

Historical Analysis of Income Statement – A Case Study Salalah Mills Company Oman

Balamurugan Muthuraman¹ and Abdullah Khalfan Salim Al Mawali²

Administrative and Financial Sciences, Oman College of Management & Technology, Sultanate of Oman

Email: ¹balamurugan.muthuraman@omancollege.edu.om, ²201822007@omancollege.edu.om

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Abstract

Purpose: The objectives of the study were to critically analyse the financial performance of Salalah Mills Company (SMC), to examine the income statement position of the company and to study the profitability position and improvements of Salalah Mills Company.

Design/methodology/approach: The secondary data was obtained from the annual reports of Salalah Mills Company through the income statement for the period 2015 to 2019. The collected data was analysed using financial ratios involving excel and SPSS, to evaluate the Salalah Mills Company (SMC) profitability.

Findings: The study revealed that the reducing in company's gross profit (profit margin), pre-tax margin was due to the increase in cost of goods sold, administrative expenses, the cost of materials consumed, the selling and distribution expenses and the labour cost.

Research implications: The study suggested that the company should reduce the cost of sales and administrative expenses to achieve increased gross profit margin. It was also suggested that the company should focus more towards marketing.

Practical implications: The study helps the stakeholders of the banks to understand the factors and the banking activities that might help to enhance the financial performances of the banks and to take necessary action and suitable decisions accordingly.

Originality / Value: This research work is of its first own kind as the study focuses on the accounting perspectives of the food company in the Sultanate of Oman.

Keywords: Direct cost of sales, Operating Income of the Flour Mills, Income Statement Analysis, Financial ratios, Market share of flour mills.

Introduction

During the financial crisis, businesses are facing different challenges. Businesses need to focus on either economic, social, political, or technological factors. To make it survive from the battling business environment characterized by intense competition, not necessarily to achieve progress and prosperity, but often for the sake of survival. The larger the size of institutions and the complexity, the intertwining activities and work necessitate accurate information that effectively benefits the decision-makers at all levels. Especially, financial information is the one which helps to improve the performance of institutions. Its quality and accuracy if it is not considered at the right time will affect the business directly. In every business, growth is focused on the financial information obtained from the financial statement of the company. Financial information is an important tool which helps to make proper financial decisions by the management. Obtaining accurate information is the basis on which financial statements of various kinds are built. Ratios analysis is one of the methods that allow the institutions to take the right decisions to position in the marketplace among the competition phases. Adopting to this technique, the institution can discover the strength and weakness that help to survive.

Statement of the problem

The food sector is one of the most important sectors that people care about for sustainability. The importance of milling companies stems from what they provide as basic products that are included in various types of food, especially in Oman. The problem of fluctuating wheat prices is the biggest challenge facing the milling sector, as it cannot establish a fixed price policy for its products. Governments support the milling sector to maintain a constant price for its products so that it is affordable for everyone. Salalah Mills Company (SMC), which was established in 1970, which is producing wheat products and marketing them to all regions of the Sultanate of Oman is facing many challenges due to huge competition from local and foreign companies. SMC is trying to reduce its market share which will make it difficult for the company to achieve the desired profitability of the shareholders and the founders.

So this study explored to analyse the impact of competition on the performance of the company and the steps involved to overcome the impacts. The study highlighted the strengths, opportunities, weaknesses, and threats. The main problem of the study was in measuring the financial performance of SMC and the future growth achievement.

