



Financial Management and Analysis

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FINANCIAL MANAGEMENT AND ANALYSIS

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About the Author

Pamela P. Peterson did her undergraduate work at Miami University in Oxford, Ohio, completing her degree in accounting in 1975. Following this, she was employed by Arthur Andersen & Co. in Chicago. She earned her Ph.D. in Business Administration at the University of North Carolina in Chapel Hill in 1981. She successfully completed the Chartered Financial Analyst (CFA) program in 1992.

At Florida State University since 1981, she has taught undergraduate and graduate courses: Introduction to Financial Management, Problems in Financial Management, Quantitative Methods in Business, and Empirical Research in Finance. Professor Peterson has been the advisor for the Florida State University student chapter of the Financial Management Association. She has also helped candidates prepare for the CFA examinations.

Professor Peterson has published over twenty-five articles in the *Financial Analysts Journal*, the *Journal of Banking and Finance*, the *Journal of Finance*, the *Journal of Financial Economics*, the *Journal of Financial and Quantitative Analysis*, and other journals. Her primary research interests are capital structure issues, dividend policy, and analysts' forecasts. She has been active in national and regional professional associations, serving as a member of the board of directors of the Financial Management Association, the Financial Management Association Student Chapters, and the Eastern Finance Association.

Preface

Financial Management and Analysis introduces the concepts, tools, and applications of finance. It is written to enable students beginning their study of finance to understand financial decision making and its role in the strategy of the entire firm. Throughout the text, you'll see how financial decision making is an integral part of the firm's overall decision-making processes. Financial decisions must be coordinated with accounting, marketing, and production decisions, not isolated from them.

The principles and tools of finance are applicable to all forms and sizes of business enterprise, not only to large corporations. Just as there are special problems and opportunities for small family-owned businesses (such as where to obtain financing), there are special problems and opportunities for large corporations (such as agency problems). However, the fundamentals of financial management are the same.

Similarly, those principles and tools are applicable to firms around the globe. While customs and laws may differ among nations, the principles, theories, and tools of financial management do not. For example, no matter where a firm is located, in deciding to buy a particular piece of equipment, a financial manager must evaluate how this decision will affect the firm's future cash flows.

A strong foundation in the principles of finance is necessary to understand investment and financing decisions. In this text I build that foundation in three ways: by presenting the principles and theories of finance through intuition, instead of proofs and theorems (for example, I walk the student through the intuition of capital structure theory with numerical and real world examples); by using careful, step-by-step examples, numerous graphs, and time lines.

ORGANIZATION

Financial Management and Analysis is presented in seven parts. Parts I, II, and III cover the basics, including the objective of financial management, valuation principles, and the relation between risk and return. Financial decision making is covered in Parts IV, V, and VI, and consists of long-term investment management, the management of long-term sources of funds, and working capital management. Part VII returns to the objective of the maximization of owners' wealth and its relationship to financial planning and strategy.

These seven parts comprise seventeen chapters—fewer than most texts. What is missing? Nothing. The text is structured in a different, yet logical manner. Differences you will notice are:

- Dividends are included in Chapter 11, *Common and Preferred Stock*, because they are one of the cash flows associated with shares of stock.
- Leasing is covered in an appendix to Chapter 9, *Evaluating Capital Projects*, because it is a special case of acquiring an asset, calling for different evaluation techniques.
- Cash management, accounts receivable, and inventory management are covered in one chapter because they involve some of the same basic techniques.

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Topics such as mergers and acquisitions, bankruptcy, and international finance, which are extensions of the basic concepts, are interwoven within fundamentals. For example, bankruptcy appears with the capital structure decision (in Chapter 13, *Capital Structure*) because the possibility of financial distress and bankruptcy affects the choice of sources of funds.

