Study Guide 17

Name	Perfect Score	Your Score
Identifying Accounting Terms	20 Pts.	
Analyzing Financial Ratios	19 Pts.	
Calculating Financial Ratios	11 Pts.	
Total	50 Pts.	

Part One—Identifying Accounting Terms

Directions: Select the one term in Column I that best fits each definition in Column II. Print the letter identifying your choice in the Answers column.

Column I	*Column II*	*Answers*
A. benchmark	**1.** A ratio that measures the ability of a business to generate income. (p. 516)	**1.** ________
B. comparative financial statements	**2.** A standard used to compare financial performance. (p. 516)	**2.** ________
C. current ratio	**3.** Financial statements that provide information for multiple fiscal periods. (p. 517)	**3.** ________
D. debt ratio	**4.** An analysis of changes over time. (p. 517)	**4.** ________
E. dividend yield	**5.** Net income after federal income tax as a percent of net sales. (p. 517)	**5.** ________
F. earnings per share	**6.** Gross profit as a percent of net sales. (p. 518)	**6.** ________
G. gross margin	**7.** Income from operations as a percent of net sales. (p. 519)	**7.** ________
H. horizontal analysis	**8.** Total operating expenses as a percent of net sales. (p. 519)	**8.** ________
I. liquidity ratio	**9.** A ratio that measures the ability of a business to pay its long-term liabilities. (p. 526)	**9.** ________
J. market ratio	**10.** Total Liabilities divided by Total Assets. (p. 526)	**10.** ________
K. operating expense ratio	**11.** A comparison of one item on a financial statement with the same item on a previous period's financial statement. (p. 528)	**11.** ________
L. operating margin	**12.** Net income after federal income tax divided by the number of outstanding shares of stock. (p. 533)	**12.** ________
M. price-earnings ratio	**13.** A ratio that measures a corporation's financial performance in relation to the market value of its stock. (p. 534)	**13.** ________
N. profit margin	**14.** The relationship between dividends per share and market price per share. (p. 534)	**14.** ________
O. profitability ratio	**15.** The relationship between the market value per share and earnings per share of a stock. (p. 534)	**15.** ________
P. quick assets	**16.** A ratio that measures the ability of a business to pay its current financial obligations. (p. 535)	**16.** ________
Q. quick ratio	**17.** The amount of total current assets less total current liabilities. (p. 535)	**17.** ________
R. solvency ratio	**18.** A ratio that measures the relationship of current assets to current liabilities. (p. 535)	**18.** ________
S. trend analysis	**19.** Cash and other current assets that can be quickly converted into cash. (p. 535)	**19.** ________
T. working capital	**20.** A ratio that measures the relationship of quick assets to current liabilities. (p. 535)	**20.** ________

Part Two—Analyzing Financial Ratios

Directions: Place a *T* for True or an *F* for False in the Answers column to show whether each of the following statements is true or false.

	Answers
1. Vertical analysis ratios are an example of a profitability ratio. (p. 516)	**1.** ________
2. A benchmark ratio can be stated as a single value or a range of values. (p. 516)	**2.** ________
3. To perform vertical analysis on an income statement, each amount is divided by net sales. (p. 516)	**3.** ________
4. An increase in merchandise costs reduces the gross margin. (p. 518)	**4.** ________
5. Gross profit is also referred to as the rate of return on sales. (p. 518)	**5.** ________
6. The operating margin gives investors the best indication of how effectively a business is earning a profit from its normal business operations. (p. 519)	**6.** ________
7. Best Company's benchmark operating expense ratio is between 29.0% and 31.0%. A decline in its operating expense ratio from 34.5% to 33.6% is a favorable trend. (p. 519)	**7.** ________
8. Reducing the amount of operating expenses always has a positive impact on a business. (p. 520)	**8.** ________
9. A business should never make a business decision for the sole purpose of meeting a benchmark ratio. (p. 524)	**9.** ________
10. A vertical analysis ratio for accounts receivable above the target range may indicate that ThreeGreen is too restrictive in extending credit to its customers. (p. 524)	**10.** ________
11. Investors use the debt ratio to rate the ability of the business to pay its current and long-term liabilities. (p. 526)	**11.** ________
12. The debt ratio is an example of a solvency ratio. (p. 526)	**12.** ________
13. Best Company's target range for its debt ratio is 20.0% to 25.0%. The company's debt ratio decreased from 34.5% to 26.7%. This is an unfavorable trend. (p. 526)	**13.** ________
14. A horizontal analysis ratio is calculated by dividing the difference between the current and prior period amounts by the current period amount. (p. 528)	**14.** ________
15. EPS is the most widely recognized measure of a corporation's financial performance. (p. 533)	**15.** ________
16. A corporation's earnings per share can only be compared to the earnings per share of other corporations in the same industry. (p. 533)	**16.** ________
17. The dividend yield is an example of a market ratio. (p. 534)	**17.** ________
18. Investors are willing to pay a higher P/E ratio for income stocks than for growth stocks. (p. 534)	**18.** ________
19. The income statement is the primary source of data to calculate liquidity ratios. (p. 535)	**19.** ________

Name ______________________ Date ____________ Class ____________

Part Three—Calculating Financial Ratios

Directions: For each of the following items, select the choice that best completes the statement. Print the letter identifying your choice in the Answers column.

Selected financial information for Lambert Company is presented below.

