

Kimberly-Clark  
Final Project: Professional Challenge

Capella University

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By

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## Table of Contents

|   |    |
|---|----|
| Introduction:.....                              | 3  |
| Primary Business: .....                         | 3  |
| Company Background: .....                       | 3  |
| Goals .....                                     | 4  |
| Projections: .....                              | 4  |
| Management Team: .....                          | 5  |
| Thomas J. Falk* .....                           | 5  |
| Kathi P. Seifert* .....                         | 6  |
| Robert E. Abernathy* .....                      | 6  |
| Competition: .....                              | 7  |
| Bond Refunding .....                            | 9  |
| Capital Spending: Investment of Machinery ..... | 11 |
| Findings: .....                                 | 12 |
| References:.....                                | 13 |

## **Introduction:**

In this somewhat hypothetical paper, I will be reviewing the current management team and their respective abilities to meet future challenges, as well as their past successes. Also taken into consideration will be the overall health of the company—for it is rumored that Proctor & Gamble and Johnson & Johnson are preparing to merge and then try to takeover Kimberly-Clark. The Board wants to make sure that if the rumors were true, they would be financially strong enough to maintain their autonomy. There are two main analyses—scenarios—to consider as well: (1) whether to refund bonds given the current interest rate, and (2) whether to replace a machine in Spain, or Mexico (this analysis will be taken from our capital spending spreadsheet and Spain represents the old Machine A, and Mexico, B).

## **Primary Business:**

### **Company Background:**

Kimberly-Clark (KC) is a truly global corporation with a tradition spanning over 100 years. Initially started in 1872 with, “Four young businessmen, John A. Kimberly, Havilah Babcock, Charles B. Clark, and Frank C. Shattuck [and] the modest sum of \$30,000” Kimberly, Clark, and Company was founded (Kimberly-Clark Corporation 2003). KC started out as a paper products company but has expanded its operations into many business units spanning many sectors, including: Personal Care, Consumer Tissue, and Business to Business divisions. KC is a, “\$13.6 billion global consumer products company employing nearly 64,000 people worldwide. [Their] tissue, personal care and health care products are manufactured in 42 countries and sold in more than 150.” KC’s products “are home to some of the world's most trusted and recognized brands, including Kleenex, Scott, Huggies, Pull-Ups, Kotex and Depend. Kimberly-Clark was recently named to *Fortune* magazine’s list of the “100 Best Companies to Work for in America” for the second consecutive year. The company has received similar recognition in the U.K., Argentina, Australia, Korea and Thailand” (Kimberly-Clark Corporation 2003).

It is said that they were selected in part due to their commitment to the overall well-being of their employees and their wellness and developmental programs that focus on health, education financial planning services—just to name a few.

The industry, for comparison issues, will consist of Personal care products—mainly to analyze and/or present competitors in a respective setting.

### **Goals:**

The overall management strategy of KC is to, "...to deliver annual sales growth of 6-8% and increase earnings per share before unusual items at a double digit rate. K-C has succeeded in delivering increased quarterly dividends for 30 years in a row. Its goals are sales growth and cost reductions. Management remains optimistic about growth prospects and the continuing ability to increase cash flow as well as buying back K-C stock. In the last 5 years, the acquisition of Scott Paper has been fully integrated and a major restructuring of the company into 3 divisions has been completed. By pursuing a global brands approach, the company can benefit from economies of scale by leveraging R&D, manufacturing expertise, advertising and marketing costs and customer loyalty. Opportunities for volume growth lie in developing countries where national product brands are important. In the last 8 years the company has made 40 acquisitions to achieve leading market shares(Marsh 2002).

