A Case Study On The Archer Daniels Midland (ADM) Company's Financial Statement Analysis: Strengths And Weaknesses

Han B. Kang, Illinois State University, USA

ABSTRACT

This article is a case study that analyzes the Archer Daniels Midland Company's financial strengths and weaknesses. The ADM is an agricultural food-processing company located in Decatur, Illinois. The firm's primary industry segments include oilseeds processing, corn processing, agricultural services and other segments, such as food and feed ingredient businesses and financial activities. The study conducts a ratio analysis that compares the ADM's key ratios to its two competitors - Corn Products International and Bunge - along with the food-processing industry. As far as turnover and return ratios are concerned, the firm seems to outperform its competitors and other firms in the industry, although its profit margins are somewhat lower. When current ratio and beta are compared to the industry average, ADM seems to be less risky. The firm has superior future earnings growth prospects in both agriculture food processing and ethanol fuel businesses. Overall, the firm can be a good investment, considering PE and other valuation ratios are considered.

Keywords: financial statement analysis, ratios, valuation

INTRODUCTION

The Archer Daniels Midland Company (NYSE: ADM) was formed in 1923 after Archer-Daniels Linseed Company acquired Midland Linseed Products Company. The ADM has been a major player of an agribusiness of milling, processing, specialty food ingredients, cocoa, etc. They trade, transport, store and process corn, oilseeds, wheat and cocoa into products for food, animal feed, chemical and energy uses. The ADM strives to meet the needs of the world's growing population. With over 550 facilities in more than 60 countries on six continents, the ADM is one of world's largest agricultural processors. The company turns crops, such as soybeans and corn, into renewable products with uses ranging from food to industrial. It is located in Decatur, Illinois and employs 28,000 workers. In May, 2009, the company completed an acquisition of the Schokinag-Schokolade-Industrie Hermann GmbH & Co. (www.adm.com)

The ADM operates using four different processes to successfully compete in this industry. The oilseed processing segment (31% of sales) extracts oils from resources like soybeans, cottonseed, sunflower seeds, canola, peanuts, and flaxseed, that can be used for food and feed products. The firm processes oilseeds and sells them in the market as raw materials for other processing. The corn processing segment (11% of sales) transforms corn into syrup, starches, glucose, dextrose, and sweeteners. These products are mostly used in the food and beverage industry, but can also be used to produce bio-products like ethanol alcohol. The agricultural services segment (46% of sales) utilizes the company's grain elevator and transportation network to buy, store, clean, and transport agricultural commodities, such as oilseeds, corn, wheat, oats, rice, barley, etc. The firm resells these commodities primarily as food and feed ingredients for the agricultural processing industry. The ADM's remaining operations (8% of sales) include food and feed ingredient businesses and financial activities. (www.reuters.com)

In the volatile industry of agricultural processing, the ADM seems to surpass its competitors in performance. The company has been able to maintain its competitive advantage throughout many difficult economic and internally stressful times. The ADM's two major competitors are Corn Products Intl, Inc. (CPO), which operates plants in 15 countries, and Bunge, Ltd. (BG), whose plants are located in over 30 countries. Cargill is another competitor, but it is a privately owned company, while other competitors are publicly traded. In order to uncover what gives the ADM its competitive edge, it is important that we analyze its financial performances and operational processes in comparison to others in the agricultural processing industry, and most importantly, to its two major publicly traded competitors - CPO and BG.

FINANCIAL OVERVIEW

The case study is based on the most recent two quarters of financial statements. The ADM had a net income of $1.7 billion for the fiscal-year-ending June 30, 2009, down 5.5% from one year ago. Revenues were almost flat year-over-year at $69.2 billion, down $0.6 billion from 2008. The firm had $1.6 billion in cash and short-term marketable security for the quarter ending June 30, 2009. The 2009 fiscal year was a bad year for the firm, but ADM did not cut dividends and actually increased it for the 77th straight year. For the first quarter ending September 30, 2009, net earnings were $496 million which translate into $0.77 earnings per share, down 53% from a year ago. Revenues for the most recent quarter were $14.9 billion, down 29% from a year ago. Operating profits were $774 million, down 34% from a year ago. These poor results were due to lower margins and production in the Oilseeds Procession units. (www.adm.com)

COMPANY QUALITY

This study discusses the company quality issue based on profitability ratios, efficiency ratios and management effectiveness ratios. Gross margin shows the amount of revenue left after all direct costs of producing goods and services are paid. Operating margin is obtained by subtracting indirect costs from gross margin. Net income margin is calculated by dividing after-tax net income by sales. Table 1, 2 and 3 present some key financial ratios for the quarter ending June, 30, 2009 while Table 4, 5 and 6 present comparable financial ratios for the most recent quarter ending September 30, 2009.

