

## Chapter 2—Financial Statement and Cash Flow Analysis

### MULTIPLE CHOICE

1. Which of the following items can be found on an income statement?
- Accounts receivable
  - Long-term debt
  - Sales
  - Inventory

ANS: C                      PTS: 1                      DIF: E                      REF: 2.1 Financial Statements  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

2. If you only knew a company's total assets and total debt, which item could you easily calculate?
- Sales
  - Depreciation
  - Total equity
  - Inventory

ANS: C                      PTS: 1                      DIF: E                      REF: 2.1 Financial Statements  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

3. How do we calculate a company's operating cash flow?
- EBIT - taxes + depreciation
  - EBIT - taxes - depreciation
  - EBIT + taxes + depreciation
  - EBIT - Sales

ANS: A                      PTS: 1                      DIF: E                      REF: 2.2 Cash Flow Analysis  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

4. Holding all other things constant, which of the following represents a cash outflow?
- The company sells a machine.
  - The company acquires inventory.
  - The company receives a bank loan.
  - The company increases accounts payable.

ANS: B                      PTS: 1                      DIF: E                      REF: 2.2 Cash Flow Analysis  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

5. Which of the following is a liquidity ratio?
- Quick ratio
  - P/E- ratio
  - Inventory turnover
  - Equity multiplier

ANS: A                      PTS: 1                      DIF: E  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Bavarian Sausage, Inc.

**Bavarian Sausage, Inc.**

Bavarian Sausage, Inc. posted the following balance sheet and income statement.

<b>Balance Sheet</b>			
Cash	\$ 50,000	Accounts Payable	\$185,000
Accounts Receivable	125,000	Notes Payable	125,000
Inventories	225,000	Long-term debt	115,000
Net Plant and Equipment	<u>525,000</u>	Common Stock	350,000
		Retained earnings	<u>150,000</u>
Total Assets	<u>\$925,000</u>	Total liabilities and Stockholders' Equity	<u>\$925,000</u>

<b>Income Statement</b>	
Sales	\$525,000
Cost of goods sold	215,000
Depreciation	<u>65,000</u>
Earnings before interest and taxes	245,000
Interest expense	<u>35,000</u>
Net profit before taxes	210,000
Taxes (@ 40%)	<u>84,000</u>
Net income	<u>\$126,000</u>

NARREND

6. What is Bavarian Sausage, Inc.'s operating cash flow?
- \$394,000
  - \$191,000
  - \$212,000
  - \$359,000

ANS: C

$$245(1-.4)+65=212$$

PTS: 1                    DIF: E                    REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

7. What is Bavarian Sausage, Inc.'s quick ratio?
- 0.5645
  - 1.2903
  - 1.9565
  - 0.8871

ANS: A

$$(CA-INV)/CL$$

$175/310=.5645$

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

8. What is Bavarian Sausage, Inc.'s average collection period?
- 14.39 days
  - 4.20 days
  - 122.56 days
  - 86.90 days

ANS: D  
ACP=AR/ADS  
ADS=SALES/365==>525/365=1.4384  
ACP=125/1.4384=86.90

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

9. Bavarian Sausage, Inc. has 100,000 shares of common stock outstanding, but no preferred stock. The current price of Bavarian's common stock is \$15. What is the company's P/E-ratio?
- 119.00
  - 1.26
  - 11.90
  - 12.60

ANS: C  
P/E=Price/EPS  
EPS=Earnings Av. Shareholders/# Shares Outstanding  
EPS=126,000/100,000=1.26  
P/E=15/1.26=11.90

PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

10. What is Bavarian Sausage, Inc.'s net profit margin?
- 40%
  - 47%
  - 15%
  - 24%

ANS: D  
NPM=NI/Sales=126/525=.24

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

11. What is Bavarian Sausage, Inc.'s debt-equity ratio?
- 0.23
  - 0.52
  - 1.25
  - 0.85

ANS: A

$$\text{LTD/Eq.} = 115 / (350 + 150) = .23$$

PTS: 1 DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

12. Calculate Bavarian Sausage, Inc.'s return on assets.
- 25.20%
  - 16.35%
  - 13.62%
  - 8.47%

ANS: C

$$\text{ROA} = \text{NI/TA} = 126 / 925 = .1362$$

PTS: 1 DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

13. If Bavarian Sausage, Inc. has 100,000 shares outstanding, what is the book value per share?
- \$5.00
  - \$9.25
  - \$3.50
  - \$1.50

ANS: A

$$\text{BV/Share} = (350 + 150) / 100 = 5.00$$

PTS: 1 DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

14. Calculate Bavarian Sausage, Inc.'s inventory turnover.
- 1.05
  - 0.96
  - 0.76
  - 1.51

ANS: B

$$\text{Inv. Turn} = \text{CGS/Inv} = 215 / 225 = .96$$

PTS: 1 DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

15. Calculate Bavarian Sausage, Inc.'s return on equity.
- a. 24.00%
  - b. 13.62%
  - c. 15.74%
  - d. 25.20%

ANS: D

$$126/(150+350)=.2520$$

PTS: 1                    DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

16. What is Bavarian Sausage, Inc.'s times interest earned ratio?
- a. 3.60
  - b. 7.00
  - c. 15.00
  - d. 6.00

ANS: B

$$\text{time interest earned}=\text{EBIT}/\text{Interest}=245/35=7.00$$

PTS: 1                    DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

17. If a company's net profit margin is 5% and its total asset turnover is 3.5, what is its ROA?
- a. 17.50%
  - b. 1.43%
  - c. 70.00%
  - d. 12.53%

ANS: A

$$\text{ROA}=\text{Net profit margine} * \text{Invintory turnover}$$

$$\text{ROA}=.05*3.5=.1750$$

PTS: 1                    DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

18. You have the following information about a firm: total asset = \$350,000; common stock equity = \$175,000; ROE = 12.5%. What is the firm's earnings available for common stockholders?
- a. \$43,750
  - b. \$21,875
  - c. \$50,000
  - d. \$47,632

