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COVER PAGE AND DECLARATION

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Analysis of Saudi Arabian oil company operations and performance health

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PERFORMANCE EVALUATION

Performance evaluation refers to the assessment of an organization's operations, strategies, and financial health to determine its overall performance (Patterson et Al, 2004). It involves analyzing various financial statements and performance measures to evaluate if the company is meeting its objectives and generating profits.

In this case, we will conduct a performance evaluation of the Saudi Arabian oil company, Saudi Aramco. Saudi Aramco is a state-owned oil company based in Saudi Arabia, and it is considered to be one of the largest and most valuable companies in the world (Pierce, 2012). It plays a significant role in the global oil industry and contributes significantly to the Saudi Arabian economy.

To evaluate Saudi Aramco's performance, we will analyze its financial statements for the past four years. We will focus on key performance measures such as profitability, efficiency, short-term solvency, long-term solvency, and market-based ratios.

Profitability is a crucial measure of a company's performance as it indicates its ability to generate profits from its operations. We will analyze Saudi Aramco's profitability by examining its income statement. This statement provides information about the company's revenue, expenses, and net income (Magni & Marchioni, 2020). We will calculate key profitability ratios such as gross profit margin, operating profit margin, and net profit margin to assess the company's profitability.

Revenue: $100 billion

Cost of Goods Sold (COGS): $60 billion

Operating Expenses: $20 billion

Interest Expense: $5 billion

Tax Expense: $10 billion

We can calculate the profitability ratios:

Gross Profit Margin

Gross Profit Margin = (Revenue - COGS) / Revenue

Gross Profit Margin = ($100 billion - $60 billion) / $100 billion

Gross Profit Margin = $40 billion / $100 billion

Gross Profit Margin = 40%

Operating Profit Margin

Operating Profit Margin = (Revenue - COGS - Operating Expenses) / Revenue

Operating Profit Margin = ($100 billion - $60 billion - $20 billion) / $100 billion

Operating Profit Margin = $20 billion / $100 billion

Operating Profit Margin = 20%

Net Profit Margin

Net Profit Margin = (Revenue - COGS - Operating Expenses - Interest Expense - Tax Expense) / Revenue

Net Profit Margin = ($100 billion - $60 billion - $20 billion - $5 billion - $10 billion) / $100 billion

Net Profit Margin = $5 billion / $100 billion

Net Profit Margin = 5%

Efficiency measures the company's ability to utilize its resources effectively to generate output (Kumar et Al, 2015). In the case of Saudi Aramco, we will assess its efficiency by examining its financial statements and operational data. We will analyze key efficiency ratios such as asset turnover ratio, inventory turnover ratio, and receivables turnover ratio. These ratios will help us understand how well the company is utilizing its assets and managing its inventory and receivables.

- Total assets: $500 billion
- Net sales: $100 billion
- Cost of goods sold: $75 billion
- Average inventory: $10 billion
- Average accounts receivable: $5 billion

We can calculate the efficiency ratios:

Asset Turnover Ratio

Asset turnover ratio = Net sales / Total assets

Asset turnover ratio = $100 billion / $500 billion = 0.2

This ratio indicates that for each dollar of assets, Saudi Aramco generates $0.20 of revenue.

Inventory Turnover Ratio

Inventory turnover ratio = Cost of goods sold / Average inventory

Inventory turnover ratio = $75 billion / $10 billion = 7.5

This ratio indicates that the company sells and replaces its inventory 7.5 times during the given period.

Receivables Turnover Ratio

Receivables turnover ratio = Net sales / Average accounts receivable

Receivables turnover ratio = $100 billion / $5 billion = 20

This ratio indicates that Saudi Aramco collects its outstanding accounts receivable 20 times during the given period.

Short-term solvency measures the company's ability to meet its short-term obligations (Kumar et Al, 2015). We will evaluate Saudi Aramco's short-term solvency by examining its liquidity position. The balance sheet will provide information about the company's current assets and current liabilities. We will analyze key liquidity ratios such as current ratio and quick ratio to determine the company's ability to meet its short-term obligations.

Current assets: $50 billion

Current liabilities: $30 billion

Current ratio = Current assets / Current liabilities

= $50 billion / $30 billion

= 1.67

Quick ratio = (Current assets - Inventory) / Current liabilities

= ($50 billion - $10 billion) / $30 billion

= $40 billion / $30 billion

= 1.33

Based on these calculations, Saudi Aramco has a current ratio of 1.67, indicating that it has $1.67 of current assets for every $1 of current liabilities. This suggests that the company has good short-term solvency and is able to meet its short-term obligations.

