



Financial Analysis of Apple Inc. Based on 2021 Apple Annual Report

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Abstract. As the benchmark of electronic industry, Apple annual report has strategic importance to the whole industry, especially for the financial information. Therefore, it is significant to analyze the annual report of Apple Inc. The research topic for this essay is to analyze the corporate strategy, important ratios, revenue forecast and risk assessment by using the method of collecting related data and then making an analysis. The researching result is that Apple Inc. has strong internal control and innovation capacity, which makes Apple maintain the leading position in the electronic industry.

Keywords: Apple Inc. · financial analysis · annual report · electronic industry

1 Introduction

1.1 General Background

Apple Inc. is a well-known multinational corporation especially in the electronic industry headquartered in California, America. The Consumer electronics, computer software, online services, and personal computers are designed, developed and sold by Apple Inc. To be detailed, the Mac computers, media player iPod, the mobile phone iPhone, and the tablet computer iPad, as Apple the most famous hardware products, gains main profit in the company. Additionally, Apple also has some online services, including iCloud, iTunes Store, and App Store. The OS X and iOS operating systems, the iTunes media browser, the Safari web browser, and the iLife and iWork creativity and productivity suites are included in Apple consumer software. As for the financial report, Apple Inc. Fiscal year is ended on the last Saturday of September, last about the 52- or 53-week period.

1.2 Research Question

Our research mainly focuses on the financial analysis of Apple Inc., including its industry analysis, corporate strategy, ratio analysis, and revenue forecast.

1.3 Key Findings

Apple Inc., which takes the leading position in the electronic product industry, has a strong capacity for innovation and strict internal control. This makes Apple easier to deal with the external changing environment and risk, and their strong internal control can make them go further in the following years.

2 Industry Analysis

Apple specialized in five industries, there are smartphones, personal computers, tablets, wearables, and accessories. Apple also provides online services to consumers (1Apple Inc. Annual Report 2021).

2.1 Smartphones Industry

The smartphone industry has been developing and growing steadily (2 S. ODEA). The total units of global smartphone shipments were estimated to be around 1.43 billion units in 2022. Apple has a total 18% share in 2022 Q1, which placed Apple second in the smartphone industry. Samsung, Xiaomi, OPPO, and Vivo are the main competitors in this industry (3 Statista 2021).

2.2 Personal Computers

Global PC unit shipments rise between 2020 and 2021, due to the global pandemic. There are three operating systems in the PC industry – Windows, MacOS, and Linux. MacOS runs on Apple personal computers only. Other companies like Lenovo, HP, Dell, and Asus sell windows PC. Apple has a 9% share in total.

2.3 Wearables

In wearable industry, it can be divided into two categories, smartwatch and traditional watch. Apple Watch has a total 36.1% market share in 2022 Q1 which sells the best in the industry (4 Counterpoint Info). Other companies like Samsung, Garmin, and Fitbit also make smartwatches.

2.4 Online Services

The two main online services which Apple provided are Apple TV and Apple Music. Apple TV is a media platform that provides entertainment for customers. HBO, Netflix, and Amazon are competitors in this industry. Apple Music is a music platform and Spotify is the main competitor for Apple Music.

3 Business Analysis

3.1 Apple Porter's Five-Force Analysis

3.1.1 The Threat of New Entrants

The threat of a new entrant is relatively low for Apple, due to the high technical barriers and large capital required to enter this industry. Also, most companies in the industry already have a group of loyal customers and a positive reputation. Therefore, the new entrants have to bear the huge initial capital expenditure to support their brand development and lack of reputation in the market. Overall, the threat of new entrants is unlikely to influence the profitability of Apple (5 Kaur D.). Apple Inc. belongs to the electronic product industry, because the main product of Apple are iPhone, iPad, MAC, Watch, AirPods, because electronic products is in the scope of the high-tech industry, so the initial investments and entering costing are expensive, and the technology barrier is also high, though this industry has a huge attraction of high return.

3.1.2 Bargain Power of Suppliers

The bargaining power of suppliers is relatively weak in the market for Apple. The suppliers for Apple are throughout the world which leads to Apple having more right to choose better suppliers and having a strong position to negotiate the price with suppliers. Also, the switching cost for Apple to change alternative suppliers is low. Apple is normally the major customer for those suppliers, they do not want to lose the business with Apple which also makes them have a lower position during negotiation.

