



NEW YORK UNIVERSITY · LEONARD N. STERN SCHOOL OF BUSINESS

FINANCIAL STATEMENT ANALYSIS

FALL 2007

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TUESDAY- THURSDAY, 11am - 1pm

COURSE OBJECTIVES

This course is designed to prepare you to interpret and analyze financial statements effectively. This course explores in greater depth financial reporting topics introduced in the core course in financial accounting and also examines additional topics not covered in that course. The viewpoint is that of the user of financial statements. However, we develop sufficient understanding of the concepts and recording procedures to enable you to interpret various disclosures in an informed manner. We discuss each financial reporting issue in terms of its effect on assessments of a firm's profitability and risk. We then apply the analytical tools and concepts in competitor analysis, credit decisions, bankruptcy prediction, and valuation. This course is designed primarily for students who expect to be intensive users of financial statements as part of their professional responsibilities.

COURSE MATERIALS

The readings, problems, and cases for the course come from *Financial Reporting, Financial Statement Analysis, and Valuation: A Strategic Perspective, 6th edition, by Stickney, Brown, and Wahlen. (FSA.)*

You will also need a copy of the **General Mills Financial Statements**, which can be downloaded at:

<http://www.generalmills.com/corporate/investors/index.aspx>.

Go to the 2007 Annual Report and download form 10-K.

THREE INTERNET ADDRESSES MAY PROVE USEFUL TO YOU AT SOME POINT IN THE COURSE:

- 1 Filings with the Securities and Exchange Commission: <http://www.sec.gov/>.
- 2 Pronouncement of the Financial Accounting Standards Board: <http://www.fasb.org>.
- 3 Pronouncement of the International Accounting Standards Committee: <http://www.iasc.org.uk/>. We will also be discussing current articles on the subject. **You may not use the 5th Edition.**

ASSIGNMENTS

Readings, cases and/or problems are assigned for each class. You should come to class prepared to discuss your analysis of the cases and problems. Regular class participation is important to the learning process for you and your classmates. Absences from class will only be excused for emergency reasons. Let me know if you expect to miss a class.

Assignments are due at the end of the class assigned. No late assignments will be accepted nor or emailed or faxed assignments.

All assignments should be prepared using word processing software with type size no smaller than 12 point. During class discussions, please feel free to make changes to your solutions, but do so in a way that clearly indicates that they are the result of class discussion (e.g., using a different color of ink).

You may work in groups to discuss homework assignments. However, each person should prepare his/her own individual homework solutions to be submitted. Ideally you should work through each day's assignment on your own before discussing it with anyone. You can then make changes to your solution based on your learning in any discussion. Interpretations of the analysis should be in your own words.

Optional problems are listed for most classes. These problems generally involve similar accounting issues and analyses as the assigned cases or problems. If you have difficulty preparing the assigned cases or problems, you may wish to study the optional problems and their solutions. Alternatively, you can use the optional problems to cement your understanding of a topic once we have covered it in class.

FINANCIAL STATEMENTS ANALYSIS PACKAGE

A Financial Statement Analysis Package (FSAP) is available to ease the calculation of financial ratios and perform other analysis. Access FSAP and the user manual at:
<http://www.thomsonedu.com/accounting/stickney/>

GROUP PROJECT

Groups may be 3 to 4 people. Each group will choose a manufacturing or merchandising (retailing) firm to analyze, and compare it to a secondary company. The analysis should cover the relevant topics discussed during the course and will be handing in (typed) and presented toward the end of the term. You are to summarize the economics and current conditions in the industry, describe the strategies each of the firms pursue, perform a profitability and risk analysis, and assess the reasonableness of the current market price. More details will be given as the semester progresses. **I will assign the groups.**

GRADING

GRADES WILL BE BASED ON THE FOLLOWING WEIGHTS:

HOMEWORK	10%
EXAM 1	30%
ORAL PRESENTATION	15%
FINAL EXAM	45%

THERE IS NO CLASS THURSDAY, SEPTEMBER 13TH

September 4th & 6th

Topic: Introduction to Course and Financial Statement Analysis

Learning Objectives:

- 1 Overview of financial reporting and financial statement analysis.
- 2 Understand most effective means of mastering course and financial statement analysis.
- 3 Discussion of General Mills Financials. Prepare problem 1.12 (p. 52 & 53).

Read: Chapter 1

September 11th & 18th

Topic: Financial Reporting Highlights

Learning Objectives:

- 1 Review the purpose, underlying concepts, and accounting principles related to the balance sheet, the income statement, and the statement of cash flows.
- 2 Use common size statements to make preliminary interpretations of the profitability and risk of a firm.
- 3 Review key principles that drive the preparation of financial reports.
- 4 Understand the environment in which financial reporting principles are determined, as well as the limitations presented when analyzing a firm using financial reports.

Read: *FSA*, Chapter 1,

Hand-in: Case 1.2 – (NIKE: Somewhere Between a Swoosh and a Slam Dunk).
Questions on Pages 78, 79, 80, 81, 82, and 84.

