Fill in the Blanks on Each Chapter

CHAPTER 1: THE ADVERSARIAL NATURE OF FINANCIAL REPORTING

1. The following are three ways that corporations can use financial reporting to enhance their value:
   a. ____
   b. ____
   c. ____
2. The true purpose of financial reporting is ______________________.
3. Corporations routinely ______________________ because the appearance of __________ receives a higher __________ multiple.
4. According to the ____________________, reversals of the excess write-offs offer an artificial means of __________ in subsequent periods.
5. The following are some of the powerful limitations to continued growth faced by companies:
   a. ____
   b. ____
   c. ____
6. Some of the commonly heard rationalizations for declining growth are:
   a. ____
   b. ____
   c. ____
7. __________ reached its zenith of popularity during the ___________ movement of the 1960s. However, by the 1980s, the stock market had converted the _________________________ into a(n) ______________________.
8. ___________ is one of the ways that the notion of diversification as a means of maintaining _____________ is revived from time to time.

9. Some of the stories used to sell stocks to individual investors are:
   a. ____
   b. ____
      i. ____
      ii. ____
   c. ____
10. When the story used to sell stocks to individual investors originates among stockbrokers or even ____________________, the zeal with which the story is disseminated may depend more on ______________ than the ____________________.
11. The ostensible purpose of financial reporting is ____________ of a corporation's earnings.
12. Mattel's internal investigation ______________ that management engaged ________, instead blaming mishandling of the discovery of the accounting error on:
   a. ____
   b. ____
   c. ____
13. The outside auditor's stamp of approval is no guarantee that __________ accurately reflect _____________.
14. When deliberate financial reporting violations come to light, the real scandal involves _____________.
15. By 2015, however, ________ of S&P 500 companies were reporting _________, up from about ___________ in 2009.
16. Between 2010 and ______, Under Armour's stock rose at an astounding compound annual growth rate of _______ percent. The manufacturer of sports and fitness apparel, shoes, and accessories was in the midst of a ________ streak of _________ or _______ year-over-year __________.
17. Concurrent with the slowdown in _________, Under Armour's _________ was slipping. Management delivered the disheartening news that _________ that investors were counting on would require ______.
18. The stock of another high-flier, ________, rose at a(n) ______ compound annual rate in the 15 years through ______. Over the next two years, shareholders of suffered a(n) _____ decline.

19. The problem for Boston Beer is that craft beer appears to have reached ________________________.
20. Analysts should view the issuers ________________ in the same manner that they temporarily ____________________________ in a friendly ______________________.
21. Viewing the production of financial statements ___________________ between _________________ may suit a(n) ____________________, but financial analysts need not join __________________ to do their job well.
22. Aside from ______________________, _______________________, and definitions of ___________________, analysts must consider the motivations of ___________________________, as well as the dynamics of _________________ in which they work.

CHAPTER 2: THE BALANCE SHEET

1. A study conducted on behalf of Big Five accounting firm Arthur Andersen showed that between _____ and _____, book value fell from ___ percent to ___ percent of the stock market value of public companies in the United States.
2. As noted by Baruch Lev of New York University, two examples of how traditional accounting systems are at a loss to capture most of what is going on today are:
   a. ____
   b. ____
3. In the examples in Question 2, there is no accounting event because _________________.
4. Some of the distinct approaches that have evolved for assessing real property are:
   a. ____
   b. ____
   c. ____
5. Some financial assets are unaffected by the difficulties of evaluating physical assets because ___________ in __________________.
6. Under the compromise embodied in SFAS 115, financial instruments are valued according to _________________ by the ___________ issuing ________________.

7. If a company wrote off a billion dollars worth of goodwill, its ratio of assets to liabilities would ________. Its ratio of _________ to _________ would not change, however.
8. Through stock-for-stock acquisitions, the sharp rise in equity prices during the late 1990s was transformed into _________________ values, despite the usual assumption that __________ in a company's ________ do not alter __________________.
9. Unlike _________ or _____________, goodwill is not an asset that can be readily ____ or _______ to raise cash. Neither can a company enter into a(n) ___________ of its goodwill as it can with its plant and equipment. In short, goodwill is not __________________ that management can either convert into _____ or use to _______ to extricate itself from a financial tight spot.
10. A reasonable estimate of a low-profit company's true equity value would be ___________ that produces ________ on equity __________ to the going rate.
11. Determining the cost of capital is a notoriously controversial subject in the financial field, complicated by thorny __________ and __________.
12. Among the advantages of market capitalization as a measure of equity are:
    a. ____
    b. ____
    c. ____
13. A limitation of the peer-group approach to valuation is that it fails to capture ___________ and therefore _________ one major benefit of using _____________________ as a gauge of actual equity value.
14. Instead of striving for theoretical purity on the matter, analysts should adopt a(n) _______________________, using the measure of equity value most useful ___________________.
15. Historical-cost-based balance sheet figures are the ones that matter in ____________ that a company will violate ________________ requiring __________ of a minimum ____ of debt to _________.
16. Users of financial statements can process only the information ____ ____, and they do not always have the information _______.
17. Deterioration in a company's financial position may catch investors by surprise because it occurs ________ and is reported _______.

CHAPTER 3: THE INCOME STATEMENT

1. Students of financial statements must keep up with ___________ of the past few years in transforming _______________ into _______ of ____________.
2. In the ____________________________, each income statement item is expressed as ________________ (sales or revenues), which is represented as _________ percent.
3. Besides facilitating comparisons between a company's present and past results, the _________________________ can highlight important facts about a company's ___________________.
4. Even within an industry, the breakdown of expenses can vary from company to company as a function of differing ______________ and ______________________.
5. Percentage breakdowns are also helpful for comparing a single company's performance with ________________________ and for comparing _________________________________ on the basis of their ______________________________.
6. Costs as percentages of sales also vary among companies within an industry for __________ than differences in _____________.
7. The more widely diversified pharmaceutical manufacturers can be expected to have _______ percentage ___________, as well as _______ percentage ______________________ expenses, than industry peers that focus exclusively on ___________.
8. Analysts must take care not to mistake difference that is actually a(n) ___________ of business strategy as evidence of _______ or ___________ managerial skills. A subtler explanation may be available at the modest cost of contacting some _________________________.
9. Executives whose bonuses rise in tandem with ____________ have a strong incentive not only to generate __________ but also to use every lawful means of ____________ through accounting ____________.
10. On a retrospective basis, a surge _______________ or an unexpected ________________ may indicate that __________ were inflated in a(n) ____________.
11. Along with ________________, another major expense category that can be controlled through assumptions is ________.

