



Questions for CMA Part 2 Section A: Financial Statement Analysis

(Các câu hỏi cho CMA Phần 2 Phần A: Phân tích Báo cáo Tài chính)

I. Trắc nghiệm

1. Gordon has had the following financial results for the last four years.

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>
Sales	\$1,250,000	\$1,300,000	\$1,359,000	\$1,400,000
Cost of goods sold	750,000	785,000	825,000	850,000
Gross profit	500,000	515,000	534,000	550,000

Inflation factor 1.00 1.03 1.07 1.10

Gordon has analyzed these results using vertical common-size analysis to determine trends. The performance of Gordon can **best** be characterized by which one of the following statements?

- a. The common-size gross profit percentage has decreased as a result of an increasing common-size trend in cost of goods sold.
 - b. The common-size trend in sales is increasing and is resulting in an increasing trend in the common-size gross profit margin.
 - c. The common-size trend in cost of goods sold is decreasing which is resulting in an increasing trend in the common-size gross profit margin.
 - d. The increased trend in the common-size gross profit percentage is the result of both the increasing trend in sales and the decreasing trend in cost of goods sold.
2. Shown below are components of a company's financial statements.

Sales revenue \$600,000



Cost of goods sold	300,000
Total assets	2,400,000
Total equity	1,500,000
Net income	120,000

What percentage value would net income be on a common size financial statement?

- a. 5%.
 - b. 8%.
 - c. 20%.
 - d. 40%.
3. A financial analyst is reviewing a competitor's income statements for the past two years.

	<u>Year 1</u>	<u>Year 2</u>
Sales	£250,000	£275,000
Cost of goods sold	<u>155,000</u>	<u>160,000</u>
Gross profit	95,000	115,000
Selling expenses	35,000	40,000
General expenses	<u>45,000</u>	<u>50,000</u>
Operating income before income taxes	15,000	25,000
Taxes related to operations	<u>2,500</u>	<u>3,500</u>
		<u>0</u>
Net income	<u>£ 12,500</u>	<u>£ 21,500</u>

The financial analyst is able to conclude that the competitor's



- a. common size income statements will show operating income before income taxes at 22% for Year 2.
 - b. common size income statements will show taxes related to operations at 16% for Year 2.
 - c. common base year income statements will show that gross profit increased by 17% in Year 2 as compared to Year 1.
 - d. common base year income statements will show that selling expenses increased by 14% in Year 2 as compared to Year 1.
4. A company's financial statements from the past two years have the following values.

	<u>Previous year</u>	<u>Current year</u>
Sales revenue	\$6,000,000	\$6,600,000
Net income	500,000	540,000
Total assets	10,000,000	10,500,000
Inventory	600,000	500,000

Using horizontal analysis, what account has the **largest** percentage change?

- a. Sales revenue.
 - b. Net income.
 - c. Total assets.
 - d. Inventory.
5. In analyzing the short-term liquidity of a firm, many analysts prefer to use the quick (or acid test) ratio rather than the current ratio. The primary reason for this preference is that the



- a. quick ratio excludes account receivables.
- b. current ratio includes marketable securities which may be mispriced.
- c. pro-forma cash flow statements focus on cash only.
- d. Conversion of inventory into cash is less reliable.

6. The balance sheet of a luggage manufacturer reports the following.

Cash	\$531,000
Accounts receivable	439,000
Inventory	300,000
Marketable securities	200,000
Current liabilities	500,000
Long term liabilities	676,000

Based on the information provided, the luggage manufacturer's quick ratio is

- a. 1.25
 - b. 1.94
 - c. 2.34
 - d. 2.94
7. Broomall Corporation has decided to include certain financial ratios in its year-end annual report to shareholders. Selected information relating to its most recent fiscal year is provided below.
- Cash \$10,000
 - Accounts receivable 20,000
 - Prepaid expenses 8,000



- Inventory 42,000
- Accounts payable 15,000
- Notes payable (due in 90 days) 25,000
- Bonds payable (due in 10 years) 35,000
- Net credit sales for year 220,000
- Cost of goods sold 140,000 Broomall's working capital at year end is
 - a. \$40,000.
 - b. \$37,000.
 - c. \$28,000.
 - d. \$10,000.

8. All of the following are affected when merchandise is purchased on credit **except**

- a. total current assets.
- b. net working capital.
- c. total current liabilities.
- d. current ratio.

9. Birch Products Inc. has the following current assets.

Cash	\$ 250,000
Marketable securities	100,000
Accounts receivable	800,000
Inventories	<u>1,450,000</u>
Total current assets	<u>\$2,600,000</u>

If Birch's current liabilities are \$1,300,000, the firm's



- a. current ratio will decrease if a payment of \$100,000 cash is used to pay \$100,000 of accounts payable.
 - b. current ratio will not change if a payment of \$100,000 cash is used to pay \$100,000 of accounts payable.
 - c. quick ratio will decrease if a payment of \$100,000 cash is used to purchase inventory.
 - d. quick ratio will not change if a payment of \$100,000 cash is used to purchase inventory.
10. Shown below are beginning and ending balances for certain of Grimaldi Inc.'s accounts.

	<u>January 1</u>	<u>December 31</u>
Cash	\$ 48,000	\$ 62,000
Marketable securities	42,000	35,000
Accounts receivable	68,000	47,000
Inventory	125,000	138,000
Plant & equipment	325,000	424,000
Accounts payable	32,000	84,000
Accrued liabilities	14,000	11,000
7% bonds payable	95,000	77,000

Grimaldi's acid test ratio or quick ratio at the end of the year is

- a. 0.83.
- b. 1.02.
- c. 1.15.
- d. 1.52.



11. Davis Retail Inc. has current assets of \$7,500,000 and a current ratio of 2.3 times before purchasing \$750,000 of merchandise on credit for resale. After this purchase, the current ratio will
- a. remain at 2.3 times.
 - b. be higher than 2.3 times.
 - c. be lower than 2.3 times.
 - d. be exactly 2.53 times.
12. Garstka Auto Parts must increase its acid test ratio above the current 0.9 level in order to comply with the terms of a loan agreement. Which one of the following actions is **most** likely produce the desired results?
- a. Expediting collection of accounts receivable.
 - b. Selling auto parts on account.
 - c. Making a payment to trade accounts payable.
 - d. Purchasing marketable securities for cash.
13. The owner of a chain of grocery stores has bought a large supply of mangoes and paid for the fruit with cash. This purchase will adversely impact which one of the following?
- a. Working capital.
 - b. Current ratio.
 - c. Quick or acid test ratio.
 - d. Price earnings ratio.



14. When reviewing a credit application, the credit manager should be **most** concerned with the applicant's
 - a. profit margin and return on assets.
 - b. price-earnings ratio and current ratio.
 - c. working capital and return on equity.
 - d. working capital and current ratio.

15. Both the current ratio and the quick ratio for Spartan Corporation have been slowly decreasing. For the past two years, the current ratio has been 2.3 to 1 and 2.0 to 1. During the same time period, the quick ratio has decreased from 1.2 to 1 to 1.0 to 1. The disparity between the current and quick ratios can be explained by which one of the following?
 - a. The current portion of long-term debt has been steadily increasing.
 - b. The cash balance is unusually low.
 - c. The accounts receivable balance has decreased.
 - d. The inventory balance is unusually high.

16. The acid test ratio shows the ability of a company to pay its current liabilities without having to
 - a. reduce its cash balance.
 - b. borrow additional funds.
 - c. collect its receivables.
 - d. liquidate its inventory.



17. All of the following are included when calculating the acid test ratio **except**
- six-month treasury bills.
 - prepaid insurance.
 - accounts receivable.
 - 60-day certificates of deposit.
18. Dedham Corporation has decided to include certain financial ratios in its year-end annual report to shareholders. Selected information relating to its most recent fiscal year is provided below.
- Cash \$10,000
 - Accounts receivable 32,000
 - Prepaid expenses 8,000
 - Inventory 30,000
 - Accounts payable 15,000
 - Notes payable (due in 90 days) 25,000
 - Bonds payable (due in 10 years) 35,000
- Dedham's quick (acid-test) ratio at year end is
- 2.00 to 1.
 - 1.925 to 1.
 - 1.80 to 1.
 - 1.05 to 1.
19. If a company has a current ratio of 2.1 and pays off a portion of its accounts payable with cash, the current ratio will



- a. decrease.
- b. increase.
- c. remain unchanged.
- d. move closer to the quick ratio.

20. A banker is reviewing the bank's current portfolio of outstanding loans and collected the following financial data (in thousands) on four companies that the bank has loaned money to.

	<u>Company A</u>	<u>Company B</u>	<u>Company C</u>	<u>Company D</u>
Earnings before interest and income taxes	¥5,000	¥12,500	¥4,300	¥2,450
Interest expense	¥3,950	¥9,000	¥2,675	¥1,250

On the basis of the information provided above, which company has the **highest** relative likelihood of defaulting on an outstanding loan?

