

Financial Modeling Fundamentals – Module 02

The Three Financial Statements –

Quiz Questions

1. **Why do companies need three financial statements instead of just an Income Statement?**
 - a. Because Net Income doesn't match cash generated if revenue has not yet been collected in cash, or if expenses have not yet been paid out in cash.
 - b. Because many items that represent uses of cash, such as CapEx, do not appear on the Income Statement.
 - c. Because the Income Statement does not directly reflect cash inflows from sources such as debt or equity issuances or asset sales.
 - d. All of the above.

2. **What is the MAIN difference between Cost of Goods Sold (COGS) and Operating Expenses (OpEx) on a company's Income Statement?**
 - a. They're both expenses, but OpEx is almost always significantly bigger than COGS.
 - b. COGS can reflect only cash expenses, whereas OpEx may include both expenses paid out in cash in the current period, as well as expenses that are owed and which will be paid out in cash in the future.
 - c. COGS corresponds to expenses that can be *directly* linked to individual products or services sold, but there is no direct relationship with OpEx.
 - d. COGS is almost always projected as a percentage of revenue, but OpEx is rarely projected that way since it can't be linked to individual units sold.

3. What's the easiest way to distinguish Assets from Liabilities on the Balance Sheet?

- a. Assets always correspond to revenue on the Income Statement, whereas Liabilities always correspond to expenses.
- b. An Asset will provide a future benefit such as additional cash flow, whereas a Liability will cost the company cash in the future.
- c. An Asset must have a useful life of longer than one year, whereas a Liability can have a useful life much shorter than a year.
- d. None of the above.

4. Suppose that a company's revenue is currently \$1,000, its Pre-Tax Income is currently \$500, and its tax rate is 40%, so its Net Income is \$300. Now suppose that the company tells you the following information:

- \$50 of its revenue corresponds to products that have been delivered to customers, for which the company has not yet collected cash payments.
- \$20 of its operating expenses have not yet been paid out in cash.
- It has purchased \$50 of Inventory, which it has not yet turned into products or sold to customers.
- It has also paid for \$30 of property insurance upfront in cash, but it has not yet received the benefit of that property insurance since it's a long-term contract.

Based on this information, how much CASH has the company generated in this particular period?

- a. \$190.
- b. \$240.
- c. \$220.
- d. \$230.

5. The exhibit below shows the three financial statements for a hypothetical company that spends \$230 on Capital Expenditures at the BEGINNING of Year 2 (January 1):

Tax Rate:

Capital Expenditures (Beginning of Year 2):

Useful Life of Purchased PP&E (# Years):

Annual Depreciation from Year 2 CapEx:

Income Statement:		
	Year 1	Year 2
Revenue:	\$ 650	\$ 700
Cost of Goods Sold (COGS):	70	70
Gross Profit:	580	630
Gross Margin %:	89.2%	90.0%
Operating Expenses:		
Sales & Marketing:	150	165
Research & Development:	75	75
General & Administrative:	50	50
Total Operating Expenses:	275	290
Depreciation:	-	<input type="text"/>
Operating Income (EBIT):	305	302
Operating Margin:	46.9%	43.1%
Other Income / (Expenses):	20	20
Interest Income / (Expense):	-	-
Pre-Tax Income (EBT):	325	322
Income Taxes:	-	-
Net Income (Profit After Taxes) \$	\$ 325	\$ 322
Net Income Margin:	50.0%	46.0%

Balance Sheet:		
	Year 1	Year 2
Assets:		
Current Assets:		
Cash:	\$ 300	\$ 350
Accounts Receivable:	-	50
Inventory:	-	30
Prepaid Expenses:	-	30
Total Current Assets:	300	460
Long-Term Assets:		
Property, Plant & Equipment:	-	<input type="text"/>
Total Long-Term Assets:	-	-
Total Assets:	\$ 300	\$ 652
Liabilities & Equity:		
Current Liabilities:		
Accounts Payable:	\$ -	\$ 15
Deferred Revenue:	-	15
Total Current Liabilities:	-	30
Long-Term Liabilities:		
Debt:	-	-
Total Long-Term Liabilities:	-	-
Equity:	300	622
Total Liabilities & Equity:	\$ 300	\$ 652