12. An unusually low ratio of ________ to _________________ with the ratios of its industry peers may indicate that management is being unrealistic in acknowledging the pace of wear and tear on fixed assets. Understatement of _______ and overstatement of ______ would result.
13. A company knows that creating _______ expectations about the future can raise _______ and lower ___________.
14. In recent years, "_________" has become a catchall for charges that companies wish analysts to consider ______________________ but that do not qualify for _______________
15. Corporate managers commonly perceive that _________ to their stock price will be ____________ if they take (for sake of argument) a $1.5 billion write-off than if _________________. The benefit of exaggerating the damage is that in subsequent years, the overcharges can be _________ in small amounts that do not generate any requirement for ____________.
16. The most dangerous trap that users of financial statements must avoid walking into, however, is inferring that the term "restructuring" connotes _______.
17. The purpose of providing pro forma results was to help analysts to project ________________ accurately when some event outside ________________ caused the _________ historical results to convey a misleading impression.
18. Computer software producers got into the act by omitting _______ of ___________ research and development from the expenses considered in calculating _______________.
19. Unlike operating income, a concept addressed by FASB standards, ______________ is a number that subjectively ___________ many ____________ "one-time events" that lack any standing under GAAP.
20. In fact, analysts who hope to forecast future financial results accurately must apply ______________ and set aside genuinely _____________ course-of-business events.
21. Analysts must exercise judgment when considering pro forma earnings; however, they must make sure to examine the actual ________ rather than ______ by relying solely on ______________.
22. An older, but not obsolete, device for beefing up reported income is _________ of selected _________.

23. A comparatively ____ ratio of PP&E to ____ or ____________ is another sign of potential trouble.
24. Management can _________ through techniques that more properly fall into the category of _________.
25. One way to increase profitability through _________ involves economies _______.
26. A corporation can easily accelerate its sales growth by buying ____ ________ and adding ________ to its own. Creating genuine value for shareholders through _________ is more difficult, although unwary investors sometimes fail to recognize the distinction.
27. Analysts need to distinguish between ________ growth and _______ growth. ________ growth consists of sales increases generated from a company's existing operations, and ________ growth represents incremental sales brought in through _________.
28. If Company A generates external growth by acquiring Company B and neither company nor its new subsidiary increases its profitability, then __________________ the merged companies is _______ than the sum of the two companies' values.
29. In general, the less ___________ the combining businesses are, the less _________ it is that the hoped-for economies of scope ___________.
30. As synergies go, projections of economies of scale in combinations of companies ________ the same business tend to be more plausible than economies of scope purportedly available to companies in ____________ businesses.
31. A company with relatively large, fixed _____ has a(n) ______ breakeven level. Even a modest economic downturn will reduce its capacity ________ below the rate required to keep the company profitable.
32. Deals that work on paper have often foundered on:
    a. ____
    b. ____
    c. ____
    d. ____
33. Financial statements cannot capture certain ____________ factors that may be essential to ___________. These include:
    a. ____
    b. ____
    c. ____

CHAPTER 4: THE STATEMENT OF CASH

1. The present version of the statement that traces the flow of funds in and out of the firm, the statement of cash flows, became mandatory under _______ for issuers with fiscal years ending after _________.
2. For financial-reporting (as opposed to ___________) purposes, a publicly owned company generally seeks to maximize ___________________, which investors use as a basis for valuing its shares.
3. A privately held company, unlike a(n) __________, which shows one set of statements to the public and another to the Internal Revenue Service, a private company typically prepares ______ of statements, with the ___________ foremost in its thinking. Its incentive is not __________ but to _________ the income it reports, thereby __________ its tax bill as well.
4. In a classic LBO, a group of investors acquires a business by putting up a(n) ______________ and __________ the balance.
5. The amount attributable to depreciation does not represent ______________ in the current year. Rather, it is a bookkeeping entry intended to represent the ____________________, through use, __________________.
6. Viewed in terms of cash inflows and outflows, rather than earnings, the ________________ begins to look like _______________.
7. Analysts evaluating the investment merits of the LBO proposal would miss the point if they focused on ________ rather than ______.
8. In an LBO, the equity investors do not reap spectacular gains without incurring significant ______. There is a danger that everything will not go ______________ and that they will lose ___________________. Specifically, there is a risk that _______________________ will fall short of expectations, perhaps as a result of __________ or because the investors' expectations were unrealistically ______________.
9. The _______ statement, rather than the _______ statement, provides the best information about a highly leveraged firm's financial health.
10. Among the applications and uses of the Statement of Cash Flows are:
    a. ____
    b. ____
    c. ____

11. When a company is _____________ bankruptcy, its balance sheet may __________ its asset value as a result of _________ having lagged the _______________ in profitability of the company's operations.
12. Revenues build gradually during the ________ phase, during which time the company is just _______ and _____________________.
13. Growth and profits accelerate rapidly during the ________ growth phase, as the company's products begin to penetrate the market and the production reaches a(n) ____________.
14. During the _________ growth period, growth in sales and earnings decelerates as the market nears _________. In the ____________ phase, sales opportunities are limited to the replacement of products previously sold, plus ____ sales derived from __________________.
15. Price competition often intensifies at this stage, as companies seek _________ through increased __________. The ________ industry stage does not automatically follow maturity, but over long periods some industries do get swept away by __________.
16. Sharply declining sales and earnings, ultimately resulting in ________ ________, characterize industries in decline.
17. ________ companies are typically voracious cash users.
18. ___________ companies are start-ups that survive long enough to reach the stage of entering the public market.
19. For a company at the _____________ stage, it may take several years for sales to reach a level ________________ sizable fixed costs that are _________ to its operations.
20. _____________ companies are in a less precarious state in terms of cash flow than their emerging growth counterparts.
21. Reflecting the __________ of its business, Kimberly-Clark generates a(n) _____________ level of cash from _________.
22. Far from depending on _________________, this mature company ____________ to investors, giving them the opportunity to ________ it in higher-growth, __________ businesses.
23. Some __________ companies choose instead to _______ their _______ cash flow internally. They either launch or acquire businesses with ______________ potential than their original, __________. The older businesses become _____________ to be milked for funding the newer activities.

