing
Total liabilities and equity	<u>\$2,868.9</u>	Total financing of resources

* Financial statement titles often begin with the word *consolidated*. This means the financial statement includes a parent company and one or more subsidiaries, which are companies the parent company controls.

† Components of equity are explained as part of Exhibit 1.5.

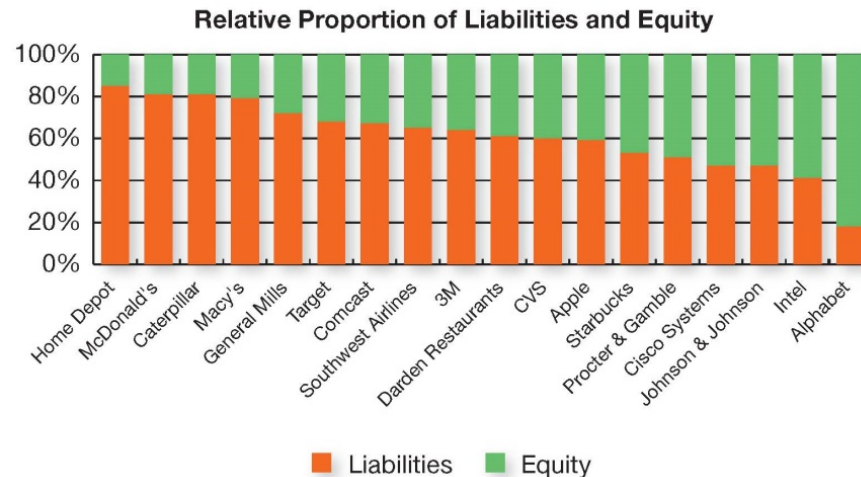
Investing Activities

- Represented by the company's assets.
- Assets are listed on the balance sheet in order of their **nearness to cash**.
- The relative proportion of short- and long-term assets is largely determined by a company's industry and business model.



Financing Activities

- Companies use a combination of **owner** (or equity) and **nonowner** financing (liabilities or debt).
- Owner financing has two components:
 - Resources contributed to the company by its owners, and
 - Profits retained by the company.



Income Statement

- Reports on a company's performance over a period of time and lists amounts for
 - Its *top line* **revenues** (also called sales) and
 - Its **expenses**.
- Revenues less expenses equals the *bottom-line* **net income** amount (also called *profit* or *earnings*).

Income Statement

UNDER ARMOUR Income Statement For Year Ended December 31, 2015		Report amounts over a period of time
Net revenues	\$3,963.3	Sales to customers
Cost of goods sold	<u>2,057.8</u>	Cost to purchase or manufacture the inventory sold
Gross profit	1,905.5	
Selling, general and administrative expenses	<u>1,497.0</u>	Company overhead
Income from operations	408.5	
Interest expense	<u>21.9</u>	Interest on borrowed money
Income before taxes	386.7*	
Provision for income taxes	<u>154.1</u>	Income taxes on profit earned
Net income	<u><u>\$ 232.6</u></u>	Remaining profit available to shareholders

* Rounding difference: Under Armour reports its financial statements in thousands, which we converted to millions.

Expenses

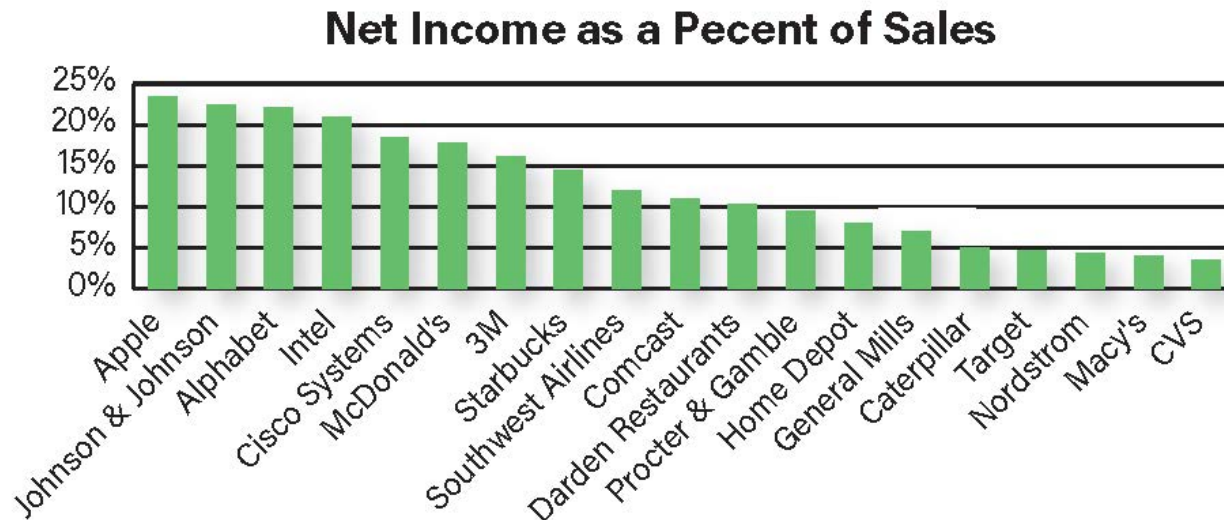
- **Cost of goods sold** (COGS, also called cost of sales)—the amount Under Armour paid to purchase or manufacture the goods (inventories) that it sold.