Objectives of the study

The objectives of the study were:

- To critically analyse the financial performance of Salalah Mills Company (SMC)
- To examine the income statement position of the company
- To study the profitability position and improvements of Salalah Mills Company

Review of Literature

[Khoja et al.](#) (2016) revealed that the managers pay less concentration on non-strategic sales to reduce susceptibility to insolvency in the GCC. [Bartoloni and Baussola](#) (2014) confirmed that the use of multiple methodological tools to correct the evaluation of firms' creditworthiness and fine-tuning procedures requiring to reach success. [Efuntade and Akinola](#) (2020) studied that the production processes lead to an increase in profit with the use of the maximum resources. [Harb](#) (2019) claimed that the focus should be on the strength of the firms' operations to improving production efficiency to avoid the impact of profitability. [Duarte et al.](#) (2011) confirmed that the effective practices on performance might be context-dependent in the industries. [Suardi and Noor](#) (2015) claimed that the total assets are reliable to cover the debt. [Capkun et al.](#) (2009) stated that the ratio between inventory and performance is more highly correlated with the operating profit measures. [Sahore and Verma](#) (2017) analysed the possible consequences in economic conditions and performance growth of the manufacturing and non-manufacturing companies. [Kaplan](#) (1983) found that the short-term financial process is more consistent to compare the long-term effectiveness and profitability. [Williams](#) (2020) claimed that U.S. Small Medium Enterprises (SMEs) need to consider financial performance growth to improve their business during the investment period. [Padma and Prabhakaran](#) (2019) used ratio analyses and found growth had a negative value in the Indian food products industry. [Yalcin et al.](#) (2012) found that the manufacturing industries' financial positions were at the same level. [Gatsi et al.](#) (2013) revealed that the corporate income tax and financial performance are negatively correlated. [Kangari et al.](#) (1992) used financial ratios, measured the grade of the construction companies.

[Gazzola and Amelio](#) (2014) revealed that the evaluation of financial performance during the investment process is informative content. [Behn and Riley](#) (1999) revealed that the expenses and operating income information appears as a non-financial performance. [Gamayuni](#) (2015) revealed that the firm value of the public company created significant influences on financial performance. [Zahra and Das](#) (1993) evaluated the innovation strategy towards to the financial performance of the manufacturing companies.

Findings

Table 1. Operational Analysis Tools

Ratio	Formula	References
Gross Profit Margin Ratio	$\frac{\text{Gross Profit}}{\text{Revenue}}$	Nariswari and Nugraha. (2020)
Net Profit Margin Ratio	$\frac{\text{Net Income}}{\text{Revenue}}$	
Operating Margin Ratio	$\frac{\text{Operating Income}}{\text{Revenue}}$	Filer and Golbe (2003)
Net Profit Ratio	$\frac{\text{Net Profit after Tax}}{\text{Net Sales}}$	

Administrative Expenses to Sales Ratio	$\frac{\text{Administrative Expenses}}{\text{Net Sales}}$	(Khan, 2019)
Selling and Distribution Expenses to Sales Ratio	$\frac{\text{Selling and Distribution Expenses}}{\text{Net Sales}}$	
Labour cost to Sales Ratio	$\frac{\text{Labour Cost}}{\text{Net Sales}}$	
Interest Coverage Ratio	$\frac{\text{Earnings Before Interest \& Taxes}}{\text{Interest Expenses}}$	
Cost of Goods sold Ratio	$\frac{\text{Cost of Goods Sold}}{\text{Net Sales}}$	
Pre-tax Profit Margin	$\frac{\text{Profit before Tax}}{\text{Net Sales}}$	
Materials consumed to Sales Ratio	$\frac{\text{Cost of direct materials}}{\text{Sales}}$	

Table 2. Gross Profit Margin Ratio

Year	Gross Profit	Revenue	Ratio
2015	9,416,857	68,342,932	13.78%
2016	8,110,017	57,299,384	14.15%
2017	8,851,816	57,170,760	15.48%
2018	7,366,644	52,022,806	14.16%
2019	4,946,050	53,662,614	9.22%

Source: Company Annual Reports

Table.2 shows that the company's sales compared to the profit realized after deducting the direct costs were in a slight growth during the first four years, as it achieved 13.78% in 2015, 14.15% in 2016, 15.48% in 2017, and 14.16% in 2018, while this percentage decreased significantly in 2019 and reached 9.22%.