### **Projections:**

The "continuing tough competitive environment and an anticipated increase in pension costs of approximately \$145 million" are areas of concern for KC. "However, the Corporation expects net sales to rise in the low-to-mid single digits with product innovation across its three global segments as the key driver of sales growth. The Corporation also has plans to reduce costs by \$175 million to \$200 million in 2003. The Corporation expects cash flow to continue to be strong in 2003 which will allow it to repurchase approximately 2 percent of its outstanding common stock in 2003, depending on market conditions. The Corporation anticipates spending approximately \$900 million on capital projects in 2003, with most of the expenditures earmarked for projects that will deliver growth, cost savings or product improvements. The Corporation's strong cash flow has given it the ability to raise its dividend by 13.3 percent for 2003, marking the 31st consecutive annual increase in its dividend"(Kimberly-Clark Corporation 2003).

## **Management Team:**

The current management team led by Thomas Falk has managed to continue the philosophy of KC and make KC number 69 in *Fortune Magazine's* top 100 companies to work for. Last years ranking was 92. The management team's experience and resourcefulness in extraordinary and has a wide range of talent—the below portions of their biographies shows this to be true (only the top three officers will be listed).

### **Thomas J. Falk\***

**Chairman of the Board and Chief Executive Officer of Kimberly-Clark Corporation.**

Mr. Falk has worked for Kimberly-Clark since 1983, holding positions of increasing responsibility and authority. Under his leadership, the company successfully integrated Kimberly-Clark and Scott Paper operations following the merger of the two companies in late 1995. Before joining the internal audit staff of Kimberly-Clark in Neenah, Wis., in 1983, Mr. Falk was with the accounting firm of Alexander Grant & Co. He became Senior Auditor at Kimberly-Clark in 1984 and Senior Financial Analyst in 1986. He was promoted to Director of Corporate Strategic Analysis in 1987. In 1988, under Kimberly-Clark sponsorship, he earned a Master of Science degree in management as a Sloan Fellow at the Stanford University Graduate School of Business. Following graduation, he became Operations Manager for Infant Care at the Beech Island, S.C., diaper plant in 1989. In 1993, Mr. Falk was elected Group President of Infant and Child Care with responsibility for Huggies diapers, the company's best-selling product, and for Pull-Ups training pants. He became Group President of North American Consumer Products in early 1995. In this role, he led the company's consumer and professional tissue businesses, U.S. consumer sales and U.S. consumer business services. He was elected Group President – Global Tissue and Paper in 1998, adding global oversight for the company's consumer and professional tissue and wet wipes businesses to his existing responsibilities. He was elected President and Chief Operating Officer and to the company's Board of Directors in 1999. Mr. Falk was elected Chief Executive Officer in 2002 and to his position as Chairman in 2003.

**Kathi P. Seifert\*****Executive Vice President for Kimberly-Clark Corporation**

Ms. Seifert oversees the company's \$5.7 billion global personal care business, which is home to some of the world's most recognized and trusted consumer brands, including Huggies, Pull-Ups, Kotex and Depend. Ms. Seifert, who was elected to her current position in 1999, was named to *Fortune* magazine's list of the 50 Most Powerful Women in Business in 2002. She also was named to Forbes.com's annual "America's Top Businesswomen" list in 2001. Only 24 women qualified for this distinction, and Ms. Seifert was among only eight women on the Forbes.com list to hold one of the top three executive positions at their company. Ms. Seifert joined Kimberly-Clark as a product manager in the then Away-From-Home Sector in 1978 and advanced through a number of marketing positions of increasing scope and responsibility in the company's household products and feminine care businesses. She was appointed Marketing Director of Feminine Care Products in 1989, and was named President of the Feminine Care Sector in 1992. In 1994, Ms. Seifert was elected Group President of Feminine and Adult Care and later that year was appointed Group President of North American Consumer Products. She was elected Group President of North American Personal Care Products in 1995.

In 1998, she was appointed Group President of Personal Care Products and was elected Group President of Global Personal Care Products the following year. Prior to joining Kimberly-Clark, Ms. Seifert held management positions at Procter & Gamble, Beatrice Foods and Fort Howard Paper Company.