ANS: B

$$.125*175,000=21,875$$

PTS: 1                    DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Tax table

**Tax Table**

<b>Taxable income over</b>	<b>Not over</b>	<b>Tax Rate</b>
\$ 0	\$ 50,000	15%
50,000	75,000	25%
75,000	100,000	34%
100,000	335,000	39%
335,000	10,000,000	34%
10,000,000	15,000,000	35%
15,000,000	18,333,333	38%
18,333,333	.....	35%

NARREND

19. Refer to Tax Table. First Watch, Inc. has a pretax income of \$3,755,250. What is the company's average tax rate?
- a. 25%
  - b. 15%
  - c. 39%
  - d. 34%

ANS: D

PTS: 1

DIF: E

REF: 2.4 Corporate Taxes

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

20. Refer to Tax Table. First Watch, Inc. has a pretax income of \$3,755,250. What is the company's tax liability?
- a. \$1,276,785
  - b. \$1,390,571
  - c. \$1,464,548
  - d. \$563,288

ANS: A

Tax on excess over 335,000 =>  $(3,755,250 - 335,000) \times .34 = 1,162,885$

Tax =  $1,162,885 + 91,650 + 8,500 + 6,200 + 7,500 = 1,276,785$

PTS: 1

DIF: E

REF: 2.4 Corporate Taxes

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

21. Refer to Tax Table. Bavarian Sausage, Inc. has a pretax income of \$325,000. What is the company's tax liability?
- a. \$126,750
  - b. \$110,000
  - c. \$81,250
  - d. \$325,000

ANS: B

Tax on excess of 100,00 =>  $(325,000 - 100,00) \times .39 = 87,750$

Tax =  $87,750 + 8,500 + 6,250 + 7,500 = 110,000$

PTS: 1                    DIF: E                    REF: 2.4 Corporate Taxes  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

22. Refer to Tax Table. Bavarian Sausage, Inc. has a pretax income of \$325,000. What is the company's marginal tax rate?
- 34%
  - 39%
  - 35%
  - 25%

ANS: B                    PTS: 1                    DIF: E                    REF: 2.4 Corporate Taxes  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

23. Refer to Tax Table. Bavarian Sausage, Inc. has a pretax income of \$325,000. What is the company's average tax rate?
- 39.00%
  - 29.55%
  - 26.75%
  - 33.85%

ANS: D  
Tax on excess of 100,00=>  $(325,000-100,00) \cdot .39=87,750$   
Tax =  $87,75+8,500+6,250+7,500=110,000$   
 $110/325=.3385$

PTS: 1                    DIF: E                    REF: 2.4 Corporate Taxes  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

24. A company has an average collection period of 52 days and accounts receivables of \$250,000. What are the company's annual sales?
- \$2,234,756
  - \$1,754,808
  - \$1,543,823
  - \$250,000

ANS: B  
Annual Sales/365 = Av. daily sales  
AR = ACP \* Av. daily sales  
 $250,000 = 52 * (\text{Annual sales}/365)$   
Annual sales = 1,754,807

PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

25. Your company has an average collection period of 40 days and accounts receivables of \$315,000. What are the company's annual sales?
- \$12,600,000
  - \$1,754,808
  - \$2,874,375

d. \$315,000

ANS: C

Annual Sales/365 = Av. daily sales

AR = ACP \* Av. daily sales

315,000 = 40 \* (Annual sales/365)

Annual sales = 2,874,375

PTS: 1 DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

26. A company has a total asset turnover of 2 and sales of \$500,000. What is the company's total assets?
- \$1,000,000
  - \$250,000
  - \$750,000
  - \$500,000

ANS: B

$500/2=250$

PTS: 1 DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

27. You have the following information about a company: quick ratio = 0.85, inventory = \$125,000 and current assets = \$375,000. What is the company's current ratio?
- 0.85
  - 1.05
  - 2.56
  - 1.28

ANS: D

Current Ratio = CA/CL

Quick Ratio = (CA-Inv)/CL

$.85=(375-125)/CL$

CL=194

Current Ratio= $375/194=1.28$

PTS: 1 DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

28. You have the following information about a company: quick ratio = 0.9, inventory = \$50,000 and current assets = \$200,000. What is the company's current ratio?
- 3.60
  - 1.80
  - 1.20
  - 1.28

ANS: C

Current Ratio = CA/CL



Quick Ratio = (CA-Inv)/CL  
.9=(200-50)/CL  
CL=166.67  
Current Ratio=200/166.67=1.20

PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

29. A company has sales of \$1,250,000, cost of goods sold of \$750,000, depreciation expenses of \$250,000 and interest expenses of \$55,000. If the company's tax rate is 34% and the income statement is complete, what is this firm's operating cash flow?
- a. \$183,700
  - b. \$433,700
  - c. \$165,000
  - d. \$415,000

ANS: B  
 $(1,250 - 750 - 250) * (1 - .34) + 250 = 415$

PTS: 1                    DIF: M                    REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

30. A company has sales of \$1,000,000, cost of goods sold of \$700,000, depreciation expenses of \$250,000 and interest expenses of \$55,000. If the company's tax rate is 34% and the income statement is complete, what is this firm's operating cash flow?
- a. \$300,000
  - b. \$246,700
  - c. \$283,000
  - d. \$33,000

ANS: C  
 $(1,000 - 700 - 250) * (1 - .34) + 250 = 283$

PTS: 1                    DIF: M                    REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

31. A company has sales of \$250,000, cost of goods sold of \$50,000, depreciation expenses of \$250,000. If the company's tax rate is 34% and the income statement is complete, what is this firm's operating cash flow?
- a. -\$132,000
  - b. \$118,000
  - c. \$217,000
  - d. \$283,000

