

LEONARD N. STERN SCHOOL OF BUSINESS
FINANCIAL STATEMENT ANALYSIS
SPRING 2008
C10.0003
SECTIONS .01 & .02

PROFESSOR AARON HIPSCHER

OFFICE:	KMC 10-89	OFFICE HOURS:	Tues. & Thurs., 1pm-3pm (or by appointment)
PHONE:	(212) 998-0011	E-MAIL:	ahipsche@stern.nyu.edu

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, and credit decisions. 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 10-K, which can be downloaded at: <http://www.generalmills.com/corporate/investors/index.aspx>. Go to the 2006 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 & ATTENDANCE

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.

Class attendance is mandatory and part of a student's grade. Absences may be excused only in the case of documented serious illnesses, family emergency, religious observance, or civic obligation. If you will miss class for religious observance or civic obligation, you must inform your instructor no later than the first week of class. Recruiting activities are not acceptable reasons for class absence. A maximum of two unexcused absences will be allowed.

Students are expected to arrive to class on time and stay to the end of the class period. Chronically arriving late or leaving class early will have an impact on a student's grade. Students may enter class late only if given permission by the instructor and must do so without disrupting the 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.

PARTICIPATION

Participation is an essential part of learning in this course. Students are expected to participate in all facets of classroom learning.

READING/HOMEWORK

Students are expected to come to class prepared, having read text and/or assigned readings prior to class. Homework, case studies, and other assignments, are expected to be completed and handed in on time.

CLASSROOM NOTES

Laptops, cell phones, Smartphones, and other electronic devices are a disturbance to both students and professors. All electronic devices must be turned off prior to the start of each class meeting.

ETHICAL GUIDELINES

Student Code of Conduct

All students are expected to follow the Stern Code of Conduct

(<http://www.stern.nyu.edu/uc/codeofconduct>)

A student's responsibilities include - but are not limited to - the following:

- A duty to acknowledge the work and efforts of others (when submitting work as one's own). Ideas, data, direct quotations, paraphrasing, creative expression, or any other incorporation of the work of others must be clearly referenced.
- A duty to exercise the utmost integrity when preparing for and completing examinations, including an obligation to report any observed violations.

STUDENTS WITH DISABILITIES

Students whose class performance may be affected due to a disability should notify the professor immediately so that arrangements can be made in consultation with the Henry and Lucy Moses Center for Students with Disabilities (<http://www.nyu.edu/csd/>) to accommodate their needs.

FINANCIAL STATEMENT ANALYSIS PACKAGE

A financial statement analysis package (FSAP) is available to ease the calculation of financial ratios and to perform other analyses. 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 Powerpoints will be handed in 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.

GRADES WILL BE BASED ON THE FOLLOWING WEIGHTS:

Homework, Class Participation, & Attendance	10%
Exam 1	35%
Oral Presentation	15%
Final Exam	40%

JANUARY 22ND & 24TH

TOPIC: INTRODUCTION TO COURSE AND FINANCIAL STATEMENT ANALYSIS

LEARNING OBJECTIVES:

READ CHAPTER 1

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 1.11 (p. 49, 50, & 51).

JANUARY 29TH & 31ST

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, & 84.

FEBRUARY 5TH & 7TH

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, on the 7th

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

FEBRUARY 12TH, 14TH, 19TH, & 21ST

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; In-Class Problems, Additional Problems, & Cases *To Be Assigned*.

FEBRUARY 26TH & 28TH

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

MARCH 4TH & MARCH 6TH

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.

MARCH 11TH

CATCH-UP

MARCH 13TH

MIDTERM EXAM

MARCH 25TH & 27TH

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

APRIL 1ST & 3RD

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

APRIL 8TH & 10TH

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

APRIL 15TH & 17TH

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

APRIL 22ND, 24TH, 29TH, & MAY 1ST:

GROUP PRESENTATIONS

TBA

FINAL EXAM