- a. Company A.
- b. Company B.
- c. Company C.
- d. Company D.

21. An accountant has determined that last year a company had earnings before interest and tax of \$750,000, interest expense of \$125,000, and an income tax rate of 40%. What was the company's degree of financial leverage last year?

- a. 0.80.
- b. 1.20.



c. 1.67.

d. 2.00.

22. The capital structure of four corporations is as follows.

	<u>Corporation</u>			
	<u>Sterling</u>	<u>Cooper</u>	<u>Warwick</u>	<u>Pane</u>
Short-term debt	10%	10%	15%	10%
Long-term debt	40%	35%	30%	30%
Preferred stock	30%	30%	30%	30%
Common equity	20%	25%	25%	30%

Which corporation is the most highly leveraged?

a. Sterling.

b. Cooper.

c. Warwick.

d. Pane.

23. A summary of the Income Statement of Sahara Company is shown below.

Sales	\$15,000,000
Cost of sales	9,000,000
Operating expenses	3,000,000
Interest expense	800,000
Taxes	<u>880,000</u>
Net income	<u>\$ 1,320,000</u>



Based on the above information, Sahara's degree of financial leverage is

- a. 0.96.
- b. 1.36.
- c. 1.61.
- d. 2.27.

24. A degree of operating leverage of 3 at 5,000 units means that a

- a. 3% change in earnings before interest and taxes will cause a 3% change in sales.
- b. 3% change in sales will cause a 3% change in earnings before interest and taxes.
- c. 1% change in sales will cause a 3% change in earnings before interest and taxes.
- d. 1% change in earnings before interest and taxes will cause a 3% change in sales.

25. Firms with high degrees of financial leverage would be **best** characterized as having

- a. high debt-to-equity ratios.
- b. zero coupon bonds in their capital structures.
- c. low current ratios.
- d. high fixed-charge coverage.

26. The use of debt in the capital structure of a firm

- a. increases its financial leverage.
- b. increases its operating leverage.
- c. decreases its financial leverage.
- d. decreases its operating leverage.



27. A financial analyst with Mineral Inc. calculated the company's degree of financial leverage as 1.5. If net income before interest increases by 5%, earnings to shareholders will increase by
- a. 1.50%.
 - b. 3.33%.
 - c. 5.00%.
 - d. 7.50%.
28. Which one of the following statements concerning the effects of leverage on earnings before interest and taxes (EBIT) and earnings per share (EPS) is correct?
- a. For a firm using debt financing, a decrease in EBIT will result in a proportionally larger decrease in EPS.
 - b. A decrease in the financial leverage of a firm will increase the beta value of the firm.
 - c. If Firm A has a higher degree of operating leverage than Firm B, and Firm A offsets this by using less financial leverage, then both firms will have the same variability in EBIT.
 - d. Financial leverage affects both EPS and EBIT, while operating leverage only effects EBIT.
29. Which one of the following is the **best** indicator of long-term debt paying ability?
- a. Working capital turnover.
 - b. Asset turnover.



- c. Current ratio.
- d. Debt-to-total assets ratio.

30. Easton Bank has received loan applications from three companies in the computer service business and will grant a loan to the company with the best prospect of fulfilling the loan obligations.

Specific data, shown below, has been selected from these applications for review and comparison with industry averages.

	<u>CompGo</u>	<u>Astor</u>	<u>SysGen</u>	<u>Industry</u>
Total sales (millions)	\$4.27	\$3.91	\$4.86	\$4.30
Net profit margin	9.55%	9.85%	10.05%	9.65%
Current ratio	1.82	2.02	1.96	1.95
Return on assets	12.0%	12.6%	11.4%	12.4%
Debt/equity ratio	52.5%	44.6%	49.6%	48.3%
Financial leverage	1.30	1.02	1.56	1.33

Based on the information above, select the strategy that would fulfill Easton's objective.

- a. Easton should not grant any loans as none of these companies represents a good credit risk.
- b. Grant the loan to CompGo as all the company's data approximate the industry average.
- c. Grant the loan to Astor as both the debt/equity ratio and degree of financial leverage are below the industry average.
- d. Grant the loan to SysGen as the company has the highest net profit margin and degree of financial leverage.



31. The following information has been derived from the financial statements of Boutwell Company.

Current assets	\$640,000
Total assets	990,000
Long-term liabilities	130,000
Current ratio	3.2 Times

The company's debt-to-equity ratio is

- a. 0.50 to 1.
 - b. 0.37 to 1.
 - c. 0.33 to 1.
 - d. 0.13 to 1.
32. Marge Halifax, chief financial officer of Strickland Construction, has been tracking the activities of the company's nearest competitor for several years. Among other trends, Halifax has noticed that this competitor is able to take advantage of new technology and bring new products to market more quickly than Strickland. In order to determine the reason for this, Halifax has been reviewing the following data regarding the two companies.

	<u>Strickland</u>	<u>Competitor</u>
Accounts receivable turnover	6.85	7.35
Return on assets	15.34	14.74
Times interest earned	15.65	12.45
Current ratio	2.11	1.23
Debt/equity ratio	42.16	55.83



Degree of financial leverage	1.06	1.81
Price/earnings ratio	26.56	26.15

On the basis of this information, which one of the following is the **best** initial strategy for Halifax to follow in attempting to improve the flexibility of Strickland?

- a. Seek cost cutting measures that would increase Strickland's profitability.
- b. Investigate ways to improve asset efficiency and turnover times to improve liquidity.
- c. Seek additional sources of outside financing for new product introductions.
- d. Increase Strickland's investment in short-term securities to increase the current ratio.

33. A wholesale supplier has collected the following financial data on three companies that only purchase their products for resale to retail consumers.

	<u>Company A</u>	<u>Company B</u>	<u>Company C</u>
Sales	£1,000,000	£1,250,000	£2,450,000
Gross profit margin	20%	30%	25%
Beginning inventory	£35,000	£80,000	£155,000
Ending inventory	£65,000	£225,000	£175,000

On the basis of the information provided above, the supplier is able to conclude that

- a. Company B is turning the product inventory the fastest.
- b. Company C is turning the product inventory the fastest.
- c. Companies B and C are both turning the product inventory faster than Company A.



- d. Companies A and C are both turning the product inventory faster than Company B.
34. A financial analyst is analyzing the accounts receivable period for three companies by comparing their days' sales in receivables. The financial analyst has collected the following information for the companies.

	<u>Company A</u>	<u>Company B</u>	<u>Company C</u>
Net credit sales	\$175,000	\$145,000	\$225,000
Average accounts receivable, net	10,000	20,000	11,500
Average allowance for uncollectible accounts	3,500	6,500	4,500

If each of the companies has credit terms of net 30 days, the financial analyst is **most** likely to conclude which one of the following?

- a. Company C is less efficient than Company A in collecting payment.
 - b. Company B is more efficient than Company C in collecting payment.
 - c. Company A is the most efficient in collecting payment.
 - d. Company B is the least efficient in collecting payment.
35. Maydale Inc.'s financial statements show the following information.

Accounts receivable, end of Year 1	\$ 320,00
Credit sales for Year 2	3,600,00
Accounts receivable, end of Year 2	400,000

Maydale's accounts receivable turnover ratio is



- a. 0.10.
- b. 9.00.
- c. 10.00.
- d. 11.25.

36. Lowell Corporation has decided to include certain financial ratios in its year-end annual report to shareholders. Selected information relating to its most recent fiscal year is provided below.

- Cash \$ 10,000
- Accounts receivable (end of year) 20,000
- Accounts receivable (beginning of year) 24,000
- Inventory (end of year) 30,000
- Inventory (beginning of year) 26,000
- Notes payable (due in 90 days) 25,000
- Bonds payable (due in 10 years) 35,000
- Net credit sales for year 220,000
- Cost of goods sold 140,000

Using a 365-day year, compute Lowell's accounts receivable turnover in days.

- a. 26.1 days.
- b. 33.2 days.
- c. 36.5 days.
- d. 39.8 days.

37. Zubin Corporation experiences a decrease in sales and the cost of goods sold, an increase in accounts receivable, and no change in inventory. If all else is held



constant, what is the total effect of these changes on the receivables turnover and inventory ratios?

Inventory	Receivables
<u>Turnover</u>	<u>Turnover</u>
a. Increased;	Increased.
b. Increased;	Decreased.
c. Decreased;	Increased.
d. Decreased;	Decreased.

38. Peggy Monahan, controller, has gathered the following information regarding Lampasso Company.

	<u>Beginning of the year</u>	<u>End of the year</u>
Inventory	\$6,400	\$7,600
Accounts receivable	2,140	3,060
Accounts payable	3,320	3,680

Total sales for the year were \$85,900, of which \$62,400 were credit sales. The cost of goods sold was \$24,500.

Lampasso's inventory turnover ratio for the year was

- a. 3.2 times.
- b. 3.5 times.
- c. 8.2 times.
- d. 8.9 times.