As shown in Table 1, the ADM's gross and operating margins lie between two competitors - BG and CPO. However, the ADM's net profit margin for trailing 12 months was much better than the two firms. The ADM is in the food processing industry that belongs to the consumer/non-cyclical sector. There are about 150 companies in the industry. When the ADM's gross, operating and net profit margin figures are compared to the food-processing industry average, the firm shows much lower margins, meaning that the ADM 's *agricultural* food processing is a lower profit margin business as compared to other types of food processing businesses. The ADM's low margin implies that they incur heavy costs that are associated with their production of agriculture goods and services. For the quarter ending September 30, 2009 shown in Table 4, we can have a similar conclusion that the ADM's margins are somewhat lower, although its net margin is higher than its competitors and the industry average.

The turnover ratio measures how a firm uses its resources efficiently, so it is a valid indication of efficiency ratios. As shown in the Table 1, the ADM's asset turnover ratio (2.0) is higher than BG (1.9) and CPO (1.1) for the quarter ending June 30, 2009, meaning that the ADM uses its assets more efficiently than the two competitors. Also, the ADM's asset turnover ratio is almost twice of the industry average. The ADM's inventory turnover ratio (7.3) is higher than BG (5.6), CPO (6.6) and the industry average, meaning that ADM outperforms the other companies by quickly turning their inventories into sales. On the other hand the ADM's receivable turnover ratio (7.4) is somewhat lower than BG and the industry average, meaning that ADM may have a lenient credit policy. When we consider the firm's turnover ratios for the quarter ending September 30, 2009, as shown in Table 4, a similar conclusion can be drawn. Overall, one can say that the ADM utilizes its resources more efficiently than other firms, which can be a strength of the firm.

Table 1: Company Quality (For Quarter Ending June 30, 2009)

Profitability Ratios (%)	**ADM**	**BG**	**CPO**	**Industry**	**Sector**	**S&P 500**
Gross Margin for Trailing 12 Months	5.9	4.9	14.7	28.5	44.4	45.5
Gross Margin for Past 5 Years	6.5	7.0	16.4	30.0	45.0	45.7
Operating Margin for Trailing 12 Months	3.9	0.2	4.8	9.5	16.9	14.0
Operating Margin for Last 5 Years	4.0	3.5	9.4	10.6	17.2	19.1
Pretax Margin for Trailing 12 Months	3.7	0.2	3.8	8.0	15.6	13.1
Pretax Margin for Past 5 Years	4.6	2.8	8.2	9.0	16.6	18.2
Net Margin for Trailing 12 Months	2.5	0.6	2.0	5.2	11.2	8.4
Efficiency Ratios (TTM)						
Asset Turnover	2.0	1.9	1.1	1.2	1.0	0.9
Receivables Turnover	7.4	16.4	6.3	11.7	13.1	10.1
Inventory Turnover	7.3	5.6	6.6	7.0	5.9	10.8
Revenue/Employee	$2,454,149	$1,852,844	$477,808	$680,393	$604,348	$843,303
Net Income/Employee	$60,532	$10,407	$9,436	$30,631	$70,591	$94,269
Management Effectiveness Ratios (%)						
Return on Assets for TTM	5.0	1.0	2.2	5.5	10.7	6.1
Return on Assets for Past 5 Years	6.3	5.3	6.1	6.1	11.7	8.6
Return on Investment for TTM	7.6	1.9	2.9	7.3	15.3	8.8
Return on Investment for Past 5 Years	9.4	8.8	7.7	8.7	16.5	12.3
Return on Equity for TTM	12.6	0.9	4.0	24.9	33.4	15.8
Return on Equity for Past 5 Years	15.0	14.0	11.8	21.6	27.7	20.1

Values are for the most recent quarter ending June 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus company Report, September, 2009.