ANS: C  
 $(200 * .66) + (250 * .34) = 217$   
alt  
 $(250 - 50 - 250) * .66 + 250 = 217$

PTS: 1                    DIF: M                    REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

32. In a given year a company decreased its inventory by \$250,000, increased its accounts receivable by \$50,000 and increased its accounts payable by \$100,000. What is the net change of the company's cash?
- a. \$400,000
  - b. \$300,000
  - c. \$200,000
  - d. \$100,000

ANS: A

$$250+50+100=400$$

PTS: 1

DIF: M

REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

33. In a given year a company decreased its inventory by \$250,000, purchased \$350,000 worth of fixed assets and took on a new \$500,000 loan. What is the net change of the company's cash as a result of these transactions?
- a. \$100,000
  - b. -\$100,000
  - c. \$400,000
  - d. -\$400,000

ANS: C

$$250-350+500=400$$

PTS: 1

DIF: M

REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

34. Given the following information, calculate the company's Current Assets.

Current assets:	???
Current liabilities:	\$ 50,000
Net fixed assets:	\$100,000
Long term Debt	
	\$100,000
Total equity:	\$180,000

- a. \$330,000
- b. \$230,000
- c. \$150,000
- d. \$50,000

ANS: D

$$TL=CL+LTD+TE$$

$$TL=50+100+180=330$$

$$TA=TL$$

$$TA=CA+NFA$$

$$TA=CA+100$$

$$330=CA+100$$

$$CA=230$$

PTS: 1                    DIF: E                    REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

35. Given the following information, calculate the company's long-term debt.

Current assets:	\$125,000
Current liabilities:	\$ 85,000
Net fixed assets:	\$250,000
Total equity:	\$200,000

- a. \$375,000
- b. \$50,000
- c. \$285,000
- d. \$90,000

ANS: D

Total Assets = 125+250=375

TA = TL + Equity

TL = CL + LTD

375 = 85 + LTD + 200

LTD = 90

PTS: 1                    DIF: E                    REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

36. Financial professionals prefer to focus on an accounting approach that focuses on
- a. governmental accounting methods.
  - b. current and prospective cash flows.
  - c. economically based accruals.
  - d. international accrual accounting standards.

ANS: B                    PTS: 1                    DIF: E                    REF: Introduction

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

37. Generally accepted accounting principles are developed by
- a. the Securities and Exchange Commission.
  - b. the Financial Accounting Standards Board.
  - c. Congress.
  - d. the New York Stock Exchange.

ANS: B                    PTS: 1                    DIF: E                    REF: 2.1 Financial Statements

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

38. Which of the following statements is not required by the SEC for publicly traded firms?
- a. the statement of cost of goods sold
  - b. the statement of retained earnings
  - c. the statement of cash flows
  - d. the balance sheet

ANS: A                    PTS: 1                    DIF: E                    REF: 2.1 Financial Statements

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

39. The balance sheet entry that represents the cumulative total of the earnings that a firm has reinvested since its inception is
- common stock.
  - paid-in-capital.
  - par value.
  - retained earnings.

ANS: D                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

40. Company X had sales of \$120 with a cost of goods sold equal to 25% of sales. In addition, X had total other operating expenses of \$50 with an interest expense of \$20. If X pays a flat 40% of its pre-tax income in income taxes, what is X's net income?
- \$20
  - \$27
  - \$12
  - none of the above

ANS: C  
 $(120 - 30 - 50 - 20) * .6 = 12$

PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

41. If you are looking to review a firm's sources and uses of cash flows over the year, the easiest place to find that information is
- the Income Statement
  - the Statement of Retained Earnings
  - the Statement of Cash Flows
  - the Balance Sheet

ANS: C                      PTS: 1                      DIF: E                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

42. In order to identify the amount of funds that a firm borrowed during the preceding year, what section is the best source within the Statement of Cash Flows?
- operating flows
  - investment flows
  - financing flows
  - total net cash flows

ANS: C                      PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

43. If you start with earnings before interest and taxes and then subtract a firm's tax expense while adding back the amount of depreciation expense for the firm during the year, the resulting figure is called
- free cash flow
  - operating cash flow
  - net cash flow

d. gross cash flow

ANS: B                    PTS: 1                    DIF: E                    REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

44. Emma Corp. had earnings before interest and taxes of \$500,000 and had a depreciation expense of \$200,000 this last year. If the firm was subject to an average tax rate of 30%, what was Emma's operating cash flow for the year? If you need to, assume that Emma's interest expense was zero for the year.
- \$175,000
  - \$82,500
  - \$25,000
  - It lost money

ANS: B  
 $(75k \cdot .7) + (100k \cdot .3) = 82,500$

PTS: 1                    DIF: H                    REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

45. Edison Bagels had operating cash flow equal to \$850 for 2012. If its earnings before interest and taxes was \$1,000 while its tax bill was \$300, what was Edison's depreciation expense for the year?
- \$150
  - \$550
  - \$1,550
  - not enough information to calculate

ANS: A  
 $OCF = EBIT - Taxes + Depreciation$   
 $850 = 1,000 - 300 + Depreciation$   
 $150 = Depreciation$

PTS: 1                    DIF: H                    REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

46. When calculating a firm's free cash flow from earnings before interest and taxes we must add back depreciation, amortization and depletion expense and allowances because
- they are non-cash expenditures.
  - the accounting method for reporting such expenses may be different from that reported to the taxing authority.
  - they approximate the value of fixed asset purchases during the year.
  - they are unrelated to the amount of taxes paid during the year.

ANS: A                    PTS: 1                    DIF: M                    REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

47. When calculating the dollar amount of fixed assets purchased during the year what information is required? Assume that no fixed assets were disposed of during the year.

