SESSION 3
ELEMENTS OF AN ANNUAL REPORT AND FINANCIAL RATIOS

Objectives
1. Become familiar with the main parts of an annual report: (a) CEO's letter, (b) description of business activity, (c) management discussion and analysis, (d) audit report, (e) financial statements, (f) description of accounting procedures, (g) footnotes.
2. Understand the purposes of the four financial statements: (a) balance sheet, (b) income statement, (c) statement of cash flows, and (d) statement of owners’ equity.
3. Become familiar with the types of economic activity that are associated with common financial-statement line items, and thus the reasons why users of financial reports might find these items useful.
4. Understand the distinction between recognition and disclosure of information.
5. Begin to understand commonly-used financial ratios.

Reading Assignment
Pratt: Chapters 3 & 5
Intel Annual Report

Class Preparation Questions
1. What was Intel’s Net Income for 2000-2002? What was Intel’s EBIT (Earnings before Income Taxes) in each year? EBITDA (Earnings before Income Taxes, Depreciation and Amortization)?
3. Compute Intel’s Return on Equity for 2002. How does it compare to other firms in Intel’s industry?
4. Compute Intel’s Asset Turnover for 2002. How does it compare to other firms in Intel’s industry?
5. Compute the ratio of Intel’s stock price to its owner's equity-per-share outstanding. This is the “market-to-book” ratio. Why are they different? How would this ratio compare to market-to-book ratio of the average firm in the steel industry?
7. Compute Intel's Gross Margin Ratio [(Sales - Cost of Sales) / Sales] for the years 2000-2002. Comment on the trend. What economic and strategic factors might contribute to changes in this ratio over time? What types of companies would tend to have a high gross margin ratio?
8. Has Intel paid dividends over the past three years? How much? Why would Intel hold so much cash rather than, say, paying out higher dividends to its shareholders?
9. Compute Intel's Long-Term-Debt-to-Equity Ratio for 2000-2002. What benchmarks might you use to judge whether a firm's D/E ratio is high or low?
10. How much cash has Intel spent each of the last 3 years for Property, Plant, and Equipment? How quickly does Intel depreciate PP&E? (See the ' Accounting Policies note.) How does deprecating PP&E affect Intel's Income Statement, Balance Sheet, and Statement of Cash Flows?
11. Calculate the average age of outstanding accounts receivable for the past two years.

Graded Assignment
Problem Set 1

Optional Problems
E5-13, P5-13, ID5-1, ID5-2, ID5-11