Apple has strong control of the supply chain management, which occupies the top level of the industry. As for the typical inventory control, Cook, as the CEO of Apple, called inventory “fundamentally evil”, so to reduce the amount of time inventory was on the company balance sheet “from months to days”, and they makes just-in-time that maintain 0 inventory, 0 raw materials and deliver the product by plane from production to customers directly, because overstock means capital cannot be withdrawn quickly, and high storage costs will affect the profit margin. In the early days of Apple, too many inventory gives them a huge bankruptcy risk.

3.1.3 Bargain Power of Customers

This bargain power of customers can cause a strong influence on Apple. For Apple, the customers could separate into two categories: individual customers and group business customers. The loss of individual customers is acceptable for Apple, they have low bargaining power. However, group business customers have more bargaining power. Apple could not accept losing this massive number of customers. Because the switching cost for Apple customers is low, Apple has to give more funds and capital to develop new and innovative products to keep their customers.

3.1.4 The Threat of Substitutes

There is barely a threat for Apple's products in the substitute area. For the apple watch, the substitute is a mechanical watch. People still will choose to buy a mechanical watch

for fame or interests. Because Five Forces Model focus on the industry, so the threats of substitutes refers to products from other industry. From the Apple official website, we can see that there are different kinds of electronic products, such as iPhone, iPad, MAC, Watch, AirPods and other wearables, and even TV and Home, it can be a conclusion that Apple wants their products to penetrate different kinds of peoples' life, which is unbreakable, so the threats of substitutes are on a low level.

3.1.5 Industry Rivalry

The competition in the technology market is strong for Apple. In the phone market, Apple is competing with Samsung, XiaoMi, Vivo, and Oppo. In the Computer Manufacturers market, Hp, Dell, Lenovo, and Asus are the competitors for Apple. According to Statista, in the global market share in Q1 2022, Apple was in fourth place, at 9%. Lenovo has the highest share at 23.6%

3.2 SWOT Analysis

3.2.1 Strengths

According to Forbes (6 Forbes 2020), Apple is the world's most valuable brand in 2020. High quality product and well design of the appearance forms a strong reputation and brand loyalty. Undoubtedly, Apple has significant brand awareness and market influence, and these competitive advantages are based on Apple's widely praised product quality. Apple also has excellent marketing strategies to stimulate consumers' purchase desires which is one of the important components of its success. In addition, Apple has strong Research and Development capacity, not only on the appearance design but also on product performance which take the leading position, such as the A series chips and unique IOS system.

3.2.2 Weaknesses

The high R&D expenditures every year may cause some profit risks, and some projects do not have any output. Hence, if the product cannot be accepted by the market, this high researching costs can be a burden for the profit margin, in the short term, a large quantity of capital and labour are put into some project which cannot guarantee any output, to some extent, Apple may have huge sunk costs and a financial crisis. It is a paradox to achieve strong R&D capacity with just a few R&D costs. Although it is a very huge expenditure for apple, it is very stable each year, just around 50% of total operating expenditure, so this cannot be an absolute weakness, especially in the long term, as they can make breakthrough of innovation which can increase revenue greatly.

3.2.3 Opportunity

The excellent brand effect, marketing strategy, and product quality could provide Apple with more opportunities in the future market. The target customer will increase consistently by providing customers with excellent products. Also, due to the high cost of modems from Qualcomm, Apple is trying to develop modems that will decrease the

costs. Also, Apple is only responsible for innovation and design, the production attributes to cheap suppliers which are located in the developing countries, such as Foxconn in China, as one of the subcontractors, it assembles products for apple at a very low price. In addition, different kinds of suppliers are seeking to make cooperation with Apple, which means that if they become the apple supplier, their products can gain a sufficient evidence of its good quality, so many suppliers are willing to work with Apple. This makes the Apple the huge bargain power to make decision.