24. ________________ companies are past the cash strain faced by growth companies that must fund large ________ programs.
25. _____________ companies struggle to generate sufficient cash as a consequence of meager earnings.
26. By studying the cash flow statement, an analyst can make informed judgments on such questions as:
    a. ____
    b. ____
    c. ____
27. In difficult times, when a company must cut back on various expenditures to __________, management faces many difficult choices. A key objective is to _______ damage to the company's ___________.
28. At times, ________ becomes ________ expensive, as a function of ____ interest rates or ________ stock prices. During the "______ crunches" that occasionally befall the business world, _______ financing is unavailable at any price.
29. If a corporation's financial strain becomes acute, the board of directors may take the comparatively extreme step of cutting or _________ ________.
30. Reducing __________ is a step that corporations try very hard to avoid for fear of _____________ with investors and consequently suffering an increase in __________.
31. A final factor in assessing financial flexibility is the change in adjusted working capital. Unlike conventional working capital (__________ minus ____________), this figure excludes ___________ as well as _____ and ______________.
32. A company with a strong balance sheet can fund much of that cash need by increasing its ____________ (credit extended by vendors). External financing may be needed, however, if accumulation of unsold goods causes ____________ to rise disproportionately to _____. Similarly, if customers begin paying more slowly than formerly, ____________ can widen the gap between working capital ____________ and ___________ availability.
33. One typical consequence of violating ___________ or striving to head off ________ is that management reduces discretionary expenditures to avoid _________.

34. Overinvestment has unquestionably led, in many industries, to prolonged periods of ______________, producing in turn chronically poor ____________. In retrospect, the firms involved would have served their shareholders better if they had increased _________________________ or ____________ stock, instead of ___________ new plants.
35. Keeping cash "trapped" in marketable securities can enable a firm to ___________ over "lean-and-mean" competitors when tight ____________ make it difficult to finance ____________ needs.
36. Another less obvious risk of eschewing financial flexibility is the danger of permanently losing ______________________ workers through ________________ occasioned by recessions.
37. The income statement is a dubious measure of the success of a highly __________ company that is being managed to ________ rather than __________ reported profits.
38. The cash flow statement is the best tool for measuring _____, which, contrary to a widely held view, is not merely a security blanket for __________ investors.
39. In the hands of an aggressive but prudent management, a cash flow cushion can enable a company to ______ essential long-term _______________ when competitors are forced to cut back.

CHAPTER 5: WHAT IS PROFIT?

1. Profitability is a yardstick by which businesspeople can measure their ___________ and justify their claims to __________.
2. When calculating __________ profits, the analyst must take care to consider only genuine revenues and deduct all relevant costs.
3. There can be no bona fide profit without an increase in ______. Bona fide profits are the only kind of profits ____________ in financial analysis.
4. Merely _________________ funds, it is clear, does not increase wealth.
5. An essential element of genuinely useful financial statement analysis is the willingness to take ______________ profits at something other than ____________.
6. The issuer of the statements can _____ or ______ its reported earnings simply by using its latitude to assume shorter or longer _______ lives for its __________ assets.

7. The rate at which the tax code allows owners to write off property overstates actual __________.
8. In the __________ business, companies typically record depreciation and amortization expense that far exceeds physical wear-and-tear on assets.
9. In many industries, fixed assets consist mainly of ________ or _____ that really __________ in value through use. The major risk of analytical error does not arise from the possibility that ________ depreciation _________ will substantially ________ economic depreciation, but the reverse.
10. Corporations have vastly increased their promulgation of non-GAAP numbers in this century. By 2017, the independent research provider Audit Analytics found that fully _________ of S&P 500 companies self-produced some measures in their earnings releases, up from a little _________ two decades earlier. Between 1996 and 2016, the average number of non-GAAP items in in those statements rose from just over ____ to more than _____.

CHAPTER 6: REVENUE RECOGNITION

1. Many corporations employ highly ________ recognition practices that comply with GAAP yet ______ the underlying ___________.
2. Under intense pressure to maintain their stock prices, companies characterized by _______________ sales growth seem particularly prone to _________.
3. To seasoned investors, a(n) _______ departure by a senior manager represents a(n) ______________ of trouble.
4. Bonus-seeking managers may initially veer off the straight-and-narrow by "__________" a small amount from _______ revenue, intending to "__________" the following year, but they instead fall further and further behind. Eventually, the gap between ________ revenues and economic ________ grows too large to sustain.
5. Even when an independent accounting firm certifies that a company's financials have been prepared ______________ with generally accepted accounting principles, the analyst must stay alert for evidence that the numbers _________ the economic _______.
6. Staying alert to evidence of flawed, or possibly _________, reporting is essential, even when the auditors put their __________ on the numbers.

7. As a rule, distorting one section of the financial statements throws the numbers ___________ in some ________. Assiduous tracking of a variety of ___________ should raise serious questions about a company's reporting, at a minimum.
8. The explanation for the sudden drop in projected earnings was that, in 2001, Bristol Myers gave _________________ to induce them to buy its _________ at a much faster rate than necessary to _____________ at pharmacies.
9. "_____________" is a security analysts' term for the financial reporting gimmick that Bristol Myers employed to _________ future _________ to the ____________.
10. Along with other pharmaceutical producers, Bristol Myers was feeling profit pressures due to difficulties in ________________________ to replace sales of products on which __________ was expiring.
11. Haydon was known for speaking candidly about Bristol Myers's declining sales prospects. Consequently, his reassignment was taken ___________ that executives _________________ at all costs.
12. Also suspect was Bristol Myers's repeated practice of establishing ______________ that exactly equaled gains __________ sales.
13. The Bristol Myers Squibb case study nevertheless illustrates the value of testing a company's ___________ against __________ provided information.
14. According to Take-Two management, the adjustment arose because the company _____________ on some games it sold to "certain independent _________ distributors" but which were later _________ or ___________ by Take-Two.
15. ________ to the lesson taught by many other cases of financial misreporting, it paid to accept the Take-Two _________ management's assurances that the company's business prospects ___________.
16. Take-Two shipped hundreds of thousands of video games to distributors who were under no ________________ for them, _________________ booked the shipments as if they were sales, then _________________ of the products in later periods.
17. Encouragingly for users of financial statements, managers who __________ recognize _________ are often betrayed by the ___________ they create.

