



2010 Spring Final

Ram T. S. Ramakrishnan
 2301, University Hall, ☎ 996-3270
 rramakri@uic.edu
Thursday, May 06, 2010
 110427

<http://www.uic.edu/classes/actg/actg516rtr/>
Open Book and Notes. No lap tops

Show all your work in the answer sheets. You will not get credit for a right answer unless you show all the steps there. As a courtesy to fellow test takers, please turnoff all pagers, telephones and PDA's.

	<i>Pages</i>	<i>Points Estimated Time</i>	
Liba	2	30	<input type="text"/>
Pepsico	11	80	<input type="text"/>
Ford Motors	5	40	<input type="text"/>
Total	18	150	<input type="text"/>

email

UIN

This course and its associated coursework are being administered under the policies of the University of Illinois at Chicago (UIC) College of Business Administration Honor Code. All students are expected to respect and uphold this code.

Signature	First name	Last name
<input type="text"/>	<input type="text"/>	<input type="text"/>

Details of Liba Inc., a US company's investment activities in Rekhi Inc are as follow

80701

Date	Activity	Shares of	Price per share
05-Jan-07	Purchased	120,000	\$32.00
31-Dec-07			\$31.00
17-Jan-08	Sold	25,000	\$30.00
31-Dec-08			\$28.00

Year Ending Dec 31,	2008	2007
• Earnings per share for Rekhi Inc.	\$0.60	\$0.50
• Dividend per share for Rekhi Inc. for stockholders of record on	\$0.20	\$0.20

The company can choose any of the following four methods to account for its investment in Rekhi Inc

- Held to maturity
- Available for sale
- Trading
- Equity

Questions

1 Under each of the four methods, compute the carrying value of Liba Inc.'s investment in Rekhi on Dec 31, 2008.

2 Under each of the four methods, compute the income from Liba Inc.'s investment in Rekhi for the year ending Dec 31, 2008.

Ford Motor Company engages in the manufacture and distribution of automobiles worldwide. It manufactures and sells cars and trucks, and related service parts under Aston Martin, Ford, Jaguar, Land Rover, Lincoln, Mazda, Mercury, and Volvo brand names. Ford Motor Credit's primary financial products comprise retail and wholesale financing, and other financing, such as making loans to dealers for working capital, improvements to dealership facilities, and the acquisition and refinancing of dealership real estate. The company operates in approximately 200 markets across 6 continents. Ford Motor was founded in 1903 and is based in Dearborn, Michigan.

The quarterly financial statements for the quarter ending 9/30/2006 and portions of the financial statements for the fiscal year ending 12/31/2005 are attached.

[For Income Statement items, the last 12 month figures should be used.]



Stock performance



Income Statement

(unaudited)



	Third Quarter		First Nine Months		Twelve
	Restated - See Note 2		Restated - See Note 2		Months
	2006	2005	2006	2005	Year
Sales and revenues					
Automotive sales	32,556	34,656	107,356	112,778	153,503
Financial Services revenues	4,554	5,854	12,449	17,793	23,586
Total sales and revenues	37,110	40,510	119,805	130,571	177,089
Costs and expenses					
Automotive cost of sales	37,554	33,471	110,340	105,786	144,944
Selling, administrative and other expenses	4,496	5,983	13,730	18,181	24,652
Interest expense	1,936	2,157	6,330	6,287	7,643
Financial Services provision for credit and insurance losses	97	182	193	350	483
Total costs and expenses	44,083	41,793	130,593	130,604	177,722
Automotive interest income and other non-operating income/(expense), net	555	307	1,080	1,111	1,249
Automotive equity in net income/(loss) of affiliated companies	61	133	345	259	285
Gain on sale of The Hertz Corporation ("Hertz")					1,095
Income/(loss) before income taxes	(6,357)	(843)	(9,363)	1,337	1,996
Provision for/(benefit from) income taxes	(1,157)	(314)	(2,499)	(328)	(512)
Income/(loss) before minority interests	(5,200)	(529)	(6,864)	1,665	2,508
Minority interests in net income/(loss) of subsidiaries	48	54	126	196	280
Income/(loss) from continuing operations	(5,248)	(583)	(6,990)	1,469	2,228
Income/(loss) from discontinued operations (Note 4)		7	2	45	47
Income/(loss) before cumulative effects	(5,248)	(576)	(6,988)	1,514	2,275
Cumulative effects of changes in accounting methods					(251)
Net income/(loss)					2,024
Average number of shares of Common and Class B stock outstanding					1,846
Amounts Per Share of Common and Class B Stock					
Basic income/(loss)					
Income/(loss) from continuing operations	-2.79	-0.31	-3.73	0.8	1.21
Income/(loss) from discontinued operations				0.02	0.03
Cumulative effects of changes in accounting principles					-0.14
Net income/(loss)	-2.79	-0.31	-3.73	0.82	1.1
Diluted income/(loss)					
Income/(loss) from continuing operations	-2.79	-0.31	-3.73	0.76	1.14
Income/(loss) from discontinued operations				0.03	0.02
Cumulative effects of changes in accounting principles					-0.11
Net income/(loss)	-2.79	-0.31	-3.73	0.79	1.05
Cash dividends	0.05	0.1	0.25	0.3	0.4