**Robert E. Abernathy\*****Group President - Business To Business**

Business To Business includes the K.C. Professional, Health Care, Neenah Paper, Technical Paper and Nonwovens businesses. K.C. Professional products include washroom, wipers and skincare products. The Healthcare business products include surgical drapes, gowns, exam gloves, face masks, and respiratory care products. The Neenah Paper products include writing, stationery and publication papers.

The Technical Paper business includes industrial papers used in adhesive and abrasive products. The Nonwovens business includes materials manufactured for consumer personal care products and other applications like filtration, wipers and car covers.

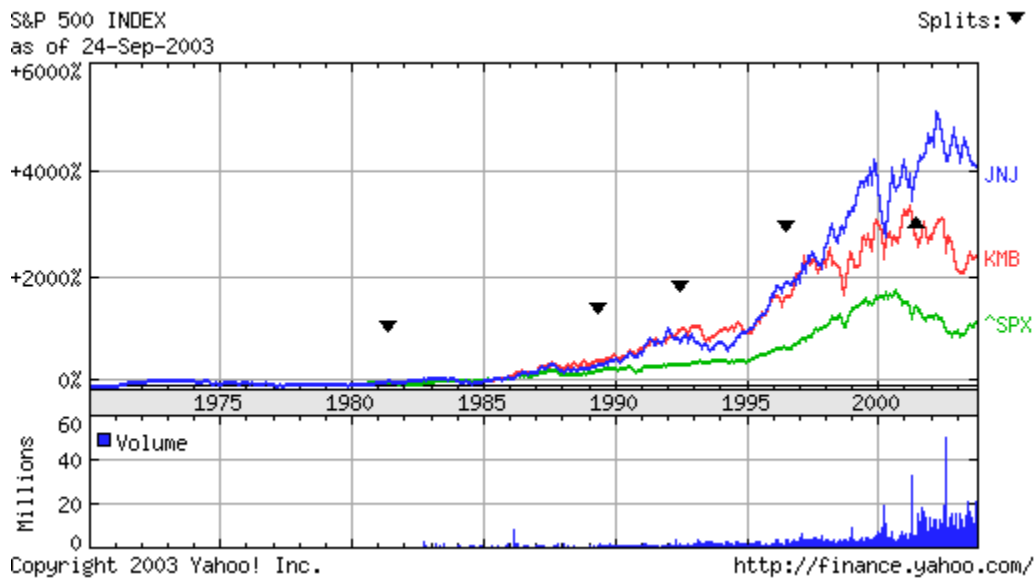
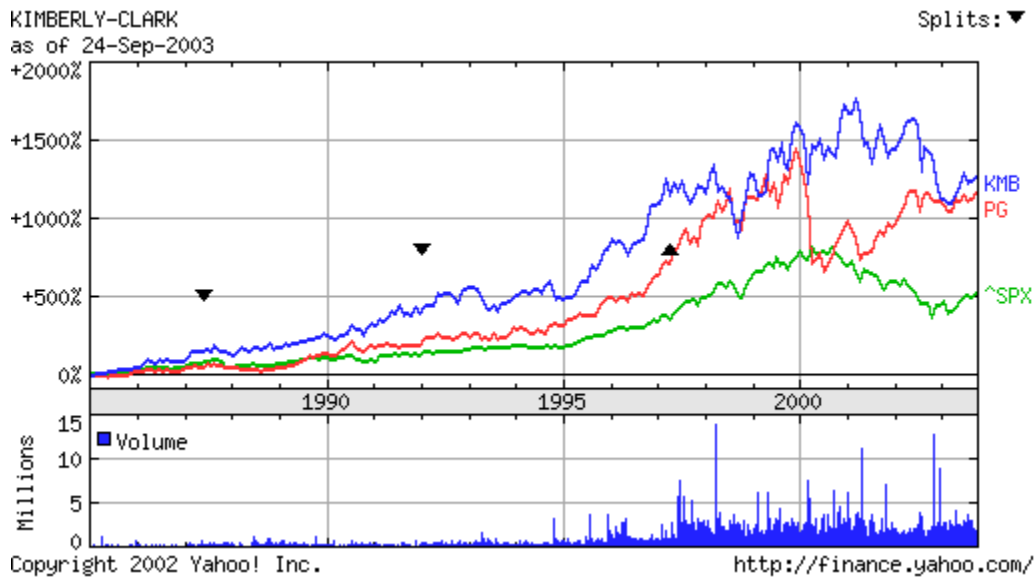
Mr. Abernathy joined Kimberly-Clark in 1982 as a research scientist and later held management positions in the company's diaper and tissue operations. He held plant manager positions at Beech Island, S.C. and Jenks, Oklahoma before being named Vice President of Diaper Operations in 1992. He was elected to Managing Director for Kimberly-Clark Australia the following year. In 1996, he was elected Group President - Kimberly-Clark and in 1998, he was appointed to his current position.

