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Financial Reporting & Analysis

Using Financial Accounting Information

CHARLES H. GIBSON

Liquidity

$$\text{Days' Sales in Receivables} = \frac{\text{Gross Receivables}}{\text{Net Sales}/365}$$

$$\text{Accounts Receivable Turnover} = \frac{\text{Net Sales}}{\text{Average Gross Receivables}}$$

$$\text{Accounts Receivable Turnover in Days} = \frac{\text{Average Gross Receivables}}{\text{Net Sales}/365}$$

$$\text{Days' Sales in Inventory} = \frac{\text{Ending Inventory}}{\text{Cost of Goods Sold}/365}$$

$$\text{Inventory Turnover} = \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$$

$$\text{Inventory Turnover in Days} = \frac{\text{Average Inventory}}{\text{Cost of Goods Sold}/365}$$

$$\text{Operating Cycle} = \frac{\text{Accounts Receivable}}{\text{Turnover in Days}} + \frac{\text{Inventory Turnover}}{\text{in Days}}$$

$$\text{Working Capital} = \text{Current Assets} - \text{Current Liabilities}$$

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Acid-Test Ratio} = \frac{\text{Cash Equivalents} + \text{Marketable Securities} + \text{Net Receivables}}{\text{Current Liabilities}}$$

$$\text{Cash Ratio} = \frac{\text{Cash Equivalents} + \text{Marketable Securities}}{\text{Current Liabilities}}$$

$$\text{Sales to Working Capital} = \frac{\text{Sales}}{\text{Average Working Capital}}$$

Formula for operating cash flow/current maturities of long-term debt and current notes payable is as follows:

$$\frac{\text{Operating Cash Flow}}{\text{Current Maturities of Long-Term Debt and Current Notes Payable}}$$

Long-Term Debt-Paying Ability

$$\text{Times Interest Earned} = \frac{\text{Recurring Earnings, Excluding Interest Expense, Tax Expense, Equity Earnings, and Noncontrolling Interest}}{\text{Interest Expense, Including Capitalized Interest}}$$

$$\text{Fixed Charge Coverage} = \frac{\text{Recurring Earnings, Excluding Interest Expense, Tax Expense, Equity Earnings, and Noncontrolling Interest} + \text{Interest Portion of Rentals}}{\text{Interest Expense, Including Capitalized Interest} + \text{Interest Portion of Rentals}}$$

$$\text{Debt Ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

$$\text{Debt/Equity Ratio} = \frac{\text{Total Liabilities}}{\text{Shareholders' Equity}}$$

$$\text{Debt to Tangible Net Worth Ratio} = \frac{\text{Total Liabilities}}{\text{Shareholders' Equity} - \text{Intangible Assets}}$$

$$\text{Operating Cash Flow/Total Debt} = \frac{\text{Operating Cash Flow}}{\text{Total Debt}}$$

Profitability

$$\text{Net Profit Margin} = \frac{\text{Net Income Before Noncontrolling Interest, Equity Income, and Nonrecurring Items}}{\text{Net Sales}}$$

$$\text{Total Asset Turnover} = \frac{\text{Net Sales}}{\text{Average Total Assets}}$$

$$\text{Return on Assets} = \frac{\text{Net Income Before Noncontrolling Interest and Nonrecurring Items}}{\text{Average Total Assets}}$$

$$\text{Operating Income Margin} = \frac{\text{Operating Income}}{\text{Net Sales}}$$

$$\text{Operating Asset Turnover} = \frac{\text{Net Sales}}{\text{Average Operating Assets}}$$

$$\text{Return on Operating Assets} = \frac{\text{Operating Income}}{\text{Average Operating Assets}}$$

$$\text{DuPont Return on Operating Assets} = \frac{\text{Operating Income}}{\text{Margin}} \times \frac{\text{Operating Assets}}{\text{Turnover}}$$

$$\text{Sales to Fixed Assets} = \frac{\text{Net Sales}}{\text{Average Net Fixed Assets}} \\ (\text{Exclude Construction in Progress})$$