Cash Flow Statement:		
	Year 1	Year 2
Cash Flow from Operating Activities:		
Net Income:	\$ 325	\$ 322
Depreciation:	-	<input type="text"/>
Change in Operating Assets & Liabilities:		
Change in Accounts Receivable:	-	(50)
Change in Prepaid Expenses:	-	(30)
Change in Inventory:	-	(30)
Change in Accounts Payable:	-	15
Change in Deferred Revenue:	-	15
Cash Flow from Operations:	\$ 325	\$ 280
Cash Flow from Investing Activities:		
Capital Expenditures (CapEx):	\$ -	\$ (230)
Cash Flow from Investing:	\$ -	\$ (230)
Cash Flow from Financing Activities:		
Cash Flow from Financing:	\$ -	\$ -
Net Change in Cash:	\$ 325	\$ 50

Based on this screenshot, calculate the Year 2 Depreciation, the Year 2 Ending PP&E Balance, and the Useful Life of the PP&E that was purchased at the beginning of Year 2.

- Year 2 Depreciation = \$12; Year 2 Ending PP&E = \$218; Useful Life = 19 Years.
- Year 2 Depreciation = \$38; Year 2 Ending PP&E = \$192; Useful Life = 6 Years.
- Year 2 Depreciation = \$18; Year 2 Ending PP&E = \$212; Useful Life = 13 Years.
- Year 2 Depreciation = \$38; Year 2 Ending PP&E = \$192; Useful Life = 5 Years.

6. Suppose that a company is deciding between raising debt (with interest and principal repayments) and raising equity, and management wants to understand the financial impact of both alternatives. Which of the following statements **CORRECTLY** describe the immediate impact and the impact after one year?
- a. *Immediately* after the company raises debt, Net Income on the Income Statement would be lower, Cash on the Balance Sheet would be lower, and Cash Flow from Financing would be higher.
 - b. *Immediately* after the company issues equity, Net Income would be unaffected, Cash on the Balance Sheet would increase, and the Equity side of the Balance Sheet would increase.
 - c. One year after the company raises debt, Net Income would be lower due to interest, and the Net Change in Cash on the CFS would be lower due to debt principal repayments.
 - d. One year after the company raises equity, Net Income would be unchanged, Cash on the Balance Sheet would be higher, and the Equity side of the Balance Sheet would remain higher.

7. Consider the screenshot below, which shows the Balance Sheet of an acquirer over two years prior to an acquisition, as well as the financial profile of the acquisition and the acquired company:

Balance Sheet:			Acquisition - Financial Profile (Assume Close at the End of Year 2):	
	Year 1	Year 2		
Assets:			Purchase Price (Paid in Cash):	\$ 500
Current Assets:			Acquired Co. Cash Balance:	\$ 120
Cash:	\$ 300	\$ 685	Acquired Co. PP&E Balance:	\$ 45
Short-Term Investments:	-	-	Acquired Co. Accounts Payable Balance:	\$ 23
Accounts Receivable:	-	50	Acquired Co. Equity Balance:	\$ 142
Inventory:	-	30	Value of Other Intangible Assets Created:	\$ 100
Prepaid Expenses:	-	30	Goodwill Created:	
Total Current Assets:	300	795		
Long-Term Assets:				
Property, Plant & Equipment:	-	40		
Goodwill:	-	-		
Other Intangible Assets:	-	-		
Long-Term Investments:	-	100		
Total Long-Term Assets:	-	140		
Total Assets:	\$ 300	\$ 935		
Liabilities & Equity:				
Current Liabilities:				
Accounts Payable:	\$ -	\$ 15		
Deferred Revenue:	-	15		
Total Current Liabilities:	-	30		
Long-Term Liabilities:				
Debt:	-	265		
Deferred Tax Liability:	-	50		
Total Long-Term Liabilities:	-	315		
Equity:	300	590		
Total Liabilities & Equity:	\$ 300	\$ 935		

Use the financial profile of the acquisition and determine the amount of Goodwill that would be created IMMEDIATELY after the acquisition closes at the end of Year 2.