39. Garland Corporation's Income Statement for the year just ended is shown below.

Net sales	\$900,000
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Cost of goods sold	
Inventory - beginning	\$125,000
Purchases	<u>540,000</u>
Goods available for sale	665,000
Inventory - ending	<u>138,000</u>
	<u>527,000</u>
Gross profit	373,000
Operating expenses	<u>175,000</u>
Income from operations	<u>\$198,000</u>

Garland's average inventory turnover ratio is

- a. 6.84.
 - b. 6.52.
 - c. 4.01.
 - d. 3.82.
40. Makay Corporation has decided to include certain financial ratios in its year-end annual report to shareholders. Selected information relating to its most recent fiscal year is provided below.

- Cash \$ 10,000
- Accounts receivable (end of year) 20,000
- Accounts receivable (beginning of year) 24,000
- Inventory (end of year) 30,000
- Inventory (beginning of year) 26,000
- Notes payable (due in 90 days) 25,000
- Bonds payable (due in 10 years) 35,000
- Net credit sales for year 220,000



- Cost of goods sold 140,000

Makay's average inventory turnover for the year was

- a. 4.7 times.
 - b. 5.0 times.
 - c. 5.4 times.
 - d. 7.9 times.
41. Globetrade is a retailer that buys virtually all of its merchandise from manufacturers in a country experiencing significant inflation. Globetrade is considering changing its method of inventory costing from first-in, first-out (FIFO) to last-in, first-out (LIFO). What effect would the change from FIFO to LIFO have on Globetrade's current ratio and inventory turnover ratio?
- a. Both the current ratio and the inventory turnover ratio would increase.
 - b. The current ratio would increase but the inventory turnover ratio would decrease.
 - c. The current ratio would decrease but the inventory turnover ratio would increase.
 - d. Both the current ratio and the inventory turnover ratio would decrease.
42. Lancaster Inc. had net accounts receivable of \$168,000 and \$147,000 at the beginning and end of the year, respectively. The company's net income for the year was \$204,000 on \$1,700,000 in total sales. Cash sales were 6% of total sales. Lancaster's average accounts receivable turnover ratio for the year is
- a. 9.51.
 - b. 10.15.
 - c. 10.79.



d. 10.87.

43. Cornwall Corporation's net accounts receivable were \$68,000 and \$47,000 at the beginning and end of the year, respectively. Cornwall's condensed Income Statement is shown below.

Sales	\$900,000
Cost of goods sold	527,000
Operating expenses	<u>175,000</u>
Operating income	198,000
Income tax	<u>79,000</u>
Net income	<u>\$119,000</u>

Cornwall's average number of days' sales in accounts receivable (using a 360-day year) is

- a. 8 days.
 - b. 13 days.
 - c. 19 days.
 - d. 23 days.
44. The following financial information is given for Anjuli Corporation (in millions of dollars).

	<u>Prior Year</u>	<u>Current Year</u>
Sales	\$10	\$11
Cost of goods sold	6	7
Current Assets		
Cash	2	3
Accounts receivable	3	4
Inventory	4	5



Between the prior year and the current year, did the days sales in inventory and days sales in receivables for Anjuli increase or decrease? Assume a 365-day year.

Days Sales <u>in Inventory</u>	Days Sales <u>in Receivables</u>
-----------------------------------	-------------------------------------

- | | |
|---------------|------------|
| a. Increased; | Increased. |
| b. Increased; | Decreased. |
| c. Decreased; | Increased. |
| d. Decreased; | Decreased. |

45. On its year-end financial statements, Caper Corporation showed sales of \$3,000,000, net fixed assets of \$1,300,000, and total assets of \$2,000,000. The company's fixed asset turnover is

- a. 1.5 times.
- b. 43.3%.
- c. 2.3 times.
- d. 65%.

46. Douglas Company purchased 10,000 shares of its common stock at the beginning of the year for cash. This transaction will affect all of the following **except** the

- a. debt-to-equity ratio.
- b. earnings per share.
- c. net profit margin.
- d. current ratio.



47. The assets of Moreland Corporation are presented below.

	<u>January 1</u>	<u>December 31</u>
Cash	\$ 48,000	\$ 62,000
Marketable securities	42,000	35,000
Accounts receivable	68,000	47,000
Inventory	125,000	138,000
Plant & equipment		
(net of accumulated depreciation)	325,000	424,000

For the year just ended, Moreland had net income of \$96,000 on \$900,000 of sales.

Moreland's total asset turnover ratio is

- a. 1.27.
- b. 1.37.
- c. 1.48.
- d. 1.50.

48. Interstate Motors has decided to make an additional investment in its operating assets which are financed by debt. Assuming all other factors remain constant, this increase in investment will have which one of the following effects?

Operating Return on

Income	Operating	Operating
<u>Margin</u>	<u>Asset Turnover</u>	<u>Assets</u>
a. Increase	No change	Increase.
b. No change	Decrease	Decrease.
c. No change	Increase	Decrease.
d. Decrease	Decrease	Decrease.



49. A company had \$450,000 in assets, \$250,000 in liabilities, and \$200,000 in common equity at the beginning of the fiscal year. The company's management is projecting that net income for the current fiscal year will be \$55,000 and common equity at the end of the fiscal year will be \$210,000. How much will the company's return on equity be at the end of the fiscal year?
- a. 12.2%.
 - b. 22.0%.
 - c. 26.8%.
 - d. 27.5%.
50. A company has a net profit margin of 5%, an operating profit margin of 10%, and a gross profit margin of 25%. Sales revenue is \$5,000,000. Selling, general, and administrative expenses are \$750,000. What is the cost of goods sold?
- a. \$4,750,000.
 - b. \$4,250,000.
 - c. \$3,750,000.
 - d. \$3,250,000.
51. A corporation had 250,000 shares of common stock outstanding on January 1. The financial manager of the corporation on September 30 is projecting net income of \$750,000 for the current year. If the management of the corporation is planning on declaring a \$55,000 preferred stock dividend and a 2- for-1 common stock split on December 31, earnings per common share on December 31 is expected to equal



- a. \$1.39.
- b. \$1.50.
- c. \$2.78.
- d. \$3.00.

52. A company's financial data for the recent fiscal year follows.

Common stock: 5,000,000 shares outstanding Preferred stock: 1,000,000 shares

Net income: \$50,000,000

Common stock dividends: \$8,000,000 Preferred stock dividends: \$2,000,000

The company would have reported basic and diluted earnings per share of

- a. \$10.00 and \$9.60, respectively.
- b. \$9.60 and \$8.00, respectively.
- c. \$10.00 and \$6.67, respectively.
- d. \$9.60 and \$9.60, respectively.

53. At the end of its fiscal year on December 31, 2000, Merit Watches had total shareholders' equity of \$24,209,306. Of this total, \$3,554,405 was preferred equity. During the 2001 fiscal year, Merit's net income after tax was \$2,861,003. During 2001, Merit paid preferred share dividends of \$223,551 and common share dividends of \$412,917. At December 31, 2001, Merit had 12,195,799 common shares outstanding and the company did not sell any common shares during the year. What was Merit Watch's book value per share on December 31, 2001?

- a. \$1.88.
- b. \$2.17.



- c. \$1.91.
 - d. \$2.20.
54. Donovan Corporation recently declared and issued a 50% stock dividend. This transaction will reduce the company's
- a. current ratio.
 - b. book value per common share.
 - c. debt-to-equity ratio.
 - d. return on operating assets.
55. The following information concerning Arnold Company's common stock was included in the company's financial reports for the last two years.

	<u>Year 2</u>	<u>Year 1</u>
Market price per share on December 31	\$60	\$50
Par value per share	10	10
Earnings per share	3	3
Dividends per share	1	1
Book value per share on December 31	36	34

Based on the price-earnings information, investors would **most likely** consider Arnold's common stock to

- a. be overvalued at the end of Year 2.
- b. indicate inferior investment decisions by management in Year 2.
- c. show a positive trend in growth opportunities in Year 2 compared to Year 1.
- d. show a decline in growth opportunities in Year 2 compared to Year 1.



56. Clark Inc. has prepared the following financial information for its initial public offering.

Long-term debt (8% interest rate)	\$10,000,000
Common equity:	
Par value (\$1 per share)	3,000,000
Additional paid-in-capital	24,000,000
Retained earnings	6,000,000
Total assets	55,000,000
Net income	3,750,000
Dividend (annual)	1,500,000

If public companies in Clark's industry are trading at twelve times earnings, what is the estimated value per share of Clark?

- a. \$9.00.
 - b. \$12.00.
 - c. \$15.00.
 - d. \$24.00.
57. Morton Starley Investment Banking is working with the management of Kell Inc. in order to take the company public in an initial public offering. Selected information for the year just ended for Kell is as follows.

Long-term debt (8% interest rate)	\$10,000,000
Common equity:	
Par value (\$1 per share)	3,000,000
Additional paid-in-capital	24,000,000



Retained earnings	6,000,000
Total assets	55,000,000
Net income	3,750,000
Dividend (annual)	1,500,000

If public companies in Kell's industry are trading at a market to book ratio of 1.5, what is the estimated value per share of Kell?