Table 2: Financial Strength & Growth Rates (For Quarter Ending June 30, 2009)

Financial Strength	**ADM**	**BG**	**CPO**	**Industry**	**Sector**	**S&P 500**
Quick Ratio	1.3	0.8	1.1	0.7	0.7	1.4
Current Ratio	2.2	1.7	1.7	1.5	1.3	2.0
Total Debt to Equity	0.6	0.8	0.6	1.5	1.4	0.8
Long Term Debt to Equity	0.6	0.5	0.5	1.3	1.2	0.7
Growth Rates (%)						
Sales Growth for Most Recent Quarter vs. 1 Yr. Ago	(24.1)	(23.5)	(11.4)	(1.6)	(4.5)	(9.9)
Sales Growth for Trailing 12 Months vs. 1 Yr. Ago	(0.9)	(6.3)	(0.1)	3.5	0.5	(3.7)
Sales Growth for Past 5 Years	13.9	18.9	13.4	8.5	8.0	13.4
EPS Growth for Most Recent Quarter vs. 1 Yr. Ago	(82.8)	(58.3)	(226.3)	22.1	10.7	(16.7)
EPS Growth for Trailing 12 Months vs. 1 Yr. Ago	(5.0)	(97.3)	(71.4)	7.7	0.7	(14.0)
EPS Growth for Past 5 Years	28.3	14.7	27.0	5.9	7.2	18.2

Values are for the most recent quarter ending June 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus Company Report, September 2009

Now let's discuss management effective ratios for the quarter ending June 30, 2009 based on return on asset ratio (ROA), return on investment ratio (ROI) and return on equity (ROE) ratios. A firm's ability to operate profitably can be measured directly by its return ratios. The Table 1 shows that the ADM's ROA (5.0%) is much higher than BG (1.0%) and CPO (2.2%). Also, the ADM has an outstanding ROI ratio of 7.6%, while BG and CPO have 1.9% and 2.9%, respectively, for the trailing twelve months. Furthermore, the ADM's ROE Figure (12.6%) is much better than BG (0.9%) and CPO (4.0%) for the trailing twelve months. For the most recent quarter ending September 30, 2009 shown in Table 4, we can draw the same conclusion that the ADM's return ratios are much higher than BG, CPO and the industry average. It confirms the ADM's superiority in generating profits over the two competitors.

Table 3: Valuation Ratios & Dividends (For Quarter Ending June 30, 2009)

Valuation Ratios	**ADM**	**BG**	**CPO**	**Industry**	**Sector**	**S&P 500**
Price/Earnings for Trailing 12 Months	11.1	198.5	33.9	17.7	18.0	21.0
High Price/Earnings for Last 5 Years	26.3	206.8	34.6	28.6	30.4	31.5
Low Price/Earnings for Last 5 Years	6.3	3.2	5.7	12.4	13.3	10.1
Beta 5 Year Monthly Average	0.3	1.3	1.2	0.6	0.6	1.0
Price/Sales for Trailing 12 Months	0.3	0.2	0.6	1.0	2.0	2.2
Price/Book for Most Recent Quarter	1.4	1.2	1.5	4.8	6.7	3.6
Price/Cash Flow for Trailing 12 Months	7.8	13.2	10.9	12.1	14.1	13.8
Dividend Comparison						
Dividend Yield	1.9%	1.3%	1.9%	3.1%	3.4%	2.4%
5 Year Average Yield	0.0%	0.0%	0.0%	2.5%	2.5%	2.0%
5 Year Dividend Growth Rate	14.9%	11.4%	21.4%	5.7%	10.6%	13.0%
Payout Ratio for Trailing 12 Months	20.3	148.5	63.2	48.6	50.9	32.2

Values are for the most recent quarter ending June 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus Company Report, September 2009.

Table 4: Company Quality (For Quarter Ending September 30, 2009)

Profitability Ratios (%)	**ADM**	**BG**	**CPO**	**Industry**
Gross Margin for Trailing 12 Months	5.1	3.3	13.8	6.7
Gross Margin for Past 5 Years	6.5	7.0	16.39	33.8
Operating Margin for Trailing 12 Months	2.9	(0.3)	3.3	2.4
Operating Margin for Last 5 Years	4.0	3.5	9.4	5.5
Pretax Margin for Trailing 12 Months	2.8	(0.3)	2.2	2.3
Pretax Margin for Past 5 Years	4.6	2.8	8.2	5.8
Net Margin for Trailing 12 Months	1.8	0.3	1.0	1.7
Efficiency Ratios (TTM)				
Asset Turnover	1.9	1.8	1.2	0.3
Receivables Turnover	8.1	14.3	6.4	2.4
Inventory Turnover	7.7	6.9	7.0	1.3
Revenue/Employee	$2,232,908	$1,711,698	$463,244	$2,756,171
Net Income/Employee	$40,922	$5,849	$4,821	$55,738
Management Effectiveness Ratios (%)				
Return on Assets for TTM	3.4	0.6	1.2	1.5
Return on Assets for Past 5 Years	6.3	5.3	6.1	3.9
Return on Investment for TTM	5.0	1.1	1.6	2.3
Return on Investment for Past 5 Years	9.4	8.8	7.7	5.7
Return on Equity for TTM	8.3	1.1	2.0	4.0
Return on Equity for Past 5 Years	15.0	14.0	11.8	9.0

Values are for the most recent quarter ending September 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus company Report, November, 2009.