18. In layaway sales, customers reserve goods ___________, and then make additional payments over a specified period, ________________________ when they have paid in full.
19. Prior to the change in accounting practice, which FAS 101 made mandatory, Walmart booked layaway sales as soon as it _________________________________. Under the new and more conservative method, the company began to recognize the sales only when customers _______________________________________ and took _________________ of the goods.
20. On the whole, Bally's reported profit margins benefited from the increase in _________ memberships as a percentage of total revenues. The reported earnings, however, rested on assumptions regarding the percentage of customers who would _____________ to make all of the ____________________.
21. As in any sales situation, aggressive pursuit of new business could result in acceptance of more ______________ customers. On average, the newer members might prove to be less ________________ or less committed to physical fitness than the previous _________ of financed ________.
22. There was no change in the accounting principle, namely, ____________. In the case of a health club, members' upfront fees represent payments for _____________ over the terms of their __________. Club operators should therefore recognize the revenue over the period in which __________________.
23. Under GAAP, the general requirement was to spread membership fees over the ______________. If a company offered refunds, it could not book _______________ until the refund period expired, unless there was _______________ long history to enable management to estimate ________________ with reasonable confidence.
24. Under certain circumstances, a company engaged in long-term contract work can book _______ before ________ its customer. This result arises from GAAP's solution to a mismatch commonly observed at __________ firms.
25. GAAP addresses the problem through the ____________________ method, which permits the company to recognize revenue in _____________ to the amount of work ________ rather than in line with its billing.

26. As is generally the case with artificial __________, taking liberties with the percentage-of-completion borrows _______________, making a surprise shortfall ________ at some point.
27. The SEC claimed that management at Sequoia Systems inflated revenue and profits by:
    a. ____
    b. ____
    c. ____
28. The SEC also claimed that management at Sequoia Systems profited from the scheme by ___________ before a(n) __________ of the company's __________________ emerged.
29. Loading the distribution channels consists of inducing _____________ or _______ to accept larger shipments of goods than their _________ sales _________ warrant.
30. Loading does not boost physical _________ but merely shifts the timing of its _____________ as ________ revenues.
31. Inevitably, the underlying trend of final sales to consumers slows down, at least temporarily. At that point, the manufacturer's growth in reported revenue will maintain its trend only if its __________ take on even ______________, relative to their sales. If the distributors balk, the ____________ will unravel, forcing a sizable ________ of previously recorded profits.
32. Krispy Kreme revised its senior executive compensation plan. Henceforth, officers would receive __________ unless the company ________ earnings in each quarter that ________ its earnings per share guidance by ________.
33. In essence, according to the *Wall Street Journal*'s story, Krispy Kreme manufactured ________ by taking money ___________ and putting it _________.
34. Had Krispy Kreme instead _______________ the franchises and then ______________, it would have incurred ________. The catch is that an asset is supposed to be something that creates _______________. Terminated stores would not seem to ______ that definition.
35. Most, if not all, of the ______ on Krispy Kreme's __________ appeared to have come from a(n) ______________ transaction rather than from ________.

36. Krispy Kreme increased the size of the corrections to its fiscal 2004 results. The previously undisclosed problems involved _______________, _____________ and improvements related to leases, and reversal of income related ______________________ a franchisee before _________________ bought that operation.
37. Krispy Kreme was not a case of ___________ fictitious earnings. Rather, the SEC complaint depicted a process of ____________, through a wide range of financial statement _____, to beat earnings ________ by $0.01 in every ________.
38. An exceptionally long record of beating ________ or posting __________ gains in ______________ is a reason to suspect earnings __________.
39. A second lesson of the Krispy Kreme case is that ___________ transactions and ________ financial reporting often go hand in hand.
40. It is impossible to assess the quality of an internal investigation without information on the ________________ and the basis for its ___________.
41. Users of financial statements should not be intimidated by corporate _______________________ that denounce allegedly irresponsible _______________ and _____________.
42. In 2001, Halliburton adopted an even more aggressive approach to ______________. For some projects, Halliburton began reporting sales months before ____________ for the work. Previously, the policy was to book revenues only if the company _______________ within one month. In addition, the company began keeping some disputed bills on the books for over ________ instead of ___________ and ______________. The previous policy was to refrain from a write-off only if it believed it would ______ most of the claim _____________.
43. Halliburton became more aggressive about ________________ before ___________, a classic technique for pumping up ________________.
44. If earnings look suspiciously ________ during a(n) ___________ for the company's industry, users of financial statements should never automatically _________ the possibility that ____________________ explains the disparity.
45. A stock's value is a function of expected ______________, which partly depend on the ___________ of the company's ________ vis-à-vis its competitors'.
46. Generally, the initial response of corporate executives caught in a lie is to ___ themselves __________, but gratifyingly often, the _______ ultimately _______.

47. Analysts who strive to go beyond routine ____________ can profit by seeking independent __________ of corporate disclosure, even when the auditors have already placed their ___________ on it.
48. Sometimes, management ___________ revenue recognition in order to ________ short-run profits. The motive for this paradoxical behavior is a desire to report the sort of smooth _______________ earnings ______ that equity investors reward with _____ price-earnings _________
49. Grace executives reckoned that with earnings already meeting Wall Street analysts' forecasts, a windfall ________ the company's _________. Such an inference would have been consistent with investors' customary ___________ of profits and losses that they perceive to be generated by _____________.
50. Grace's 1998 statement that its auditors had raised no objections to its accounting for the Medicare ______________ was true only in the _________ that Price Waterhouse issued clean financials, based on materiality considerations. As a spokeswoman for the auditing firm pointed out, such an opinion does not imply _________ with ___________ in the statements.
51. According to Michael Jensen, "Tell a manager that he will get a bonus when targets are realized and two things will happen":
    a. ____
    b. ____
52. All too often, companies wouldn't be able to accomplish the frauds without the assistance of ______________.
53. According to Jensen, almost every company uses a budget system that _________ employees for ________ and punishes them for _________ the _____. He proposes reforming the system by severing the link between _____________ and ___________.
54. Even in the case of the bluest of the blue chips, watching for rising levels of _______________ or ___________, relative to sales, should be standard operating procedure.
55. When the revenues derived from _________________ fail to materialize, the managers may resort to _____ to maintain the ________. The positive mental attitude that overstates revenues in the early stage is no _____________, however, than the _______ responsible at a later point.
56. Clues to the fraudulent accounting responsible for Gowex's downfall were detectable by astute ______________. In fact, it was a report alleging a(n) ________ overstatement of _________, published on July 1, 2014, by ________________ LLC, that precipitated the stock price collapse.