- a. \$13.50.
- b. \$16.50.
- c. \$21.50.
- d. \$27.50.

58. At the beginning of the year, Lewis Corporation had 100,000 shares of common stock outstanding. During the year, the following transactions occurred.

<u>Date</u>	<u>Transaction</u>
April 1	Issued 10,000 shares in exchange for land
July 1	Declared and distributed a 10% stock dividend
October 1	Purchased 5,000 shares of treasury stock

The number of shares that Lewis should use when computing earnings per share at the end of the year is

- a. 117,000.
- b. 116,000.
- c. 111,750.
- d. 106,250.



59. Selected financial data for ABC Company is presented below.

- For the year just ended ABC has net income of \$5,300,000.
- \$5,500,000 of 7% convertible bonds were issued in the prior year at a face value of \$1,000. Each bond is convertible into 50 shares of common stock. No bonds were converted during the current year.
- 50,000 shares of 10% cumulative preferred stock, par value \$100, were issued in the prior year. Preferred dividends were not declared in the current year, but were current at the end of the prior year.
- At the beginning of the current year 1,060,000 shares of common stock were outstanding.
- On June 1 of the current year 60,000 shares of common stock were issued and sold.
- ABC's average income tax rate is 40%.

ABC Company's basic earnings per share for the current fiscal year is

- a. \$3.67.
- b. \$4.29.
- c. \$4.38.
- d. \$4.73.

60. Devlin Inc. has 250,000 shares of \$10 par value common stock outstanding. For the current year, Devlin paid a cash dividend of \$3.50 per share and had earnings per share of \$4.80. The market price of Devlin's stock is \$34 per share. Devlin's price/earnings ratio is



- a. 2.08.
- b. 2.85.
- c. 7.08.
- d. 9.71.

61. At year-end, Appleseed Company reported net income of \$588,000. The company has 10,000 shares of \$100 par value, 6% preferred stock and 120,000 shares of \$10 par value common stock outstanding, and 5,000 shares of common stock in treasury. There are no dividend payments in arrears, and the market price per common share at the end of the year was \$40. Appleseed's price- earnings ratio is

- a. 9.47.
- b. 9.09.
- c. 8.50.
- d. 8.16.

62. Archer Inc. has 500,000 shares of \$10 par value common stock outstanding. For the current year, Archer paid a cash dividend of \$4.00 per share and had earnings per share of \$3.20. The market price of Archer's stock is \$36 per share. The average price/earnings ratio for Archer's industry is

14.00. When compared to the industry average, Archer's stock appears to be

- a. overvalued by approximately 25%.
- b. overvalued by approximately 10%.
- c. undervalued by approximately 10%.
- d. undervalued by approximately 25%.



63. A steady drop in a firm's price/earnings ratio could indicate that

- a. earnings per share has been increasing while the market price of the stock has held steady.
- b. earnings per share has been steadily decreasing.
- c. the market price of the stock has been steadily rising.
- d. both earnings per share and the market price of the stock are rising.

64. Collins Company reported net income of \$350,000 for the year. The company had 10,000 shares of \$100 par value, non-cumulative, 6% preferred stock, and 100,000 shares of \$10 par value common stock outstanding. There were also 5,000 shares of common stock in treasury during the year.

Collins declared and paid all preferred dividends as well as a \$1 per share dividend on common stock. Collins' earnings per share of common stock for the year was

- a. \$3.50.
- b. \$3.33.
- c. \$2.90.
- d. \$2.76.

65. Ray Company has 530,000 common shares outstanding at year-end. At December 31, for basic earnings per share purposes, Ray computed its weighted average number of shares as 500,000. Prior to issuing its annual financial statements, but after year-end, Ray split its stock 2 for 1. Ray's weighted average number of shares to be used for computing annual basic earnings per share is

- a. 500,000.



- b. 530,000.
- c. 1,000,000.
- d. 1,060,000.

66. On January 1, Esther Pharmaceuticals had a balance of 10,000 shares of common stock outstanding. On June 1, the company issued an additional 2,000 shares of common stock for cash. A total of 5,000 shares of 6%, \$100 par, nonconvertible preferred stock was outstanding all year. Esther's net income was \$120,000 for the year. The earnings per share for the year were

- a. \$7.50.
- b. \$8.06.
- c. \$10.00.
- d. \$10.75.

67. Roy company had 120,000 common shares and 100,000 preferred shares outstanding at the close of the prior year. During the current year Roy repurchased 12,000 common shares on March 1, sold 30,000 common shares on June 1, and sold an additional 60,000 common shares on November 1.

No change in preferred shares outstanding occurred during the year. The number of shares of stock outstanding to be used in the calculation of basic earnings per share at the end of the current year is

- a. 100,000.
- b. 137,500.
- c. 198,000.
- d. 298,000.



68. Selected information regarding Dyle Corporation's outstanding equity is shown below.

Common stock, \$10 par value,	
350,000 shares outstanding	\$3,500,000
Preferred stock, \$100 par value,	
10,000 shares outstanding	1,000,000
Preferred stock dividend paid	60,000
Common stock dividend paid	700,000
Earnings per common share	3
Market price per common share	18

Dyle's yield on common stock is

- a. 11.11%.
- b. 16.66%.
- c. 16.88%.
- d. 20.00%.

69. For the most recent fiscal period, Oakland Inc. paid a regular quarterly dividend of \$0.20 per share and had earnings of \$3.20 per share. The market price of Oakland stock at the end of the period was

\$40.00 per share. Oakland's dividend yield was

- a. 0.50%.
- b. 1.00%.
- c. 2.00%.
- d. 6.25%.



70. The dividend yield ratio is calculated by which one of the following methods?
- a. Market price per share divided by dividends per share.
 - b. Earnings per share divided by dividends per share.
 - c. Dividends per share divided by market price per share.
 - d. Dividends per share divided by earnings per share.
71. Mayson Company reported net income of \$350,000 for last year. The company had 100,000 shares of \$10 par value common stock outstanding and 5,000 shares of common stock in treasury during the year. Mayson declared and paid \$1 per share dividends on common stock. The market price per common share at the end of last year was \$30. The company's dividend yield for the year was
- a. 30.03%.
 - b. 28.57%.
 - c. 11.11%.
 - d. 3.33%.
72. The following information concerning Arnold Company's common stock was included in the company's financial reports for the last two years.

	<u>Year 2</u>	<u>Year 1</u>
Market price per share on December 31	\$60	\$50
Par value per share	10	10
Earnings per share	3	3
Dividends per share	1	1
Book value per share on December 31	36	34



Arnold's dividend yield in Year 2

- a. has increased compared to Year 1.
 - b. is indicative of the company's failure to provide a positive return to the investors.
 - c. is the same as Year 1.
 - d. has declined compared to Year 1.
73. A company is currently reviewing the most recent fiscal year's results of operations and noted an increase in the return on assets ratio when compared to the prior year. Which one of the following could have caused the increase?
- a. Sales decreased by the same dollar amount that expenses increased.
 - b. Sales increased by the same dollar amount as expenses and total assets.
 - c. Sales remained the same and expenses and total assets decreased.
 - d. Sales remained the same and ending inventory decreased.
74. At the end of Year 1, a company had average total assets of ¥450 million, average total liabilities of ¥150 million, and net income of ¥135 million. The company's management projects average total assets to increase by ¥50 million in Year 2 due to the planned purchase of a new manufacturing plant. The company will issue ¥30 million in new debt at the beginning of Year 2. No debt was paid down during Year 1. If the company's management projects net income to increase by 25% in Year 2, by approximately how much does the company's return on total assets increase between Year 1 and Year 2?
- a. 11%.
 - b. 13%.



c. 17%.

d. 20%.

75. A company's finished goods inventory was miscounted, and the correct balance is \$130,000 lower. Management is concerned about correcting the error because bonuses are only earned if the minimum gross profit margin is 45%. Selected financial information is shown below.

Revenues	\$1,000,000
Cost of goods sold	500,000
Salaries	57,000
Accounts receivable	22,000
Cash	43,000

With the corrected inventory, will the bonus target be met?

- a. Yes, the gross profit margin will increase.
 - b. No, the working capital will decrease.
 - c. Yes, the gross profit margin will not change.
 - d. No, the cost of goods sold will increase.
76. According to its public financial statements, a company's gross profit margin decreased by 5% while its operating profit margin increased by 3%. Which one of the following factors could cause both of these changes?
- a. An increase in the cost per unit of the goods purchased from a supplier.
 - b. A change to the variable costing income statement format.
 - c. A lowered selling price to increase quantities sold.



- d. Sale of fully-depreciated production machinery at a gain and replacement of the machines with newer models.
77. A company's Year 4 gross profit margin remained unchanged from Year 3. However, the company's Year 4 net profit margin increased from Year 3. Which one of the following could explain the change from Year 3 to Year 4?
- a. Sales decreased at a faster rate than operating expenses.
 - b. Corporate income tax rates decreased.
 - c. Preferred dividends increased.
 - d. Cost of goods sold decreased relative to sales.
78. Selected items from the equity section of a company's balance sheet are shown below.