Table 3. Profit Margin Ratio

Year	Net Profit	Revenue	Ratio
2015	5,240,842	68,342,932	7.67%
2016	3,519,078	57,299,384	6.14%
2017	3,927,298	57,170,760	6.87%
2018	3,237,526	52,022,806	6.22%
2019	1,582,367	53,662,614	2.95%

Source: Company Annual Reports

According to table.3, it is clear that the profit margin was the highest in 2015 reaching 7.67%, while it got decreased in the following years, in 2016, 6.14%, in 2017, 6.87%, and in 2018, 6.22%, until it reached its lowest in 2019, reaching 2.95%. This is because the net profit decreased in 2019 to RO 1.5 million while it was RO 5.2 million and the revenue decreased in 2019 to R.O. 53.6 million compared to R.O. 68.3 million in 2015.

Table 4. Operating Margin Ratio

Year	Operating income	Revenue	Ratio
2015	5,883,925	68,342,932	8.61%
2016	4,844,379	57,299,384	8.45%
2017	5,455,850	57,170,760	9.54%
2018	4,436,702	52,022,806	8.53%
2019	2,078,437	53,662,614	3.87%

Source: Company Annual Reports

Table.4 indicates that the company achieved the highest profit margin from operations in 2017 (9.54%), while in the years 2015, 2016, and 2018 it was relatively close, as it reached 8.16%, 8.45%, and 8.53% respectively. However, in the year 2019 it witnessed a significant decrease as it reached 3.87%.

Table 5. Administrative Expense to Sales Ratio

Year	Administrative Expenses	Net Sales	Ratio
2015	3,110,558	68,342,932	4.55%
2016	3,221,646	57,299,384	5.62%
2017	3,354,064	57,170,760	5.87%
2018	3,334,521	52,022,806	6.41%
2019	3,415,994	53,662,614	6.37%

Source: Company Annual Reports

It appeared from table.5 that the ratio of sales to administrative expenses of the company was at its highest in 2018 as it reached 6.41%, followed by 6.37% in 2019, and it reached similar proportions in 2016 and 2017 5.62% and 5.87% respectively, while the lowest percentage was 4.55 % in 2015.

Table 6. Selling and Distribution Expenses to Sales Ratio

Year	Selling and Distribution Expenses	Net Sales	Ratio
2015	208,973	68,342,932	0.31%
2016	240,343	57,299,384	0.41%
2017	144,998	57,170,760	0.25%
2018	163,301	52,022,806	0.31%
2019	125,188	53,662,614	0.23%

Source: Company Annual Reports

It is clear from table.6 that the ratio of selling and distribution expenses to sales recorded the highest (0.41%) in 2016, while in 2015 and 2018 it was 0.31%, and in 2017 it scored 0.25%, while 2019 recorded the lowest (0.23%).

Table 7. Labour Cost to Sales Ratio

Year	Labour Cost	Net Sales	Ratio
2015	4,691,299	68,342,932	6.86%
2016	4,620,120	57,299,384	8.06%
2017	4,750,443	57,170,760	8.31%
2018	4,805,676	52,022,806	9.24%
2019	5,271,262	53,662,614	9.82%

Source: Company Annual Reports

Table.7 shows that the ratio of labour cost to sales was in an annual increase, as it was lowest in 2015 (6.86%), and in 2016, it rose to 8.06%, in 2017 - 8.31%, and 2018 - 9.24%, until it reached its highest - 9.82% in 2019.

Table 8. Interest Coverage Ratio

Year	EBIT	Interest Expenses	Ratio
2015	5,918,176	360,374	16.42
2016	4,138,630	676,158	6.12
2017	4,732,333	723,517	6.54
2018	3,856,170	580,532	6.64
2019	1,326,951	751,486	1.77

Source: Company Annual Reports

Table.8 shows that the company had the highest ability to pay interest in 2015, equivalent to 16.42 times, but this percentage decreased in 2016 to 6.12 times, in 2017 6.54 times, and in 2018 6.64 times, until it reached its lowest in 2019 as it reached 1.77 times.