- the current and prior year's gross fixed assets
- the current and prior year's net fixed assets
- the current and prior year's net fixed assets plus the firm's depreciation expense for the

year.

- d.** either a or c will suffice

ANS: D                      PTS: 1                      DIF: H                      REF: 2.2 Cash Flow Analysis

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Cold Weather Sports

**Cold Weather Sports, Inc. (CWS)**

Cold Weather Sports, Inc. (CWS) just completed its 2012 fiscal year. During the year, CWS had sales of \$10,000 and total expenses (no interest expenses were incurred) of \$6,000. Assume that CWS pays 30% of its EBIT in taxes and that depreciation expense of \$1,200 is included in the total expense number listed above. A list of some balance sheet items for CWS for end of fiscal year 2011 and 2012 is as below.

2011

Current Assets	\$1,000
Net Long-Term Assets	5,000
Accounts Payable	600
Accrued Expenses	500
Short-Term Debt	2,000
Long-Term Debt	3,000

2012

Current Assets	\$1,200
Net Long-Term Assets	5,600
Accounts Payable	800
Accrued Expenses	600
Short-Term Debt	2,100
Long-Term Debt	3,200

No fixed assets were disposed of during the year.

NARREND

48. What is Cold Weather Sports' operating cash flow for 2012?
- a. \$2,400
  - b. \$2,800
  - c. \$4,000
  - d.** none of the above

ANS: C

10,000 sales - 6,000 expense = 4,000 EBIT

4,000 EBIT - 1,200 tax + 1,200 depreciation expense = 4,000

PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

49. What was the dollar amount of fixed assets purchased during the year for Cold Weather Sports?
- a. \$600
  - b. \$1,200
  - c. \$1,800
  - d.** none of the above

ANS: C  
 $5,600 - 5,000 + 1,200 = 1,800$

PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

50. What is the amount of free cash flow generated by Cold Weather Sports in 2012?
- a. \$100
  - b. \$2,100
  - c. \$2,300
  - d. none of the above**

ANS: C  
Change in CA =  $1,200 - 1,000 = 200$   
Change in AP =  $800 - 600 = 200$   
Change in Accrued =  $600 - 500 = 100$

OCF =  $10,000 \text{ sales} - 6,000 \text{ expense} - 1,200 \text{ tax} + 1,200 \text{ depreciation expense} = 4,000$

Change in FA =  $5,600 - 5,000 + 1,200$

FCF =  $\text{OCF} - \text{Change FA} - (\text{Change in CA} - \text{Change in AP} - \text{Change in Accrued})$   
 $= 4,000 - 1,800 - (200 - 200 - 100) = 2,300$

PTS: 1                      DIF: H                      REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

51. The effect of an increase in a firm's accounts payable during the year, assuming that the current asset portion of the balance sheet remains the same, is
- a. an outflow of cash.
  - b. an inflow of cash.
  - c. neither an inflow nor an outflow of cash.
  - d. a decrease in the equity of the firm.**

ANS: B                      PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

52. Roxy Corp. has total current liabilities of \$22,000 and an inventory of \$7,000. If its current ratio is 1.2, then what is Rocy's quick ratio?
- a. .88
  - b. .75
  - c. .64
  - d. .36**

ANS: A  
 $1.2 = \text{CA} / 22,000$   
 $\text{CA} = 26,400$

quick ratio =  $(\text{CA} - \text{Inv}) / \text{CL}$   
quick ratio =  $(26,400 - 7,000) / 22,000 = 2.0$

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

53. Granny's Jug Herbal Shop has total current liabilities of \$2,000 and an inventory of \$1,000. If its current ratio is 2.5, then what is its quick ratio?
- 2.0
  - 2.5
  - 3.0
  - 3.5

ANS: A

$$2.5 = CA / 2,000 \implies CA = 5,000$$

$$\text{quick ratio} = (CA - \text{Inv}) / CL = (5,000 - 1,000) / 2,000 = 2.0$$

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

54. BadBanna Co. has an average age of inventory equal to 25 days. If its end of year inventory level is \$8,500, then what does that imply for the cost of goods sold during the year? (round to the nearest dollar)
- \$582
  - \$4964
  - \$21,250
  - \$124,100

ANS: C

$$25 = (365 / \text{inventory turnover})$$

$$\text{inventory turnover} = 14.6$$

$$\text{Inv. turn} = (CGS / \text{inventory})$$

$$14.6 = (CGS / 8500)$$

$$CGS = 21,250$$

PTS: 1                      DIF: H

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

55. Wunder Boy Bat Co. has an average age of inventory equal to 121.67 days. If its end of year inventory level is \$4,000, then what does that imply for the cost of goods sold during the year? (round to the nearest dollar)
- \$1,333
  - \$3,000
  - \$12,000
  - \$16,000

ANS: C

$$121.67 = (365 / \text{inventory turnover}) \implies \text{inventory turnover} = 2.9992$$

$$2.9992 = (CGS / \text{inventory}) \implies 2.992 = (CGS / 4,000) \implies CGS = 11,999.67 \implies 12,000$$



PTS: 1                    DIF: H  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

56. Emma Corp. had credit sales of \$300,000 last year and on average had \$25,000 in its accounts receivable during the year. What is its average collection period?
- a. about 30 days
  - b. about 12 days
  - c. about 1 day
  - d.** about 3 days

ANS: A  
 $300,000 / 365 = 821.92$  average sales per day  
average collection period =  $25,000 / 821.92 = 30.41$  days

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

57. The firm that you work for had credit sales of \$3,500,000 last year and on average had \$33,000 in its accounts receivable during the year. What is its average collection period?
- a. 3 days
  - b. 3.44 days
  - c. 3.5 days
  - d.** none of the above

ANS: A  
 $3,500,000 / 365 = 9,589.04$  average sales per day =====>  
average collection period =  $33,000 / 9,589.04 = 3.44$  days

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

58. In general, the more debt a firm uses in relation to its total assets
- a. the less risk there is to the equity holders of the firm.
  - b. the less financial leverage it uses.
  - c. the greater the financial leverage it uses.
  - d. the greater extent to which it uses equity.