Gross profit = Revenues – Cost of goods sold

- **Selling, general, and administrative expenses (SG&A)**—the overhead of the company, including
 - Salaries
 - Marketing costs
 - Occupancy costs
 - HR and IT costs
 - All the other operating expenses the company incurs.

Net Income

- The ability of companies to create **barriers to competitive pressure**, either by **patent protection**, **effective marketing**, etc. is a key factor in determining their level of profitability.



Statement of Stockholders' Equity

- Reports on year-over-year changes in the equity accounts that are reported on the balance sheet:
 - **Contributed capital**, the stockholders' net contributions to the company,
 - **Retained earnings**, net income over the life of the company minus all dividends ever paid.
 - *Other equity*, consists of amounts we explain later in the book.

Statement of Stockholders' Equity

UNDER ARMOUR Statement of Stockholders' Equity For Year Ended December 31, 2015					Report amounts over a period of time
	Contributed Capital	Retained Earnings	Other Equity	Total	Beginning period amounts
December 31, 2014	\$508.4	\$ 856.7	\$(14.8)	\$1,350.3	Change in balances during the period
Net income		232.6		232.6	
Stock issuance	22.0			22.0	
Dividends		0.0		0.0	
Other	106.3	(12.7)	(30.2)	63.3*	
December 31, 2015	<u>\$636.7</u>	<u>\$1,076.6</u>	<u>\$(45.0)</u>	<u>\$1,668.2</u>	Ending period amounts

* Rounding difference: Under Armour reports its financial statements in thousands, which we converted to millions.

Statement of Cash Flows

- Reports cash inflows and outflows from **operating**, **investing**, and **financing** activities over a period of time.

UNDER ARMOUR Statement of Cash Flows For Year Ended December 31, 2015	
Operating cash flows	\$ (44.1)
Investing cash flows	(847.5)
Financing cash flows	428.3*
Net decrease in cash	(463.3)
Cash, December 31, 2014	593.2
Cash, December 31, 2015	<u>\$129.9</u>

Report amounts over
a period of time

Cash amounts per balance sheet

* Includes \$(11.8) mil. in foreign currency exchange rate changes.