Balance Sheet	9/30/06 (unaudited)	12/31/05 , Restated
Assets		
Cash and cash equivalents	25,511	28,406
Marketable securities	14,552	10,672
Loaned securities	564	3,461
Other receivables, net	8,004	8,536
Net investment in operating leases	30,943	27,099
Retained interest in sold receivables	1,073	1,420
Inventories (Note 6)	11,997	10,271
Current assets	92,644	89,865
Equity in net assets of affiliated companies	2,828	2,579
Finance receivables, net	106,685	105,975
Net property	37,844	40,676
Deferred income taxes	4,197	5,880
Goodwill and other intangible assets (Note 9)	6,396	5,945
Assets of discontinued/held-for-sale operations		5
Other assets	16,871	18,534
Total assets	267,465	269,459
Liabilities and Stockholders Equity		
Payables	22,738	22,910
Accrued liabilities and deferred revenue	28,733	29,700
Debt	978	977
Deferred income taxes	2,774	5,660
Current liabilities	55,223	59,247
Accrued liabilities and deferred revenue	48,632	43,347
Long term debt	153,432	152,301
Minority interests	1,015	1,122
Stockholders equity		
Capital stock		
Common Stock, par value \$0.01 per share (1,837 million shares issued)	18	18
Class B Stock, par value \$0.01 per share (71 million shares issued)	1	1
Capital in excess of par value of stock	4,579	4,872
Accumulated other comprehensive income/(loss)	(785)	(3,680)
Treasury stock	(258)	(833)
Retained earnings	5,608	13,064
Total stockholders equity	9,163	13,442
Total liabilities and stockholders equity	267,465	269,459

[For Income Statement items, the last 12 month figures should be used.]

- 1 Compute the Z-score for Ford on two dates:
- | | |
|---|------------|
| a | 9/30/2006 |
| b | 12/31/2005 |

- 2 Based on those Z-scores what can you say about the probability of Ford going bankrupt ?
What are the main reasons for the worsening of the z-score over the nine months?

- 3 Use two ratios to predict the ratings for Ford debt on the two dates. Do not use information from the accompanying article. Justify you ratings based on S & P key industrial financial ratios.

- 4 A recent article which describes Ford's attempt to increase its debt is attached. What do you think will happen to the ratings of Ford debt already in the books? How will the new issues be rated - higher or lower than the current debt ratings before the new issues?

- 5 Mention two possible financial measures that Ford could take to boost its bond ratings.

Extracts from the 10-K report filed by PepsiCo in 2003 are given below.

PepsiCo, Inc. was incorporated in Delaware in 1919 and was reincorporated in North Carolina in 1986. When used in this report the terms "we," "us," "our" and the "Company" mean PepsiCo and its divisions and subsidiaries.

Our Divisions

We are a leading, global snack and beverage company. We manufacture, market and sell a variety of salty, convenient, sweet and grain-based snacks, carbonated and noncarbonated beverages and foods. We are organized in six divisions:

- Frito-Lay North America,
- Frito-Lay International,
- Pepsi-Cola North America,
- Gatorade/Tropicana North America,
- PepsiCo Beverages International, and
- Quaker Foods North America.