	<u>Year 2</u>	<u>Year 1</u>
Common stock, 5,000,000 shares	\$ 50,000,000	\$ 50,000,000
Total equity	200,000,000	182,500,000

The increase in equity was caused by \$20,000,000 in net income less a common stock dividend payment of \$0.50 per share. The company's sustainable growth rate is

- a. 10.46%.
- b. 9.59%.
- c. 9.15%.
- d. 8.75%.



79. A U.S. based publicly traded company has a Swedish subsidiary. For the Swedish subsidiary, the Euro impacts the cost of goods sold and revenue. The primary source of long-term debt financing for the U.S. company is Canadian investors. The functional currency of the Swedish subsidiary is the
- a. U.S. dollar.
 - b. Canadian dollar.
 - c. Euro.
 - d. Swedish krona.
80. A firm's functional currency should be
- a. selected on the basis of several economic factors including cash flow, sales price, and financing indicators.
 - b. the currency of the foreign environment in which the firm primarily generates and expends cash.
 - c. selected on the basis of cost-benefit analysis and ease of preparing consolidated financial statements.
 - d. the currency of the parent organization as the firm operates as an extension of the parent's operations.
81. The functional currency of an entity is defined as the currency
- a. of the entity's parent company.
 - b. of the primary country in which the entity is physically located.
 - c. in which the books of record are maintained for all entity operations.
 - d. of the primary economic environment in which the entity operates.



82. During inflationary periods, last-in, first-out inventory accounting will generally have a
- a. lower cost of goods sold and lower inventory value.
 - b. lower cost of goods sold and higher inventory value.
 - c. higher cost of goods sold and higher inventory value.
 - d. higher cost of goods sold and lower inventory value.
83. During the current year, an entity changed its method of accounting for depreciation because it believed that the result would provide more reliable and relevant information. In its financial statements for the year, how should the entity report the adjustment resulting from the change in accounting principle?
- a. Disclose as a separate type of depreciation expense, directly following depreciation expense in the current year.
 - b. Report as an adjustment to beginning retained earnings of the earliest period presented in the financial statements.
 - c. Include in the determination of profit or loss for the current period as a cumulative effect adjustment.
 - d. Not disclose in the financial statements.
84. The concept of economic profit is **best** defined as total
- a. revenue minus all accounting costs.
 - b. income minus the sum of total fixed and variable costs.
 - c. revenue minus the sum of total fixed and variable costs.
 - d. revenue minus all explicit and implicit costs.



85. “Economic costs” often differ from costs shown in a firm’s financial statements. For a corporation, a major difference would arise due to
- a. interest costs.
 - b. salary and wage costs.
 - c. opportunity costs.
 - d. state and local tax costs.
86. Which of the following costs, when subtracted from total revenue, yields economic profit?
- a. Variable costs.
 - b. Recurring operating costs.
 - c. Fixed and variable costs.
 - d. Opportunity and explicit costs.
87. Williams makes \$35,000 a year as an accounting clerk. He decides to quit his job to enter an MBA program full-time. Assume Williams doesn’t work in the summer or hold any part-time jobs. His tuition, books, living expenses, and fees total \$25,000 a year. Given this information, the annual total economic cost of Williams’ MBA studies is
- a. \$10,000.
 - b. \$35,000.
 - c. \$25,000.
 - d. \$60,000.



88. The financial statements of Lark Inc. for last year are shown below.

Income Statement (\$000)

Revenue	\$4,000
Cost of sales	<u>2,900</u>
Gross margin	1,100
General & administrative	500
Interest	100
Taxes	<u>150</u>
Net income	<u>\$ 350</u>

Balance Sheet (\$000)

Current assets	\$ 800	Current liabilities	\$ 500
Plant & equipment	3,200	Long-term debt	\$1,000
		Common equity	<u>2,500</u>
Totals	<u>\$4,00</u>	Totals	<u>\$4,000</u>
	<u>0</u>		

If Lark's book values approximate market values and if the opportunity costs of debt and equity are 10% and 15%, respectively, what was the economic profit for Lark last year?

- a. (\$125,000).
- b. (\$25,000).
- c. \$0.
- d. \$350,000.

89. A company with a lower quality of earnings is **most** likely to



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- a. hire lower-skilled workers or purchase lower-quality materials.
 - b. manage the recognition of revenues, expenses, gains, and losses.
 - c. present an operating profit margin lower than the industry average.
 - d. rely on a few large customers to generate a large portion of its sales.
90. A company could negatively affect its earnings quality if it frequently
- a. constructed plants in countries with unstable currency.
 - b. invested long-term in an erratic stock or bond market.
 - c. materially changed accounting estimates.
 - d. offered significant sales discounts.
91. A manufacturing company operates in an environment of significant inflationary pressures. Which one of the following inventory methods should the company choose to produce financial statements considered to be of the highest earnings quality?
- a. Specific identification.
 - b. First-in, first-out.
 - c. Last-in, first-out.
 - d. Average cost.



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II. Tự luận

1. Sentech Scientific Inc., a manufacturer of test instruments, is in contract negotiations with the labor union that represents its hourly manufacturing employees. Negotiations have reached an impasse, and it appears that a strike is imminent. The controller has called the general accounting manager into his office to discuss liquidity issues if and when a strike does occur.

The controller asks the accounting manager to recommend measures to assess liquidity if a strike were to occur. Although some of the nonunion employees could probably produce test instruments during a strike, the controller would rather be conservative and assume no shipments during this time frame. Since the customers may go to other sources to obtain the products they need during a strike, cash receipts for current outstanding amounts owed by customers may not be paid on a timely basis.

Questions

- A. Define liquidity and explain its importance to Sentech.
 - B. Identify three measures that could be used to assess liquidity and explain how to calculate these measures.
 - C. Determine which liquidity measure identified above would **best** fit the controller's requirements, and explain why. Include in your discussion the reasons why the other measures would not be as appropriate.
2. In the Statements of Financial Accounting Concepts, the Financial Accounting Standards Board (FASB) set forth the fundamentals on which financial accounting and reporting standards are to be based. Specifically, the FASB intends that these concept statements establish objectives and concepts that can be used to develop standards for financial accounting and reporting, and to resolve new and emerging problems. Knowledge of the FASB objectives and concepts should enable those affected by financial accounting standards to better understand the content and limitations of the information provided by financial accounting and reporting. Statement of Financial Accounting Concepts No. 1 discusses the objectives of financial reporting by business enterprises, and Statement of Financial Accounting Concepts No. 5 recommends the composition of a full set of financial statements.

Questions

Identify and describe the major sections of the Statement of Cash Flows.



Answer for Section A: Financial Statement Analysis

(Trả lời phần A: Phân tích báo cáo tài chính)

I. Trắc nghiệm

1. Correct answer a. Gordon's common-size gross profit percentage has decreased as a result of an increasing common-size trend in cost of goods sold as shown below.

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>
Sales	100%	100%	100%	100%
Cost of goods sold ($\div$ Sales)	60.0%	60.3%	60.7%	60.7%
Gross profit ($\div$ Sales)	40.0%	39.6%	39.2%	39.2%

2. Correct answer c. $120,000/600,000 = 0.20$ or 20%
3. Correct answer d. 14% increase in selling expenses = $\frac{\pounds 40,000}{\pounds 35,000} - 1$.
4. Correct answer d.
- a. Sales revenue \$6,000,000 \$6,600,000 increased by $600,000/6,000,000 = 10\%$
- b. Net income \$500,000 \$540,000 increased by $40,000/500,000 = 8\%$
- c. Total assets \$10,000,000 \$10,500,000 increased by $500,000/10,000,000 = 5\%$
- d. Inventory \$600,000 \$500,000 decreased by $100,000/600,000 = 17\%$
5. Correct answer d. Both the current ratio and the quick ratio include cash, accounts receivable, and marketable securities; therefore a, b, and c are incorrect. Choice d is correct because the quick ratio does not include inventory, which is considered less liquid than the other current assets.
6. Correct answer c. $(\$531,000 + \$439,000 + \$200,000) / \$500,000 = 2.34$



7. Correct answer a. Broomall's working capital is \$40,000 calculated as follows.

$$\begin{array}{rcl} \text{Current assets} - \text{Current liabilities} & = & \text{Net working capital} \\ \$10,000 + \$20,000 + \$8,000 + \$42,000 & = & \$80,000 \text{ current assets} \\ \$15,000 + \$25,000 & = & \$40,000 \text{ current liabilities} \\ \$80,000 - \$40,000 & = & \underline{\$40,000} \text{ net working} \\ & & \text{capital} \end{array}$$

8. Correct answer b. When merchandise is purchased on credit, accounts payable increases and inventory increases by the same amount so net working capital remains unchanged.
9. Correct answer c. If \$100,000 is used to purchase inventory, the firm's quick ratio will decrease. Since inventory is not included in the calculation of current assets for the quick ratio, current assets will decrease while liabilities remain unchanged.
10. Correct answer d. Grimaldi's quick ratio at the end of the year is 1.52 as shown below.