57. In a classic response, Garcia initially ________ the research report's ________, calling it "____________" and "__________."
58. In 2003, Garcia stated that the company cleared a large profit on turnover (revenue) of ________ million in 2002. According to Gowex's IPO offering circular in ___________, however, revenues totaled only _______ million in 2003.
59. Formerly, the company recognized revenue when the ___________ sold M/A-Com's products to end users. Under the newly instituted procedure, M/A-Com recognized revenue _____________ to distributors and established a(n) ________ against future ________.
60. Worryingly, M/A-Com's days sales outstanding (________) increased to ____ days in the fiscal second quarter ending April 3, 2015, from ___ days one year earlier. This kind of rise, coinciding with a shift to "_______," could be a sign of ________________, which is otherwise difficult to detect. Companies are not required to disclose the amount of their products ___________ distributor ___________.
61. Strong margins in a business in which ___________________ were losing money justified skepticism about the _________ of the profits Globo was reporting.
62. Long before October 2015, however, there were numerous clues that something was amiss. To begin with, in 2014's first quarter Globo ________________.
63. Further evidence that Globo's sales were inflated appeared in the form of its ________ days sales outstanding (____) of trade receivables. That was almost _______ the level reported by industry leader Good Technology.
64. As a result of its high ____ and low ___________, Globo required substantial _____________ of its _________. Its peers, on the other hand, generated sizable funds from ___________.

CHAPTER 7: EXPENSE RECOGNITION

1. Corporate managers are just as creative in __________ and ___________ the recognition of _________ as they are in maximizing and speeding up the _________ of revenues.
2. Investors attach little significance to _____________ profits and losses in valuing stocks. Therefore, a public company has a strong incentive to __________ cumulative ______ into a one-time event and to break up a(n) ________, nonrecurring _____ into smaller pieces and _______ it over ___________.

3. Nortel Networks illustrated the __________ power of _________, one of the most _________ features of financial reporting.
4. Between September 2000 and August ____, Nortel's market capitalization sank by ____ percent, devastating Canadian ___________ that were heavily invested in its shares.
5. The company had to wave a classic _______________ with respect to the __________ of its financial _________ by ________ the filing of its _____ financial reports.
6. In addition to dashing hopes that the _________ of accounting _______ would be _____, Nortel rattled the market by ______ CEO Dunn, CFO Beatty, and controller Gollogly.
7. Nortel's management's credibility continued to ______ as the company kept __________ back its ___________ for producing definitive earnings __________.
8. Nortel's investigation, which previously had focused on ________ and ___________, had turned to _____________.
9. Incorrect recognition of that amount resulted from a combination of:
   a. ____
   b. ____
   c. ____
   d. ____
10. Nortel followed a strategy of __________________ in its money-losing period of 2001–2002. Overstating ________ created "_____________" reserves that could be taken into ________ in __________.
11. Nortel's experience shows that if a company uses ___________ to _____________ profits, it will have no compunction about ____________ profits through ___________ revenue __________.
12. An important takeaway from the Nortel case is that seemingly ______ items can prove ________ significant.
13. ________ are another frequently abused element of ________ recognition. General Motors' fiddling with this device shows the important role of _____________ in the __________ of financial reporting.
14. At issue in GM's restatement was the recording of ________ and other _______ from ________.
15. GM said that some cash flows from its ______________ that should have been classified among its ___________ activities were instead booked as ___________ activities.

16. This revelation puzzled accounting experts because the applicable rules were unambiguous. __________ a loan or ________ repayment fell into investing ________; interest __________ were included in ____________ cash flow.
17. GM management said it had ___________ increased the _____ of vehicles it was leasing to car-rental companies, assuming they would be _____ more after those companies were through ______ them.
18. Ordinarily, a company's stock price ________ when its reported earnings __________ increase.
19. Freddie Mac steadfastly ______ that its handling of ________ was aimed at __________ its earnings.
20. Even if it was true that intentional ___________________ represented the __________ part of the earnings ________________, Freddie Mac's _________________ had a huge impact that even ___________ analysts could not detect from __________.
21. Freddie Mac's manipulation did not end there. Another ploy to _______ earnings consisted of ceasing to use ____________ for certain _________.
22. Companies can follow a variety of approaches in downplaying expenses such as:
    a. ____
    b. ____
    c. ____
    d. ____
23. On February 8, 2012, Diamond Foods announced that it would restate its earnings for the _______________. CEO Michael J. Mendes and CFO Steven M. Neill were placed on ______________ and ______ the following day. The company's planned earnings restatement involved ________ to walnut growers of $20 million in August ______ and $60 million in September _____ that were booked in the wrong periods.
24. Notably, Diamond Foods's earnings manipulation commenced after the passage of the _______________ Act that is appropriately credited with ___________________ the incidence of financial _______________ in the United States. Diamond did not even go public until ____________ after _____ became the law of the land in ____.
25. On November 15, _______, Bill Alpert presciently wrote in *Barron's Online,* "After Diamond's walnut accounting ____________, the stock could __________ again." In short, the stock plunge that was triggered by the ________________________ three months later was by no means _______________.

CHAPTER 8: THE APPLICATIONS AND LIMITATIONS OF EBITDA

1. The impetus for trying to redirect investors' focus to ________ income or other variants has been the minimal __________ recorded by many "new economy" companies.
2. Users of financial statements had discovered certain limitations in net income as a(n) ______________. They observed that two companies in the same industry could report similar ________, yet have substantially different _______________ values.
3. Net income is not, to the disappointment of analysts, a standard by which every company's _____ can be compared.
4. The accounting standards leave companies considerable discretion regarding the depreciable ______ they assign to their _______, _____, and _____________. The same applies to amortization schedules for __________ assets.
5. For some companies, the sum of net income, income taxes, and interest expense is not equivalent to EBIT, reflecting the presence of such factors as ______________ items and __________ interest below the ________ income ____.
6. Shifting investors' attention away from traditional fixed-charge coverage and toward __________ coverage of _______ was particularly beneficial during the 1980s, when some buyouts were so highly __________ that projected _____ would not cover pro forma interest expense even in a good year.
7. Capital spending is likely to exceed depreciation over time as the company ________ its productive ________ to accommodate ______ _______. Another reason that capital spending may run higher than depreciation is that newly acquired equipment may be ________ than the old equipment being written off, as a function of _________.
8. Delaying equipment purchases and repairs that are needed but not ________ should inflict no lasting damage on the company's __________ provided the profit ______ lasts for only a few quarters.
9. Depreciation is not available as a long-run source of cash for ________________________. This was a lesson applicable not only to extremely ________________ deals of the 1980s but also to the more __________ capitalized transactions of later years.
10. Beaver's definition of cash flow was more stringent than _______ since he did not add back either ______ or _______ to net income.