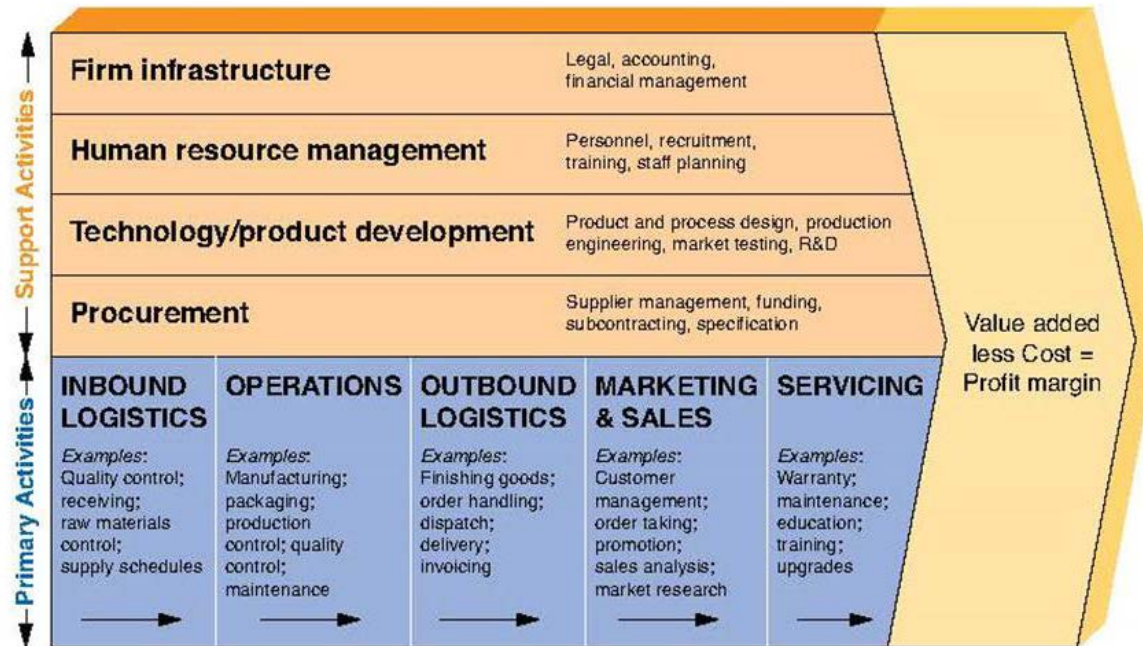
Information Beyond Financial Statements

- Management Discussion and Analysis (MD&A)
- Independent auditor report
- Financial statement footnotes
- Regulatory filings, including proxy statements and other SEC filings

Learning Objective 4

Assess business operations
within the context of
a competitive environment.