- Goodwill Created = \$258.
- Goodwill Created = \$358.
- Goodwill Created = \$142.
- Goodwill Created = \$238.

8. Consider the scenario shown below, in which a company uses straight-line depreciation over three years for book purposes, but accelerated depreciation over three years for cash tax purposes. The book accounting version contains all the calculations, but the tax accounting version is mostly blank:

Tax Rate:	40.0%
CapEx Spending @ Beginning of Year 1:	\$ 300

Depreciation %:	33.3%	33.3%	33.3%
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Depreciation %:	50.0%	33.3%	16.7%
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	Book Accounting		
	Year 1	Year 2	Year 3
Revenue:	\$ 1,000	\$ 1,000	\$ 1,000
COGS & OpEx:	500	500	500
Depreciation:	100	100	100
Pre-Tax Income:	400	400	400
Taxes:	160	160	160
Net Income:	240	240	240

	Tax Accounting		
	Year 1	Year 2	Year 3
Revenue:	\$ 1,000	\$ 1,000	\$ 1,000
COGS & OpEx:	500	500	500
Depreciation:			
Pre-Tax Income:			
Taxes:			
Net Income:			

Which of the following statements are TRUE about the Deferred Taxes and the Deferred Tax Liability over Years 1 – 3 in this scenario?

- Initially, Deferred Taxes will be negative since tax Depreciation is higher than book Depreciation, but that will reverse and Deferred Taxes will turn positive by Year 3.
- The Deferred Tax Liability balance will increase to \$20 in Year 1, before declining back to \$0 by the end of Year 3.
- Although the DTL will be different on the book and tax versions of the statements, PP&E will change in the same way in both versions: it will start at \$300 and then decline to \$0 evenly over time.
- Tax Net Income will be lower than Book Net Income in Year 1, but by Year 3, Tax Net Income will be higher than Book Net Income.

9. Which of the following **TWO** conditions must **BOTH** be true for an expense to appear on the income statement?

- a. It must be paid in cash with in the period the income statement covers.
- b. It must correspond to the period that the income statement covers.
- c. It must be tax-deductible for book-tax purposes.
- d. It must be tax-deductible for both book- and cash-tax purposes.

10. You are analyzing the Net Income and Cash balances of a company over the past three years (shown below). You find that Net Income is increasing, but Cash is decreasing. What are possible explanations for this trend?

	Net Income and Cash Balances		
	Year 1	Year 2	Year 3
Ending Cash Balance:	\$ 250	\$ 200	\$ 150
Annual Net Income:	50	100	150

- a. In Years 2 and 3, the company made large capital expenditures.
- b. The company has high working capital requirements (such as purchasing inventory in advance of selling products).
- c. The company has a large debt balance that requires high annual principal repayments.
- d. None of the above – this scenario could never happen in real life.