$$(\text{Current assets} - \text{Inventory}) \div \text{Current liabilities} = \text{Quick ratio} (\$62,000 + \$35,000 + \$47,000) \div (\$84,000 + \$11,000) = \underline{1.52}$$

11. Correct answer c. Davis' current ratio will be lower than 2.3 times as shown below.

$$\begin{array}{lcl} \text{Before purchase:} & \$7,500,000 \div X & = 2.3 \\ X & = & \$3,260,870 \\ \text{After purchase:} & (\$7,500,000 + \$750,000) \div (\$3,260,870 + \$750,000) & = \underline{2.05} \end{array}$$



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12. Correct answer b. To increase its acid test ratio, Gratska should sell auto parts on account. This transaction will increase accounts receivable and thus the numerator of the ratio. Inventory is not included in the ratio so the change in inventory will not affect the ratio.
13. Correct answer c. The purchase will adversely affect the quick ratio by reducing the cash balance. Since inventory is not included in the quick ratio, the change in inventory will not offset the reduction in cash.
14. Correct answer d. A comparison of current assets with current liabilities gives an indication of the short-term debt-paying ability of a firm. Both working capital and the current ratio compare current assets with current liabilities and, therefore, measure credit worthiness.
15. Correct answer d. The current ratio and the quick ratio both compare current assets with current liabilities, however, the quick ratio eliminates inventory from current assets as it may not be readily converted into cash. Therefore, the disparity between the ratios is caused by the high level of inventory.
16. Correct answer d. The acid test (quick) ratio does not include inventory in the calculation of current assets and, therefore, measures debt-paying ability without liquidating inventory.
17. Correct answer b. The purpose of the acid test ratio is to measure debt-paying ability using highly liquid assets. Items such as prepaid insurance may be excluded as they do not represent current cash flow.



18. Correct answer d. Dedham's acid test ratio is 1.05 as shown below. $(\$10,000 + \$32,000) \div (\$15,000 + \$25,000) = \underline{1.05}$
19. Correct answer b. Because the payment will have a proportionally greater effect on current liabilities than on current assets, the company's current ratio will increase.
20. Correct answer a. The interest coverage ratio is calculated by dividing a company's earnings before income taxes by the company's interest expense. The lower the interest coverage ratio the higher the likelihood that the company will not have the ability to offer assured payment of interest to a lender. In this example, Company A has the lowest interest coverage ratio and the highest likelihood of defaulting on an outstanding loan from the bank.

	Company A	Company B	Company C	Company D
Earnings before income taxes	¥5,000,000	¥12,500,000	¥4,300,000	¥2,450,000
Interest expense	¥3,950,000	¥9,000,000	¥2,675,000	¥1,250,000
Interest coverage ratio	1.27	1.39	1.61	1.96

21. Correct answer b. $1.20 = \text{A\$750,000 earnings before interest and tax} / (\text{A\$750,000 earnings before interest and tax} - \text{A\$125,000 interest expense})$.
22. Correct answer a. Sterling is the most highly leveraged corporation because it has the greatest percentage of debt or financing with a fixed charge, e.g., interest.
23. Correct answer b. Sahara's degree of financial leverage is 1.36 as shown below.

$$\begin{aligned} \text{Degree of financial leverage} &= \text{EBIT} \div \text{EBT} \\ &= (\$1,320,000 + \$880,000 + \$800,000) \div (\$1,320,000 + \$880,000) \end{aligned}$$



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$$= \$3,000,000 \div \$2,200,000$$

$$= \underline{1.36}$$

24. Correct answer c. The degree of operating leverage measures the percent change in EBIT caused by a percent change in sales. Therefore, a degree of operating leverage of 3 indicates that a 1% change in sales will cause a 3% change in EBIT.
25. Correct answer a. Financial leverage is defined as the use of financing with a fixed charge such as interest. Firms with a high degree of financial leverage make significant use of debt and, therefore, have high debt-to-equity ratios.
26. Correct answer a. Financial leverage is defined as the use of financing with a fixed charge such as interest. Since debt is financing with a fixed charge, the use of debt increases financial leverage.
27. Correct answer d. Earnings to Mineral's shareholders will increase by 7.5% as shown below.

$$\text{Degree of financial leverage} = \% \text{ change in net income} \div \% \text{ change in EBIT}$$

$$1.5 = X \div 5\%$$

$$X = \underline{7.5\%}$$

28. Correct answer a. Because of the magnification of financial leverage, a decrease in earnings before interest and taxes will result in a proportionally larger decrease in earnings per share.
29. Correct answer d. The debt-to-total assets ratio indicates the percentage of assets financed by creditors and helps to determine how well creditors are protected in case



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of insolvency. From the perspective of debt-paying ability, the lower this ratio, the better.

30. Correct answer c. Since Easton Bank is seeking the company that is most likely to meet its loan obligations, the bank should select Astor. Both the degree of financial leverage and the debt/equity ratio are measures of debt-paying ability; Astor is below the industry average for both measures, indicating a low level of financial risk.

31. Correct answer a. The company's debt/equity ratio is .5 to 1 as shown below.

$$\begin{aligned}\text{Current liabilities} &= \$640,000 \div 3.2 \\ &= \$200,000 \\ \text{Equity} &= \$990,000 - (\$200,000 + \\ &\quad \$130,000) \\ &= \$660,000 \\ \text{Debt/equity ratio} &= (\$130,000 + \$200,000) \div \\ &\quad \$660,000 \\ &= \underline{\underline{.5 \text{ to } 1}}\end{aligned}$$

32. Correct answer c. As shown by the data, Strickland's competitor has a greater degree of financial leverage and a higher debt/equity ratio. The two measures indicate that the competitor makes greater use of outside financing than Strickland. Strickland should, therefore, consider increased outside borrowing to increase flexibility and fund research and development.
33. Correct answer d. The inventory turnover ratio is calculated by dividing cost of goods sold by the average inventory. The average inventory is the simply average of the beginning and ending inventory balances. A low inventory turnover ratio would



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signify that inventory does not sell fast. In this example, both Company A and Company C have higher calculated inventory turnover ratios than Company B and therefore sell the supplier's product inventory faster than Company B.

Company A inventory turnover ratio = 16.0 times per year = $((£1,000,000 \times (1-0.20)) / ((£35,000 + £65,000) / 2))$

Company B inventory turnover ratio = 5.7 times per year = $((£1,250,000 \times (1-0.30)) / ((£80,000 + £225,000) / 2))$

Company C inventory turnover ratio = 11.1 times per year = $((£2,450,000 \times (1-0.25)) / ((£115,000 + £175,000) / 2))$

34. Correct answer d.

Company B has collection problem as its days' sales in receivables exceeds the company's credit terms of net 30 days.

	<u>Company A</u>	<u>Company B</u>	<u>Company C</u>
Net credit sales [A]	\$175,000	\$145,000	\$225,000
Accounts receivable, net [B]	10,000	20,000	11,500
Allowance for uncollectible accounts [C]	3,500	6,500	4,500
Gross receivables [B + C = D]	13,500	26,500	16,000
Avg. daily sales on account [A / 365 days = E]	479.45	397.26	616.44
Days' sales in receivables [D / E]	28.16 days	66.71 days	25.96days

35. Correct answer c. Maydale's accounts receivable turnover ratio is 10.00 as shown below.



$$\begin{aligned}\text{Accts receivable turnover ratio} &= \text{Credit sales} \div \text{Average accounts receivable} \\ &= \$3,600,000 \div [(\$320,000 + \$400,000) \div 2] \\ &= \$3,600,000 \div \$360,000 \\ &= \underline{10.00}\end{aligned}$$

36. Correct answer c. Lowell's accounts receivable turnover in days is 36.5 as shown below.

$$\begin{aligned}\text{Accts receivable turnover (days)} &= 365 \div (\text{Credit sales} \div \text{Average accounts receivable}) \\ &= 365 \div [\$220,000 \div (\$20,000 + \$24,000) \div 2] \\ &= 365 \div (\$220,000 \div \$22,000) \\ &= 365 \div 10 \\ &= \underline{36.5 \text{ days}}\end{aligned}$$

37. Correct answer d. Both Zubin's inventory turnover and accounts receivable turnover ratios will decrease under these circumstances. The numerator values of these are cost of goods sold and credit sales, respectively. If these values both decline, the value of both ratios will decline.