\*(Kimberly-Clark Corporation 2003)

## **Competition:**

The major competitors in the field of consumer durables and consumables are Johnson & Johnson (JNJ) and Proctor & Gamble (PG). They are led by competent CEOs that have continued to build their companies financial structure. Alan Lafley of PG has increased the value of stocks by over 40% in recent years, and under the leadership of Ralph Larson (retried in July) of JNJ, its value increased ten-fold in a ten year period. Together these two very strong and highly competitive companies bring in a combined \$80 Billion a year in revenues and have an ROE of 31.96% and 42.07% respectively. Furthermore their ROAs average out to approximately 15%. In comparison to KC their ratios are slightly higher; however, the overall cash flows and balance sheet totals, as well as their cash reserves, are healthy.

Below find market comparisons in chart form of the performance of KC and competitors.



(Yahoo Inc. 2003)

As the above graph indicated, KC has outperformed the ^SPX in all the most recent years and rivals competition. JNJ has an improved performance ration; however, pharmaceuticals play a large role in that increase.

The following table shows the details of KC's key ratios.

| Key Ratios & Statistics     |           |                           |       |
|-----------------------------|-----------|---------------------------|-------|
| <b>Price &amp; Volume</b>   |           | <b>Valuation Ratios</b>   |       |
| Recent Price \$             | 50.24     | Price/Earnings (TTM)      | 15.87 |
| 52 Week High \$             | 61.05     | Price/Sales (TTM)         | 1.87  |
| 52 Week Low \$              | 42.92     | Price/Book (MRQ)          | 4.03  |
| Avg Daily Vol (Mil)         | 1.595     | Price/Cash Flow (TTM)     | 11.24 |
| Beta                        | 0.444     |                           |       |
| <b>Share Related Items</b>  |           | <b>Per Share Data</b>     |       |
| Mkt. Cap. (Mil) \$          | 25,454.15 | Earnings (TTM) \$         | 3.17  |
| Shares Out (Mil)            | 506.65    | Sales (TTM) \$            | 26.93 |
| Float (Mil)                 | 504.70    | Book Value (MRQ) \$       | 12.47 |
|                             |           | Cash Flow (TTM) \$        | 2.32  |
|                             |           | Cash (MRQ) \$             | 0.74  |
| <b>Dividend Information</b> |           | <b>Mgmt Effectiveness</b> |       |
| Yield %                     | 2.71      | Return on Equity (TTM) %  | 27.21 |
| Annual Dividend \$          | 1.36      | Return on Assets (TTM) %  | 9.94  |
| Payout Ratio (TTM) %        | 40.32     |                           |       |
| <b>Financial Strength</b>   |           | <b>Profitability</b>      |       |
| Quick Ratio (MRQ)           | 0.56      | Gross Margin (TTM) %      | 34.40 |
| Current Ratio (MRQ)         | 1.08      | Operating Margin (TTM) %  | 17.07 |
| LT Debt/Equity (MRQ)        | 0.44      | Profit Margin (TTM) %     | 11.28 |
| Total Debt/Equity (MRQ)     | 0.60      |                           |       |

(Pinnacorp Inc. 2003)

## Bond Refunding

Regarding the issue of refunding outstanding bonds and reissuing at the current 10% interest rate for duration of 15 years proves to be uneconomical. The following chart gives the details and illustrates why KC should not call the bonds for refunding purposes.