11. The screenshot below shows the Income Statement and partial Cash Flow Statement for an online education and training company:

Income Statement:		Cash Flow Statement:	
	Year 1		Year 1
Revenue:		Net Income:	\$ 120
Online Courses:	\$ 550	Addback of Non-Cash Charges:	
Resume/CV Editing and Coaching:	100	Depreciation & Amortization:	125
Total Revenue:	650	Stock-based Compensation:	20
		Deferred Taxes:	10
Cost of Goods Sold (COGS):		Change in Operating Assets & Liabilities:	
Online Courses:	20	Accounts Receivable:	(10)
Resume/CV Editing and Coaching:	50	Inventory:	(5)
Total Cost of Goods Sold (COGS):	70	Accounts Payable:	12
		Accrued Expenses:	13
Gross Profit:		Cash Flow from Operations:	\$ 285
Online Courses:	530		
Resume/CV Editing and Coaching:	50		
Total Gross Profit:	580		
<i>Gross Margin %:</i>	<i>89.2%</i>		
Operating Expenses:			
Sales & Marketing:	150		
Research & Development:	75		
General & Administrative:	50		
Depreciation & Amortization:	75		
Total Operating Expenses:	350		
Operating Income (EBIT):	230		
<i>Operating Margin:</i>	<i>35.4%</i>		
Other Income / (Expenses):	20		
Interest Income / (Expense):	-		
Pre-Tax Income (EBT):	250		
Income Taxes:	(130)		
Net Income (Profit After Taxes):	\$ 120		
<i>Net Income Margin:</i>	<i>18.5%</i>		

You want to calculate EBITDA and Free Cash Flow for this company in Year 1. Which Depreciation & Amortization figure should you use in these calculations?

- a. \$75, the D&A figure listed on the Income Statement.
- b. \$125, the D&A figure listed on the Cash Flow Statement.
- c. Either one is acceptable to use in the calculations.
- d. None of the above – we need a full Cash Flow Statement to determine the proper D&A figure, since we need to see the full amount of CapEx first.
- e. \$75, the Income Statement figure, should be used for EBITDA since EBITDA is based on Operating Income, but \$125, the CFS figure, should be used for Free Cash Flow.

12. A friend who is struggling with accounting has asked you to explain the rules for determining what constitutes an Asset and what constitutes a Liability or Equity line item. To help him out, you write brief descriptions of why various items on the Balance Sheet are categorized as Assets, Liabilities, or Equity. Which of the following descriptions is INCORRECT?

- a. Accounts Receivable – It's an ASSET because it means the company will collect more cash from customers in the future.
- b. Goodwill – It's an ASSET because it corresponds to previous acquisitions that may generate more cash for the company in the future.
- c. Accounts Payable – It's a LIABILITY because the company must spend cash in the future to pay for the expense.
- d. Deferred Revenue – It's a LIABILITY because the company will never generate additional cash from customers; the cash has already been collected.
- e. Common Stock & APIC – It's an EQUITY line item because it's a funding source for the company that, unlike Debt, will not *necessarily* result in future cash outflows.

13. Roughly speaking, which of the following pairings of “Balance Sheet Items” and “Sections of the Cash Flow statement” are correct?

- a. Changes in operationally related Current Assets and Current Liabilities, as well as the occasional longer-term item, are reflected in Cash Flow from Operations.
- b. Changes in Long-Term Assets, as well as shorter-term investments, show up within Cash Flow from Investing.
- c. Changes in Equity line items appear in BOTH Cash Flow from Investing and Cash Flow from Financing.
- d. Changes in Long-Term Liabilities show up under Cash Flow from Financing, and some items may also show up in Cash Flow from Operations.

14. You are comparing the Working Capital requirements of Wal-Mart, Amazon, and Salesforce. You have calculated the Change in Working Capital as a % of Revenue, the Change in Revenue, and Net Income, which are shown in the screenshot below:

Wal-Mart - Working Capital Excerpt from Cash Flow Statement:

Changes In Certain Assets and Liabilities:	Year 1	Year 2	Year 3
Accounts Receivable:	\$ (796)	\$ (614)	\$ (566)
Inventories:	(3,727)	(2,759)	(1,667)
Accounts Payable:	2,687	1,061	531
Accrued Liabilities:	(935)	271	103
Accrued Taxes:	994	981	(1,224)
Net Change in (Operating) Working Capital:	(1,777)	(1,060)	(2,823)
Annual Revenue:	\$ 421,395	\$ 446,509	\$ 476,294
Change in Annual Revenue:	25,114	22,142	7,643
Annual Net Income:	16,387	17,756	16,695
Net Change as a % of Revenue:	(0.4%)	(0.2%)	(0.6%)
Net Change as a % of Change in Revenue:	(7.1%)	(4.8%)	(36.9%)
Net Change as a % of Net Income:	(10.8%)	(6.0%)	(16.9%)