3.2.4 Threats

Apple specialized in smartphones, personal computers, tablets, wearables, and accessories. Apple company not only should consider the powerful competitor–Samsung, but also should consider the threats from Xiaomi, Vivo and OPPO, as their market share increased rapidly (7 Grey B 2022). With the progression of technology, the competition become more intense. Apple needs to introduce new and innovative technology to stay ahead of other competitors. Another reason is attributable by knock off, which means they are pirated mobile phones with similar appearance and functions made by some informal and small manufacturers. Since the price is much lower than the real products, although this kind of manufacturing is illegal, it brings high profit. So knock off products with a very low quality, if they enter the market largely, can affect the apple reputation negatively.

4 Financial Analysis

4.1 Apple Inc. Important Ratios

4.1.1 Profitability

Apple margin is increasing dramatically from even 2019 to 2021. Comparing with 2020, gross margin of products increased during 2021, which is caused primarily by higher product volume, a different product portfolio, and the foreign currencies relative has become strengthened to the U.S. dollar (8 stock-analysis-on 2021). However, as for services gross margin, it grew up during 2021 which is higher than 2020, and this is mainly due to service net sales and a different service mix and improved leverage, also partially offset by higher Services costs (9 Strategy Analysis 2021) (Table 1).

Table 1. Profitability Ratios of Apple Inc.

Profitability Ratio	2021	2020	2019
Gross Profit Margin	41.779%	38.233%	37.818%
Net Profit Margin	25.882%	20.914%	21.238%
Return on Equity	1.501	0.879	/
ROCE	1.727	1.015	/

4.1.2 Liquidity

These show a negative sign: the benchmark of the current ratio is 2:1, and the ratio of Apple is much lower than the criteria. Although Apple's current assets can cover its current liabilities. However, it is not that safe because 1.075 is much lower than 2. The annual report illustrates that they believe its cash balances, cash equivalents, and marketable securities which is unrestricted. It was totaled \$172.6 billion when the day is September 25, 2021, following with cash generated by ongoing operations and having ability to get access to debt markets. These two factors will be sufficient to meet the requirements of cash and capital return over the next 12 months and beyond (Table 2).

4.1.3 Efficiency

As calculations showed, all of the holding periods are increased, which means Apple need more time to sell inventories and collect receivables, as well as extended period to pay for the supplier. Although these increases are bad signs, from the working capital cycle, we can know that Apple Co still use supplier money to invest their own projects (Table 3).

That is because Apple as the top position of this industry, which is attributable to the strong innovation and its advanced technology, it has very strong bargain power to both suppliers and customers. However, as far as I am concerned, the company should consider the early discount given by suppliers and customer goodwill, though Apple has a strong brand and reputation.

4.2 Apple Inc. Revenue Recognition

4.2.1 STEP1: Identify the Contract with Customers

Apple Inc. Links legal contracts together with customer into the sales contract.

Table 2. Liquidity Ratios of Apple Inc.

Liquidity Ratio	2021	2020
Current Ratio	1.075	1.364
Quick Ratio	1.022	1.325

Table 3. Efficiency Ratios of Apple Inc.

efficiency ratio	2021	2020
inventory days	11.277	8.742
receivables days	45.034	34.701
payable days	93.851	91.048
working capital cycle	-37.540	-47.606

4.2.2 STEP2: Identify the Separate Performance Obligations in the Contract

Apple Inc. has identified less than three performance obligations regularly, including in arrangements about the sale of iPhone, Mac, iPad and certain other products.

- PO 1: hardware and bundled software delivered at the time of sale.
- PO 2: the right to accept certain bundled services relating to product, which include iCloud®, Siri and Maps.
- PO 3: the right to receive, on a when-and-if available basis, future unspecified software upgrades relating to the software bundled with each device

4.2.3 STEP3: Determine the Transaction Price

(Which is based on the costs incurred and market research).

4.2.4 STEP4: Allocate the Transaction Price

The Company allocates revenue and any related discounts to these performance obligations based on their relative SSPs (stand-alone selling price). Because the Company lacks observable prices for the undelivered performance obligations, the allocation of revenue is based on the Company's estimated SSPs.

- Delivered both hardware and software: Apple recognized revenue when control has transferred to the customer. Usually when the Apple product is shipped, the company will recognize the revenue.
- Product-related bundled services and unspecified software upgrade rights: deferred and recognized on a straight-line basis over the estimated period they are expected to be provided.