FINANCIAL STRENGTHS

The Table 2 reports financial strength and growth rates for the quarter ending June 30, 2009. Financial strength is related to business risk to some extent. The stronger a firm is from a financial standpoint, the less risky it is. For a comparison of the ADM's financial strength across the board, let's take a look at current ratio first. The current ratio compares a firm's total current assets relative to total current liabilities. It is a measure of a firm's ability to meet short-term obligations that need to be paid within a year or so. The ADM's current ratio (2.2) is higher than BG (1.7), CPO (1.7) and the industry average (1.5) for the quarter ending June 30, 2009, meaning that ADM's short-term solvency risk is somewhat less than other firms in the industry. The quick ratio is very similar to the current ratio, but it excludes inventories in current assets. Again, as shown in the Table 2, the ADM's quick ratio (1.3) is higher than BG (0.8), CPO (1.1) and the industry average of 0.7. A similar conclusion can be made for the quarter ending September 30, 2009 shown in Table 5; i.e., the ADM's quick and current ratios are higher than its two competitors and the industry average. It confirms that the ADM's financial risk, in terms of meeting short-term liabilities, is lower than its competitors and other firms in the food-processing industry.

Table 5: Financial Strength & Growth Rates (For Quarter Ending September 30, 2009)

Financial Strength	**ADM**	**BG**	**CPO**	**Industry**
Quick Ratio	1.4	1.2	1.1	1.2
Current Ratio	2.2	1.9	1.7	1.6
Total Debt to Equity	0.55	0.59	0.44	0.50
Long Term Debt to Equity	0.53	0.38	0.34	0.31
Growth Rates (%)				
Sales Growth for Most Recent Quarter vs. 1 Yr. Ago	(29.5)	(23.5)	(10.5)	(3.3)
Sales Growth for Trailing 12 Months vs. 1 Yr. Ago	(19.4)	(21.6)	(8.2)	1.0
Sales Growth for Past 5 Years	13.9	18.9	13.4	4.2
EPS Growth for Most Recent Quarter vs. 1 Yr. Ago	(52.5)	(4.8)	(39.6)	122.1
EPS Growth for Trailing 12 Months vs. 1 Yr. Ago	(52.0)	(97.8)	(88.5)	
EPS Growth for Past 5 Years	28.3	14.7	27.0	2.2

Values are for the most recent quarter ending September 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus Company Report, November 2009

The sales growth rates in Tables 2 and 5 indicate that ADM is worse than BG and CPO for the quarter ending June 30, 2009. However, when we look at the sales growth rate for the past five years, the ADM's sales growth rate is in line with the two competitors and is actually much better than the food-processing industry average. It seems that the ADM had bad two quarters in 2009 in sales, but it may be a temporary problem when the long-term trend of sales growth is considered. The ADM's earnings per share (EPS) growth was negative for the quarters ending June 30 and September 30, 2009. But, when we look at the EPS growth rate for the trailing twelve months and five years, ADM is in a much stronger position than the two competitors and the industry average. This is true for both quarters as shown in Tables 2 and 5. The ADM's EPS growth rate for past five years was 28.3%, whereas the industry average reached only 5.9%. As shown in Table 2, the ADM's long-term debt to equity is 60% and relatively weak in comparison to the two competitors; i.e., the BG and CPO's comparable ratio is 50%. That is the case also for the quarter ending September 30, 2009 as shown in Table 5.

Table 6: Valuation Ratios & Dividends (For Quarter Ending September 30, 2009)

Valuation Ratios	**ADM**	**BG**	**CPO**	**Industry**
Price/Earnings for Trailing 12 Months	17.8	258.3	73.6	505.2
High Price/Earnings for Last 5 Years	26.3	206.8	34.6	1.0
Low Price/Earnings for Last 5 Years	6.3	3.2	5.7	0.3
Beta 5 Year Monthly Average	0.31	1.3	1.1	0.5
Price/Sales for Trailing 12 Months	0.33	0.2	0.6	0.3
Price/Book for Most Recent Quarter	1.44	1.1	1.4	1.7
Price/Cash Flow for Trailing 12 Months	10.77	16.8	13.6	2.5
Dividend Comparison				
Dividend Yield	1.8%	1.3%	1.9%	0.1%
5 Year Average Yield	1.4%	0.9%	1.2%	1.5%
5 Year Dividend Growth Rate	14.9%	11.4%	21.4%	6.9%
Payout Ratio for Trailing 12 Months	30.6	123.6	131.4	388.4

Values are for the most recent quarter ending September 30, 2009 unless noted otherwise.
Source: Reuters ProVestor Plus Company Report, November 2009.