Table 9. Cost of Goods Sold Ratio

Year	Cost of Goods sold	Net Sales	Ratio
2015	58,926,075	68,342,932	86.22%
2016	49,189,367	57,299,384	85.85%
2017	48,318,944	57,170,760	84.52%
2018	44,656,162	52,022,806	85.84%
2019	48,716,614	53,662,614	90.78%

Source: Company Annual Reports

Table.9 shows that the ratio of cost of goods sold to sales was at its highest in 2019 (90.78%), while its lowest was 84.52% in 2017, and it recorded close proportions in the years 2015, 2016 and 2018, 86.22% and 85.85 % and 85.84%, respectively.

Table 10. Pre-tax Profit Margin Ratio

Year	Profit before Tax	Net Sales	Ratio
2015	5,918,176	68,342,932	8.66%
2016	4,138,630	57,299,384	7.22%
2017	4,732,333	57,170,760	8.28%
2018	3,856,170	52,022,806	7.41%
2019	1,326,951	53,662,614	2.47%

Source: Company Annual Reports

From table.10, it is clear that the pre-tax profit margin ratio was at its high (8.66%) in 2015, followed by 8.28% in 2017, whereas the company recorded close rates in 2016 and 2018 of 7.22% and 7.41%, respectively. However, this percentage decreased sharply in 2019, reaching 2.47%.

Table 11. Materials consumed to Sales Ratio

Year	Cost of direct materials	Net Sales	Ratio
2015	50,989,089	68,342,932	74.61%
2016	41,648,562	57,299,384	72.68%
2017	39,930,469	57,170,760	69.84%
2018	36,299,783	52,022,806	69.78%
2019	39,895,663	53,662,614	74.35%

Source: Company Annual Reports

Table.11 shows that the year 2018 recorded the lowest ratio of materials consumed to sales (69.78%), while the highest rate was (74.61%) in 2015. In 2019, it recorded 74.35%, which is slightly higher compared to the previous years. Overall, the cost of materials consumed to sales increased due to higher wheat prices and losses of the pasta manufacturing sector in 2019.

Observations

The company's Gross profit were increasing during the first four years, while it decreased significantly in 2019. The company achieved the highest profit margin from operations in 2017. The pre-tax profit margin was high in 2015 and decreased sharply in 2019.

The ratio of cost of goods sold to sales was high in 2019. It appears that the ratio of sales to administrative expenses in the company was at highest in 2018 while it was lowest in 2015. Materials consumed to sales was low in 2018 but the cost of materials consumed to sales has was high due to wheat prices in 2019. The selling and distribution expenses to sales recorded the highest in 2016, while recorded the lowest in 2019. Labour cost to sales was at low in 2015 and was high in 2019. The company had the highest ability to pay interest in 2015 and this percentage kept decreasing from 2016 to 2019.

Suggestions

The company should reduce the cost of sales so as to achieve increased gross profit margin. The company needs to reduce expenses so as to achieve higher profits. The company should increase its operating income by putting in place, mechanisms that could help to compete in the market. The company should focus more to manage its administrative expenses and should pay more attention towards marketing. The company should review its human resources policy towards evaluating the performance of its employees.

The company should manage to pay off its debts to win the confidence of lenders/suppliers in the future. The company should look for alternative for the raw materials such as buying wheat from the local farmers. The company should work on finding ways and means to achieve good profits so as to satisfy the shareholders.

Conclusion

Salalah Mills Company has a good position in the local market, through maintaining 40% of the market share during the past five years. However, the presence of huge competition from local companies and the entry of foreign companies in the local market has affected its share. Therefore, the company must work to introduce new strategies to market its products locally, and expand its activities in the foreign markets. The company should also work on to develop a business strategy that helps to reduce direct and indirect costs and achieve higher profits.

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