4.2.5 STEP 5: Recognize the Revenue When a Performance Obligation is Satisfied

In conclusion, Apple's revenue recognition is complied with general principle of IFRS 15: "transfer of control". As for products net sales in most of the companies, the risk and uncertainty transfer as products are shipped. However, for the services net sales in most companies, risk and uncertainty transfers over time as services are delivered (10 Craft 2021).

4.3 Apple Inc. Revenue Forecast

4.3.1 Forecast

- Americas: $(23\% + 7\%)/2 = 15\%$
- Europe: $(30\% + 14\%)/2 = 22\%$
- Greater China: $(70\% - 8\%)/2 = 31\%$
- Japan: $(33\% + 0\%)/2 = 16.5\%$
- Rest of Asia Pacific: $(35\% + 10\%)/2 = 22.5\%$ (Table 4)

Table 4. Revenue Forecast for 2022–2026 of Apple Inc.

APPLE Inc. Revenue Forecast for 2022–2026					
\$m Revenue	2022	2023	2024	2025	2026
Americas (15%)	153,306.00	176,301.90	202,747.19	233,159.26	268,133.15
Europe (22%)	89,307.00	108,954.54	132,924.54	162,167.94	197,844.88
Greater China (31%)	68,366.00	89,559.46	117,322.89	153,692.99	201,337.82
Japan (16.5%)	28,482.00	33,181.53	38,656.48	45,034.80	52,465.54
Rest of Asia Pacific (22.5%)	26,356.00	32,286.10	39,550.47	48,449.33	59,350.43

4.3.2 Assumptions

Apple Inc. manages its business mainly on a geographic basis. Apple Inc. reportable segments consist of the Americas, Europe, Greater China, Japan, and the Rest of Asia Pacific. Though the reportable segments provide similar products of hardware and software as well as similar services, each part is managed individually to better aligned with the location of the Apple customers in each geographic region, so I use the average segment performance growth to estimate the revenue growth rate individually, which can reflect a more accurate prediction.

5 Risks Discussion

According to Apple's 2020 annual report, the popularity of COVID-19 has had a significant negative impact on the normal operation of global enterprises, including the adoption of isolation and restrictions on the import and export of goods measures by governments. In this case, this global health and safety problem has seriously hit the global economic activities, hindering the circulation of goods and greatly affecting the revenue of enterprises. Specifically, Apple Inc. closed many retailing stores and outlets during 2020 and disclosed the increased transportation and storage costs in the financial statements. Meanwhile, Apple Inc. revealed in its annual report that its internal risk assessment team has completed an effective assessment of the economic activity environment faced by the company, including the time, scope, and trajectory of the pandemic, and the impact of the vaccine epidemic on the global demand for consumer goods. In this case, Apple Inc. quickly developed corresponding strategies to deal with potential risks and minimized high expenditure costs by using online offices. Moreover, Apple Inc.'s 2021 annual report revealed that the impact of the epidemic was still persistent, affecting the company's production and operation. Specifically, in the fourth quarter of 2021, the service of some suppliers of the company was interrupted, resulting in a shortage of product supply. It can be predicted that the impact of the epidemic will hit the company's operation for a long time in the future. Hence, Apple Inc. needs to establish more sophisticated business models and sales channels, to weaken the impact of the epidemic as much as possible.

6 Conclusion

In this essay, our team has completed an overall analysis of the company's business operation, financial situation, and related risk assessment. However, the essay still has some limitations in the part of information collection and integration. Specifically, our team completes the revenue forecast for the next five years by calculating the average growth rate of each operating segment in the past two years and taking it as the future annual growth rate. In this case, we ignore the annual growth fluctuations and global health events including COVID-19 to some extent. This is because we lack the relevant internal information about the company's prediction model, so we cannot adjust the future growth rate of each operating segment in combination with the company's risk assessment of the market and the company's response strategies. Furthermore, the five-year forecast cycle amplifies the possibility of floating factors, which may cause large errors in the long-term forecast. Therefore, in future research, our team will try to collect data from multiple enterprises in the industry and establish a risk prediction model that conforms to industry characteristics. In this case, our team can minimize the negative impact of unexpected events on forecast's accuracy while considering the industry periodicity.

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