Porter's Value-Chain Model



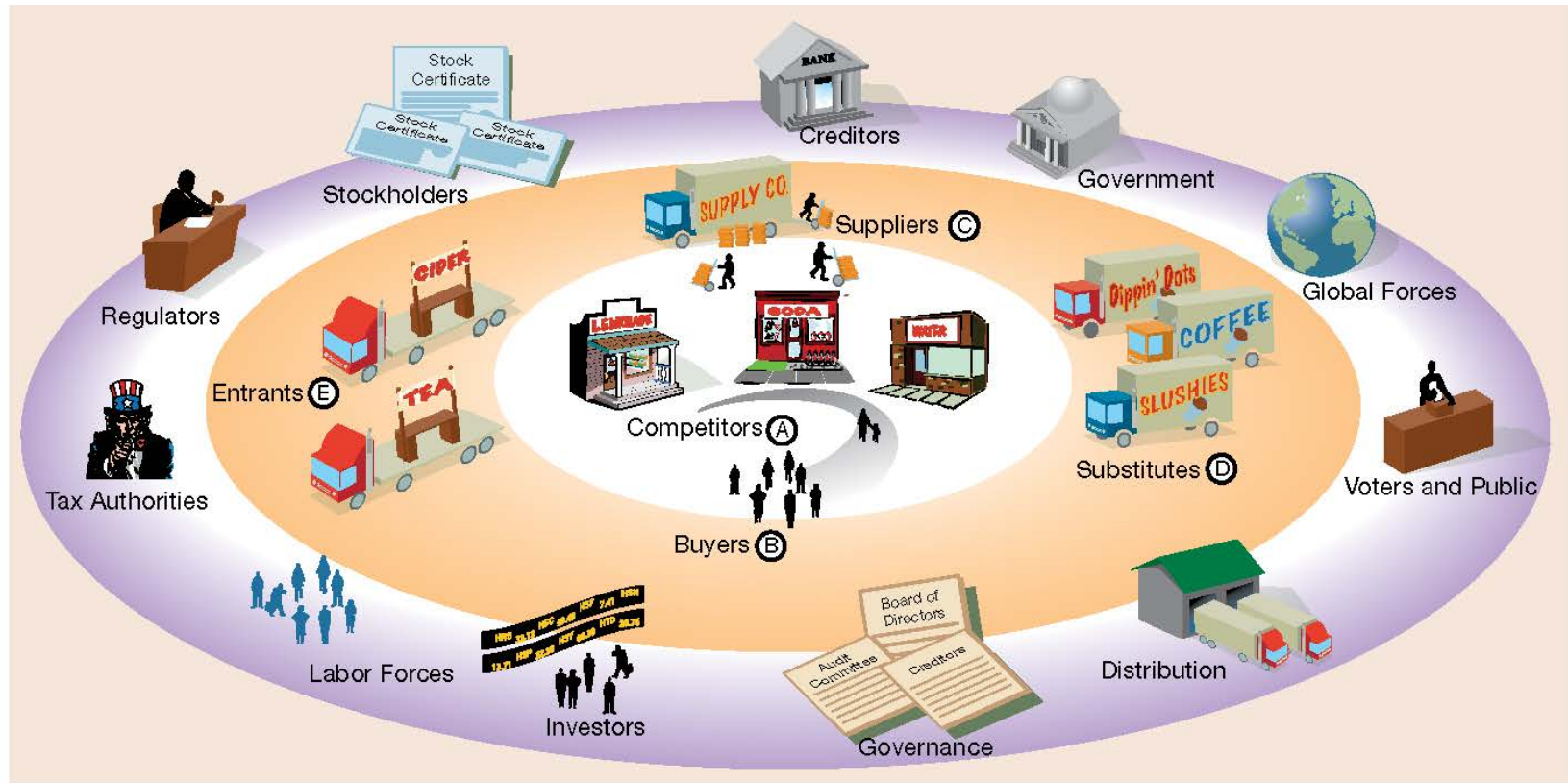
■ Primary activities

- Inbound logistics
- Operations
- Outbound logistics
- Marketing and sales
- Servicing

■ Support activities

- Firm infrastructure
- Human resource management
- Technology/product development
- Procurement

Analyzing the Competitive Environment

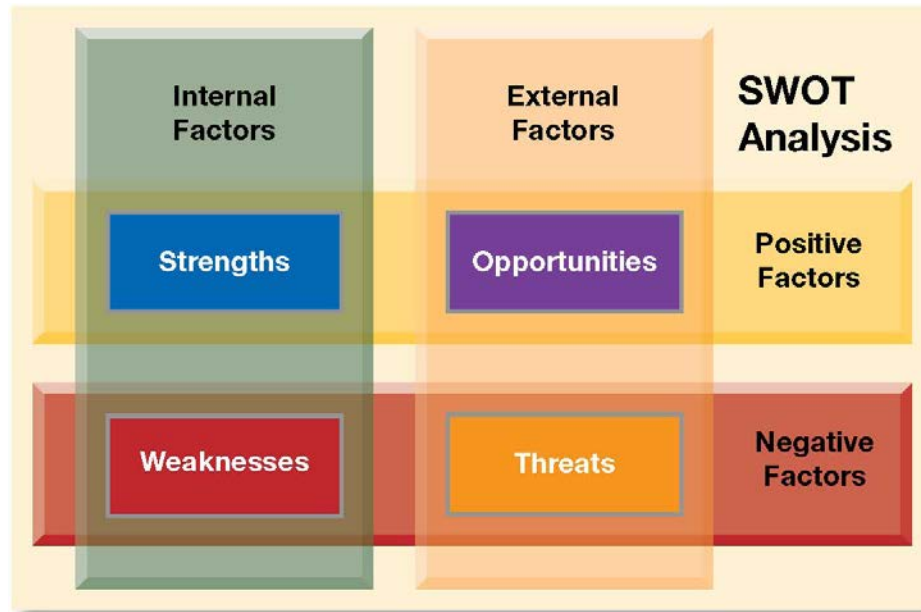


Competitive Forces within the Broader Business Environment

- **Industry competition.** Competition and rivalry raise the cost of doing business.
- **Bargaining power of buyers.** Buyers with strong bargaining power can extract price concessions.
- **Bargaining power of suppliers.** Suppliers with strong bargaining power can demand higher prices.
- **Threat of substitution.** As the number of product substitutes increases, sellers have less power to raise prices and/or pass on costs to buyers.
- **Threat of entry.** New market entrants increase competition and companies must expend monies on activities such as new technologies, promotion, and human development to erect *barriers to entry* and to create *economies of scale*.

SWOT Analysis of the Business Environment

- SWOT—strengths, weaknesses, opportunities and threats.



- **Internal**—strengths and weaknesses
- **External**—opportunities of and threats

Analyzing Competitive Advantage

- Does the company have a competitive advantage, and, if so, what factors explain it?
- Is the competitive advantage **sustainable**?
- If the company has no competitive advantage, does its management have a **plan** to develop a sustainable competitive advantage that can be implemented in an acceptable period of time and with a reasonable amount of investment?

Achieving Competitive Advantage

- **Product differentiation**
 - Technological innovation
 - Product design
 - Marketing, distribution, and after-sale customer support
- **Cost leader**
 - Access to low-cost raw materials or labor
 - Manufacturing or service efficiency, and
 - Manufacturing scale efficiencies, greater bargaining power with suppliers, sophisticated IT systems, etc.

