

Review for Exam #1

Exam #1

- *Don't Forget:*

- Scan Sheet
- Calculator
- Pencil
- Picture ID
- Cheat Sheet

Things To Do...

- Study both the notes and the book.
- Remember the Panopto Recordings in Canvas.
- Do suggested problems.
- Do more problems!
- Be comfortable with calculator, but understand concepts (e.g., timeline).
- Get help if you are having problems.

HELP!

○ Office Hours

✦ _____

✦ _____

or by appointment

Things NOT To Do...

- Study solutions and not do problems.
- Memorize all the formulas.
- Miss the exam.
- Forget your calculator.
- Cheat.
- Think bad thoughts about me between now and the exam.

Conceptual Exercise

Which of the following is a great reason to take Yost's 3610 class?

- I. It is the easiest class in the College.
 - II. He's the best looking professor at AU.
 - III. His outstanding use of colors and diagrams cannot be duplicated.
- A) I only
 - B) I and II
 - C) I and III
 - D) II and III
 - E) I, II, and III

Warning

The following may not contain everything we covered, and therefore, may not contain all testable material.

Introduction to Corporate Finance

- Chapter 1
- What is corporate finance? What are the three functions?
- What is the goal of the firm?
- What are the benefits/drawbacks of sole proprietorships, general and limited partnerships, and corporations?
- What are agency costs and how do we mitigate them?

Financial Statements and Cash Flow

- Chapter 2 and section 3.1 of Chapter 3
- Balance Sheet
 - Book Values versus Market Values
- Income Statement
 - Accounting Numbers versus Cash Flows
- Statement of Cash Flows
 - Sources and Uses of Cash
- Taxes
 - Average versus Marginal

Financial Statement Analysis

- Chapter 3
- Ratios
 - How to calculate them.
 - What they tell us.
 - DuPont Identity
- Common size balance sheets and income statements
- Potential Problems for Ratio Analysis

The Time Value of Money

- Chapter 5
- Present and Future Values of Single Cash Flows (and multiple cash flows by adding them up)
- Calculate N, I/Y, PV, and FV.
- *Cannot compare cash flows across periods.*
- *Moving along time line.*
- *Understand concepts.*

Practice Problem #1

Which of the following actions are likely to reduce the agency problem between stockholders and managers?

- a. Congress passes a law that severely restricts hostile takeovers.
- b. A manager receives a lower salary but receives additional shares of the company's stock.
- c. The board of directors has become more vigilant in its oversight of the company's management.
- d. Statements b and c are correct.
- e. All of the statements above are correct.

Practice Problem #2

Information on the Statement of Cash Flows comes from...

- a. The Income Statement.
- b. The Balance Sheet.
- c. Both the Income Statement and the Balance Sheet.
- d. Market values not found on the Income Statement or Balance Sheet.
- e. Both c and d.

Practice Problem #3

Which of the following statements is most correct?

- a. Many large firms operate different divisions in different industries, and this makes it hard to develop a meaningful set of industry benchmarks for these types of firms.
- b. Financial ratios should be interpreted with caution because there exist seasonal and accounting differences that can reduce their comparability.
- c. Financial ratios should be interpreted with caution because it may be difficult to say with certainty what is a “good” value. For example, in the case of the current ratio, a “good” value is neither high nor low.
- d. Ratio analysis facilitates comparisons by standardizing numbers.
- e. All of the statements above are correct.

Practice Problem #4

Other things equal, present value...

- a. Increases as the number of periods increases.
- b. Increases as the rate of interest increases.
- c. Increases as the future value increases.
- d. Decreases as the rate of interest decreases.
- e. None of the above.

Practice Problem #5

The goal of the company is generally presumed to be...

- a. Sales maximization.
- b. Profit maximization.
- c. Shareholder wealth maximization.
- d. Cost minimization.
- e. Profit stabilization.

Practice Problem #6

On the Statement of Cash Flows, depreciation will be found in the section entitled...

- a. Cash Flow from Operating Activities.
- b. Cash Flow from Investing Activities.
- c. Cash Flow from Financing Activities.
- d. Cash Flow from Non-cash Adjustments.
- e. None of the above.

Practice Problem #7

Which of the following statements is most correct?

- a. A firm with financial leverage has a larger equity multiplier than an otherwise identical firm with no debt in its capital structure.
- b. The use of debt in a company's capital structure results in tax benefits to the investors who purchase the company's bonds.
- c. All else equal, a firm with a higher debt ratio will have a lower return on equity.
- d. All of the answers above are correct.
- e. Answers a and c are correct.

Practice Problem #8

Your dentist mentions that if you earn 15% for two years, you will have more money than if you earn 10% for one year and 20% for the other year. What do you think about your dentist's statement?

- a. The dentist is correct.
- b. The dentist is incorrect. Both sets of returns result in the same value.
- c. The dentist is incorrect. You will actually have more money if you earn 20% in the first year and 10% in the second year.
- d. The dentist is incorrect. You will actually have more money if you earn 10% in the first year and 20% in the second year.
- e. The dentist is incorrect. You will have more money if you earn 10% in one year and 20% in the other year, and it makes no difference what order the two returns occur in.

Practice Problem #9

Which of the following is not a significant advantage of the corporate form of organization over the partnership or proprietorship forms?

- a. Limited liability
- b. Double taxation
- c. Ease of transferring ownership
- d. Unlimited life
- e. Ability to raise funds

Practice Problem #10

The current Federal income tax system gives corporate financial managers the incentive to use _____ financial leverage and to _____ a higher proportion of corporate earnings.

- a. more; retain
- b. more; pay out
- c. less; retain
- d. less; pay out
- e. None of the above

Practice Problem #11

You observe that a firm's profit margin is below the industry average, its debt ratio is below the industry average, and its return on equity exceeds the industry average. What can you conclude?

- a. Inventory turnover is above the industry average.
- b. Total assets turnover is above the industry average.
- c. Total assets turnover is below the industry average.
- d. Both statements a and b are correct.
- e. None of the statements above is correct.

Practice Problem #12

Compute the present value of \$1,910 received after three years if the appropriate discount rate is 6.3%.

- a. \$1,431
- b. \$1,272
- c. \$1,590
- d. \$1,113
- e. Not enough information.

Answers

- | | | | |
|----|---|-----|---|
| 1. | D | 7. | A |
| 2. | C | 8. | A |
| 3. | E | 9. | B |
| 4. | C | 10. | A |
| 5. | C | 11. | B |
| 6. | A | 12. | C |