$$\text{Return on Investment} = \frac{\text{Net Income Before Noncontrolling Interest and Nonrecurring Items} + [(\text{Interest Expense}) \times (1 - \text{Tax Rate})]}{\text{Average (Long-Term Liabilities + Equity)}}$$

$$\text{Return on Total Equity} = \frac{\text{Net Income Before Nonrecurring Items} - \text{Dividends on Redeemable Preferred Stock}}{\text{Average Total Equity}}$$

$$\text{Return on Common Equity} = \frac{\text{Net Income Before Nonrecurring Items} - \text{Preferred Dividends}}{\text{Average Common Equity}}$$

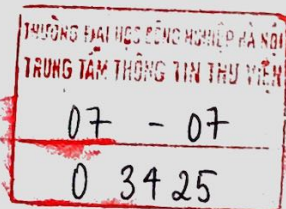
$$\text{Gross Profit Margin} = \frac{\text{Gross Profit}}{\text{Net Sales}}$$

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CHARLES H. GIBSON

The University of Toledo, Emeritus



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**Financial Reporting & Analysis,
Thirteenth Edition****Charles H. Gibson**Vice President of Editorial, Business: Jack W.
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Cover Designer: KeDesign, Mason, OH

Cover Image: R Sherwood Veith/iStockphoto.com

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Library of Congress Control Number: 2012930416

Student Edition ISBN 13: 978-1-133-18876-6

Student Edition ISBN 10: 1-133-18876-1

Student Edition package ISBN-13: 978-1-133-18879-7

Student Edition package ISBN-10: 1-133-18879-6

South-Western Cengage Learning5191 Natorp Boulevard
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Dedication

This book is dedicated to my wife, Patricia, and daughters Anne Elizabeth and Laura.

Special Dedication

To hardworking students mastering financial reporting and analysis.

About the Author

Charles Gibson is a certified public accountant who practiced with a Big Four accounting firm for four years and has had more than 30 years of teaching experience. His teaching experience encompasses a variety of accounting courses, including financial, managerial, tax, cost, and financial analysis.

Professor Gibson has taught seminars on financial analysis to financial executives, bank commercial loan officers, lawyers, and others. He has also taught financial reporting seminars for CPAs and review courses for both CPAs and CMAs. He has authored several problems used on the CMA exam.

Charles Gibson has written more than 60 articles in such journals as the *Journal of Accountancy*, *Accounting Horizons*, *Journal of Commercial Bank Lending*, *CPA Journal*, *Ohio CPA*, *Management Accounting*, *Risk Management*, *Taxation for Accountants*, *Advanced Management Journal*, *Taxation for Lawyers*, *California Management Review*, and *Journal of Small Business Management*. He is a co-author of the Financial Executives Research Foundation Study entitled, "Discounting in Financial Accounting and Reporting."

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Dr. Gibson received the 1989 Outstanding Ohio Accounting Educator Award jointly presented by the Ohio Society of Certified Public Accountants and the Ohio Regional American Accounting Association. In 1993, he received the College of Business Research Award at the University of Toledo. In 1996, Dr. Gibson was honored as an "Accomplished Graduate" of the College of Business at Bowling Green State University. In 1999, he was honored by the Gamma Epsilon Chapter of Beta Alpha Psi of the University of Toledo.

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Learn to prepare and analyze real financial information with Gibson's *Financial Reporting & Analysis: Using Financial Accounting Information*, 13e. By connecting what you are learning to actual financial statements and their analysis and preparation, you will build critical skills that set you apart in your professional life.

- Real company reports, 10-Ks, proxy statements, cases, and exhibits are drawn from a variety of relevant companies. Nike is used extensively, providing a meaningful example for reviewing financial statement analysis as a whole.
- With a significantly expanded coverage of ethics and updated discussion of international accounting that reflects current IFRS standards and codification, this text ensures you are knowledgeable about the daily challenges faced by today's financial analysts and by the business world at large.
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ISBN-13: 978-1-133-18879-7
ISBN-10: 1-133-18879-6



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Mã sách: 070703425