Our North American divisions operate in the United States and Canada. Our international divisions operate in over 175 countries, with our largest operations in Mexico and the United Kingdom operations in Mexico and the United Kingdom

The financial statements of the company for the year ending December 28 2002 are given below. Selected footnotes are attached.

Consolidated Statement of Income

PepsiCo, Inc. and Subsidiaries

Fiscal years ended December 28, 2002, December 29, 2001

in millions except per share amounts

	2,002	2,001
Net Sales	25,112	26,112
Cost of sales	11,497	12,397
Selling, general and administrative expenses	8,523	8,523
Amortization of intangible assets	138	138
Merger-related costs	224	224
Other impairment and restructuring charges	20,382	21,282
Operating Profit	4,730	4,830
Bottling equity income	280	280
Interest expense	(178)	(178)
Interest income	36	36
Income before Income Taxes	4,868	4,968
Provision for Income Taxes	1,555	1,655
Net Income	3,313	3,313
Net Income per Common Share		
Basic	1.890	1.510
Diluted	1.850	1.470

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

PepsiCo, Inc. and Subsidiaries
December 28, 2002 and December 29, 2001
(in millions except per share amounts)

	2,002	2,001
ASSETS		
Current Assets		
Cash and cash equivalents	1,638	683
Short-term investments, at cost	207	966
	1,845	1,649
Accounts and notes receivable, net	2,531	2,142
Inventories	1,342	1,310
Prepaid expenses and other current assets	795	752
Total Current Assets	6,513	5,853
Property, Plant and Equipment, net	7,290	6,876
Amortizable Intangible Assets, net	801	875
Nonamortizable Intangible Assets	4,418	3,966
Investments in Noncontrolled Affiliates	2,611	2,871
Other Assets	1,841	1,254
Total Assets	23,474	21,695
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Short-term obligations	562	354
Accounts payable and other current liabilities	4,998	4,461
Income taxes payable	492	183
Total Current Liabilities	6,052	4,998
Long-Term Debt Obligations	2,187	2,287
Other Liabilities	4,226	4,126
Deferred Income Taxes	1,718	1,496
Preferred Stock, no par value	41	41
Repurchased Preferred Stock	(48)	(15)
Common Shareholders' Equity		
Common stock, par value 1 2/3¢ per share (issued 1,782 shares)	30	30
Capital in excess of par value		13
Retained earnings	13,464	11,519
Accumulated other comprehensive loss	(1,672)	(1,646)
	11,822	9,916
Less: repurchased common stock, at cost (60 and 26 shares, respectively)	(2,524)	(1,268)
Total Common Shareholders' Equity	9,298	8,648
Total Liabilities and Shareholders' Equity	23,474	21,581

See accompanying notes to consolidated financial statements.

Consolidated Statement of Cash Flows

PepsiCo, Inc. and Subsidiaries

Fiscal years ended December 28, 2002, December 29, 2001

(in millions)

	2,002	2,001
Operating Activities		
Net income	3,313	2,662
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	1,112	1,082
Merger-related costs	224	356
Other impairment and restructuring charges		31
Cash payments for merger-related costs and other restr	(123)	(273)
Pension plan contributions	(820)	(446)
Bottling equity income, net of dividends	(222)	(103)
Deferred income taxes	288	162
Deferred compensation – ESOP	–	48
Other noncash charges and credits, net	263	209
Changes in operating working capital, excluding effects of acquisitions and dispositions		
Accounts and notes receivable	(260)	7
Inventories	(53)	(75)
Prepaid expenses and other current assets	(78)	(6)
Accounts payable and other current liabilities	426	(236)
Income taxes payable	278	394
Net change in operating working capital	313	84
Other	279	8
Net Cash Provided by Operating Activities	4,627	3,820
Investing Activities		
Capital spending	(1,437)	(1,324)
Sales of property, plant and equipment	89	
Acquisitions and investments in noncontrolled affiliates	(351)	(432)
Divestitures	376	
Short-term investments, by original maturity		
More than three months – purchases	(62)	(2,537)
More than three months – maturities	833	2,078
Three months or less, net	(14)	(41)
Snack Ventures Europe consolidation	39	
Net Cash Used for Investing Activities	(527)	(2,256)
Financing Activities		
Proceeds from issuances of long-term debt	11	324
Payments of long-term debt	(353)	(573)
Short-term borrowings, by original maturity		
More than three months – proceeds	707	788
More than three months – payments	(809)	(483)
Three months or less, net	40	(397)
Cash dividends paid	(1,041)	(994)
Share repurchases – common	(2,158)	(1,716)
Share repurchases – preferred	(32)	(10)
Quaker share repurchases		(5)
Proceeds from reissuance of shares		524
Proceeds from exercises of stock options	456	623
Net Cash Used for Financing Activities	(3,179)	(1,919)