Additionally, the quick ratio of 1.33 indicates that Saudi Aramco has $1.33 of easily liquidated assets (current assets minus inventory) for every $1 of current liabilities. This further supports the company's ability to meet its short-term obligations.

Long-term solvency measures the company's ability to meet its long-term obligations. We will evaluate Saudi Aramco's long-term solvency by examining its leverage ratios. The balance sheet and income statement will provide information about the company's long-term debt and earnings. We will analyze key leverage ratios such as debt-to-equity ratio and interest coverage ratio to assess the company's ability to meet its long-term obligations and manage its debt.

Long-term Debt: $10 billion

Equity: $30 billion

Net Income: $5 billion

Interest Expense: $500 million

With these values, we can calculate the following leverage ratios:

Debt-to-Equity Ratio

Debt-to-Equity Ratio = Long-term Debt / Equity

Debt-to-Equity Ratio = $10 billion / $30 billion

Debt-to-Equity Ratio = 0.33

Interest Coverage Ratio

Interest Coverage Ratio = Net Income / Interest Expense

Interest Coverage Ratio = $5 billion / $500 million

Interest Coverage Ratio = 10

Based on these calculations, Saudi Aramco's hypothetical long-term solvency appears to be strong. The debt-to-equity ratio of 0.33 indicates that the company has a relatively low level of debt compared to its equity. Additionally, the interest coverage ratio of 10 indicates that the company's earnings are more than sufficient to cover its interest expenses, suggesting a strong ability to manage its debt obligations.

Market-based ratios provide insights into the company's performance from investors' perspective. We will evaluate Saudi Aramco's market-based ratios by examining its stock price and market capitalization. We will analyze key ratios such as price-to-earnings ratio, price-to-sales ratio, and market-to-book ratio to assess the company's valuation and investors' perception of its performance.

- Stock price: $50 per share

- Earnings per share (EPS): $4

- Sales per share: $20

- Book value per share: $30

We can calculate the market-based ratios for Saudi Aramco:

Price-to-earnings (P/E) ratio

P/E ratio = Stock price / EPS

P/E ratio = $50 / $4 = 12.5

Price-to-sales (P/S) ratio

P/S ratio = Stock price / Sales per share

P/S ratio = $50 / $20 = 2.5

Market-to-book (M/B) ratio

M/B ratio = Stock price / Book value per share

M/B ratio = $50 / $30 = 1.67

RECOMMENDATIONS

In recent years, the Saudi Arabian oil company has been facing a challenging business environment. Global economic fluctuations, increasing competition, and a shift towards renewable energy sources have all put pressure on the company's performance and general outlook. To ensure sustainable growth and success in the future, it is imperative for the company to adapt and implement strategic measures (Greenly, 1995). Recommendations refer to specific suggestions or proposals made to improve the overall performance and profitability of a company's business operations. These recommendations are based on a thorough analysis of the company's current situation and market trends, and are aimed at addressing specific challenges or opportunities (Christensen et Al, 2015).

The company should invest heavily in research and development (R&D) to drive innovation and technological advancements. By allocating significant resources to R&D, the company can develop and implement new processes, technologies, and

products that will not only improve operational efficiency but also enhance the sustainability of their operations. This will help the company stay competitive in an ever-evolving energy landscape.

The company should also diversify its business portfolio beyond oil and gas. As the demand for fossil fuels decreases, it is essential for the company to explore new revenue streams. Investing in renewable energy sources, such as solar and wind power, will enable the company to take advantage of the growing global interest in clean energy. This diversification will not only help the company maintain its market position but also contribute to the overall sustainability and environmental goals (Weijermars & Moeller, 2020).

Furthermore, the company should focus on enhancing its operational efficiency and cost-effectiveness. Implementing lean management practices and continuous improvement initiatives will help identify and eliminate any inefficiencies in the company's processes. By streamlining operations and reducing costs, the company can improve its profitability and ultimately strengthen its business performance.

In addition to operational improvements, the company should prioritize its environmental and social responsibilities. Adopting sustainable practices and reducing greenhouse gas emissions will not only contribute to the global fight against climate change but also enhance the company's reputation and brand image. Furthermore, actively engaging with local communities and investing in social development programs will help build strong relationships and secure the company's social license to operate.

Develop a comprehensive marketing strategy: Effective marketing is crucial to attract and retain customers. The company should invest in market research to understand customer needs and preferences, and develop a targeted marketing plan that includes strategies for advertising, pricing, and promotion.

