This page of the Footwear Industry Report provides comparative income statement data for all companies in the industry, selected balance sheet data for all companies, dividend data, an assortment of financial and operating ratios for each company, and credit rating information. (In the real world, this information is always available for companies whose stock is publicly traded and can be gotten from company annual reports and other public sources.)

This page of information makes it easy for you to see how your company's financial performance compares with that of any and all rival companies.

Using the Income Statement Data

The comparative income statement data is primarily useful for seeing which companies are the largest and smallest in the industry, who is earning the biggest profits, and who is probably burdened with excessive interest costs. Each company began with same revenues and profits, so those with the largest revenues have grown faster than those with the least revenues over the course of the exercise. Those with the biggest net income have been able to grow their company's profits faster than those with lesser net income. Companies with the highest interest costs either have the most debt outstanding or weak credit ratings (which drives up the interest rates they are paying).

The data on shares of stock for each company at the end of the column is useful for tracking (1) which companies have issued new shares of stock (which tends to dilute earnings per share, but which may be necessary to raise equity capital, pay down debt, and protect their credit ratings) and (2) which companies have repurchased shares (usually to boost EPS, ROE and their stock price, all three of which are important factors in scoring company performance).

It is generally useful to scan this data each year just to stay on top of such matters. But the real meat on this page is in the other sections.

Using the Balance Sheet Data

The balance sheet data in the FIR is useful for tracking which companies have plenty of cash on hand, which ones have large amounts of the outstanding debt in the form of 5-year and 10-year loans (and thus may be overextended and headed for possible financial trouble), and which companies have how much in shareholders’ equity investment and how much their total shareholder equity changed during the year. Changes in total shareholder equity are important because higher/lower ending equity values translate into lower/higher returns on average equity (ROE).

Just as with the income statement data, you should scan the comparative balance sheet statistics each year just to stay on top of how well your company stacks up relative to the other companies in the industry. The most interesting data is what is on the rest of this page.

Using the Dividend Data

The dividend statistics for all the companies in the industry provide information that can help you decide:

- Whether you need to consider raising your company’s dividend, in light of the dividends being paid by other companies in the industry. Dividend increases generally have a positive impact on your company’s stock price (unless they involve paying out more than the company is earning — i.e. a dividend payout ratio greater than 100%). Companies with a low dividend relative to other companies may want to consider a dividend increase (if the company’s financial condition permits).

- Whether you should consider increasing your company’s dividend on a more regular basis. The last column of dividend statistics reports the number of times each company has cut/increased its dividends since the end of Year 10. You can use this data as a guide in deciding whether the number of dividend increases your company has declared measure up.

A steadily rising dividend is much preferred to a roller coaster dividend stream; thus, a decision to raise the dividend should be made only if you think your company can afford to pay higher dividends over the long term.

Using the Financial and Operating Statistics
The financial and operating ratios are the most important pieces of information on this page of the FIR. You should make a habit of scrutinizing these numbers carefully.

**The ratios relating to costs and profit as a percentage of net revenues are of particular interest because they indicate which companies are most cost efficient and have the best profit margins:**

- **Lower percentages for cost of pairs sold** are generally preferable to higher percentages because they signal a bigger margin for covering all other costs and earning a profit — the company with the lowest percentage may be the industry's low cost producer or the company with one of the highest overall prices per pair sold. A company's cost of pairs sold includes all production costs, any exchange rate adjustments, any tariff payments, and freight charges on pairs shipped from plants to distribution warehouses. The lower the percentage of cost of pairs sold to net revenues the bigger a company's margin for covering other expenses and earning a profit. Companies having the highest percentages for cost of pairs sold are likely to be caught in a profit squeeze, with margins too small to cover warehouse, marketing, and administrative costs and interest costs and still have a comfortable margin for profit. The cost of pairs sold at such companies are usually too high relative to the price they are charging (their strategic options for boosting profitability are to cut costs, raise prices, or try to make up for thin margins by somehow selling additional pairs).

- A **low percentage of warehouse expenses costs to net revenues** is preferable to a higher percentage, indicating that a smaller proportion of revenues is required to cover warehouse costs (which leaves more room for covering other costs and earning bigger margins on each pair sold).

- A **low percentage of marketing costs to net revenues** relative to other companies signals good efficiency of marketing expenditures (more bang for the buck), provided unit sales volumes are attractively high. However, a low percentage of marketing costs, if coupled with low unit sales volumes, generally signals that a company is spending too little on marketing. The optimal condition, therefore, is a low marketing cost percentage coupled with high sales, high revenues, and above-average market share (all sure signs that a company has a cost-effective marketing strategy and is getting a nice return in the marketplace on the marketing dollars it is spending).

- A **low ratio of administrative costs to net revenues** signals that a company is spreading its fixed administrative costs out over a bigger volume of sales. Companies with a high percentage of administrative costs to net revenues generally need to pursue additional sales or market share or risk squeezing profit margins and being at a cost disadvantage to bigger-volume rivals (although a higher administrative cost ratio can sometimes be offset with lower costs/ratios elsewhere).