11. Beaver did not conclude that analysts should rely solely on the ____-____-to-________, but merely that it was the single best _________________.
12. Some investment managers consider that the single ratio of __________ (as they define it) to ____________ predicts bankruptcy better than all of the ____________' quantitative and qualitative considerations combined.
13. Aside from ____________ variations, the amount of working capital needed to run a business represents a fairly constant ________ of a company's sales. Therefore, if inventories or receivables ________ materially as a percentage of sales, analysts should strongly suspect that the earnings are ________, even though management will invariably offer a(n) ____________ explanation.
14. If a company resorts to stretching out its payables, two other ratios that will send out warning signals are:
    a. ____
    b. ____
15. Merrill Lynch investment strategist Richard Bernstein points out that __________ earnings tend to be more stable than ________ earnings, EBIT tends to be more stable than _________ earnings, and ________ tends to be more stable than EBIT.
16. Strategist Bernstein found that by attempting to filter out the ________ inherent in companies' earnings, investors reduced the _____________ of their stock selection.

CHAPTER 9: THE RELIABILITY OF DISCLOSURE AND AUDITS

1. Fear of the consequences of breaking the law keeps corporate managers in line. ________ the law is another matter, though, in the minds of many executives. If their bonuses depend on ______________ in an unfairly ________ light, they can usually see their way clear to adopting that course.
2. Technically, the __________________ appoints the auditing firm, but _______________ is the point of contact in hashing out the details of presenting financial events for _______________.
3. At some point, ______________ becomes a moral imperative, but in the real world, accounting firms must be _____________ to reach that point.

4. It is common for front-line auditors to balk at a(n) ________________ treatment proposed by a company's management, only to be overruled by their ____________.
5. _____ is an unambiguous violation of accounting standards, but audits do not _________ catch it.
6. Extremely clever scamsters may even succeed in undermining the auditors' efforts to select ________________, a procedure designed to foil concealment of fraud.
7. When challenged on inconsistencies in their numbers, companies sometimes _________ rather than any intention to _______ the users of ______________.
8. Seasoned followers of the corporate scene realize that companies are not always as ____________ as investors might _____________.
9. Abundant evidence has emerged over the years of corporate managers ____________ to paint as rosy a picture as possible.
10. To say that no ___________ can be _______, however, is quite different from saying that:
    a. _______________,
    b. ___________________, and
    c. ________________ are as good as real-world conditions permit.
11. Popular outrage over the post–_________ accounting scandals created political _________ to eliminate the _______________ conflict.
12. Systematic problems in the audit process arise not only from the ______________________ but also from the ____________________ of ______________ accounting firms.
13. In the 1990s, "____________" emerged as a means of keeping a lid on costs. Instead of focusing on ________ of __________ transactions, they identified the areas that in their ________ presented the greatest risk of error or fraud, such as _____________. Incredibly, these judgments in some cases were based on _____________.
14. In WorldCom's early days, Arthur Andersen audited the company in a meticulous, __________ way. As the company grew, however, Andersen migrated toward a(n) __________. If a question arose about controls or procedures, Andersen relied on the ______ provided by __________.
15. Congress's unwillingness to give the SEC the _______________ to do its job reflected more than __________ claims on the ___________.

16. One final line of defense for users of a company's financial statements is the ________________ of its board of directors. This protection has _________ infallible over the years.
17. In one of the few encouraging notes of recent years, the SEC has imposed a(n) "____________" requirement on audit committee members.
18. Many companies are either ______ with __________ or ________ about the way they ____________. Rather than laying down the law (or GAAP), the auditors typically wind up ____________ with management to arrive at a point where they can convince themselves that the _____________ requirements of __________ have been satisfied.
19. Given the observed gap between ___________ and ___________ in financial reporting, users of financial statements must provide themselves a(n) ________________ of protection through tough ___________ of the numbers.
20. Even if a company's management is inclined to _______, investors have a second line of defense in the form of ____________ annual _________ of the financials by __________ trained ___________. The Securities and Exchange Commission's (___) Corporation Finance and Enforcement divisions provide an additional line of defense.
21. At the extreme, executives may falsify their results. ______ is an unambiguous violation of accounting standards, but _____ do not invariably catch it.
22. Following the standard script in such situations, Wirecard ______ any __________, charging that the FT story was not only ____, _________, __________, and _________, but that it lacked any substance and was completely __________.
23. According to KPMG, ________________ from three third-party processors of payments for Wirecard customers made it impossible to __________ any ___________ transactions for 2016–2018. Consequently, KPMG was _______ to state one way or the other whether the _________ sales _______ existed or was ________.
24. Auditors are ___________ and ____ by the companies they audit. The corporate clients want audits completed swiftly and inexpensively, enabling them to release their results and move on. Failing to satisfy management's desire for quick, no-hassle audits ____________ business because the clients are also _________ for _______________ consulting and tax services.

25. Zatarra Research & Investigations found evidence of ____________ as far back as 2009. This scam consists of one company ______________ to another company, while concurrently agreeing to ______________ the same or similar assets. Scams associated with round-tripping include _________ the buyer/seller's ___________________, _________________, ____________, and _______________.
26. ARCP's 2014 experiences upholds the "_______________." The name derives from the popular belief that seeing one of these pests ________ many more are _________. This bit of market wisdom holds that when a company _________________ on the financial _______________, other, ________________ news is likely to follow.
27. Auditing firms are _______________ businesses that face _____________ between upholding professional standards, on the one hand, and ____________ clients and ______________, on the other.