Sales	$840,000.00
Cost of Merchandise Sold	$400,000.00
Total Operating Expenses	$360,000.00
Net Income after Federal Income Taxes	$68,000.00
Quick Assets	$38,000.00
Current Assets	$95,000.00
Total Assets	$175,000.00
Total Liabilities (all current)	$25,000.00
Dividends per Share	$3.00
Market Price	$60.00
Number of Shares Outstanding	10,000

Answers

1. The earnings per share is
   (A) $3.00 (C) $6.80
   (B) $14.70 (D) 8.1% (p. 533) — 1. ______

2. The debt ratio is
   (A) 26.3% (C) 7.00
   (B) 14.3% (D) 17.0% (p. 526) — 2. ______

3. The current ratio is
   (A) $70,000.00 (C) 54.3%
   (B) 0.74 (D) 3.80 (p. 535) — 3. ______

4. The dividend yield is
   (A) 5.00% (C) 20.00%
   (B) 0.03% (D) 10.00% (p. 534) — 4. ______

5. The gross margin is
   (A) 42.9% (C) 52.4%
   (B) 9.5% (D) 54.3% (p. 518) — 5. ______

6. The price-earnings ratio is
   (A) 8.8 (C) 5.0%
   (B) 17.6 (D) 11.3% (p. 534) — 6. ______

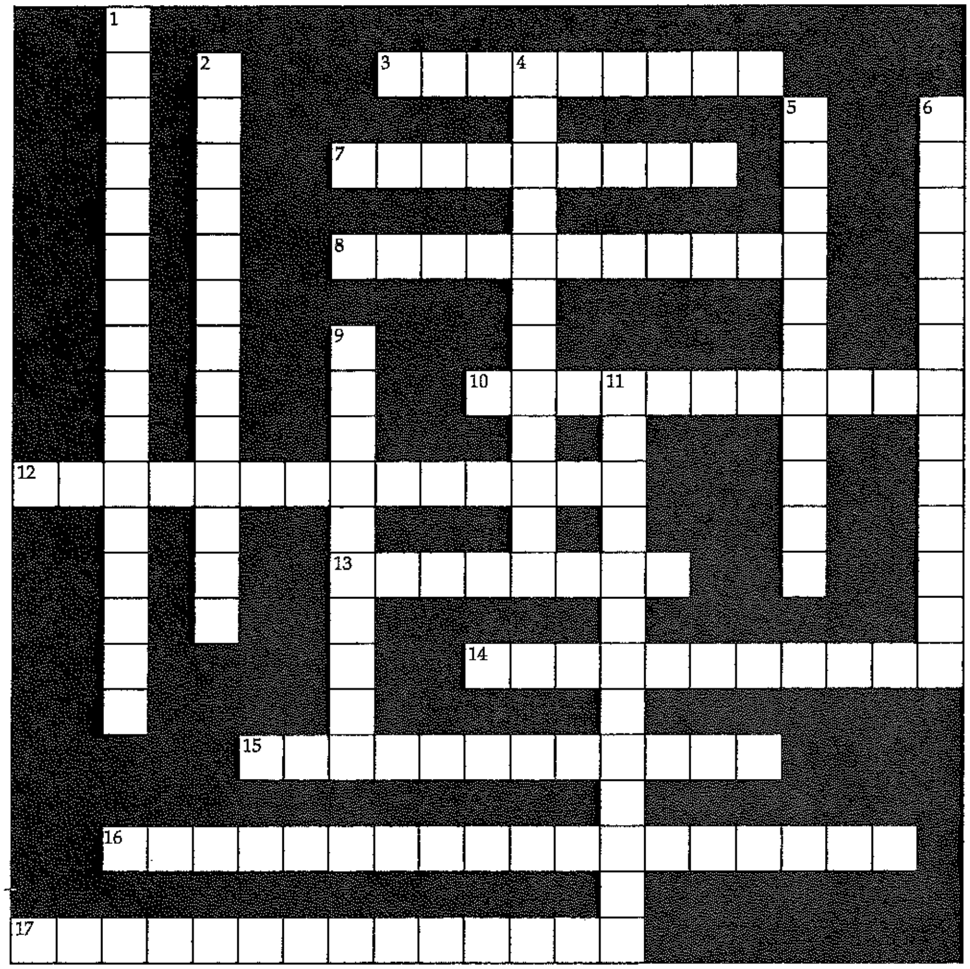
7. The operating margin is
   (A) 19.0% (C) 54.3%
   (B) 42.9% (D) 9.5% (p. 519) — 7. ______

8. The working capital is
   (A) $95,000.00 (C) $120,000.00
   (B) $70,000.00 (D) 26.3% (p. 535) — 8. ______

9. The operating expense ratio is
   (A) 54.3% (C) 42.9%
   (B) 47.6% (D) 9.5% (p. 519) — 9. ______

10. The gross profit margin is
    (A) 52.4% (C) 47.6%
    (B) 54.3% (D) 42.9% (p. 518) — 10. ______

11. The quick ratio is
    (A) 0.4 (C) 0.2
    (B) 1.5 (D) 2.5 (p. 535) — 11. ______



Across

3. A standard used to compare financial performance.
7. Total liabilities divided by total assets.
8. A ratio that measures a corporation's financial performance in relation to the market value of its stock.
10. Gross profit as a percent of net sales.
12. The amount of total current assets less total current liabilities.
13. The movement of funds from one qualified retirement plan to another.
14. Cash and other current assets that can be quickly converted into cash.
15. Net income after federal income tax as a percent of net sales.
16. A ratio that measures the ability of a business to generate income.
17. A ratio that measures the ability of a business to pay its current financial obligations.

Down

1. Net income after federal income tax divided by the number of outstanding shares of stock.
2. The relationship between dividends per share and market price per share.
4. A ratio that measures the relationship of current assets to current liabilities.
5. The amount of dividends divided by net income.
6. An analysis of changes over time.
9. A ratio that measures the relationship of quick assets to current liabilities.
11. A ratio that measures the ability of a business to pay its long-term liabilities.