- A **higher operating profit margin** (defined as operating profits as a percentage of revenue) is a sign of competitive strength and cost competitiveness. The bigger the percentage of operating profit to net revenues, the bigger the margin for covering interest payments and taxes and moving revenues to the bottom-line.

- The bigger a company's **net profit margin** (its ratio of net profits to net revenues), the better the company's profitability in the sense that a bigger percentage of the dollars it collects from footwear sales flows to the bottom-line. The net profit margin is sometimes called “net return on sales” because it represents the percentage of revenues that end up as after-tax profit or net profit.

- The **current ratio** (defined as current assets divided by current liabilities) measures the company's ability to pay its current liabilities as they become due. At the least, the current ratio should be a bit greater than 1.0; a current ratio in the 1.5 to 2.5 range provides a much healthier cushion for meeting current liabilities.

- A **large number of days of inventory** signals that a company “overproduced” and thus has pairs remaining unsold in the one or more of their distribution centers over and above the minimum required inventory. The bigger the number of days of inventory, the more likely that a company's co-managers will consider having inventory clearance sales at the beginning of the upcoming year to clear out excess inventory. However, because inventory clearance sales usually result in a sizable loss on the pairs sold at deeply discounted clearance prices, some companies with excessively large inventories may forego the use of inventory clearance sales and, instead, opt for either of two alternatives:
  1. Curtailing production at one or more plants in the coming year in order to work off excess inventory or
  2. Increasing their marketing efforts so as to boost unit sales volumes enough to both absorb current production and sell off some of the excess pairs in inventory.

Because the actions of companies with large “surplus” inventories can affect your company in the upcoming year, it is always wise to monitor the days of inventory data and be on the lookout for how many and which companies have inventories problems that they need to deal with in the upcoming year.
The statistics relating to credit ratings show where each company stands on the three credit rating determinants, and which companies have default risk ratio problems. These statistics are definitely worth perusing each year. Companies with very strong numbers on the three credit rating measures almost certainly have ample financial resources to fund aggressive strategic moves in the marketplace if they are so inclined. Companies whose measures of creditworthiness are eroding are not only troubled financially but also are good candidates for making fresh strategic moves aimed at improving their performance both in the marketplace and on the bottom-line.

Below are descriptions of each of the three factors determining your company’s credit rating:

1. **The debt-to-assets ratio** (defined as all loans outstanding divided by total assets—both numbers are shown on the company’s balance sheet). A debt-to-assets ratio of .20 to .35 is considered “good”. As a rule of thumb, it will take a debt-to-assets ratio close to 0.10 to achieve an A+ credit rating and a debt-asset ratio of about 0.25 to achieve an A- credit rating (unless the interest coverage ratios are in the 5 to 10 range and the default risk ratio is above 3.00). Debt-to-asset ratios above 0.50 (or 50%) are generally alarming to creditors and signal “too much” use of debt and creditor financing to operate the business, although such a debt level could still produce a B+ or A- credit rating if a company can maintain very strong interest coverage ratios (say 8.0 or higher) and default risk ratios above 3.00.

2. **The interest coverage ratio** (defined as annual operating profit divided by annual interest payments). Your company’s interest coverage ratio is used by credit analysts to measure the “safety margin” that creditors have in assuring that company profits from operations are sufficiently high to cover annual interest payments. An interest coverage ratio of 2.0 is considered “rock-bottom minimum” by credit analysts. A coverage ratio of 5.0 to 10.0 is considered much more satisfactory for companies in the footwear industry because of earnings volatility over each year, intense competitive pressures which can produce sudden downturns in a company's profitability, and the relatively unproven management expertise at each company. It usually takes a double-digit times-interest-earned ratio to secure an A- or higher credit rating, since this credit measure is strongly weighted in the credit rating determination.

3. **The default risk ratio** (defined as free cash flow divided by the combined annual principal payments on all outstanding loans; free cash flow is defined as net profit plus depreciation minus dividend payments). This credit measure also carries a high weighting in the credit rating determination. A company with a default risk ratio below 1.0 is automatically assigned “high risk” status (because it is short of cash to meet its principal payments) and cannot be given a credit rating higher than C+. Companies with a default risk ratio between 1.0 and 3.0 are designated as “medium risk”, and companies with a default ratio of 3.0 and higher are classified as “low risk” because their free cash flows are 3 or more times the size of their annual principal payments.

The interest coverage ratio and the default risk ratio are the two most important measures in determining a company’s credit rating. Thus, as long as a company is financially strong in its ability to service its debt — as measured by the interest coverage ratio and the default risk ratio, then the company can maintain a higher debt-to-assets ratio without greatly impairing its credit rating. However, weakness on just one of the three measures, particularly the two most important ones, can be sufficient to knock a company’s credit rating down a notch. Weakness on two or three can reduce the rating by several notches.