



## FIN 360: PRINCIPLES OF FINANCIAL MANAGEMENT FINANCIAL STATEMENTS AND CASH FLOW CRITICAL THINKING & CONCEPTUAL QUESTIONS

1. Why does the SEC require publicly traded companies to have their financial statements available?
2. What does it mean to be a *residual claimant* to a firm? Why would any one *want* to be a residual claimant instead to a firm instead of a lender?
3. What is liquidity and the two components of liquidity? What are the benefits and costs of liquidity to the firm?
4. How might you determine how liquid a firm is at a point in time?
5. Explain the *book value* of equity and *market value* of equity.
6. Explain it means if a firm's book value of equity becomes negative. Explain why *market* value of equity going negative is not possible.
7. Explain the difference between **accrual accounting** and the **matching principle**. Explain how each may each cause a firm's cash flow to differ from its profits or accounting income.
8. Explain in simple terms what a (1) *positive* number and (2) *negative* number for each of the following means.
  - a. Net working capital
  - b. Operating cash flow
  - c. Net capital spending
  - d. Cash flow to creditors
  - e. Cash flow to stockholders
  - f. Net new borrowing
  - g. Net new equity raised
  - h. Cash flow from assets
9. How much would a firm's retained earnings increase from last year to this year if it had a net income of \$500 million this year and paid dividends of \$200 million. Why?
10. Explain how the cash flow identity and the balance sheet are related.
11. Why do we frequently "add back" depreciation when we compute cash flows?
12. Explain in simple terms why an increase in net working capital is a cash "outflow" while a decrease in net working capital is a cash "inflow".
13. Review the Excel file "*Balance Sheet and Income Statement Review*." Can you define all the balance sheet items? Can you create from memory your own balance sheet and income statement if given an alphabetical list of accounts?