ANS: C                    PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

59. Devil Inc. has total liabilities equal to \$3,500 and total assets equal to \$5,000. What is Devil's asset-to-equity ratio?
- a. 1.43
  - b. 2.33
  - c. 3.33
  - d.** none of the above

ANS: C

$$TA = 5,000 \implies \text{Equity} = 5,000 - 3,500 = 1,500$$

$$\text{asset-to-equity} = 5,000 / 1,500 = 3.33$$

PTS: 1

DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

60. Roxy Corp has an operating profit of \$15,000 produced from \$12,000 in sales. If Roxy has no interest expense and currently pays 35% of its operating profits in taxes, what is Roxy's net profit margin?
- 81.25%
  - 12.50%
  - 1.25%
  - 65.00%

ANS: A

$$[15,000 - (.35 \times 15,000)] / 12,000 = 81.25\%$$

PTS: 1

DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

61. Straw Corp has an operating profit of \$1,200 produced from \$9,800 in sales. If Straw has no interest expense and currently pays 35% of its operating profits in taxes and \$200 per year in preferred dividends, then what is Straw's net profit margin?
- 5.92%
  - 7.96%
  - 7.96%
  - 10.20%

ANS: A

$$[1,200 - (.35 \times 1,200) - 200] / 9,800 = 5.92\%$$

PTS: 1

DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

62. Straw Corp has an operating profit of \$1,200 produced from \$20,000 in total assets. If Straw has no interest expense and currently pays 35% of its operating profits in taxes and \$200 per year in preferred dividends, then what is Straw's net profit margin?
- 2.90%
  - 3.90%
  - 5.0%
  - none of the above

ANS: A

$$[1,200 - (.35 \times 1,200) - 200] / 20,000 = 2.90\%$$

PTS: 1

DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Import

**Import, Inc.**

Import, Inc. has earnings available for common shareholders of \$700 produced by sales of \$10,000. It also has total assets of \$20,000 and an assets to equity ratio of 2.5.

NARREND

63. What is Import Inc.'s return on assets?

- a. 14%
- b. 7%
- c. 3.5%
- d.** none of the above

ANS: C

$$\text{ROA} = (\text{earnings avail for common/sales}) \times (\text{sales/TA})$$
$$= (700/10,000) \times (10,000/20,000) = .035$$

PTS: 1                      DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

64. What is Import Inc.'s return on common equity?

- a. 7.0%
- b. 8.75%
- c. 17.5%
- d.** none of the above

ANS: A

$$\text{ROE} = (\text{earnings avail for common/sales}) \times (\text{sales/TA}) \times (\text{TA/equity})$$
$$= (700/10,000) \times (10,000/20,000) \times (20,000/8,000) = .0875$$

PTS: 1                      DIF: H

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

65. EmmaCor is currently selling for \$22 per share. If it is selling at a P/E ratio of 12, calculate EmmaCor's recent earnings per share.

- a. \$0.45
- b. \$0.55
- c. \$1.83
- d.** \$2.20

ANS: C

$$\text{P/E} = \text{market price per share} / \text{earnings per share}$$

$$12 = 22/\text{EPS}$$

$$\text{EPS} = 1.83$$

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

66. FactorMax is currently selling for \$75 per share. If it is selling at a P/E ratio of 50, calculate FactorMax's recent earnings per share.
- \$.15
  - \$.67
  - \$1.50
  - none of the above

ANS: C

P/E = market price per share / earnings per share

$$50 = 75/\text{EPS} \implies \text{EPS} = 1.50$$

PTS: 1

DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

67. What is the financial ratio that measures the price per share of stock divided by earnings per share?
- Return on assets
  - Return on equity
  - Debt-equity ratio
  - Price-earnings ratio

ANS: D

PTS: 1

DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Stone Cold

**Stone Cold Incorporated**

**Balance Sheet: 12/31/12**

<b>Assets</b>	<b>2012</b>	<b>2011</b>
Cash and Marketable Securities	10	80
Accounts Receivable	375	315
Inventories	<u>615</u>	<u>415</u>
Total Current Assets	1,000	810
Net plant and equipment	<u>1,000</u>	<u>870</u>
<b>TOTAL ASSETS</b>	<b>2,000</b>	<b>1,680</b>

<b>Liabilities and Equity</b>	<b>2012</b>	<b>2011</b>
Accounts Payable	60	40
Notes Payable	140	60
Accruals	<u>110</u>	<u>130</u>
Total Current Liabilities	310	230
Long Term Bonds	<u>754</u>	<u>580</u>
<b>TOTAL DEBT</b>	<b>1,064</b>	<b>810</b>
Preferred Stock	40	40
Common Stock	130	130
Retained earnings	766	700
<b>TOTAL COMMON EQUITY</b>	<b>896</b>	<b>830</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>2,000</b>	<b>1,680</b>

<b>Income Statement: 12/31/12</b>	<b>2012</b>	<b>2011</b>
Net Sales	3,200	2,850
Operating Costs (excludes Dep/Amortization)	<u>2,700</u>	<u>2,497</u>
EBITDA	<u>500</u>	<u>353</u>
Depreciation	100	90
Amortization	<u>0</u>	<u>0</u>
Depreciation and Amortization	<u>100</u>	<u>90</u>
EBIT	400	263
Less Interest	<u>88</u>	<u>60</u>
EBT	312	203
Taxes (40%)	<u>124.8</u>	<u>81.2</u>
NET INCOME (before Preferred Dividends)	187.2	121.8
Preferred Dividends	<u>4</u>	<u>4</u>
NET INCOME	<u>183.2</u>	<u>117.8</u>
Common Dividends	117	53
Addition to Retained Earnings	66.2	64.8