(Thousands of US dollars)

|                                   |                  |                                 |                  |
|-----------------------------------|------------------|---------------------------------|------------------|
| <b>Existing bond issue</b>        | <b>\$288,000</b> | <b>New bond issue</b>           | <b>\$288,000</b> |
| <b>Original flotation cost</b>    | <b>\$18,000</b>  | <b>New flotation cost</b>       | <b>\$14,400</b>  |
| <b>Maturity of original debt</b>  | <b>32</b>        | <b>New bond maturity</b>        | <b>15</b>        |
| <b>Years since old debt issue</b> | <b>16</b>        | <b>New cost of debt</b>         | <b>10%</b>       |
| <b>Call premium (%)</b>           | <b>10%</b>       |                                 |                  |
| <b>Original coupon rate</b>       | <b>6%</b>        | <b>Tax rate</b>                 | <b>40%</b>       |
| <b>After-tax cost of new debt</b> | <b>6.0%</b>      | <b>Short-term interest rate</b> | <b>5%</b>        |

### Schedule of cash flows

|   | Before-tax | After-tax  |
|---|------------|------------|
| <i>Investment</i>                                   |            |            |
| <i>Outlay</i>                                       |            |            |
| Call premium on the old bond                        | (\$28,800) | (\$17,280) |
| Flotation costs on new issue                        | (14,400)   | (14,400)   |
| Immediate tax savings on old flotation cost expense | 9,000      | 3,600      |
| Extra interest paid on old issue                    | (1,440)    | (864)      |

|  |              |                   |
|--|--------------|-------------------|
| Interest earned on short-term investment               | 1,200        | 720               |
| Total after-tax investment                             |              | <b>(\$28,224)</b> |
| <i>Annual Flotation Cost Tax Effects: t=1 to 15</i>    |              |                   |
| Annual tax savings from new issue flotation costs      | \$960        | \$384             |
| Annual lost tax savings from old issue flotation costs | <b>(563)</b> | <b>(225)</b>      |
| Net flotation cost tax savings                         | \$398        | <b>\$159</b>      |

*Annual Interest Savings Due to Refunding: t=1 to 15*

|                      |                   |                  |
|----------------------|-------------------|------------------|
| Interest on old bond | \$17,280          | \$10,368         |
| Interest on new bond | <b>(28,800)</b>   | <b>(17,280)</b>  |
| Net interest savings | <b>(\$11,520)</b> | <b>(\$6,912)</b> |

**Calculating the annual flotation cost tax effects and the annual interest savings**

| <u>Annual flotation Cost Tax Effects</u> |                | <u>Annual Interest Savings</u>    |                   |
|--|----------------|-----------------------------------|-------------------|
| Maturity of the new bond (Nper)          | 15             | Maturity of the new bond (Nper)   | 15                |
| After-tax cost of new debt (Rate)        | 6.0%           | After-tax cost of new debt (Rate) | 6.0%              |
| Annual flotation cost tax savings (Pmt)  | \$159          | Annual interest savings (Pmt)     | (\$6,912)         |
| NPV of annual flotation cost savings     | <b>\$1,544</b> | NPV of annual interest savings    | <b>(\$67,131)</b> |

Hence, the net present value of this bond refunding project will be the sum of the initial outlay and the present values of the annual flotation cost tax effects and interest savings.