CHAPTER 10: MERGERS-AND-ACQUISITIONS ACCOUNTING

1. The acquiring company's shareholders can benefit when an M&A deal ___________________, but they must be on guard against corporate managers' efforts to produce the ___________ of ____________ through financial reporting ___________.
2. In 2019, MarketWatch reported that the SEC had stepped up its efforts to discourage ______________________ adjustments for ___________ that was written off under GAAP. Some acquisitive companies were adding back this "__________" in calculating ____________________ numbers commonly used by analysts.
3. Under the old standard, the more ________ that was created in an acquisition, the greater was the _____________ to earnings from mandatory goodwill amortization. Now, companies could _____ earnings through acquisitions at rich prices with ____________.
4. Between the November 2, 2015, close of the ______ deal and the October 1, 2018, __________ of the former Alstom businesses and other _____ division _______, GE's stock plunged by __ percent while the S&P 500 climbed by __ percent. In short, the market imposed a large penalty on shareholders well before the company _________________ that the goodwill it recorded in the Alstom deal was ________.

5. On November 20, 2012, Hewlett-Packard announced that it would take a(n) $___ billion _________ on the UK software company Autonomy Corp. that it acquired on October 3, ____. HP's share price dropped by __ percent on the day of the announcement while the S&P 500 edged ___ percent higher.
6. Autonomy co-founder Mike Lynch denied the claims of ________ __________. He blamed the __________ on post-acquisition __________ by Hewlett-Packard. The stock market's ________________ of HP management lent some ________________. In the five years preceding the Autonomy write-down, HP's stock price declined by ___ percent.
7. More important for analysts than the _____________ for the $23 billion write-down are _____ that can be _____________.
8. Leaving aside issues of quality of ______________, which require study of corporate ___________ and _________, the lessons to derive from this case study fall into two categories—___________________ matters and ________ of ___________ targets.
9. Software companies ordinarily have very few __________ because they sell their products ________ and for _____. At the same time, they have obligations to ________ their ________ for a long period after they _____ it. Consequently, software companies' _______________ is typically a multiple of __________. Autonomy's balance sheet, on the other hand, showed _____ receivables.
10. The length of Autonomy's ______________________ "should ring alarm bells for investors." One implication of this ______________ from the _______________ was that the company was generating growth through ___________ rather than _______ growth.
11. HP was proposing to pay _____ times ________ while similar companies were trading at ______ times _______.
12. The financial reporting red flags spied by critics of Autonomy and of its acquisition by HP included Autonomy's ___________________ with ____ on the level of _________ and the length of the _________________. Similarly pointing to trouble were valuation metrics that were out of line with those of __________ companies.

CHAPTER 11: IS FRAUD DETECTABLE?

1. Beneish defines manipulation to include both actual _____ and the management of ________ or __________ within ____.

2. Beneish finds, by statistical analysis, that the presence of any of the following five factors increases the probability of earnings manipulation:
   a. ________________________________
   b. ________________________________
   c. ________________________________
   d. ________________________________
   e. ________________________________
3. The evidence of criminal misrepresentation often ___________ obvious after ___________, but not even the most ________________ definitively identified some of the most famous frauds until the __________ became ____________ and the companies ________.
4. In studying these notorious frauds, readers should pay close attention not only to the ____________ financial statement ________ but also to the _________ of senior _________ as the validity of their stated profits is challenged.
5. Unexpected _________ in _________________ is a classic warning sign of financial misrepresentation.
6. When Enron at long last conceded that it was overly indebted, management tried to:
   a. ________________________________
   b. ________________________________
   c. ________________________________
   d. ________________________________
7. Enron also misled investors by aggressively exploiting wiggle room in the accounting rules. The company booked revenue from its energy-related derivatives contracts on the basis of _______ value, rather than ___ value, as is the norm for other _________________.
8. Excessive liberties with ____________ accounting rules constituted yet one more element of Enron's misrepresentation.
9. On a conference call dealing with Enron's earnings, analyst Richard Grubman complained that the company was __________ in refusing to include a(n) ______________ in its earnings release.
10. Still, the _____________ vehicles, combined with ___________________, enabled Enron to make itself look less ________ than it really was.
11. Although Enron grossly misled investors by _____________, a large part of its deception consisted of ____________ of basic accounting standards, with the ______________ of its auditor.

12. Equally crude was a scheme in which Enron reportedly borrowed $500 million from a bank and bought ______________. A few days later it sold the ________________ and repaid the bank, reporting the proceeds from the meaningless transaction as _____________.
13. The ________ of Enron's ____________ assumptions was a major concern. "Ultimately they're telling you what ________ the ________ is, but they're not telling you how they got to __________," Business Valuation Services analyst Stephen Campbell complained. "That is essentially saying '__________.'"
14. Off Wall Street, a consulting group, recommended a short sale of Enron based on two factors identifiable from the financial statements, namely, the _________________ on non-traded assets and ______________ transactions with private __________.
15. Analysts should be especially wary when a strong likelihood of ______________________, as indicated by tools such as the ___________ model, coincides with ____________ financial reporting.
16. According to the SEC's complaint, HealthSouth's falsification began ______________ the company __________ in ____.
17. Flat denial by Scrushy, regardless of the ________ that ________, was a consistent theme as the _____________ story unfolded.
18. The complaint stated that when HealthSouth officials and accountants urged Scrushy to cease ______________, he replied, in effect, "not until _____________."
19. The "Sarbox" provision requiring CFOs and CEOs to attest to the accuracy of financial statements gave prosecutors a powerful weapon to wield against falsifiers, but ________________ dispelled any notion that the tough new law would end ______________ misreporting altogether.
20. HealthSouth exaggerated its earnings by understating the gap between the ____________ and the amount that the __________ would cover.
21. If the auditors did question an accounting entry, HealthSouth executives reportedly ____________________________ to validate the item.
22. HealthSouth also propped up profits by failing to ___________________ with ____________________________. In addition, the company did not ___________________ when it sold assets that had ________ in value.