Effect of exchange rate changes on cash and cash equivalents	34	
Net Increase/-Decrease) in Cash and Cash Equivalents	955	(355)
Cash and Cash Equivalents, Beginning of Year	683	1,038
Cash and Cash Equivalents, End of Year	1,638	683

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1 – Basis of Presentation and Our Divisions

Basis of Presentation

Our financial statements include the consolidated accounts of PepsiCo, Inc. and the affiliates that we control. In addition, we include our share of the results of certain other affiliates based on our ownership interest. We do not control these other affiliates as our ownership in these other affiliates is generally less than fifty percent. Our share of the net income of noncontrolled bottling affiliates is reported in our income statement as bottling equity income. See Note 8 for additional information on our noncontrolled bottling affiliates. Our share of other noncontrolled affiliates is included in division operating profit. As a result of changes in the operations of our European snack joint venture, Snack Ventures Europe (SVE), we determined that effective in 2002, consolidation was required. Therefore, SVE's results of operations are consolidated with PepsiCo in 2002. Intercompany balances and transactions are eliminated.

Note 6 – Pension and Retiree Medical Plans

Our pension plans cover full-time U.S. employees and certain international employees. Benefits are determined based on either years of service or a combination of years of service and earnings. U.S. employees are also eligible for medical and life insurance benefits (retiree medical) if they meet age and service requirements and qualify for retirement benefits. We use a September 30 measurement date. Prior service costs are amortized on a straight-line basis over the average remaining service period of employees expected to receive benefits.

For additional unaudited information on our pension and retiree medical plans and related accounting policies and assumptions, see "Our Critical Accounting Policies" in Management's Discussion and Analysis.

Weighted average pension assumptions	2,002	2,001	2,000
Liability discount rate	6.70%	7.40%	7.70%
Expected return on plan assets	9.10%	9.80%	9.90%
Rate of salary increases	4.40%	4.60%	4.50%

Note 8 – Noncontrolled Bottling Affiliates

Our most significant noncontrolled bottling affiliates are The Pepsi Bottling Group (PBG) and PepsiAmericas (PAS). These affiliates account for over 40% of our worldwide bottler case sales.

The Pepsi Bottling Group

In addition to approximately 38% of PBG's outstanding common stock that we own at year-end 2002, we own 100% of PBG's class B common stock and approximately 7% of the equity of Bottling Group, LLC, PBG's principal operating subsidiary. This gives us economic ownership of approximately 42% of PBG's combined operations. PBG's summarized financial information is as follows:

	2002	2001
Current assets	1,737	1,548
Noncurrent assets	8,290	6,309
Total assets	<u>10,027</u>	<u>7,857</u>
Current liabilities	1,248	1,081
Noncurrent liabilities	6,607	4,856
Minority interest	348	319
	<u>8,203</u>	<u>6,256</u>
Our investment	884	762
	2002	2,001
Net sales	9,216	8,443
Gross profit	4,215	3,863
Operating profit	898	676
Net income	<u>428</u>	<u>305</u>

"We Sell Soda"



Our investment in PBG was \$118 million higher than our ownership interest in their net assets at year-end 2002. Based upon the quoted closing price of PBG shares at year-end 2002, the calculated market value of our shares in PBG, excluding our investment in Bottling Group, LLC, exceeded our investment balance by approximately \$1.9 billion.