$$\begin{aligned}
 \text{Bond Refunding NPV} &= \text{Initial Outlay} + \text{PV of flotation costs} + \text{PV of interest savings} \\
 \text{Bond Refunding NPV} &= \text{\$28,224} + \text{\$1,544} + \text{\$67,131} \\
 \text{Bond Refund NPV} &= \text{\$93,810.817}
 \end{aligned}$$

## Capital Spending: Investment of Machinery

| Invoice Price                 | Shipping Installation | Inventory Increase | Accounts Payable Increase | Project Life | Salvage Value | Incremental Revenues | MACRS Class |
|-------------------------------|-----------------------|--------------------|---------------------------|--------------|---------------|----------------------|-------------|
| <b>Machine-A</b><br>\$100,000 | \$20,000              | \$10,000           | \$10,000                  | 5-years      | \$10,000      | \$100,000            | 3           |
| <b>Machine-B</b><br>\$100,000 | \$20,000              | \$10,000           | \$10,000                  | 5-years      | \$10,000      | \$ 500,000           | 3           |

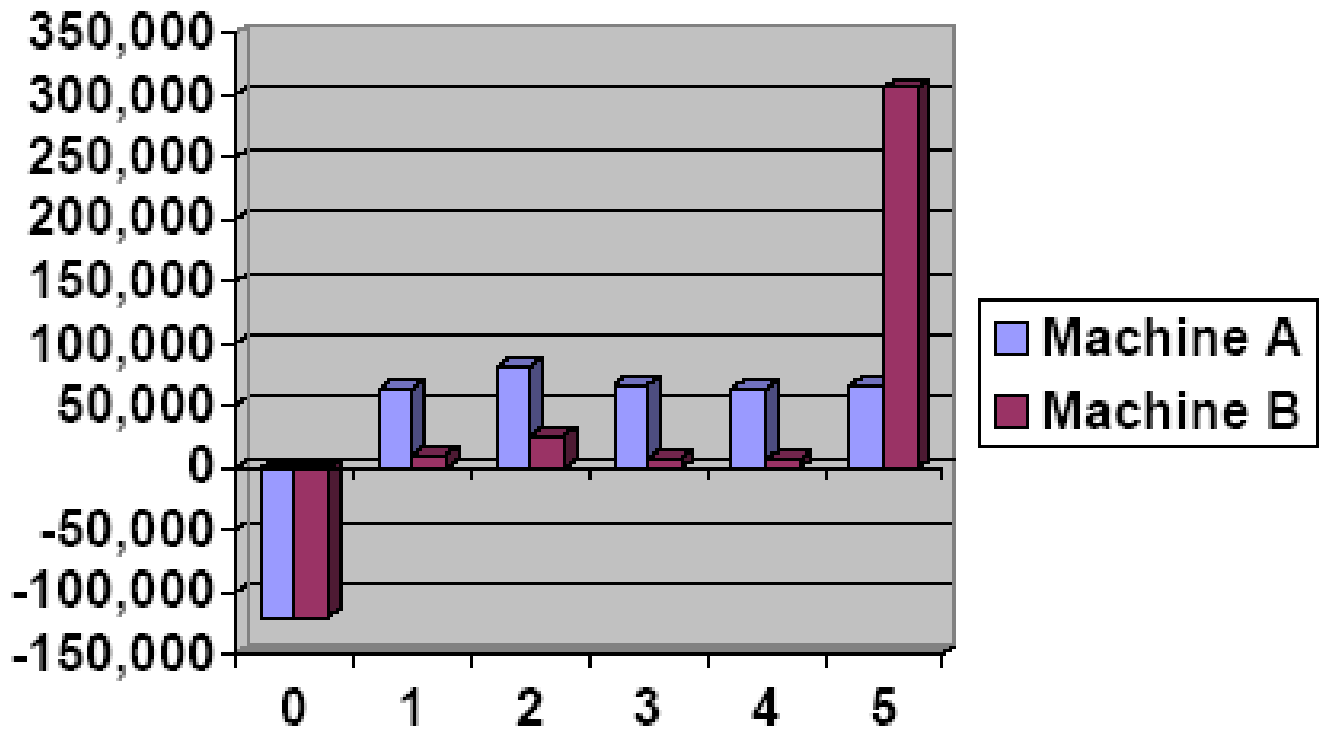
(year-5 only)