Amazon - Working Capital Excerpt from Cash Flow Statement:

Changes In Operating Assets and Liabilities:	Year 1	Year 2	Year 3
Accounts Receivable:	\$ (866)	\$ (861)	\$ (846)
Inventories:	(1,777)	(999)	(1,410)
Accounts Payable:	2,997	2,070	1,888
Accrued Liabilities:	1,067	1,038	736
Deferred Revenue:	43	275	399
Net Change in (Operating) Working Capital:	1,464	1,523	767
Annual Revenue:	\$ 34,204	\$ 48,077	\$ 74,452
Change in Annual Revenue:	13,873	13,016	13,359
Annual Net Income:	631	(39)	274
Net Change as a % of Revenue:	3.0%	2.5%	1.0%
Net Change as a % of Change in Revenue:	10.6%	11.7%	5.7%
Net Change as a % of Net Income:	232.0%	(3905.1%)	279.9%

Salesforce - Working Capital Excerpt from Cash Flow Statement:

Changes In Operating Assets and Liabilities:	Year 1	Year 2	Year 3
Accounts Receivable:	\$ (245)	\$ (183)	\$ (425)
Deferred Commissions:	(167)	(233)	(265)
Prepaid Expenses:	(8)	(10)	105
Accounts Payable:	80	193	(29)
Deferred Revenue:	445	479	612
Net Change in (Operating) Working Capital:	105	247	(1)
Annual Revenue:	\$ 1,657	\$ 2,267	\$ 4,071
Change in Annual Revenue:	609	784	1,021
Annual Net Income:	(12)	(270)	(232)
Net Change as a % of Revenue:	4.6%	8.1%	(0.0%)
Net Change as a % of Change in Revenue:	17.2%	31.5%	(0.1%)
Net Change as a % of Net Income:	(907.5%)	(91.4%)	0.5%

Which of the following conclusions about the Working Capital requirements of these companies might be justified, based on the metrics shown above?

- a. As Wal-Mart's revenue increases each year, it requires additional cash, primarily because it must purchase additional inventory in advance of selling its products.
- b. As a result of Wal-Mart's high Working Capital requirements, it will almost certainly have to raise debt or equity as it grows beyond a certain level.
- c. While Amazon also must purchase inventory prior to selling products, its business generates additional cash as it grows – primarily because its Accounts Payable balance is increasing by more than its Inventory balance.
- d. Sales force has far lower Working Capital requirements than either Amazon or Wal-Mart, primarily because it has no Inventory and collects significant cash from customers upfront, boosting its Deferred Revenue balance.
- e. Over any given 3-year period, Sales force would raise the LEAST amount of debt and equity, and Wal-Mart and Amazon would both raise more in funding.

15. Which type of company is likely to have the HIGHEST Working Capital requirements as its revenue increases?

- a. A manufacturing company, since purchasing plants and factories requires significant Working Capital.
- b. An airline, because high CapEx requirements tend to imply that Working Capital requirements are also high.
- c. An offline retailer, because of the need to buy inventory upfront before selling products.
- d. A professional consulting company, because it will need to spend money on additional staff in advance of sales growth.