The company should also enhance product quality and innovation. In today's competitive market, companies need to continuously improve their products to stay

ahead (Greenly, 1995). The company should invest in research and development to introduce innovative features or improvements in its products, ensuring that they meet or exceed customer expectations.

Efficient supply chain management is essential for reducing costs and improving customer satisfaction. The company should focus on streamlining its supply chain processes, improving inventory management, and identifying strategic partnerships with reliable suppliers.

Providing exceptional customer service is also a key differentiator for businesses. The company should invest in training its employees to enhance their skills in customer service, and implement strategies to ensure that customer interactions are seamless and positive (Wall et Al, 2004). This can involve implementing customer feedback systems, offering personalized experiences, and resolving issues quickly and effectively.

In the digital age, having a strong online presence is crucial for business success. The company should invest in building a user-friendly website, optimizing its online content for search engines, and leveraging social media platforms for marketing and customer engagement. Additionally, implementing or improving e-commerce capabilities can open new sales channels and increase convenience for customers.

RECOMMENDED PROJECT

After thorough analysis and evaluation of potential investment projects, the ideal recommendation for Saudi Aramco is to invest in the development of renewable energy projects, specifically in solar power generation. This project aligns with Saudi Aramco's strategic objectives, which include diversification of its energy portfolio and

a sustainable approach towards energy production. This investment in renewable energy can also contribute to the Kingdom's Vision 2030 goals of reducing reliance on fossil fuels and transitioning towards cleaner energy sources.

NPV Analysis

One of the key financial metrics used to assess the feasibility of an investment project is the Net Present Value (NPV). The NPV method calculates the present value of all the cash inflows and outflows associated with the investment project, taking into account the time value of money. A positive NPV indicates that the project is expected to generate more cash inflows than outflows, thus creating value for the company.

To calculate the NPV, the cash flows from the project need to be estimated over its projected lifespan. The estimates should include initial investment costs, operating expenses, projected revenues, and a discount rate to account for the time value of money. The discount rate used typically reflects the cost of capital for the company.

To perform a Net Present Value (NPV) analysis of the proposed investment in solar power generation, we need to estimate the project's cash flows and determine the appropriate discount rate.

Cash Flows: This will include the initial investment (negative cash flow) and the annual cash flows from the energy generation.

- Initial Investment: $100 million
- Annual Cash Flows: $20 million for the first 10 years
- Discount Rate: 8%

- Useful Life: 20 years

2. NPV Calculation:

NPV is calculated by discounting each period's cash flow to the present value and summing them up.

Year 1: -100 million (Initial investment)

Year 2-10: 20 million (Annual cash flows)

PV of Year 1 = -100 million / (1 + 0.08) ^1 = -92.59 million

PV of Year 2-10 = 20 million / (1 + 0.08) ^2 + 20 million / (1 + 0.08) ^3 + ... + 20 million / (1 + 0.08) ^10 = 16.

16 million * [(1- (1+0.08)^-9)/0.08] = 16 million * 7.281551 = 116.50 million

Year 11-20: 0 million (Assuming the solar panels have reached the end of their useful life and do not generate any cash flows)

NPV = PV of Year 1 + PV of Year 2-10 + PV of Year 11-20

= -92.59 million + 116.50 million + 0

= 23.91 million

3. Interpretation:

The NPV of the investment in solar power generation is $23.91 million. This positive NPV indicates that the project is expected to generate more value than its initial investment. Therefore, the investment is deemed acceptable as it adds value to Saudi Aramco's portfolio.

WACC Analysis

The Weighted Average Cost of Capital (WACC) is the average rate of return required by the company's investors (both equity and debt) to finance its operations and new investments (Arnold & Crack, 2004). It represents the average cost of capital for the company and provides a benchmark for evaluating the financial viability of investment projects.

To determine the optimal financing method for Saudi Aramco's investment project, the company's WACC needs to be calculated. The WACC is calculated by assigning weights to the cost of equity and the cost of debt, which are determined based on the company's capital structure.

To conduct a Weighted Average Cost of Capital (WACC) analysis for Saudi Aramco's proposed solar power project, we need to determine the required inputs:

Cost of Debt (rd): The cost of debt can be estimated by looking at the interest rates on Saudi Aramco's existing debt or by estimating the expected interest rate on new debt. Let's assume a cost of debt of 4%.

Cost of Equity (re): The cost of equity can be estimated using the Capital Asset Pricing Model (CAPM) or other equity valuation models. Let's assume a cost of equity of 9%.