Tax rate= 40%

Discount rate= 20%

Cash Flows for Year:

|                        | 0                | 1          | 2          | 3         | 4         | 5         |
|------------------------|------------------|------------|------------|-----------|-----------|-----------|
| <b>Machine A</b>       |                  |            |            |           |           |           |
| Investment             | \$ (120,000)     |            |            |           |           |           |
| EBITD                  |                  | \$100,000  | \$100,000  | \$100,000 | \$100,000 | \$100,000 |
| Depreciation           |                  | \$40,000   | \$53,333   | \$17,778  | \$8,889   | \$0       |
| Taxes @ 40%            |                  | \$36,800   | \$18,667   | \$32,889  | \$36,444  | \$40,000  |
| After tax gain on Sale |                  | \$0        | \$0        | \$0       | \$0       | \$8,000   |
| Total Incr. Cash Flows | \$ (120,000)     | \$63,200   | \$81,333   | \$67,111  | \$63,556  | \$66,000  |
| Discount factors       | 1.00             | 0.83       | 0.69       | 0.58      | 0.48      | 0.40      |
| <b>NPV&gt;</b>         | <b>\$179,061</b> |            |            |           |           |           |
| <b>IRR&gt;</b>         | <b>78.77%</b>    |            |            |           |           |           |
| Total Paid Back        | \$(120,000)      | \$63,200   | \$144,533  | \$211,644 | \$275,200 | \$341,200 |
| <b>Payback&gt;</b>     | <b>1.7</b>       |            |            |           |           |           |
| <b>Machine B</b>       |                  |            |            |           |           |           |
| Investment             | \$ (120,000)     |            |            |           |           |           |
| EBITD                  |                  | \$0        | \$0        | \$0       | \$0       | \$500,000 |
| Depreciation           |                  | \$40,000   | \$53,333   | \$17,778  | \$8,889   | \$0       |
| Taxes @ 40%            |                  | (\$10,720) | (\$25,621) | (\$7,111) | (\$3,556) | \$200,000 |
| After tax gain on Sale |                  | \$0        | \$0        | \$0       | \$0       | \$8,000   |
| Total Incr. Cash Flows | \$ (120,000)     | \$(10,720) | \$(25,621) | \$(7,111) | \$(6,400) | \$306,000 |
| Discount factors       | 1.00             | 0.83       | 0.69       | 0.58      | 0.48      | 0.40      |
| <b>NPV&gt;</b>         | <b>\$80,938</b>  |            |            |           |           |           |
| <b>IRR&gt;</b>         | <b>33%</b>       |            |            |           |           |           |
| Total Paid Back        | \$(120,000)      | \$10,720   | \$36,341   | \$43,452  | \$49,852  | \$355,852 |
| <b>Payback&gt;</b>     | <b>4.56</b>      |            |            |           |           |           |



Based upon the current rating and history of Kimberly-Clark, choice, machine, (A) would be a more stable and suitable investment because it begins to yield results immediately and the NPV and IRR are greater, while the payback period is less than 2 years.

Furthermore, the total taxes paid out over the total 5-year period is approximately \$40,000 less when choosing (A), the machine in Spain, over (B), the machine in Mexico. My recommendation would be to invest in (A) and give investors the immediate returns on this particular investment. Continued stable returns on this smaller investment can hedge against other losses.

## Findings:

Kimberly-Clark Corporation is financially healthy and stable and has an excellent management team that is very capable of making decisions that benefit the company, as well as take the consumer's interests and the stakeholder's interests. Competition is strong, yet KC's products are known for their quality and performance. Overall, KC's outlook is very bright.

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