38. Correct answer b. Lampasso's inventory turnover ratio is 3.5 times as shown below.

$$\begin{aligned}\text{Inventory turnover ratio} &= \text{Cost of goods sold} \div \text{Average inventory} \\ &= \$24,500 \div [(\$6,400 + \$7,600) \div 2] \\ &= \$24,500 \div \$7,000 \\ &= \underline{3.5 \text{ times}}\end{aligned}$$



39. Correct answer c. Garland's inventory turnover ratio is 4.01 as shown below.

$$\begin{aligned}\text{Inventory turnover ratio} &= \text{Cost of goods sold} \div \text{Average} \\ &\text{inventory} \\ &= \$527,000 \div [(\$125,000 + \$138,000) \div 2] \\ &= \$527,000 \div \$131,500 \\ &= \underline{4.01}\end{aligned}$$

40. Correct answer b. Makay's inventory turnover ratio is 5.0 times as shown below.

$$\begin{aligned}\text{Inventory turnover ratio} &= \text{Cost of goods sold} \div \text{Average} \\ &\text{inventory} \\ &= \$140,000 \div [(\$30,000 + \$26,000) \div 2] \\ &= \$140,000 \div \$28,000 \\ &= \underline{5.0 \text{ times}}\end{aligned}$$

41. Correct answer c. Globetrade's current ratio would decrease as a result of the change to LIFO because the value of ending inventory would be lower, thus decreasing the firm's current assets. Globetrade's inventory turnover ratio would increase as a result of the change to LIFO because the cost of goods sold would increase.

42. Correct answer b. Lancaster's accounts receivable turnover ratio is 10.15 as shown below.

$$\begin{aligned}\text{ccts. receivable turnover} &= \text{Credit sales} \div \text{Average accounts receivable} \\ &= [\$1,700,000 \times (1 - .06)] \div [(\$168,000 + \$147,000) \div 2] \\ &= \$1,598,000 \div \$157,500 \\ &= \underline{10.15}\end{aligned}$$



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43. Correct answer d. Cornwall's days' sales in accounts receivable is 23 as shown below.

$$\begin{aligned}\text{Days' sales in Accts. Rec.} &= \text{Average accounts receivable} \div (\text{Credit sales} \div 360) \\ &= [(\$68,000 + \$47,000) \div 2] \div (\$900,000 \div 360) \\ &= \$57,500 \div \$2,500 \\ &= \underline{23 \text{ days}}\end{aligned}$$

44. Correct answer a. Both measures have increased because both sales and cost of goods sold have increased while average accounts receivable and average inventory have remained the same.

45. Correct answer c. Caper's fixed asset turnover is 2.3 times calculated as follows.

$$\begin{aligned}\text{Fixed asset turnover} &= \text{Sales} \div \text{Average net property, plant, \& equipment} \\ &= \$3,000,000 \div \$1,300,000 \\ &= \underline{2.3 \text{ times}}\end{aligned}$$

46. Correct answer c. The only measure not affected by the purchase of its own common stock is Douglas' net profit margin. Both the debt/equity ratio and the earnings per share are affected by the number of outstanding shares of common stock, while the current ratio is affected by the amount of cash held.

47. Correct answer b. Moreland's total asset turnover is 1.37 as calculated below.



$$\begin{aligned}\text{Total asset turnover} &= \text{Sales} \div \text{Average total assets} \\ &= \$900,000 \div [(\$48,000 + \$42,000 + \$68,000 + \$125,000 + \\ &\quad \$325,000 \\ &\quad + \$62,000 + \$35,000 + \$47,000 + \$138,000 + \$424,000) \div 2] \\ &= \$900,000 \div \$657,000 \\ &= \underline{1.37}\end{aligned}$$

48. Correct answer b. Interstate's additional investment in operating assets will increase the total value of the firm's net property, plant, and equipment and will, therefore, decrease the operating asset turnover and the return on operating assets. The firm's operating income margin will be unaffected by this investment.

49. Correct answer c. $26.8\% = \$55,000 \text{ net income} / ((\$200,000 \text{ beginning of year common equity} + \$210,000 \text{ end of year common equity}) / 2)$

50. Correct answer c. 5,000,000 Sales

-3,750,000 CGS must find this so gross profit margin is 25%

$= 1,250,000 \quad 1,250,000 / 5,000,000 = 0.25 \quad (1 - .25) \times 5,000,000 = 3,750,000$

-750,000 OE

$= 500,000 \quad 500,000 / 5,000,000 = 0.10$ operating profit margin

-other expenses ... but irrelevant to question

$= 250,000 \quad \text{net income } 250,000 / 5,000,000 = .05$ net profit margin

51. Correct answer a.

$\$1.39 = (\$750,000 \text{ net income} - \$55,000 \text{ preferred dividends declared}) / (250,000 \text{ shares beginning of year} \times 2 \text{ for the 2-for-1 stock split}).$



52. Correct answer d.

Basic = $(50,000,000 - 2,000,000) / 5,000,000 = \$9.60$

Diluted = same \$9.60 (no convertible securities to change numerator or denominator)

53. Correct answer a. Merit's book value per share is \$1.88 as calculated below.

$$\begin{aligned}\text{Book value per share} &= (\text{Total equity} - \text{Preferred equity}) \div \text{Common shares outstanding} \\ &= (\$26,433,841 - \$3,554,405) \div 12,195,799 \\ &= \$22,879,436 \div 12,195,799 \\ &= \underline{\underline{\$1.88}}\end{aligned}$$

$$*\$24,209,306 + \$2,861,003 - \$223,551 - \$412,917$$

54. Correct answer b. Because a stock dividend increases the number of common shares outstanding, Donovan's book value per common share will decrease.

55. Correct answer c. Because the market price per share has increased while earnings per share remained the same, Arnold's price/earnings ratio has increased showing a positive trend in growth opportunities in Year 2.

56. Correct answer c. The estimated per share value of Clark's common stock is \$15.00 as calculated below.

$$\begin{aligned}\text{Estimated value per share} &= (\text{Net income} \div \text{Shares outstanding}) \times \text{Price/earnings ratio} \\ &= (\$3,750,000 \div 3,000,000) \times 12 \\ &= \underline{\underline{\$15.00}}\end{aligned}$$



57. Correct answer b. The value per share of Kell's common stock is \$16.50 as shown below.

Market to book ratio = Current price ÷ Book value per share

$$1.5 = X \div [(\$3,000,000 + \$24,000,000 + \$6,000,000) \div 3,000,000]$$

$$1.5X = \$11.00$$

$$X = \underline{\$16.50}$$

58. Correct answer a.

$$\text{Beg. Balance } 100,000 \quad \times 3/12 \times 1.1 \quad 27,500$$

$$\text{April 1st} \quad 110,000 \quad \times 3/12 \times 1.1 \quad 30,250$$

$$\text{July 1st} \quad 121,000 \quad \times 3/12 \quad 30,250$$

$$\text{October 1st} \quad 116,000 \quad \times 3/12 \quad \underline{29,000}$$

$$\underline{117,000}$$

59. Correct answer c. ABC's earnings per share is \$4.38 as shown below.

Weighted average shares	1,060,000 x 5/12	441,667
	1,120,000 x 7/12	<u>653,333</u>
		1,095,000

$$\begin{aligned} \text{Earnings per share} &= (\text{Net income} - \text{Preferred dividends}) \div \text{Weighted average shares} \\ &= [\$5,300,000 - (10\% \times \$100 \times 50,000)] \div 1,095,000 \end{aligned}$$



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$$= \$4,800,000 \div 1,095,000$$

$$= \underline{\underline{\$4.38}}$$

60. Correct answer c. Devlin's price/earnings ratio is 7.08 as shown below.

$$\begin{aligned} \text{Price/earnings ratio} &= \text{Market price per share} \div \text{Earnings per share} \end{aligned}$$

$$= \$34 \div \$4.80$$

$$= \underline{\underline{7.08}}$$

61. Correct answer b. Appleseed's price/earnings ratio is 9.09 as shown below.

$$\begin{aligned} \text{Earnings per share} &= (\text{Net income} - \text{Preferred dividends}) \div \text{Common shares outstanding} \end{aligned}$$

$$= [\$588,000 - (\$6 \times 10,000)] \div 120,000$$

$$= \$528,000 \div 120,000$$

$$= \$4.40$$

$$\begin{aligned} \text{Price/earnings ratio} &= \text{Market price per share} \div \text{Earnings per share} \end{aligned}$$

$$= \$40 \div \$4.40$$

$$= \underline{\underline{9.09}}$$

62. Correct answer d. Archer's stock is undervalued by approximately 25% as calculated below.

$$\begin{aligned} \text{Estimated market value} &= \text{Industry average P/E ratio} \times \text{Archer earnings per share} \end{aligned}$$

$$= 14.00 \times \$3.20$$

$$= \$44.80$$

$$\begin{aligned} \text{Archer market value difference} &= \$44.80 - \$36.00 \end{aligned}$$



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= \$8.80

Percentage difference = $\$8.80 \div \$36.00$

= 24.4%

63. Correct answer a. The price/earnings (P/E) ratio expresses the relationship between the market price of a stock and the stock's earnings per share. A steady drop in a firm's P/E ratio could, therefore, indicate that earnings per share has been increasing while the market price of the stock has held steady.