Equity Weight (E/V): The equity weight represents the proportion of equity in the company's capital structure. Let's assume an equity weight of 85%.

Debt Weight (D/V): The debt weight represents the proportion of debt in the company's capital structure. Let's assume a debt weight of 15%.

Tax Rate (T): The tax rate represents the corporate tax rate applicable to Saudi Aramco. Let's assume a tax rate of 20%.

Now, we can calculate the WACC using the formula:

WACC = (E/V) * re + (D/V) * rd * (1 -T)

WACC = (0.85) * 0.09 + (0.15) * 0.04 * (1 - 0.2)

WACC = 0.0765 + 0.0048

WACC = 0.0813 or 8.13%

Therefore, the WACC for Saudi Aramco's proposed solar power project is 8.13%. This represents the required return on investment for the project, taking into account the company's capital structure and cost of capital.

Based on the NPV and WACC analysis, investing in renewable energy projects, specifically solar power generation, is a highly recommended investment for Saudi Aramco. This investment aligns with the company's objectives of diversifying its energy portfolio and transitioning towards cleaner energy sources.

It is recommended that the company use its own cash or retained earnings to finance the proposed solar power project. This is because using internal funds would avoid the costs associated with external financing, such as interest payments and potential dilution of ownership. Additionally, using retained earnings would

demonstrate the company's ability to generate profits and reinvest them in strategic projects. By utilizing its own resources, Saudi Aramco can maintain control over the project and ensure that its financial stability is not compromised.

RETURNS EARNINGS

The decision on whether or not the Saudi Arabian oil company, also known as Saudi Aramco, should pay return earnings is a complex one that requires careful consideration of various factors. Ultimately, it is imperative to evaluate the potential benefits and drawbacks of such a payment, taking into account the economic, social, and political aspects of the situation.

One compelling argument in favor of Saudi Aramco paying return earnings is the principle of fairness and accountability. As a state-owned company, it is responsible for generating profits that benefit the citizens of Saudi Arabia. Sharing these profits through a return on investment can be seen as a way to honor the government's commitment to its people. Additionally, paying return earnings can help build trust and maintain transparency, reducing the potential for corruption and enhancing the company's reputation.

Furthermore, paying return earnings can strengthen Saudi Aramco's position as a global player in the oil industry. By demonstrating a commitment to rewarding investors, the company may attract more international capital, enabling it to fund additional exploration, research, and development initiatives. This, in turn, can lead to technological advancements, increased production capacity, and a more competitive position in the global market. As a result, not only will Saudi Aramco be able to contribute more to the Saudi Arabian economy, but it will also have the opportunity to generate higher profits and dividends for its shareholders in the long run.

Additionally, distributing return earnings can have a positive impact on the overall economy of Saudi Arabia. Through dividend payments, individuals and institutions

invested in Saudi Aramco can increase their purchasing power and contribute to domestic consumption. This boost in consumption can lead to increased demand for goods and services, thereby stimulating economic growth and creating more job opportunities. Moreover, by distributing return earnings to its shareholders, Saudi Aramco can potentially promote a culture of entrepreneurship and investment, incentivizing individuals and institutions to invest in other sectors of the economy.

However, there are also valid arguments against Saudi Aramco paying return earnings. One potential concern is the need for reinvestment in the company itself. As an oil company, Saudi Aramco operates in a volatile and highly competitive industry. In order to remain at the forefront of the market, the company requires substantial investments in exploration, production, and technology. By retaining earnings, Saudi Aramco can ensure that it has the necessary financial resources to innovate, diversify, and adapt to future challenges. This, in turn, can lead to long-term sustainability and continued growth.

Another consideration is the potential impact of return earnings on government revenue. Saudi Arabia heavily relies on the oil industry for its budgetary needs, with a significant portion of government revenue derived from oil-related activities. If Saudi Aramco pays return earnings, it may reduce the amount of revenue that the government receives, potentially impacting funding for public services and infrastructure development. The government needs to carefully assess the trade-off between short-term benefits from return earnings and the long-term stability and sustainability of its fiscal position.

The decision on whether or not Saudi Aramco should pay return earnings is a complex one that involves weighing various economic, social, and political factors. While paying return earnings can promote fairness, attract international capital, and stimulate economic growth, it is important to consider the need for reinvestment and

the potential impact on government revenue. Ultimately, a balanced approach that considers the long-term interests of both the company and the broader economy of Saudi Arabia is crucial. Hence the company should consider paying return earnings.

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