NARREND

68. Refer to Stone Cold. For 2012, what was the return on assets?
- 9.16%
  - 12.40%
  - 15.60%
  - 20.00%

ANS: A  
 $=183.2/2000 = 9.16\%$

PTS: 1                    DIF: E  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

69. Refer to Stone Cold. For 2012, what was the return on common equity?
- 9.36%
  - 12.40%
  - 20.44%
  - 20.90%

ANS: C  
 $183.2/896 = 20.44\%$

PTS: 1                    DIF: E  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

70. Refer to Stone Cold. For 2012, what was the debt-to-equity ratio?
- 0.81
  - 0.84
  - 0.98
  - 1.19

ANS: A

$$=754/(896+40) = .81$$

PTS: 1                    DIF: H  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

71. Refer to Stone Cold. For 2012, what was the average collection period for the firm in 2004?
- 6.84 days
  - 8.77 days
  - 42.77 days
  - 51.22 days

ANS: C  
 $=3200/365 = 8.767$   
 $=375/8.767 = 42.77$

PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

72. Refer to Stone Cold. For 2012, what was the total asset turnover for 2012?
- 0.80
  - 1.20
  - 1.40
  - 1.60

ANS: D  
 $=3200/2000 = 1.60$

PTS: 1                    DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

73. Refer to Stone Cold. For 2012, what was the times interest earned ratio for 2012?
- 2.13
  - 2.77
  - 3.55
  - 4.55

ANS: D  
 $=400/88 = 4.55$

PTS: 1                    DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

74. What was the free cash flow in 2012 for Stone Cold Incorporated?
- \$55.20
  - \$44.80
  - \$145.20
  - \$215.00

ANS: A

FCF = OCF - chFA - (chCA - chA/P - chAccruals) where

OCF = EBIT - Taxes + Depreciation

OCF = \$400 - \$124.8 + \$100 = \$375.2

chFA = Change in Gross Fixed Assets = Change in Net Fixed Assets + Depreciation

chFA = (\$1,000 - \$870) + \$100 = \$230

chCA = Change in Current Assets

chCA = \$1,000 - \$810 = \$190

chA/P = Change in A/P

chA/P = \$60 - \$40 - \$20

chAccruals = Change in Accruals.

chAccruals = \$110 - \$130 = -\$20

FCF = OCF - chFA - (chCA - chA/P - chAccruals)

FCF = \$375.2 - \$230 - (\$190 - \$20 - -\$20)

FCF = \$375.2 - \$230 - \$190

FCF = -\$44.8

PTS: 1                      DIF: H                      REF: 2.2 Cash Flow Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

75. Consider the following financial information for Classic City Ice Cream Corporation:

2012 Financial Data

Net Income	\$ 50,000
Total Assets	\$300,000
Total Shareholder Equity	\$200,000
Net Sales	\$100,000

What is the total asset turnover for the firm in 2012?

- a. 16.67%
- b. 25.00%
- c. 33.33%
- d. 40.00%

ANS: C

=100000/300000=33.33%

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

76. Consider the following financial information for Classic City Ice Cream Corporation:

2012 Financial Data

Net Income	\$ ???,???
------------	------------

Total Assets	\$250,000
Total Shareholder Equity	\$200,000
Net Sales	\$100,000

If the return on equity is 20%, what was Net Income for 2012?

- a. \$25,000
- b. \$40,000
- c. \$50,000
- d. \$65,000

ANS: B

$$.20 = X / \$200,000$$

$$X = \$40,000$$

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Titans Electronics

**Titans Electronics**

Titans Electronics reports the following data for the past year:

EBIT	\$1,000,000	# of Common shares	400,000
Net Income	\$ 480,000	Total Dividends Paid	\$120,000
Interest Paid	\$ 200,000	Current Assets	\$ 80,000
Total Assets	\$6,000,000	Current Liabilities	\$ 60,000
		Market Price of Common equity	\$ 20

NARREND

77. What is the current P/E ratio for the Titans?

- a. 8.00
- b. 10.00
- c. 15.50
- d. 16.67

ANS: D

$$= \$20 / (\$480,000 / 400,000) = 16.67$$

PTS: 1                      DIF: M

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

78. Titans Electronics is applying for a new line of credit from their banking partner. To issue the credit, the bank requires the following cutoffs for certain financial ratios:

TIE ratio of 4.25    Current Ratio of 1.50    ROA of 5%.

What is a likely response from the bank to the application?

- a. The bank will have reservations, as the TIE ratio does not meet requirements.
- b. The bank will have concerns, as the current ratio does not meet requirements.



- c. The bank will have concerns, as the ROA is not high enough.
- d. The bank will have concerns, as two or more of the requirements are not met.

ANS: B                      PTS: 1                      DIF: M  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

NARRBEGIN: Exhibit 2-1

**Exhibit 2-1**

The tax schedule for corporate income is shown in the table below:

Taxable Income Over	Not Over	Tax Rate
\$ 0	\$ 50,000	15.00%
50,000	75,000	25.00%
75,000	100,000	34.00%
100,000	335,000	39.00%
335,000	500,000	34.00%
10,000,000	15,000,000	35.00%
15,000,000	18,333,333	38.00%
18,333,333	.....	35.00%

NARREND

79. Refer to Exhibit 2-1. Pale Rider Corporation reports taxable income of \$500,000 in 2011. What was their tax liability for the year?
- a. \$56,100
  - b. \$91,650
  - c. \$170,000
  - d. \$200,000

ANS: C  
 $=50000 \cdot .15 + 25000 \cdot .25 + 25000 \cdot .34 + 235000 \cdot .39 + 165000 \cdot .34 = 170000$

PTS: 1                      DIF: E                      REF: 2.4 Corporate Taxes  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

80. Refer to Exhibit 2-1. Pale Rider Corporation reports taxable income of \$500,000 in 2011. What was the average tax rate they paid for the year?
- a. 23.25%
  - b. 25.00%
  - c. 29.40%
  - d. 34.00%

ANS: D  
 $\text{Taxes Paid} = 50000 \cdot .15 + 25000 \cdot .25 + 25000 \cdot .34 + 235000 \cdot .39 + 165000 \cdot .34 = 170000$   
 $170000 / 500000 = .34$

PTS: 1                      DIF: E                      REF: 2.4 Corporate Taxes  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

81. Refer to Exhibit 2-1. Big Diesel Incorporated reports taxable income of \$200,000 in 2011. What was the average tax rate they paid for the year?

