

Procter and Gamble Analysis

- A. The Max Factor acquisition effect must be removed as the purchase is an investing activity does not affect operations.

110712

Consolidated Statement of Cash Flows

Years Ended June 30 (Millions of Dollars Except Per Share Amounts)

	As reported	1994 Less Max Factor	
Operating Activities			
Net earnings before prior years' effect of accounting changes			2,211
Depreciation and depletion in 1994			1,045
Amortization of goodwill in 1994			89
Post retirement healthcare and life insurance benefits (not cash)	63	(10)	53
Increase in deferred income taxes	Asset (24)	8	32
	Liability		164
Increase in taxes payable			(286)
Change in accounts receivable	4	44	40
Change in inventories	(26)		26
add currency translation gains			36
Increase in payables	353	(92)	261
Increase in accrued liabilities			123
Increase in prepaid expenses and other current assets			(31)
Cash flow from operating activities			<u>3,763</u>
			(50)
Investing Activities			
<u>B</u> Property Plant and Equipment, purchased	(1,584)		
Assets written down from restructuring	(577)	(2,161)	
Acquisitions			(56)
Other assets			
Goodwill			
Max Factor		(1,031)	
Change in marketable securities		23	
Cash flow from investing activities		<u>(3,225)</u>	
Financing Activities			
Net income	2,211		
Retained earnings	Change	<u>1,248</u>	
Dividends to stockholders			(963)
Change in short-term debt			(437)
Additions to long-term debt			806
Proceeds from preferred stock			(27)
Proceeds from common stock	2	+ 83 =	85
Proceeds from treasury stock sales			49
Cash flow from financing activities			<u>(487)</u>
Increase in Cash and Cash Equivalents			51
Cash and cash Equivalents Beginning of Year	2,322		
Cash and Cash Equivalents End of Year	2,373		51

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Notes

Max Factor

Accounts receivable	44		
Deferred Income taxes (asset)	8		52
Accounts payable	92		
Post retirement healthcare and life insurance b	10		102
Book value of Equity			-50
Goodwill from Max Factor	1,031	-	-50 = 1,081

Intangible Assets, Cost

Begin Balance	4,429	
<u>Goodwill from Max Factor</u>	1,081	
<u>A Purchases</u>		
End balance	5,510	

Property and Equipment

	Property and equipment, at cost			Accumulated Depreciation		
Begin Balance	14,877			Begin Balance	5,392	
<u>B Purchases</u>	1,584			<u>Depreciation and amortization</u>	1,045	
			565	<-	<u>Sold</u>	565
End balance	15,896			End balance	5,872	

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B1 Return on equity

$$\frac{\text{Net income}}{\text{Average equity}} = \frac{2,211}{8,137} = 27.17\%$$

B2 P & G's effective tax rate in 1993

$$1,135 \div 3,346 = 33.92\%$$

B3 Return on assets

Net income		2211		2211	
+ (1-Tax rate)	+	66.08%	+		
• Interest expense	•	482		318.5003	2529.5
÷ Average assets	÷	25,735	÷	25735	25735
					= 9.83%

B4 Debt to equity ratio

Average total debt					
Short term		1,594			
+ Long term	+	5,577		7,171	
÷ Average equity	÷		÷	8,137	= 88.13%

Operating Liabiltied to equity ratio

$$\frac{\text{Assets - Equity - debt}}{\text{Average equity}} = \frac{10,428}{8,137} = 128.16\%$$

B5 Average interest rate

Interest expense		482			
÷ Average total debt	÷	7170.5	=	6.72%	
After tax interest rate	=	66.08%	•	6.72%	= 4.44%

ROE	=	ROA	+ [	ROA	-	After tax interest rate	]x (Debt/equity)
			+ [	ROA	-	0	]x (Trade debt / equity)
	=	9.83%	+ [	9.83%	-	4.44%	]x 88.13%
			+ [	9.83%			]x 128.16%
	=	9.83%	+ 4.75%	+ 12.60%			= 27.17%

B6	Book value of equity	Ending equity	8,832	
	per share on	Number of shares	÷ 684.3	
	December 31, 1994	Book value of equity per share	=	\$12.91
	Stock Price of P & G on June 30, 1994			\$51.25

B7	Operating margin	Operating Income / Revenue	
		3,580 / 30,296 =	11.82%

B8	Total asset turnover	Revenue / Average assets	
		30,296 / 25,735 =	1.18

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C. Inventories

June 30 (Millions of Dollars)	1994	Change	1993
Total inventory as reported	2,877		2,903
LIFO reserve layer	225	141	84
FIFO value (= approximates current cost)	3,102		2,987

In the beginning inventory, the FIFO cost of

FIFO layer that was sold:	2,903	-	1,013	=	1,890
Layer valued as LIFO					1,097
Specific inflation rate	141	÷	1,097	=	12.85%
Additional LIFO cost of the FIFO layer that was sold	12.85%	•	1,890	=	242.93

	Partial LIFO	100.00% FIFO	100.00% LIFO
Effect on cost of goods sold		141.00	(242.93)
After tax effect • 65.00%		91.65	(157.90)
Income as reported	2,211.00	2,211.00	2,211.00
Income	2,211.00	2,302.65	2,053.10

Answer

C1

C2

Only US allows LIFO. So US statutory rates are used.

C3 FIFO value (= approximates current cost) of inventories at the end of 1994					3102
If P & G maintains the same real level of inventories, then the FIFO value of the inventories at the end of 1993 should be					
Real increase in inventories	112.85%	•	2987	=	$\frac{3370.926}{-268.9262}$
So real inventories decreased.	Rate	-268.926	÷	3370.926	= (7.98)%

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D. Taxes

D1 Taxes paid in fiscal year 1994 = Current tax expense - Increase in taxes payable
 = 939 - (286) = 1,225

D2 Taxable income = Earnings before Taxes - [Increase in deferred taxes ÷ tax rate]
 = 3,346 - 196 ÷ 33.92%
 = 2,768

D3 Deferred taxes due to depreciation: 1,173 - 1,133 = 40
 Increase in 1994 Balance, 1994 Balance, 1993

Tax deductible depreciation is more by = 40 ÷ 33.92% = 117.92

D4 Restructuring losses taken by 1993, not recognized for tax purposes:				In 1994
Current	234			274
Noncurrent	623			364
Total	857			638
	÷ 33.92%			33.92%
	= 2,526			1,881

D5 Amount of assets that P & G wrote off in fiscal year 1994, for tax purposes
 = 2526.451 - 1880.835 = 645.6159

D6 P & G's reported expense for postretirement benefits in fiscal year 1994.
 = Cash paid + Increase in deferred tax asset ÷ tax rate
 = 23 + [540 - 522] ÷ 33.92%
 = 23 + 53 = **76.06**