Financial accounting cat 1

Type your answer. Insert space as you need to show your calculation

1. (20 points) Linda’s Clothing is a retailer of contemporary women’s clothing. Selected financial information for Linda’s appears below:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **2011** | **2010** | **2009** | **2008** |
| Net sales | $978,560 | $786,500 | $520,650 | $245,820 |
| Net Income | $  56,759 | $  31,150 | $  15,375 | $14,750 |
| Total Assets at year-end | $381,500 | $246,250 | $145,490 | $71,268 |
| Weighted Average number of shares |  |  |  |  |
| Outstanding | 84,215 | 80,546 | 77,965 | 75,888 |
| Total Liabilities at year-end | 205,967 | 119,657 | 60,522 | 17,623 |
| Common Stockholders' Equity at year-end | $175,533 | $126,593 | $  84,968 | $53,645 |
| Interest Expense | 165 | 195 | 258 | 368 |

Required:

|  |  |
| --- | --- |
| a.  | Compute the rate of return on assets for the years 2009-2011. Linda’s has an effective tax rate of 35%. (6 points) |
| b. | Compute the rate of return on common shareholders’ equity for the years 2009-2011. (6 points) |

 c. If Linda wants to improve its ROA, propose two scenarios to improve the operation by breaking down the ROA. Provide your numeric analysis by inserting a spreadsheet of proposed change of one item at a time. (8 points) (Answer to this part of question is used to assess Morgan student's mastery of Excel presentation and/or chart-making ability. Do your best presentation of an analysis to demonstrate your Excel ability. The presentation will not be evaluated as part of your semester grade; the content of the answer will).

2. (22 points)

a). Explain the difference between the Basic EPS and the Diluted EPS. (8 points)

b). Identify two capital structures that require the calculation of diluted EPS. (8 points)

c). Mathematically present the calculation of an anti-dilution scenario. (6 points)

3. (20 points) Below is selected data of Pronto Company:

|  |  |
| --- | --- |
| **Balance Sheet Data** | **As of December 31:** |
|  | **2012** | **2011** |
| Accounts receivable | $671,000 | $642,000 |
| Allowance for doubtful accounts |  31,000 |  22,000 |
| Net accounts receivable | $640,000 | $620,000 |
|  |  |  |
| Inventories - LCM | $542,500 | $642,500 |
|  |  |  |
| **Income Statement Data** |  |  |
| Net credit sales | $3,150,000 | $3,000,000 |
| Net cash sales |  800,000 |  600,000 |
| Net sales | $3,950,000 | $3,600,000 |
| Cost of goods sold | $2,390,000 | $2,160,000 |
| Selling, general and adm. expenses | 475,000 | 350,000 |
| Other | 150,000 | 125,000 |
| Total operating expenses | $3,015,000 | $2,635,000 |
| Net income |  $ 935,000 | $ 965,000 |

**Required:**

a. What is the accounts receivable turnover for 2012? (5 points)

b. What is the inventory turnover for 2012? (5 points)

c. Comment on the change of quality of the account receivables from 2011 to 2012. Assuming the estimate of the Allowance account is about right, is it justifiable to accept the change of account receivable quality from 2011 to 2012? (10 points)

4. (24 points) Watson manufactures and sells appliances. Intro develops and manufactures computer technology. Trenton operates general merchandise retail stores. Selected data for these companies appear in the following table (dollar amounts in millions). For each firm, assume that the market value of the debt equals its book value.

|  |  |  |  |
| --- | --- | --- | --- |
| ($ amounts in millions) | Watson | Intro | Trenton |
| Total Assets | $13,532 | $109,524 | $44,106 |
| Interest-Bearing Debt  | $ 2,597 | $ 33,925 | $18,752 |
| Average Pretax Borrowing Cost | 6.1% | 4.3% | 4.9% |
| Common Equity: |  |  |  |
|  Book Value | $ 3,006 | $ 13,465 | $13,712 |
|  Market Value | $ 2,959  | $110,984  | $22,521 |
| Income Tax Rate | 35.0% | 35.0% | 35.0% |
| Market Equity Beta  | 2.27 | 0.78 | 1.2 |

**Required**

**a.** Assume that the intermediate-term yields on U.S. Treasury securities

are roughly 3.5 percent. Assume that the market risk premium is 5.0 percent.

Compute the cost of equity capital for each of the three companies. (6 points)

**b.** Compute the weighted average cost of capital for each of the three companies. (6 points)

**c.** Compute the unlevered market (asset) beta for each of the three companies. (6 points)

d. You just acquired the company Intro, given the unlevered market (asset beta), you want to have an equity beta not higher than 0.9, say, exactly 0.9. How should you structure your capital, that is, what percentage of debt can you use in your total capital? (6 points)

5. (14 points) Below is information from the statement of cash flow and income statement for Garland Products, Inc. for 2012 and 2011. Marketable securities represent investments of excess cash that Garland Products does not need for operations. Garland Products' tax rate is 35%.

|  |  |  |
| --- | --- | --- |
| **Cash Flow Statement** |  |  |
| (in thousands) |  |  |
|  | **12/30/2012** | **12/30/2011** |
| **Cash from operations** |  |  |
| Net cash provided by operations | 106,484 | 113,880 |
|  |  |  |
| **Cash from investments** |  |  |
| (Increase) decrease in property & plant |  -31,536 | -47,960 |
| Acquisition (disposition) of subsidiaries or other business | -702 | -19 |
| Increase (decrease) in marketable securities | -18,825 | 380,737 |
|  |  |  |
| Net cash provided by (used in) investing | -51,063 | 332,758 |
|  |  |  |
| **Cash from financing** |  |  |
| Issuances (purchases) of equity shares | -370 | -434,570 |
| Issuances (repayment) of debt | - | - |
| Increase (decrease) in bank, or other borrowings | -25,000 | 25,000 |
| Dividends, other distributions | -29,377 | -37,202 |
|  |  |  |
| Net cash provided by (used in) financing | -54,747 | -446,772 |
|  |  |  |
| Net change cash & cash equivalents | 674 | -134 |
| Cash and cash equivalents at start of year | 3,255 | 3,389 |
| Cash and cash equivalents at year end | 3,929 | 3,255 |
|  |  |  |
| Interest Revenue | 50 | 35 |
| Interest Paid | 394 | 1400 |

a. (7 points) Using the above information calculate the amount of free cash flows to all debt and equity capital stakeholders for Garland Products for year 2012

b.(7 points) Using the above information calculate the amount of free cash flows for common equity shareholders for Garland Products for year 2012.