- a. 25.00%
- b. 29.40%
- c. 30.63%
- d. 34.00%

ANS: C

$$\text{Taxes Paid} = 50000 \cdot .15 + 25000 \cdot .25 + 25000 \cdot .34 + 100000 \cdot .39 = 61250$$

$$61250 / 200000 = .3063$$

PTS: 1                    DIF: E                    REF: 2.4 Corporate Taxes  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

82. Refer to Exhibit 2-1. Big Diesel Incorporated currently predicts taxable income of \$200,000 for the next year. If this is their actual income, what will be the tax liability for Big Diesel?
- a. \$45,250
  - b. \$56,500
  - c. \$61,250
  - d. \$91,650

ANS: C

$$\text{Taxes Paid} = 50000 \cdot .15 + 25000 \cdot .25 + 25000 \cdot .34 + 100000 \cdot .39 = 61250$$

PTS: 1                    DIF: E                    REF: 2.4 Corporate Taxes  
 NAT: Analytic skills  
 LOC: acquire knowledge of financial analysis and cash flows

83. What ratio measures the ability of the firm to satisfy its short term obligations as they come due?
- a. Activity ratio
  - b. Times interest earned ratio
  - c. Current ratio
  - d. Inventory turnover ratio

ANS: C                    PTS: 1                    DIF: E  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Reflective thinking  
 LOC: acquire knowledge of financial analysis and cash flows

84. The asset to equity ratio for a firm is 1.5, and the firm has total assets of \$3,000,000. Last year, net income for the firm was \$250,000, and the earnings per share for the firm was reported as \$0.50. What is the current book value per share for the firm?
- a. \$2
  - b. \$4
  - c. \$6
  - d. \$8

ANS: B

$$1.5 = 3,000,000 / X; X = \text{shareholder equity} = \$2,000,000$$

$$\text{EPS} = \$0.50 = \$250,000 / Y; Y = \# \text{ of shares} = 500,000$$

$$\text{Book value per share} = \$2,000,000 / 500,000 = \$4$$

PTS: 1                    DIF: M  
 REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
 NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

85. Which financial ratio measures the effectiveness of management in generating returns to common stockholders with its available assets?
- Gross profit margin
  - Return on equity
  - Return on assets
  - Current ratio

ANS: C                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

86. When is the return on assets equal to the return on equity?
- When the current ratio of the firm equals 1.
  - When the firm issues equal amounts of long term debt and common stock.
  - When the firm issues no dividends for a given time period.
  - When the firm only issues equity to finance its borrowing.

ANS: D                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

87. Consider the following working capital information for Full House Corporation:

Year	2011	2012
Accounts Receivable	\$ 0	\$100
Inventory	\$100	\$100
Accounts Payable	\$ 0	\$ 50

What was the effect on free cash flow for the firm this past year?

- Increase of \$100
- Increase of \$150
- Decrease of \$50
- Decrease of \$100

ANS: C  
change in NWC = change in CA - change in CL  
change in CA = (\$200-\$100)= \$100  
change in CL = (\$50-\$0) = \$50  
change in NWC = +\$50  
Effect on free cash flow = -\$50

PTS: 1                      DIF: H                      REF: 2.2 Cash Flow Analysis  
NAT: Analytic skills  
LOC: acquire knowledge of financial analysis and cash flows

88. A firm reports net income of \$500,000 for 2011. The most recent balance sheet for the reports retained earnings of \$2,000,000. The firm will pay out 25% of net income as dividends. What will the new balance be for retained earnings?
- \$1,875,000
  - \$2,125,000
  - \$2,375,000
  - \$2,500,000

ANS: C

Addition to RE =  $\$500,000 \times (1 - .25) = \$375,000$

New RE =  $\$2,000,000 + \$375,000$

PTS: 1

DIF: M

REF: 2.1 Financial Statements

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

89. Emmacorp reports a current ratio of 2 and a quick ratio of 1.4. The firm has total current assets of \$8,000. If Emmacorp reports cost of goods sold at \$30,000 for the given year, what is Emmacorp's inventory turnover?
- 12.5
  - 15.5
  - 21.4
  - 5.2

ANS: A

Current = 2 =  $CA/CL = \$8000/CL$ ,  $CL = \$4000$

Quick = 1.4 =  $(\$8000 - INV)/\$4000$

INV = \$2,400

Inventory turn =  $\$30,000/\$2400 = 12.5$

PTS: 1

DIF: H

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

90. A firm reports a current ratio of 2 and a quick ratio of 1.2. The firm has total current assets of \$4,000. If the firm reports cost of goods sold at \$25,000 for the given year, what is the average age of their inventory?
- 12.35 days
  - 15.63 days
  - 18.24 days
  - 23.36 days

