

Module 2 – Financial Accounting for MBAs, 7th Edition by Easton, Wild, Halsey & McAnally

Practice Quiz Solutions

1. Following are selected income statement and balance sheet data for companies in different industries.

\$ millions	Sales	Cost of goods sold	Gross profit	Net income	Assets	Liabilities	Equity
Harley-Davidson	\$ 5,342	\$ 3,302	\$ 2,040	\$ 960	\$ 5,255	\$ 2,171	\$ 3,084
Nike, Inc.	13,740	7,624	6,116	1,212	8,794	3,149	5,645
Starbucks Corp.	6,369	2,605	3,764	494	3,514	1,423	2,091
Target Corp.	51,271	34,927	16,344	2,408	34,995	20,790	14,205

Which company reports the highest ratio of net income to equity?

- a. Harley-Davidson
- b. Nike, Inc.
- c. Starbucks Corp.
- d. Target Corp.

Answer: a

Harley-Davidson = 31.1%; Nike = 21.5%; Starbucks = 23.6%; Target = 17.0%

Harley enjoys the highest profitability as measured by net income to equity, followed by Starbucks and Nike. These are all premium brands that have effectively differentiated their products and can, therefore, enjoy above-average returns on stockholder investment. Although Target is well run, it operates in the highly competitive retail segment where it is nearly impossible to differentiate products. Its returns on shareholder investment are the lowest of the four companies, although still above the median of 12% for all publicly traded companies.

2. Following are selected income statement and balance sheet data for companies in different industries.

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Which company has financed itself with the highest percentage of liabilities to equity?

- a. Harley-Davidson
- b. Nike, Inc.
- c. Starbucks Corp.
- d. Target Corp.

Answer: d

Harley-Davidson = 70.4%; Nike = 55.8%; Starbucks = 68.1%; Target = 146.4%

Target has the highest proportion of debt in its capital structure mostly because it has its own, proprietary credit card. The credit card industry is similar to a bank – high debt levels and relatively low margins. Target consolidates its credit card operations with those of its retail sales. This inflates Target's consolidated debt level above what we typically observe for stand-alone retail operations. Finally, companies that enjoy relatively stable cash flows can afford higher debt levels because there is some assurance that future cash flows will be sufficient to cover fixed debt payments. The other three companies operate with a greater proportion of equity than of debt.

3. Following are selected income statement accounts for Apple Inc.

(\$ millions)	
Sales	\$233,715
Cost of goods sold	<u>140,089</u>
Gross profit	93,626
Total expenses	<u>40,232</u>
Net income	<u>\$ 53,394</u>

Compute Apple's gross profit margin.

- a. 22.7%
- b. 40.0%
- c. 17.2%
- d. 11.2%

Answer: b

Gross Profit Margin = $\$93,626 / \$233,715 = 40.0\%$

4. Indicate which of the following items would be reported in the balance sheet.

- | | | |
|-------------------------|-----------------------------|---------------------|
| A. Net income | D. Accumulated depreciation | G. Interest expense |
| B. Retained earnings | E. Wages expense | H. Interest payable |
| C. Depreciation expense | F. Wages payable | I. Sales |

- a. C, E, G, I
- b. A, D, F, G
- c. B, C, E, H
- d. B, D, F, H

Answer: d

Retained earnings, Accumulated depreciation, Wages payable, and Interest payable would all be reported in the balance sheet.

5. Indicate which of the following items would be reported in the income statement.

- | | | |
|-------------------------|------------------------|---------------------|
| A. Sales | D. Accounts receivable | G. Inventories |
| B. Retained earnings | E. Dividends | H. Accounts payable |
| C. Depreciation expense | F. Cost of goods sold | I. Net income |

- a. C, E, G, I
- b. A, C, F, I
- c. B, C, E, H
- d. A, E, F, I

Answer: b

Sales, depreciation expense, Cost of goods sold, and Net income would all be reported in the income statement.

6. Following is financial information from Johnson & Johnson for a recent fiscal year.

(\$ millions)			
Retained earnings, January 1	\$35,223	Dividends	\$3,793
Net Earnings	10,411	Retained earnings, December 31	?
Other retained earnings changes	(370)		

What is the retained earnings balance at December 31?

- a. \$24,442 million
- b. \$31,430 million
- c. \$41,471 million
- d. \$49,057 million

Answer: c

Retained earnings, January 1	\$35,223
Add: Net income	10,411
Less: Dividends	(3,793)
Other retained earnings changes	(370)
Retained earnings, December 31	<u>\$41,471</u>

7. Daniels Company reports the following year-end account balances at December 31, 2017.

Accounts payable	\$20,000	Inventory	\$40,000
Accounts receivable	\$40,000	Land	\$100,000
Bonds payable, long-term	\$250,000	Goodwill	\$10,000
Buildings	\$160,000	Retained earnings	\$115,000
Cash	\$50,000	Sales revenue	\$500,000
Common stock	\$100,000	Supplies inventory	\$5,000
Cost of goods sold	\$200,000	Supplies expense	\$20,000
Equipment	\$80,000	Wages expense	\$100,000

What is Daniels Company's net income for 2017?

- a. \$380,000
- b. \$375,000
- c. \$180,000
- d. \$300,000

Answer: c

Sales revenue.....		\$500,000
Expenses		
Cost of goods sold	\$200,000	
Wages expense	100,000	
Supplies expense	<u>20,000</u>	
Total expenses		<u>320,000</u>
Net income.....		<u>\$180,000</u>

8. Identify which of the following accounts would appear as assets in the balance sheet?

- | | | |
|----------------------|---------------------|--------------------------|
| A. Dividends | D. Goodwill | G. Cash |
| B. Retained earnings | E. Deferred revenue | H. Interest payable |
| C. Prepaid insurance | F. Wages payable | I. Marketable securities |

- a. C, D, G, I
- b. A, C, D, E
- c. B, C, E, H
- d. C, D, E, G

Answer: a

Prepaid insurance, Goodwill, Cash, and Marketable securities are all accounts that would appear in the asset section of the balance sheet.

9. Following is selected financial information for Aiello, Inc. for the years 2017 and 2016.

(\$ millions)	2017	2016
Beginning retained earnings	\$?	\$245,870
Net income (loss)	88,030	79,980
Dividends	25,120	?
Ending retained earnings	?	290,570

What is Aiello, Inc.'s ending retained earnings balance for 2017?

- a. \$403,720
- b. \$227,660
- c. \$353,480
- d. \$290,570

Answer: c

Beginning retained earnings = Prior year's ending retaining earnings.

2017 Beginning retained earnings	\$290,570
Add Net income	88,030
Less Dividends	<u>(25,120)</u>
2017 Ending retained earnings	<u>\$353,480</u>

10. Selected balance sheet amounts for Reed Corporation for 2017 follow.

Current assets	Long-term assets	Total assets	Current liabilities	Long-term liabilities	Total liabilities	Equity
\$9,540	?	?	\$14,520	\$12,340	?	\$15,990

What is the balance sheet amount for Long-term assets?

- a. \$42,850
- b. \$33,310
- c. \$26,860
- d. \$29,500

Answer: b

Total assets = Total liabilities (current liabilities + long-term liabilities) + Equity
 $\$14,520 + \$12,340 + \$15,990 = \$42,850$ total assets - $\$9,540$ current assets
 $= \$33,310$ long-term assets