Forecasting Financial Numbers

- Forecasting is a step where we proceed from our understanding of the company's current environment and what has occurred with the company to a prediction of what will occur next.
- The quality of our forecasts is dependent on at least two factors:
 - Our understanding of the business environment.
 - If we fail to effectively understand the context in which a company operates, we will not be able to make appropriate estimates going forward.
 - Our assumptions being realistic and achievable.

Business Valuation

- The key to good valuation estimates is accurate forecasts of future cash flows.
- And, the key to forecasting is having a good understanding of where the firm currently is and the business environment in which it competes.
- In general, the worth of a company is the current value of expected payoffs, and an accurate forecast of future earnings and cash flows is essential.

Financial Statement Analysis in an Efficient Capital Market

- Some question the value of financial statement analysis if capital markets are efficient. They incorrectly believe that this implies there is no gain to engaging in financial statement analysis.
- Market-efficiency is predicated on the efforts of many individuals (investors and analysts) who gather information, interpret it, then engage in trades based on their analysis.
 - Capital markets function well in the U.S., particularly for the largest firms, because of self-interested buy-side and sell-side analysts, institutional investors, and others.
 - Nonetheless, academic research has found many anomalies where markets appear to not fully reflect information, or reflect it with a lag.

Management Incentives

- Management often has an incentive to report favorable financial information due to a desire to maximize share price for compensation contracts or other reasons. While U.S. GAAP and IFRS put some restrictions on what is reported, the financial data can be potentially biased, misleading, or obfuscated.
- If we are able to perform effective analysis and gain a thorough understanding of where the firm operates, is currently situated, and is going, then even in an efficient market there are gains available through financial statement analysis.

Learning Objective 5

Explain and apply
basic profitability analysis.

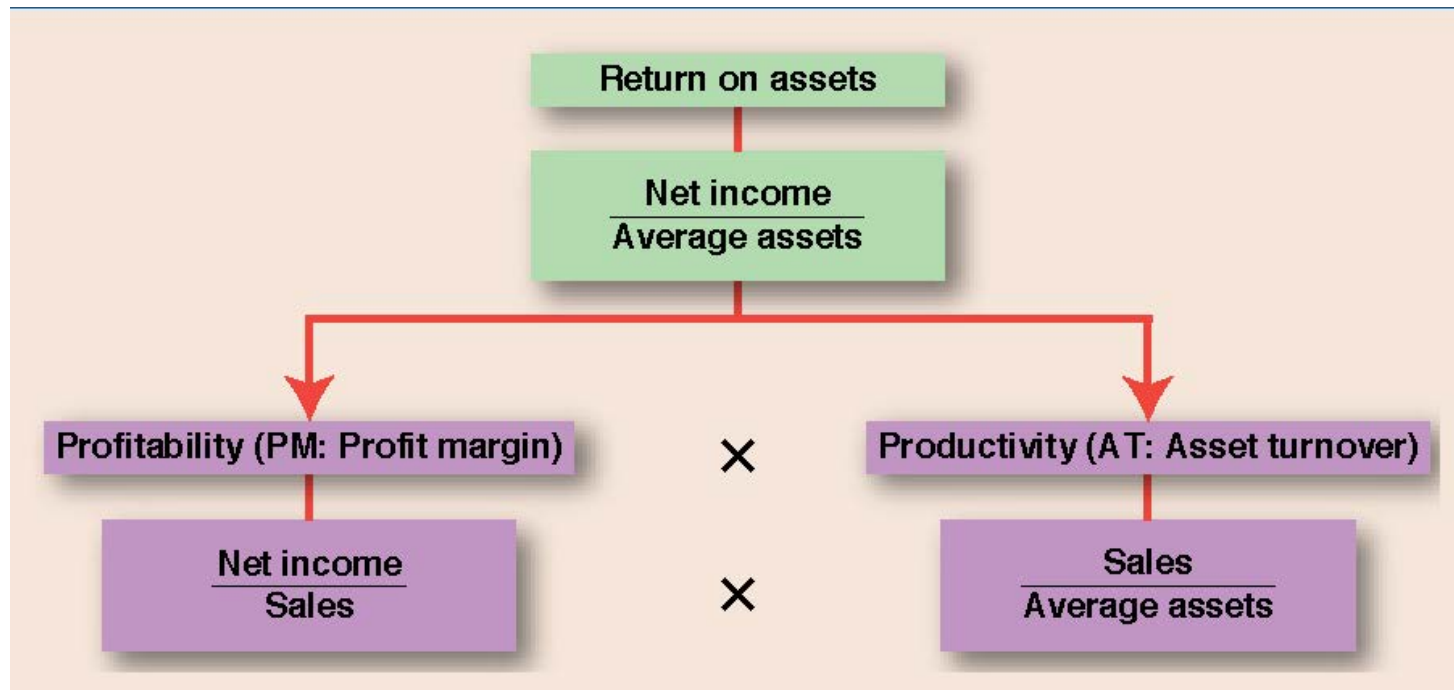
Managerial Choices in Financial Accounting

- GAAP allows companies **choices** in preparing financial statements.
 - The choice of **methods** can yield financial statements that are markedly different from one another in terms of reported income, assets, liabilities, and equity amounts.
- Financial statements also comprise numerous **estimates**.