ANS: D

Current = 2 =  $CA/CL = \$4000/CL$ ,  $CL = \$2000$

Quick = 1.2 =  $(\$4000 - INV)/\$2000$

INV = \$1,600

Inventory turn =  $\$25000/\$1600 = 15.625$

Average age =  $365/15.625 = 23.36$

PTS: 1

DIF: H

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

91. The average age of the inventory for a firm is 10 days old. If the current dollar amount of inventory is \$1,000, what is a good estimate for the cost of goods sold over the last year?
- \$16,500
  - \$26,500
  - \$32,500

d. \$36,500

ANS: D

$10 = 365/\text{Inv turn}$ , Inventory turn = 36.5

$36.5 = \text{COGS}/\text{INV} = \text{COGS} / \$1000$

COGS = \$36500

PTS: 1                      DIF: H

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows

92. Accountants:

- a. generally construct financial statements using the cash-based approach
- b. generally construct financial statements using the accrual-based approach
- c. must apply Generally Accepted Accounting Principles to fairly portray how the firm has performed in the past
- d. must apply Generally Accepted Accounting Principles to fairly portray how the firm will perform in the future
- e. both (b) and (c)

ANS: E                      PTS: 1                      DIF: E                      REF: 2.1 Financial Statements

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

93. Which of the following statements is TRUE?

- a. Financial professionals prefer the accrual-based approach as it focuses more attention on cash inflows and outflows
- b. Financial managers do not need to make any adjustments to financial statements for decision-making
- c. Financial managers must convert cash-based financial statements to accrual-based ones before they can begin analyzing a firm
- d. Financial professionals prefer the cash-based approach as it focuses more attention on cash inflows and outflows

ANS: D                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

94. Which of the following statements is FALSE?

- a. On the balance sheet a firm's assets are listed in ascending order of liquidity.
- b. In a common size balance sheet, all assets are expressed as a percentage of sales.
- c. Net property, plant and equipment represents the original value of all real property, structures and long-lived equipment owned by the corporation.
- d. all of the above statements are false

ANS: D                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements

NAT: Reflective thinking

LOC: acquire knowledge of financial analysis and cash flows

95. The Statement of Retained Earnings

- a. reconciles the net income earned during a given time period and any cash dividends paid with the change in Retained Earnings between the start and end of that period.
- b. shows a snapshot of the firm's financial position at a specific point in time

- c. reconciles the net income earned during a given time period and any cash dividends and interest on debt paid with the change in Retained Earnings between the start and end of that period
- d. shows the impact of Treasury Stock on the firm's Common Equity

ANS: A                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

96. Which of the following statements is FALSE?

- a. The Notes to Financial Statements provide little information that is relevant to professional security analysts.
- b. The Notes to Financial Statements provide additional information about a firm, including employee compensation plans, revenue recognition practices and leases.
- c. The Notes to Financial Statements provide detailed explanatory information that is keyed to various accounts on the financial statements.
- d. all of the above statements are true
- e. both (a) and (c) are false

ANS: A                      PTS: 1                      DIF: M                      REF: 2.1 Financial Statements  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

97. Which of the following is NOT a classification of a firm's cash flows:

- a. investment flows
- b. financial flows
- c. operating flows
- d. capital flows

ANS: D                      PTS: 1                      DIF: E                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

98. Which of the following represents an inflow of cash?

- a. A decrease in any liability
- b. Dividends paid
- c. Repurchase or retirement of stock
- d. An increase in any asset
- e. A decrease in any asset

ANS: E                      PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

99. How is depreciation accounted for on the Statement of Cash Flows?

- a. Depreciation is irrelevant for cash flow purposes and has no place on the Statement of Cash Flows.
- b. Depreciation expense is included in the operating activities section of the statement.
- c. As depreciation is deducted to determine Net Income there is no need to include it on the statement.
- d. None of the above

ANS: B                      PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

100. The Statement of Cash Flows is helpful to financial managers in that:
- a. It calls attention to unusual changes in either the major categories of cash flow or specific items so that the financial manager can pinpoint problems the firm may be having
  - b. It calls attention to the expenses deducted to determine net income.
  - c. Financial managers can create pro forma statements to determine whether or not the firm will need additional external financing.
  - d. All of the above
  - e. Both (a) and (c)

ANS: E                      PTS: 1                      DIF: M                      REF: 2.2 Cash Flow Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

101. Which of the following statements is FALSE?
- a. A firm's creditors are primarily interested in a firm's Activity Ratios.
  - b. Norms exist for all financial ratios that can be applied across all industries.
  - c. Current and future stockholders are most interested in a firm's short-term liquidity ratios.
  - d. All of the above statements are false.

ANS: D                      PTS: 1                      DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

102. Which of the following statements is TRUE?
- a. Net working capital is a firm's current assets divided by its current liabilities.
  - b. Net working capital is a firm's current assets minus its current liabilities.
  - c. Net working capital measures a firm's ability to meet its short-term obligations.
  - d. All of the above statements are false.

ANS: B                      PTS: 1                      DIF: E  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

103. The DuPont system:
- a. breaks the ROA and ROE ratios into component pieces
  - b. requires data from only the balance sheet
  - c. evaluates ROA the product of a firm's profit on its sales and the efficiency of the firm to generate sales from its investment in its assets
  - d. all of the above
  - e. Both (a) and (c)

ANS: E                      PTS: 1                      DIF: M  
REF: 2.3 Analyzing Financial Performance Using Ratio Analysis  
NAT: Reflective thinking  
LOC: acquire knowledge of financial analysis and cash flows

104. Use the following information to determine Bill's Solvency Ratio.

Total net worth: \$150,000  
Cash surplus: \$15,000  
Income after taxes: 105,000  
Total assets: \$300,000

- a. 14.29%
- b. 50%
- c. 2
- d.** None of the above

ANS: B

$$150,000/300,000 = 50\%$$

PTS: 1                      DIF: E

REF: 2.3 Analyzing Financial Performance Using Ratio Analysis

NAT: Analytic skills

LOC: acquire knowledge of financial analysis and cash flows