64. Correct answer c. Collins earnings per share is \$2.90 as shown below.

$$\begin{aligned}\text{Earnings per share} &= (\text{Net income} - \text{Preferred dividends}) \div \text{Common shares} \\ &\quad \text{outstanding} \\ &= (\$350,000 - \$60,000*) \div 100,000 \\ &= \underline{\underline{\$2.90}}\end{aligned}$$

*Preferred dividends = $(\$100 \times .06) \times 10,000 = \$60,000$

65. Correct answer c. When the common shares outstanding increase as the result of a stock dividend or a stock split, retroactive recognition must be given to these events for all comparative earnings per share presentations. Therefore, Ray Company would use 1,000,000 shares for computing earnings per share.

66. Correct answer b. Esther's earnings per share was \$8.06 as shown below.

Weighted average shares	<u>Shares</u>	<u>Months</u>	<u>Weighted Average</u>
	10,000	5/12	4,170



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12,000	7/12	<u>6,996</u>
		11,166

Preferred dividends = $(\$100 \times .06) \times 5,000$

Earnings per share = \$30,000

= $(\text{Net income} - \text{Preferred dividends}) \div \text{Common shares}$

= outstanding $(\$120,000 - \$30,000) \div 11,166$

= \$8.06

67. Correct answer b. Ray Company's weighted average number of shares for calculating earnings per share is 137,500 calculated as follows.

Weighted average shares	<u>Shares</u>	<u>Months</u>	<u>Weighted Average</u>
	120,000	2/12	20,000
	108,000	3/12	27,000
	138,000	5/12	57,500
	198,000	2/12	<u>33,000</u>
			<u>137,500</u>

68. Correct answer a. Dyle's yield on common stock is 11.11% as shown below.

Dividend yield = Dividends per common share $\div$ Market price per common share

= $(\$700,000 \div 350,000) \div \$18$

= 11.11%

69. Correct answer c. Oakland's dividend yield was 2.00% calculated as follows.



$$\begin{aligned}\text{Dividend yield} &= \text{Dividends per common share} \div \text{Market price per common share} \\ &= (4 \times \$0.20) \div \$40.00 \\ &= \underline{2.00\%}\end{aligned}$$

70. Correct answer c. Dividend yield indicates the relationship between the dividends per common share and the market price per common share and is calculated by dividing the dividends by the market price.

71. Correct answer d. Mayson's dividend yield was 3.33% as shown below.

$$\begin{aligned}\text{Dividend yield} &= \text{Dividends per common share} \div \text{Market price per common share} \\ &= \$1 \div \$30 \\ &= \underline{3.33\%}\end{aligned}$$

72. Correct answer d. Arnold's dividend yield has declined when compared to Year 1.

$$\begin{aligned}\text{Dividend yield} &= \text{Dividends per common share} \div \text{Market price per common share} \\ \text{Year 1} &= \$1 \div \$50 = 2.00\% \\ \text{Year 2} &= \$1 \div \$60 = 1.67\%\end{aligned}$$

73. Correct answer c. If sales remained the same and expenses increased, the net income increased. Additionally, the decrease in total assets means that the denominator of the ROA (net income divided by total assets) was smaller. Therefore, the overall result is an increase in the ratio.

74. Correct answer b.

$$13\% = (\text{¥}135 \text{ million} \times 1.25 / (\text{¥}450 \text{ million} + \text{¥}50 \text{ million})) / (\text{¥}135 \text{ million} / \text{¥}450 \text{ million}) - 1.$$

75. Correct answer d.



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Correcting the inventory error will cause cost of goods sold to increase, leading to a decrease in the gross profit margin. As a result, management will not be able to meet the 45% minimum required level of gross profit margin.

76. Correct answer c. Lowering the selling price would decrease the gross profit margin. If this increased units sold, both sales dollars and gross profit dollars could increase. If selling and administrative costs are primarily fixed, the company's operating income dollars would increase as well, and this could be sufficient to increase the operating profit margin.

77. Correct answer b.

Gross profit margin is net sales minus cost of goods sold. Net profit margin is gross profit margin minus all remaining expenses and losses, one of which is income taxes. If corporate tax rates decreased, net profit margin would increase. Leaving gross profit margin unchanged.

78. Correct answer c.

$$\{1 - [(5,000,000 \times .50)/20,000,000]\} \times \{20,000,000/[(200,000,000 + 182,500,000)/2]\}$$

79. Correct answer c. It is the currency in which prices and costs are most influenced.

80. Correct answer a. A firm's functional should be the currency of the primary economic environment in which the firm operates and should be selected on the basis of several economic factors including cash flow, sales price, and financing indicators.

81. Correct answer d. A firm's functional should be the currency of the primary economic environment in which the firm operates and should be selected on the



basis of several economic factors including cash flow, sales price, and financing indicators.

- 82. Correct answer d. With LIFO and inflation, inventory will be reported a lower than replacement cost (on balance sheet) so will underestimate inventory asset value (on balance sheet) and overstate inventory cost (cost of goods sold on income statement).
- 83. Correct answer b. A voluntary change in accounting principle or policy should be applied retrospectively unless any resulting adjustment that relates to prior periods is not reasonably determinable. Thus, if it is not impracticable to apply the new policy retroactively, the policy should be applied to comparative information as far back as practicable. The entity should determine the cumulative effect on the opening and closing balance sheets for the earliest period for which it is practicable to do so.
- 84. Correct answer d. Economic profit is defined as revenue minus all explicit and implicit costs. The implicit costs are generally referred to as opportunity costs.
- 85. Correct answer c. Economic profit is defined as revenue minus all explicit and implicit costs. The implicit costs are generally referred to as opportunity costs.
- 86. Correct answer d. Economic profit is defined as revenue minus all explicit and implicit costs. The implicit costs are generally referred to as opportunity costs.
- 87. Correct answer d. The economic cost of Williams' MBA studies is \$60,000.

Opportunity cost of quitting job \$35,000



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Explicit cost of studies	<u>25,000</u>
Economic cost	<u>\$60,000</u>

88. Correct answer b. Lark's economic profit was (\$25,000) as shown below.

$$\begin{aligned}\text{Economic profit} &= (\text{Net income} + \text{interest}) - (\text{Debt} + \text{Equity Opportunity Cost}) \\ &= (\$350,000 + \$100,000) - [(\$1,000,000 \times .1) + (\$2,500,000 \times .15)] \\ &= \$450,000 - \$475,000 \\ &= \underline{(\$25,000)}\end{aligned}$$

89. Correct answer b. Earnings management negatively affects the quality of earnings.

90. Correct answer c. Last-in-first-out, (LIFO), would result in the highest earnings quality via the most conservative use of available accounting policies by the company resulting in the matching of current costs against current revenues during periods of inflationary pressures.

91. Correct answer c. Choice c is correct because earnings quality refers to earnings attributable to higher sales or lower costs, rather than artificial profits created by changes in accounting estimates.

II. Tự luận

1. Answer A:

Liquidity is the ability of an asset to be converted into cash without significant price concessions. Liquidity is important to Sentech because current obligations will continue if there is a strike. Understanding the company's ability to meet its obligations even if normal cash receipts are not forthcoming would give management an indication of whether or not – and for how long – it could weather a strike. Lack of liquidity can limit a company's financial flexibility, making it unable to take advantage of discounts and other profitable opportunities. Liquidity problems can also lead to financial distress or bankruptcy.

Answer B:

Measures of liquidity include the following.

- Current ratio: current assets/current liabilities
- Quick ratio (or acid-test ratio): (cash + marketable securities + accounts receivable)/current liabilities



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Topic 4: The quick ratio excludes inventory and prepaid expenses from cash resources.

- Cash ratio: $(\text{cash} + \text{marketable securities}) / \text{current liabilities}$

Topic 5: Only cash and securities that are easily convertible into cash are used.

- Net working capital: $\text{current asset} - \text{current liabilities}$
- Net working capital ratio: $\text{net working capital} / \text{total assets}$
- Sales to working capital: $\text{sales} / \text{average net working capital}$
- Accounts receivable turnover: $\text{net sales} / \text{average gross receivables}$

Topic 6: This ratio can also be calculated in days.

- Inventory turnover: $\text{cost of goods sold} / \text{average inventory}$

Topic 7: This ratio can also be calculated in days.

Answer C:

Based on the parameters set down by the controller, either the quick ratio or the cash ratio would be best. The reason that these ratios are best is because they focus on the most liquid assets, excluding prepaid expenses and inventories. During a strike, inventories would not be a source of cash. The cash ratio excludes receivables as well, and would be the most conservative measure. The cash ratio would reflect the fact that the collection of receivables would be slowed during a strike.

2. The major sections of the Statement of Cash Flows describe the cash flows from

- Operating activities, which involves the cash effects of transactions that enter into the determination of net income, such as cash receipts from sales and cash payments to suppliers and employees.
- Investing activities, which includes making and collecting loans, and obtaining and disposing of investments and long-term assets.
- Financing activities, which includes borrowing and repaying cash from creditors (long-term debt), and obtaining funds from owners (investments) while providing a return on their investment (dividends).