Financial Accounting for Executives & MBAs, 3rd Edition by Simko, Ferris & Wallace

Practice Quiz

Chapter 4 – Using Financial Statements for Investing and Credit Decisions

Multiple Choice Questions. Identify the answer that BEST completes the statement or answers the question.

1. The Claremont Company reported an ROE of 13.1% and a ROA of 5.3% for the year. Which statement is *true* concerning the company?

a. It generated more operating income than cash flows during the year.
b. It effectively utilized financial leverage.
c. It distributed 5.3% of its profits as dividends to its investors.
d. Its debt is equal to 5.3% of total assets.

Information from The Pomona Company is presented below for use in Questions 2, 3, and 4:

Amounts in millions	**Year 2**	**Year 1**
Balance sheet		
Total assets	$18,155	$16,377
Shareholders' equity	3,152	3,939
Income statement		
Net sales	$17,686	$17,517
Net income	3,115	1,965

2. During Year 2, Pomona paid dividends totaling $800 million. What rate of return did the company generate during Year 2 for its common shareholders?

a. 12.3 percent
b. 17.4 percent
c. 36.6 percent
d. 98.8 percent

3. What percentage of Pomona's Year 2 net income remains from each dollar of sales after subtracting all expenses?

a. 17.4 percent
b. 17.6 percent
c. 36.6 percent
d. 67.0 percent

4. What is Pomona's Year 2 (levered) return on assets?

a. 12.7 percent
b. 17.2 percent
c. 13.6 percent
d. 13.3 percent

Select financial data from Smith & Sons is presented below for use in Questions 5, 6, and 7:

Amounts in millions	**Year 1**	**Year 2**
Balance sheet		
Accounts receivable (net)	$9,367	$11,765
Inventory	6,660	6,039
Income statement		
Net sales	$52,516	$59,298
Cost of goods sold	7,541	8,525

5. What can be said regarding Smith & Son's accounts receivable turnover for Year 2?

a. It improved from Year 1 to Year 2.
b. It collected its accounts receivables less effectively in Year 2 as compared to Year 1.
c. Fewer customers purchased items on account during Year 2 as compared to Year 1.
d. Customers paid their account balances more quickly during Year 2 as compared to Year 1.

6. How many days, on average, did it take the company to collect an outstanding receivable during Year 2?

a. 37.7 days
b. 7.2 days
c. 72.4 days
d. 4.5 days

7. If the company were to allow its inventory level to drop to zero units on hand at December 31, Year 2, and its sales remained steady, how long would it take to sell its entire inventory?

a. 58.1 days
b. 85.8 days
c. 144.2 days
d. 258.6 days

8. Presented below are select ratios from The Claremont Company annual report:

	Year 1	**Year 2**
Accounts receivable turnover	8.2x	7.2x
Receivable collection period	44.5 days	50.7 days
Inventory turnover	12.6x	14.2x
Inventory-on-hand period	29.0 days	25.7 days

Which statement is true concerning the above ratios?

a. Claremont's accounts receivable collection period improved from Year 1 to Year 2.
b. The company's inventory management improved over the two year period.
c. The company sold more inventory during Year 2 than during Year 1.
d. It took the company longer to collect amounts due from customers during Year 1 than it did during Year 2.

9. Assessing a company's inventory turnover helps evaluate the:

a. Effectiveness of a company's receivable collection activities
b. Ability to measure the quality of the inventory on hand
c. Speed at which inventories move through a company's operations
d. Profitability of a company

10. If a company with a current ratio of 2.0 pays $2,000 of its salaries payable, then its current ratio will:

a. Change, but not enough information is provided to determine if it will increase or decrease
b. Decrease
c. Remain the same.
d. Increase