16. Consider an analysis of Wal-Mart's Free Cash Flow over the past three years, as depicted in the screenshot below:

Wal-Mart - FCF Excerpt from Financial Statements:				
Free Cash Flow Calculation:		Year 1	Year 2	Year 3
Cash Flow from Operations:	\$ 23,643	\$ 24,255	\$ 25,591	\$ 23,257
Less: Capital Expenditures:	(12,699)	(13,510)	(12,898)	(13,115)
Free Cash Flow:	\$ 10,944	\$ 10,745	\$ 12,693	\$ 10,142
Changes In Certain Assets and Liabilities:		Year 1	Year 2	Year 3
Accounts Receivable:	\$ (796)	\$ (614)	\$ (566)	
Inventories:	(3,727)	(2,759)	(1,667)	
Accounts Payable:	2,687	1,061	531	
Accrued Liabilities:	(935)	271	103	
Accrued Taxes:	994	981	(1,224)	
Net Change in (Operating) Working Capital:	(1,777)	(1,060)	(2,823)	
Annual Revenue:	\$ 421,395	\$ 446,509	\$ 468,651	\$ 476,294
Annual Net Income:	16,993	16,387	17,756	16,695
<i>Net Change in WC % Change in Revenue:</i>	<i>(7.1%)</i>	<i>(4.8%)</i>	<i>(36.9%)</i>	
<i>Free Cash Flow Growth Rate:</i>	<i>(1.8%)</i>	<i>18.1%</i>	<i>(20.1%)</i>	
<i>CapEx as a % of Cash Flow from Operations:</i>	<i>55.7%</i>	<i>50.4%</i>	<i>56.4%</i>	
<i>CapEx as a % of Revenue:</i>	<i>3.0%</i>	<i>2.8%</i>	<i>2.8%</i>	
<i>Revenue Growth Rate:</i>	<i>6.0%</i>	<i>5.0%</i>	<i>1.6%</i>	
<i>Cash Flow from Operations Growth Rate:</i>	<i>2.6%</i>	<i>5.5%</i>	<i>(9.1%)</i>	

Which of the following conclusions might you draw, based on this analysis?

- Wal-Mart's Free Cash Flow has increased primarily because of organic sales growth that flowed down into its CFO and FCF.
- Although Wal-Mart's FCF declined in Year 3, that's primarily because of owed tax payments that were finally paid out in cash in Year 3.
- Wal-Mart's FCF fluctuated over these three years because its CapEx spending also varied, and it did not trend with revenue.
- It appears that Wal-Mart has delayed payments to suppliers more and more each year to boost its Free Cash Flow.

17. Even though Amazon and Wal-Mart are both retailers, Amazon's Free Cash Flow profile looks significantly different from Wal-Mart's. Amazon's FCF is not shown here, but based on your knowledge of the business models and this lesson in the course, why might you expect the Free Cash Flows to differ so much?

- a. Because Amazon is spending far less on Inventory than Wal-Mart since it's an online retailer.
- b. Because Amazon is a high-growth company, whereas Wal-Mart is a mature, stable company.
- c. Because Amazon is re-investing in its business more aggressively with higher CapEx as a percentage of revenue, whereas Wal-Mart is spending less as a percentage of revenue and is keeping its spending in about the same range.
- d. Because Amazon requires upfront payment for 100% of products' prices, whereas Wal-Mart allows for installment payments.
- e. Because Amazon tends to delay payments to suppliers for as long as possible, whereas Wal-Mart pays suppliers more quickly.

18. The screenshot below shows various financial metrics, as well as ROE, ROA, and ROIC for Wal-Mart, Amazon, and Sales force over three years:

Wal-Mart - Key Metrics and Ratios:

Financial Information:	Year 1	Year 2	Year 3
Annual Revenue:	\$ 421,395	\$ 446,509	\$ 476,294
% Growth:	6.0%	5.0%	1.6%
Annual COGS:	334,993	352,297	358,069
% Revenue:	75.0%	75.2%	75.2%
Annual Net Income:	16,387	17,756	16,695
% Revenue:	3.7%	3.8%	3.5%
Annual Net Interest Expense:	2,159	2,063	2,216
EBIT:	26,491	27,725	26,872
EBITDA:	34,597	36,203	35,742
Free Cash Flow (FCF):	\$ 10,745	\$ 12,693	\$ 10,142
<i>EBIT Margin:</i>	5.9%	5.9%	5.6%
<i>EBITDA Margin:</i>	7.7%	7.7%	7.5%
<i>FCF Margin:</i>	2.4%	2.7%	2.1%
Net Operating Profit After Taxes (NOPAT):	18,014	18,853	18,273
Return on Equity (ROE):	23.4%	24.1%	21.9%
Return on Assets (ROA):	8.8%	9.0%	8.2%
Return on Invested Capital (ROIC):	14.4%	14.2%	13.3%

Amazon - Key Metrics and Ratios:

Financial Information:	Year 1	Year 2	Year 3
Annual Revenue:	\$ 34,204	\$ 48,077	\$ 61,093
% Growth:	40.6%	27.1%	21.9%
Annual COGS:	37,288	45,971	54,181
% Revenue:	77.6%	75.2%	72.8%
Annual Net Income:	631	(39)	274
% Revenue:	1.3%	(0.1%)	0.4%
Annual Net Interest Expense:	4	52	103
EBIT:	862	676	745
EBITDA:	1,945	2,835	3,998
Free Cash Flow (FCF):	\$ 2,092	\$ 395	\$ 2,031
<i>EBIT Margin:</i>	1.8%	1.1%	1.0%
<i>EBITDA Margin:</i>	4.0%	4.6%	5.4%
<i>FCF Margin:</i>	4.4%	0.6%	2.7%
Net Operating Profit After Taxes (NOPAT):	586	460	507
Return on Equity (ROE):	8.6%	(0.5%)	3.1%
Return on Assets (ROA):	2.9%	(0.1%)	0.8%
Return on Invested Capital (ROIC):	7.0%	4.3%	3.8%

Salesforce - Key Metrics and Ratios:

Financial Information:	Year 1	Year 2	Year 3
Annual Revenue:	\$ 1,657	\$ 2,267	\$ 3,050
% Growth:	36.8%	34.6%	33.5%
Annual COGS + OpEx:	2,302	3,161	4,357
% Revenue:	101.5%	103.6%	107.0%
Annual Net Income:	(12)	(270)	(232)
% Revenue:	(0.5%)	(8.9%)	(5.7%)
Annual Net Interest Expense:	(6)	11	67
EBIT:	(35)	(111)	(286)
EBITDA:	240	285	328
Free Cash Flow (FCF):	\$ 440	\$ 561	\$ 576
<i>EBIT Margin:</i>	(1.5%)	(3.6%)	(7.0%)
<i>EBITDA Margin:</i>	10.6%	9.3%	8.0%
<i>FCF Margin:</i>	19.4%	18.4%	14.2%
Net Operating Profit After Taxes (NOPAT):	(23)	(72)	(186)
Return on Equity (ROE):	(0.8%)	(13.9%)	(8.7%)

Which of the following conclusions might you draw from this analysis and the fact that Amazon and Sales force are valued at significantly higher multiples than Wal-Mart?

- a. Amazon and Sales force are clearly overvalued, because they are trading at higher multiples but have lower ROE, ROA, and ROIC figures than Wal-Mart.
- b. While the returns-based metrics are higher for Wal-Mart, you can't directly compare these companies because Amazon and Sales force are growing far more quickly than Wal-Mart and are in different industries.
- c. On average, equity investors in Wal-Mart can expect to earn \$0.20 to \$0.25, after taxes, for each \$1.00 invested in the company.
- d. Amazon is attempting to optimize its ROIC rather than its ROE or ROA, as it knows investors will pay more attention to ROIC for a high-growth company.
- e. Salesforce is likely to generate the LEAST amount of stock price appreciation over the next two years because its ROE, ROA, and ROIC are substantially lower than the figures for Wal-Mart or Amazon.