Related Party Transactions

Our significant related party transactions involve our noncontrolled bottling affiliates. We sell concentrate to these affiliates that is used in the production of carbonated soft drinks and noncarbonated beverages. The sale of concentrate is reported net of bottler funding. We also sell certain finished goods to these affiliates and we receive royalties for the use of our trademark for certain products. For further unaudited information on these bottlers, see "Our Customers" in Management's Discussion and Analysis. These transactions with our bottling affiliates are reflected in the Consolidated Statement of Income as follows:

	2,002	2,001	2,000
Net sales	3,455	2,262	1,978
Selling, general and administrative expenses	83	57	5

As of December 28, 2002, the receivables from these bottling affiliates were \$126 million and payables to these affiliates were \$122 million. As of December 29, 2001, the receivables from these bottling affiliates were \$119 million and payables to these affiliates were \$108 million. Such amounts are settled on terms consistent with other trade receivables and payables. See Note 9 regarding our guarantee of certain PBG debt.

Note 9 – Debt Obligations and Commitments

Long-Term Contractual Commitments and Off-Balance Sheet Arrangements

Payments Due by Year	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-term contractual commitments ^(a)					
Long-term debt obligations ^(b)	2,187		603	699	885
Non-cancelable operating leases	526	129	169	91	137
Purchasing commitments	3,307	773	1,006	569	959
Capital equipment commitments	34	34			
Marketing commitments	251	75	115	52	9
Other commitments	31	23	8		
	6,336	1,034	1,901	1,411	1,990

- (a) Reflects non-cancelable commitments as of December 28, 2002 based on year-end foreign exchange rates
- (b) Excludes current maturities of long-term debt of \$485 million which are classified within current liabilities.

Long-term contractual commitments, except for our long-term debt obligations, are not recorded in our Consolidated Balance Sheet. Non-cancelable purchasing, capital equipment and marketing commitments are in the normal course of our business for our projected needs. Our non-cancelable capital equipment commitments primarily relate to our new concentrate plant in Ireland. As bottler funding is negotiated on an annual basis, these commitments are not reflected in our long-term contractual commitments. See Note 8 regarding our commitments to noncontrolled bottling affiliates.

Off-Balance Sheet Arrangements

It is not our business practice to enter into off-balance sheet arrangements nor is it our policy to issue guarantees to our bottlers, noncontrolled affiliates or third parties. However, certain guarantees were necessary to facilitate the separation of our bottling and restaurant operations from us. In connection with these transactions, we have guaranteed \$2.3 billion of Bottling Group, LLC's long-term debt through 2012 and \$68 million of YUM! Brand's, Inc. (YUM) outstanding obligations, primarily property leases. The terms of our Bottling Group, LLC debt guarantee are intended to preserve the structure of PBG's separation from us and our payment obligation would be triggered if Bottling Group, LLC failed to perform under these debt obligations or the structure significantly changed. Our guarantees of certain obligations ensured YUM's continued use of these properties. These guarantees would require our cash payment if YUM failed to perform under these lease obligations

Required

In answering the following questions, combine the line items of PepsiCo statements into groups that correspond to line items that are reported in note 8. Compute the answers only for year ending 28-Dec-02. Ignore note 9 in answering questions 1 to 4. Do not use averages for any ratios from balance sheets.

- 1** Compute the following ratios for PepsiCo using figures in the reported statements.

Do not use averages for denominator, use only Dec 28, 2002 data.

a Current ratio.

b Debt to equity.

c Operating income to sales.

d Return on assets (After tax).

e Times interest Earned

f Return on Equity

- 2a** Prepare a pro forma Dec 28, 2002, balance sheet for PepsiCo with its unconsolidated equity companies fully consolidated.

- 2a** Prepare a pro forma income statement for the year ending Dec 28, 2002, for PepsiCo with its unconsolidated equity companies fully consolidated.

3 Compute the ratios listed in 1 for PepsiCo using the pro forma statements prepared under 2.

a Current ratio.

b Debt to equity.

c Operating income to sales.

d Return on assets (After tax).

e Times interest Earned

f Return on Equity

- 4 Which ratios worsened due to full consolidation ? Why?
Why do you think PepsiCo did not consolidate all its affiliates on its financial statements ?

-
- 5 Consider note 9. Will the estimate of the risk profile of PepsiCo change if you consider the information in Note 9. Recompute the ratios listed in 1 for PepsiCo. Note that all ratios will not change with the new information. List the assumptions you make in your analysis.