September 20th & 25th

Topic: Statement of Cash Flows

Learning Objectives:

- 1 Understand the relation between net income and cash flow from operations for firms in various industries.
- 2 Understand the relation between cash flows from operating, investing, and financing activities for firms in various stages of their life cycles.
- 3 Prepare a statement of cash flows from balance sheet and income statement data.

Read: *FSA*, Chapter 3 General Mills Cash Flow Statement – hand in WT Grant Case 3.3 (May 25th)

Prepare: Problems 3.14, 3.15, 3.16, 3.17, 3.18, 3.23

September 27th, October 2nd & 4th

Topic: Profitability and Risk Analysis

Learning Objectives:

- 1 Analyze and interpret changes in the operating profitability of a firm using the rate of return on assets and its components, profit margin and total assets turnover.
- 2 Analyze and interpret changes in the rate of return on common shareholders' equity including the conditions when a firm uses financial leverage successfully.
- 3 Understand the importance of effective working capital management and apply analytical tools for assessing short-term liquidity risk.
- 4 Understand the benefits and risks of financial leverage and apply analytical tools for assessing long-term solvency risk.

Read: *FSA*, Chapter 4 & 5

Prepare: Case 4.2 Wal-Mart, Pages 272-282

October 9th & 11th

Topic: Data Issues in Analyzing Financial Statements

Learning Objectives:

- 1 Develop an understanding of the concept of “earnings quality,” with emphasis on the sustainability, measurement and manageability of reported earnings.
- 2 Master the ability for deciding when and how to adjust reported income in order to use it in evaluating performance and in predicting future earnings of a firm.

Read: *FSA*, Chapter 6

Prepare: Problem 6.10

October 16th & 18th

Topics: Income Recognition, LIFO Footnote adjustments, Fixed Assets, Intangibles, Software Development Costs

Income Recognition

Learning Objectives:

- 1 Observe the effects on the financial statements of recognizing income prior to the time of sale, at the time of sale, and subsequent to the time of sale.
- 2 Observe the time series pattern of income when firms recognize income prior to the time of sale, at the time of sale, and subsequent to the time of sale.
- 3 Review the accounting for inventories and depreciable assets.
- 4 Examine the impact on assets and net income of capitalizing and amortizing intangibles development
- 5 Identify the financial statement effects of alternative ways of organizing research and development activities and restate the income statement to a format that enhances analysis of the profitability of a technology-based firm.

Read: *FSA*, Chapter 7

Prepare: Problem 7.9, 7.14 a & b, 7.15 a, b, f, g

October 25th

MIDTERM

October 23rd & 30th

Accounting for Income Taxes Learning Objectives:

- 1 Understand the need for recognizing deferred income tax expense when book income differs from taxable income because of temporary differences.
- 2 Understand the conditions that give rise to deferred tax assets and deferred tax liabilities.
- 3 Use disclosures of individual deferred tax assets and deferred tax liabilities to study amounts recognized for financial and tax reporting.
- 4 Use disclosures of the effective tax rate to understand why a firm's average tax rate differs from the statutory tax rate.
- 5 Analyze the impact of income taxes on assessments of profitability.

Read: *FSA*, Chapter 2, Pages 97-105, & Chapter 8, Pages 575-587. General Mills Footnote 16.

Prepare: Problem 8.26

November 1st & 6th

Liability Recognition and Valuation

Learning Objectives:

- 1 Understand and apply the concept of an accounting liability to various transactions intended to keep debt off of the balance sheet.
- 2 Observe the importance of identifying the entity bearing the risks and enjoying the economic return when deciding liability recognition issues.

Read: *FSA*, Chapter 8 (pages 522 – 545)

Prepare: Problem 8.10

November 8th & 13th

Topics: Leases/Pension and Healthcare Benefits

Leases

Learning Objectives:

- 1 Understand the distinction between the operating lease method and the capital lease method, including the criteria for using each method and their financial statement effects.
- 2 Convert firms using the operating lease method to the capital lease method.

Read: *FSA*, Chapter 8

November 15th & 20th

Pension and Healthcare Benefits

Learning Objectives:

- 1 Distinguish between the amounts that firms report on their financial statements with respect to a pension or healthcare benefit plan and to the amounts that appear on the financial statements of the pension or healthcare benefits fund and understand why the two differ.
- 2 Use pension and healthcare disclosures to measure the economic status and financial performance of a pension or a healthcare benefits plan.
- 3 Observe the role of actuarial assumptions in accounting for pensions and healthcare benefits.
- 4 Understanding reserves in the financial statements

Read: *FSA*, Chapter 8 (pages 561-575)

Catch Up & Review

November 27th & 29th

PROFORMA FINANCIALS

December 4th, 6th, 7th, 11th, & TBA:

GROUP PRESENTATIONS

REVIEW

FINAL EXAM