VALUATION

As shown in Chart 1, the ADM's 52-week stock price ranged from $21.03 to $33.00 with the price to earning (PE) ratio of 17.90 and the earnings per share (EPS) of $1.80 as of November 18, 2009 when the stock was closed at $32.20 per share. Its dividend per share is $0.56 with the dividend yield of 1.7%. When it comes to the ADM's stock and the indications of whether it is over-valued or under-valued, we need to consider several things. The PE ratios in Tables 3 and 6 are based on the trailing twelve months. The ADM's PE ratios for the trailing 12 months and last five years in Tables 3 (11.1) and 6 (17.8) are much lower than BG, CPO and the industry average. The firm's PE ratio on November 18, 2009 seems to be in line with the overall stock market average. Therefore, the ADM's PE ratio does not seem to indicate that the firm is over-valued relative to its earnings. (www.finance.yahoo.com)

Chart 1: The ADM Stock Data (November 18, 2009)

Ticker Symbol:	ADM	**Sector:**	Consumer Staples
Recent Price:	$32.20	**Industry:**	Agricultural Products
52-Week Range:	$21.03-$33.00	**Market Cap:**	20.68 Billion
P/E:	17.90	**Dividend:**	$0.56
Beta:	0.34	**Payout Ratio:**	31%
Yield:	1.78%	**Credit Rating:**	A (S&P)

Also, the firm's price to book ratio (1.4) for the quarter ending June 30, 2009 is in line with its competitors (1.2 and 1.5), but much lower than the food-processing industry average (4.8) as shown in Table 3. A similar conclusion can be drawn for the quarter ending September 30, 2009 shown in Table 6. The price to cash flow ratio is also less than its competitors and the industry average, reinforcing the notion that the firm is somewhat undervalued as compared to other firms in the industry. The ADM's beta for the five-year monthly average is only 0.3, whereas the BG and CPO's corresponding figures are 1.3 and 1.2, respectively. The ADM's beta is also lower than the industry average (0.6), indicating that ADM is not riskier than other firm in the industry. The ADM's five-year dividend growth rate (14.9%) is much higher than the industry average of 5.7%. That is the case also for the quarter ending for September 30, 2009. It implies that the firm can be a good investment opportunity, especially for long-term investors. Furthermore, the ADM is the second leading producer of ethanol in the world. Alternative fuels made by cons and soybeans have a bright future, considering the current trend toward a more environment friendly generation.

SUMMARY AND CONCLUSION

This case study analyzes the ADM's financial statements and key financial ratios for the most recent two quarters of 2009. Overall, the ADM's financial conditions are solid as compared to its main competitors, BG and CPO. One of the weaknesses that the firm has to deal with is the fact that its profit margin is somewhat lower than the food-processing industry average. As far as turnover ratios are concerned, ADM seems to outperform its leading competitors in the industry. It implies that the firm uses its resources more efficiently than others. When we look at management effective or return ratios, the firm is superior to BG and CPO in generating profits. Also, the current ratio comparison indicates that the ADM's financial risk to manage and pay off short-term debt obligations is lower than its leading competitors in the food-processing industry. The firm's beta, or overall risk, is a lot lower than the industry average. When the PE ratio and the price to book ratio are concerned, the ADM stock does not seem to be over-valued. Also, the production of alternative fuels can contribute to the firm's revenue growth in the future. We can observe a positive outlook for future growth of the company. Therefore, the firm can be a good investment, considering a low risk and a potential for a higher growth.

AUTHOR INFORMATION

Han Bin Kang is a professor at the Department of Finance, Insurance and Law, Illinois State University. He joined the University in 1983 and taught corporate finance, insurance and real estate courses. Dr. Kang's insurance research includes insurance fraud, service quality in automobile insurance, redlining, distribution systems, premiums comparisons, economies of scale, and underwriting profit cycles. He has published articles in the Journal of Banking and Finance, the Journal of Real Estate Research, the American Real Estate and Urban Economics Association Journal, Southern Business Review, the Journal of Business and Behavioral Science, Managerial Finance, etc.