Question #1 of 9

Question ID: 1573572

Joplin Corporation reports the following in its year-end financial statements:

- Net income of $43.7 million.
- Depreciation expense of $4.2 million.
- Increase in accounts receivable of $1.5 million.
- Decrease in accounts payable of $2.3 million.
- Sold equipment for $15 million.
- Purchased equipment for $35 million.

Joplin's free cash flow to the firm (FCFF) is closest to:

A) $39 million.

B) $24 million.

C) $28 million.

Explanation

Free cash flow to the firm = net income + noncash charges + after-tax interest – fixed capital investment – working capital investment.

Net income is $43.7 million.

Noncash charges are $4.2 million (depreciation expense).

No interest expense is shown.

Fixed capital investment is $35 million purchased – $15 million sold = $20 million.

Working capital investment is $1.5 million increase in accounts receivable + $2.3 million decrease in accounts payable = $3.8 million. (Both are uses of cash)

FCFF = $43.7 million + $4.2 million – $20 million – $3.8 million = $24.1 million.

(Module 33.1, LOS 33.b)

Question #2 of 9

Question ID: 1573571

The RR Corporation had cash flow from operations of $20 million. RR purchased $5 million in equipment and sold $3 million of equipment during the period. What is RR's free cash flow to equity for the period?

A) $15 million.

B) $18 million.

C) $22 million.

Explanation

Free cash flow to equity (FCFE) is generally defined as cash flow from operations (CFO) less net fixed capital expenditures plus net borrowing. No information on borrowing is given here, so FCFE = 20 – (5 – 3) = $18 million.

(Module 33.1, LOS 33.b)

Question #3 of 9

Question ID: 1573568

A common-size cash flow statement is *least likely* to provide payments to employees as a percentage of:

A) revenues for the period.

B) operating cash flow for the period.

C) total cash outflows for the period.

Explanation

There are two formats for a common-size cash flow statement, expressing each type of outflow as a percentage of total cash outflows or as a percentage of total revenue for the period. Operating cash flow for the period mixes inflows and outflows and is not used to calculate percentage flows for payment made.

(Module 33.1, LOS 33.a)

Question #4 of 9

Question ID: 1573574

A common-size cash flow statement is *least likely* to show each cash inflow as a percentage of:

A) revenue.

B) all cash inflows.

C) total cash flows.

Explanation

Common-size cash flow statements show each cash flow item as a percentage of revenue or show each cash flow outflow as a percentage of all cash outflows and each cash inflow as a percentage of all cash inflows. (Module 33.1, LOS 33.b)

Question #5 of 9

Question ID: 1573566

How does decreasing accounts payable turnover affect a company's cash flow from financing activities and is this source of cash sustainable?

	Financing cash flow	Sustainable source	
A)	Increase	No	✗
B)	No impact	No	✓
C)	No impact	Yes	✗

Explanation

Decreasing accounts payable turnover saves cash by delaying payments to suppliers. The result is an *operating* source of cash, not a financing source. Decreasing accounts payable turnover is not a sustainable source of cash flow because suppliers will refuse to extend credit, at some point, if payment is slower and slower.

(Module 33.1, LOS 33.a)

Question #6 of 9

Question ID: 1573569

Which of the following *best* describes a ratio that measures a firm's ability to acquire long-term assets with cash flows from operations, and a performance ratio, respectively?

	Acquire assets with CFO	Performance ratio	
A)	Investing and financing ratio	Cash-to-income ratio	✗
B)	Reinvestment ratio	Cash-to-income ratio	✓
C)	Reinvestment ratio	Debt payment ratio	✗

Explanation

The reinvestment ratio measures a firm's ability to acquire long-term assets with cash flows from operations. In contrast, the investing and financing ratio, which is more comprehensive, measures the firm's ability to purchase assets, satisfy debts, and pay dividends.

The cash-to-income ratio measures the ability to generate cash from a firm's operations and is a performance ratio for cash flow analysis purposes. The debt payment ratio measures the firm's ability to satisfy long-term debt with cash flow from operations but it is more of a coverage ratio than a performance ratio.

(Module 33.1, LOS 33.b)

Question #7 of 9

Question ID: 1573570

Selected information from the most recent cash flow statement of Thibault Company appears below:

Cash collections	€8,900
Cash paid to suppliers	(€3,700)
Cash operating expenses	(€1,500)
Cash taxes paid	(€2,400)
Cash from operating activities	**€1,300**
Cash paid for plant and equipment	(€2,600)
Cash interest received	€700
Cash dividends received	€600
Cash from investing activities	**(€1,300)**
Cash received from debt issuance	€2,000
Cash interest paid	(€400)
Cash dividends paid	(€600)
Cash from financing activities	**€1,000**
Total change in cash	**€1,000**

Thibault's reinvestment ratio for this period is *closest* to:

A) 0.50.

B) 0.75.

C) 1.00.

Explanation

The reinvestment ratio is CFO divided by cash paid for long-term assets: €1,300 / €2,600 = 0.5. (Note that on this cash flow statement, CFI includes interest and dividends received and CFF includes interest paid, which is acceptable under IFRS.)

(Module 33.1, LOS 33.b)

Question #8 of 9

Question ID: 1573573

David Chance, CFA, is analyzing Grow Corporation. Chance gathers the following information:

Net cash provided by operating activities	$3,500
Net cash used for fixed capital investments	$727
Cash paid for interest	$195
Income before tax	$4,400
Income tax expense	$1,540
Net income	$2,860

Grow's free cash flow to the firm (FCFF) is *closest* to:

A) $2,640.

B) $2,900.

C) $2,260.

Explanation

$$\text{FCFF} = \text{CFO} + \text{Int}(1 - \text{tax rate}) - \text{capital expenditures}$$

$$\text{FCFF} = 3{,}500 + \left[195 \times \left(1 - \left(\frac{1{,}540}{4{,}400}\right)\right)\right] - 727 = 2{,}899.75 \approx 2{,}900$$

(Module 33.1, LOS 33.b)

Question #9 of 9

Question ID: 1573567

Consider the following:

Statement #1: One approach to presenting a common-size cash flow statement is to express each inflow of cash as a percentage of total cash inflows and each outflow of cash as a percentage of total cash outflows.

Statement #2: Expressing each line item of the cash flow statement as a percentage of revenue is useful in forecasting future cash flows.

Which of these statements regarding a common-size cash flow statement is (are) CORRECT?

A) Only statement #1 is correct.

B) Only statement #2 is correct.

C) Both statements are correct.

Explanation

A cash flow statement can be presented in common-size format by expressing each line item as a percentage of total revenue or by expressing each inflow of cash as a percentage of total cash inflows and each outflow as a percentage of total cash outflows. Expressing each line item of the cash flow statement as a percentage of revenue is useful in forecasting future cash flows since revenue usually drives the forecast.

(Module 33.1, LOS 33.a)