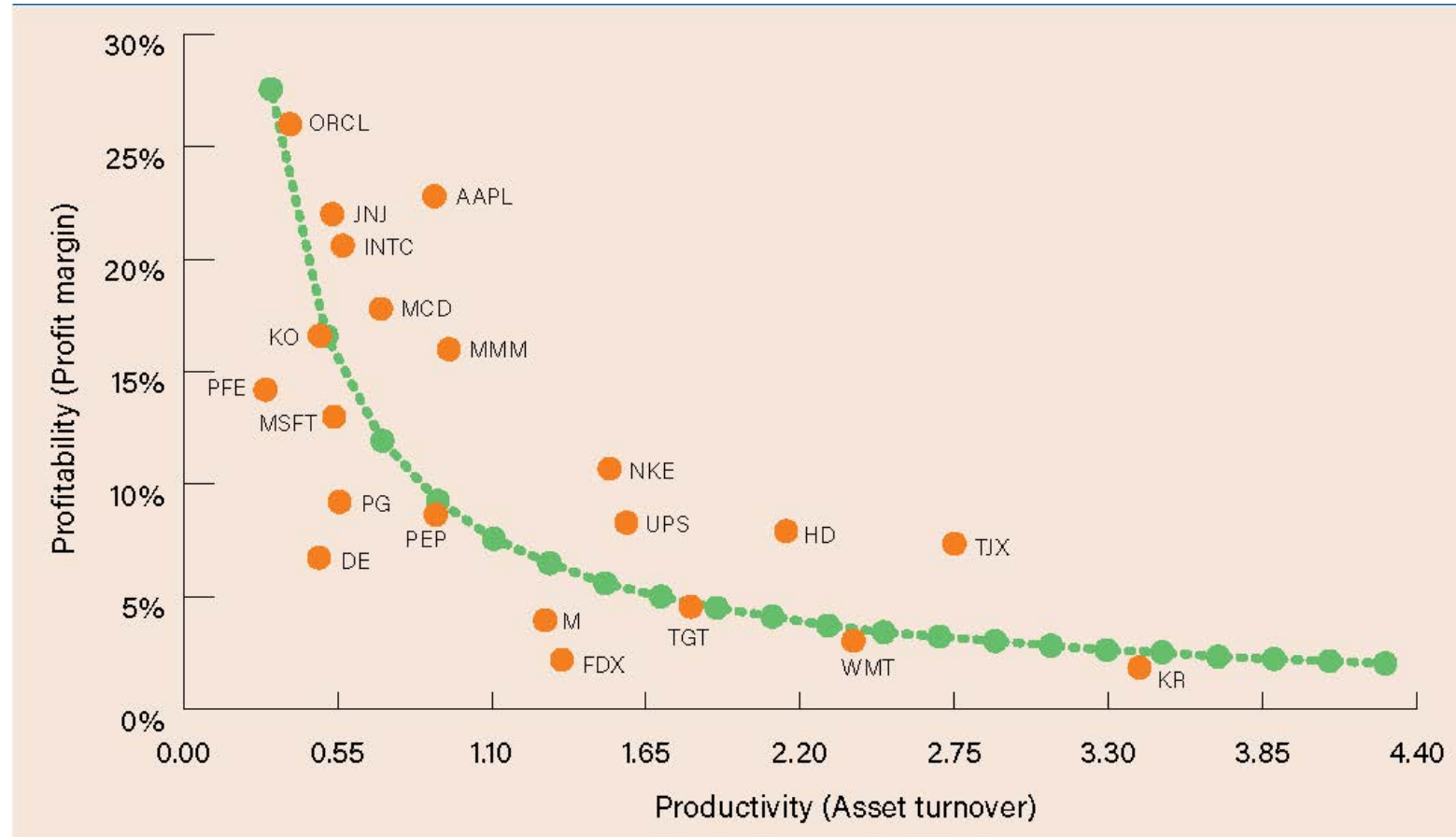
Sarbanes-Oxley Act (SOX)

- The statements signed by both the CEO and CFO contain the following declarations:
 - Both the CEO and CFO have **personally reviewed** the annual report.
 - There are **no untrue statements** of a material fact that would make the statements misleading.
 - Financial statements **fairly present** in all material respects the financial condition of the company.
 - All **material facts** are disclosed to the company's auditors and board of directors.
 - **No changes** to its system of internal controls are made unless properly communicated.