DISTINGUISHING FEATURES OF THE TEXT

- **Logical structure.** The text begins with core principles and tools, followed by long-term investment and financing decisions. The first three parts lay out the basics, the fourth part is the “left side” of the balance sheet (assets), and the fifth part is the “right side” of the balance sheet (liabilities and equity). Working capital decisions, which are made to support day-to-day operations of the firm, are discussed in the sixth part. The last is a reprise of the objective of financial management: the maximization of owners’ wealth.
- **Numerous illustrations.** Graphs and illustrations have been developed to clarify and visually reinforce mathematical concepts. For example, the growth of a bank balance is shown in several ways: mathematically, in a displayed time line, and with a bar graph.
- **Research questions and problems.** Each chapter contains questions or problems that require research on actual companies. These problems can be answered using library resources or computer databases, such as Standard & Poor’s *Compustat PC Plus* (CD-ROM). Computer resources are not required to complete any end-of-chapter question or problem, but students are encouraged to gain experience in the use of these resources. A data disk from Standard & Poor’s *Compustat* database is available for use by instructors and students.
- **Applications.** As much as possible, I develop concepts and mathematics using examples from actual practice. For example, first I present the basic ideas of financial analysis using a simplified set of financial statements for a fictitious company. Then I demonstrate the tools of financial analysis using real data from Wal-Mart Stores, Inc. To help students better grasp and retain major concepts and tools, I make use of over 200 actual company examples.
- **International and ethical issues.** As in the real world, international and ethical issues are integrated, not artificially separated from financial decision making. For example, international securities markets are discussed in Chapter 2, *Securities and Markets*, following the discussion of U.S. securities markets. In Chapter 16, *Management of Short-Term Financing*, the ethics related to late payments owed creditors is discussed with the techniques for managing accounts payable, making clear the ethics are an integral part of financial management.
- **Stand-alone nature of the chapters.** Chapters are written so that they may easily be rearranged to fit different course structures. An instructor can tailor this book to fit his or her course and its time frame, as well as the students’ level of preparation (for example, if students enter the course with sufficient background in accounting and taxation, Chapter 3 could be skipped).
- **End-of-text material.** I’ve included student-friendly end-of-text material. Aside from the time-value-of-money tables, you will find appendixes

illustrating how to use financial calculators, demonstrating how to read securities quotes in the financial press, and summarizing key statistical techniques. In addition to the appendixes, I have also included a thorough glossary. Along with brief solutions to each end-of-chapter problem in the text, you will find a set of hints for guiding students in problem solving without revealing the key elements in the solution.

SUPPLEMENTAL MATERIAL

Standard & Poor's Compustat Data Disk

Each adopting instructor can be provided with a data disk containing financial data on over thirty U.S. corporations. This data can be used to complete the research questions and problems requiring individual company data. These questions and problems are coded with a **PC+** "logo."

This disk contains a small portion of Standard & Poor's *Compustat* data, which is available on either magnetic tape or CD-ROM. Standard & Poor's *Compustat* data is a valuable research resource, consisting of twenty years of financial statement data on over 10,000 corporations.

Study Guide

Professor Marianne Westerman of the University of Colorado at Denver and I have prepared the *Study Guide* to accompany the text. It provides for each chapter:

- An outline.
- Fill-in questions.
- True-False questions.
- Multiple choice questions and problems.
- Short-answer questions and problems.

Instructor's Manual

I've prepared the *Instructor's Manual*, which contains material to assist in preparation of class lectures. It includes:

- A detailed chapter outline, suitable for use as a lecture outline.
- Additional real world examples to illustrate key concepts and applications.
- Additional questions and problems (with solutions).
- Additional problems and overhead masters to illustrate calculations.
- Sample solutions to end-of-chapter **Research** questions and problems.
- Overhead transparency acetates for key figures, tables, and equations developed in the text.
- References to resource material to assist in preparing and presenting class lectures and exams.
- Alternative chapter sequences and outlines for one-semester, one-quarter, two-semester, and two-quarter courses.

Solutions Manual

In addition to the hints and brief solutions at the end of the text, I have prepared detailed solutions to all end-of-chapter questions and problems.¹ Step-by-step solutions are provided with extra help for more challenging problems.

¹ Solutions to **Research** questions and problems are not provided in the manual since these require research on individual firms assigned by the instructor or chosen by the student. Sample solutions to **Research** questions and problems are provided in the *Instructor's Manual*.

Test Bank

Prepared by Professor Westerman, the *Test Bank* has over 1,000 questions. They are chosen to test students' understanding of both concepts and tools. A computerized *Test Bank* is also available.

Transparencies

Transparency masters in the *Instructor's Manual*:

- Describe or illustrate key concepts and tools.
- Demonstrate problems that are similar, but not identical, to examples shown in the text.
- Guide the students through lecture material.

In addition, color acetates for many illustrations in the text will be provided to adopters.

**Spreadsheet
Templates**

Spreadsheet programs are available to assist the students solving end-of-chapter problems. Though these programs are not necessary to complete any problems in the text, they will help students understand how computer software can be used in financial analysis. Programs are provided for such uses as the calculation of the yield to maturity, the calculation of basic financial ratios, and the generation of pro forma financial statements.

Videos

A program of videos will be available to adopters of *Financial Management and Analysis*. These videos are useful in supplementing lecture material, bringing the real world of finance closer to the student.

**PROBLEM
CHECKING**

All in text, end-of-chapter, *Test Bank*, and *Study Guide* problems and questions have been independently checked for accuracy. The efforts by Stuart Michelson, at Eastern Illinois University, and Stephen P. Huffman, at the University of Wisconsin—Oshkosh, to verify the accuracy of the text examples and solutions to the end-of-chapter problems are greatly appreciated.

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Pamela P. Peterson

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