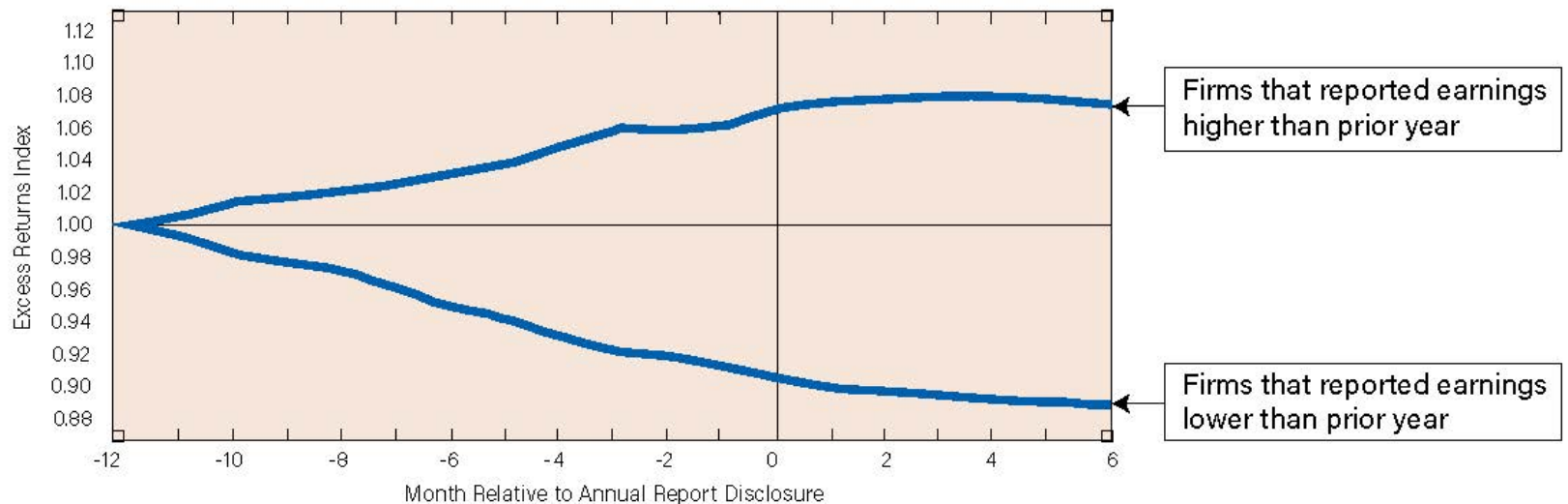
Return on Assets



Profitability and Productivity Across Companies



Relation Between Earnings and Stock Prices



Ball, R., and P. Brown. 1968. "An empirical evaluation of accounting income numbers." *Journal of Accounting Research* (Autumn): 159–178.

Relation between Financial Ratios and Credit Ratings

Moody's Financial Ratios	Aaa	Aa	A
Debt/EBITDA	<0.5	0.5–1.0	1.0–2.0
FCF/Debt	≥25%	15%–25%	10%–15%
(EBITDA-CAPEX)/Gross Int. Exp.	≥8.0%	6.5–8.0	5.0–6.5
Moody's Financial Ratios	Baa	Ba	B
Debt/EBITDA	2.0–2.75	2.75–3.75	3.75–6.0
FCF/Debt	8%–10%	6%–8%	4%–6%
(EBITDA-CAPEX)/Gross Int. Exp.	3.5–5.0	2%–3.5%	1.0–2.0
Moody's Financial Ratios	Caa		
Debt/EBITDA	>6.0		
FCF/Debt	<4%		
(EBITDA-CAPEX)/Gross Int. Exp.	<1		

Appendix 1A

Accessing SEC Filings

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Under Armour, Inc. CIK#: 0001336917 (see all company filings)

SIC: 2300 - APPAREL & OTHER FINISHED PRODS OF FABRICS & SIMILAR MATERIAL
State location: MD | State of Inc.: MD | Fiscal Year End: 1231
(Assistant Director Office: 9)
Note: Ownership filings are available at this link: Reports containing extracted ownership data are temporarily unavailable.

Business Address
1020 HULL STREET
3RD FLOOR
BALTIMORE MD 21230
410-454-6758

Mailing Address
1020 HULL STREET
3RD FLOOR
BALTIMORE MD 21230

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Filings	Format	Description	Filing Date	File/Film Number
8-K	Documents	Current report, Items 5.02, 8.01, and 9.01 Acc-no: 0001336917-16-000081 (34 Act) Size: 68 KB	2016-05-03	001-33202 161615711
8-K	Documents	Current report, Item 5.07 Acc-no: 0001336917-16-000079 (34 Act) Size: 45 KB	2016-05-02	001-33202 161612392
10-Q	Documents Interactive Data	Quarterly report [Sections 13 or 15(d)] Acc-no: 0001336917-16-000077 (34 Act) Size: 3 MB	2016-04-29	001-33202 161606788
8-K	Documents	Current report, Items 2.02 and 9.01 Acc-no: 0001336917-16-000073 (34 Act) Size: 391 KB	2016-04-21	001-33202 161582677

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Under Armour, Inc. CIK#: 0001336917 (see all company filings)

SIC: 2300 - APPAREL & OTHER FINISHED PRODS OF FABRICS & SIMILAR MATERIAL
 State location: MD | State of Inc: MD | Fiscal Year End: 1231
 (Assistant Director Office: 9)
 Note: Ownership filings are available at this link. Reports containing extracted ownership data are temporarily unavailable.

Business Address
 1020 HULL STREET
 3RD FLOOR
 BALTIMORE MD 21230
 410-454-6758

Mailing Address
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 3RD FLOOR
 BALTIMORE MD 21230

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Filings	Format	Description	Filing Date	File/Film Number
10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-16-000064 (34 Act) Size: 11 MB	2016-02-22	001-33202 161442999
10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-15-000006 (34 Act) Size: 13 MB	2015-02-20	001-33202 15636415
10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-14-000008 (34 Act) Size: 13 MB	2014-02-21	001-33202 14633178



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Filing Detail

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Form 10-K - Annual report [Section 13 and 15(d), not S-K Item 405] SEC Accession No. 0001336917-16-000064

Filing Date 2016-02-22	Period of Report 2015-12-31
Accepted 2016-02-19 17:42:07	Filing Date Changed 2016-02-19
Documents 112	

[Interactive Data](#)

Document Format Files

Seq	Description	Document	Type	Size
1	FORM 10-K	ua-20151231x10k.htm	10-K	2162809
2	EXHIBIT 10.04	ua-12316316xex1004.htm	EX-10.04	94762
3	EXHIBIT 10.07	ua-12312015xex1007.htm	EX-10.07	39542
4	EXHIBIT 10.08	ua-12312015xex1008.htm	EX-10.08	50720

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SIC: 2300 - APPAREL & OTHER FINISHED PRODS OF FABRICS & SIMILAR MATERIAL
 State location: MD | State of Inc: MD | Fiscal Year End: 1231
 (Assistant Director Office: 9)
 Note: Ownership filings are available at this link. Reports containing extracted ownership data are temporarily unavailable.

Business Address
 1020 HULL STREET
 3RD FLOOR
 BALTIMORE MD 21230
 410-454-6738

Mailing Address
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10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-16-000064 (34 Act) Size: 11 MB	2016-02-22	001-33202 161442999
10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-15-000006 (34 Act) Size: 13 MB	2015-02-20	001-33202 15636415
10-K	Documents Interactive Data	Annual report [Section 13 and 15(d), not S-K Item 405] Acc-no: 0001336917-14-000008 (34 Act) Size: 13 MB	2014-02-21	001-33202 14633178

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	Document and Entity Information - USD (\$)	12 Months Ended		
		Dec. 31, 2015	Jan. 31, 2016	Jan. 30, 2015
Cover	Entity Information (Line Items)			
Financial Statements	Document Type	10-K		
Notes to Financial Statements	Amendment Flag	false		
Accounting Policies	Document Period End Date	Dec. 31, 2015		
Notes Tables	Document Fiscal Year Focus	2015		
Notes Details	Document Fiscal Period Focus	FY		
All Reports	Trading Symbol	UA		
	Entity Registrant Name	Under Armour, Inc.		
	Entity Central Index Key	0001336917		
	Current Fiscal Year End Date	--12-31		



The End