23. Compounding Scushy's legal problems, federal prosecutors disclosed in July 2003 that they had uncovered evidence of:
    a. ____
    b. ____
    c. ____
    d. ____
    e. ____
24. The most dismaying aspect of the performance of HealthSouth's auditor, EY LLP, was its _________ to challenge a ________, large ________ in cash.
25. In the view of experts in the field, internal checks and balances also broke down at HealthSouth. The board's audit committee met only ____ during 2001, _______________ than the minimum recommended by the SEC.
26. Investors had little official warning of trouble until the ________ before Parmalat's collapse. As late as October 2003, Deutsche Bank's equity research group rated the company's stock a(n) _____, highlighting its strong _____________________, and Citibank put out a(n) __________ report in November. Furthermore, the company's debt carried a(n) ___________ grade rating up until ___________ before the bankruptcy filing.
27. A major red flag was Parmalat's _________________, despite claiming to have a huge _________.
28. Merrill Lynch analysts downgraded Parmalat to SELL, saying that the company's _____________________ to the ____________, while reporting ______________, threw into question its ________________________.
29. Another hazard signal emerged on February 26, 2003, when Parmalat suddenly canceled its plan to sell ________ bonds. The company said it would instead issue bonds with maturities of just ___________, suggesting the market had less confidence in Parmalat's ______________ than management had thought.
30. Oddly, the person who achieved the greatest renown for early recognition of the Parmalat's house of cards was not a(n) ______________, but a(n) ________.
31. Public market investors probably should have been _________ that some of Luckin's ______________ cashed out their holdings _________.

32. Luckin's share price did not collapse completely without warning. On January 31, 2020, Muddy Waters announced that it ____________ Luckin after receiving a(n) ________ 89-page report alleging ____________________ and a broken ___________ at Luckin. The shares promptly dropped by ____ percent.
33. On cue, Luckin _______________ the allegations against it, labeling the report's methodology ________, its evidence ________________, and its interpretation of events _________.
34. Scrutiny of financial statements _________ a role in the report's claim that management ________ its 3Q 2019 ___________ expenses by more than 150 percent. According to the author(s), the discrepancy was uncovered by comparing the ______________ expenditures with media revenues tracked by a(n) _________. The report speculated that Luckin _________ its ___________ outlays in order to recycle the amounts into _____________ of ________ and _____________.
35. Luckin escalated its __________ of revenues following the IPO by selling __________________ for tens of millions of cups of coffee to companies linked to _________ and __________ shareholder Charles Lu.
36. Two lessons emerge from this incident. One is that nearly two decades after Sarbanes-Oxley reduced (_________________) outright fraud in financial reporting by _____________, securities of certain other countries continued to pose ________________ to users of financial statements. The second takeaway is that in some instances, even a _______________________ of the issuer's financial statements will not bring the _______________ to light. In such cases, exposing the _____________________ depends on some combination of ________________, access to ______________________, and large-scale _________________.

CHAPTER 12: FORECASTING FINANCIAL STATEMENTS

1. It is future _________ and _________ that determine the value of a company's stock and the relative likelihood of future _________ payments of __________ that determines credit quality.
2. The process of financial projections is an extension of _________ patterns and __________, based on assumptions about future __________________, market ________, and managerial _______.

3. Sales projections for the company's business can be developed with the help of such sources as trade __________, trade __________, and firms that sell econometric __________ models.
4. Basic industries such as __________, _____, and ____________ tend to lend themselves best to the ___________________ approach described here. In technology-driven industries and "hits-driven" businesses such as ______________ and ____, the connection between _____ and the general _____________ trend will tend to be looser.
5. The expected intensity of industry competition, which affects a company's ________ to pass _______________ on to customers or to retain ____________, influences the _____________ forecast.
6. Since the segment information may show only operating income, and not _____________, the analyst must add ___________ depreciation to operating income, then make assumptions about the allocation of ________, ________, and ____________ expense and _________ and ____________ expense by segment.
7. The R&D percentage may change if, for example, the company makes a(n) ______________________ in an industry that is either significantly more, or significantly less, ______________ than its existing operations.
8. The key to the forecasting interest expense method employed here is to estimate the firm's embedded cost of debt, that is, the ________________ interest rate on the company's existing __________.
9. Accurately projecting interest expense for __________________ companies is important because their _______________ may depend on the size of the interest ______ "___" they must cover each quarter.
10. The completed income statement projection supplies the __________ lines of the projected statement of cash flows.
11. Before assuming a constant-percentage relationship, the analyst must verify that the ___________ year's ratios are ____________ of experience over ____________.
12. A sizable ____________ might be presumed to be directed toward share repurchase, reducing ________________, if management has indicated a desire to _________ and is ___________ to do so by its board of directors.
13. Typically, the analyst must modify the underlying ________ assumptions, and therefore the projections, several times during the year as _______________ diverges from ___________.
14. A firm may have considerable room to cut its ______________ in the short run if it suffers a decline in funds provided by __________. A projection that ignored this ______________ could prove overly pessimistic.

15. An interest rate decline will have limited impact on a company for which interest costs represent a(n) _______________ of expenses. The impact will be greater on a company with a large interest cost component and with much of its debt at ___________. This assumes the return on the company's assets is ______________________.
16. Analysts are generally not arrogant enough to try to forecast the figures accurately to the first decimal place, that is, to the _____________ for a company with revenues in the ______________.
17. It is generally inappropriate to compare a(n) ___________ income statement item (EBITDA) with a balance sheet figure, especially in the case of a(n) ______________ company.
18. It is unwise to base an investment decision on historical statements that antedate a major financial change such as:
    a. ____
    b. ____
    c. ____
    d. ____
19. A pro forma income statement for a single year provides no information about the ___________ growth in sales and earnings of the _________ that is being spun off.
20. Pro forma adjustments for a divestment do not capture the potential benefits of increased ___________________________ on the company's _________________.
21. The earnings shown in a merger-related pro forma income statement may be higher than the company can sustain because:
    a. The acquired company's owners may be shrewdly selling out at dollar, anticipating a(n) _________ in ______ growth that is foreseeable by ____________, but not to the acquiring corporation's management.
    b. Mergers of companies in the same industry often work out poorly due to _______ of ____________.
    c. Inappropriately applying its _____________ to an industry with very different requirements.
22. A(n) ____________ investor buying a 30-year bond is certainly interested in the issuer's financial prospects beyond a(n) _________ horizon. Similarly, a substantial percentage of the present value of future dividends represented by a stock's price lies in __________ beyond the __________.
23. Radical financial restructurings such as ___________, ___________ massive stock, and _________ necessitate _________ projections.

24. Of the various types of analysis of financial statements, projecting ____________ and _______ requires the greatest skill and produces the most ______________.
25. The lack of ______________ _____________ is what makes financial forecasting so ____________. When betting huge sums in the face of __________________, it is essential that investors understand the ______ as fully as they possibly can.

CHAPTER 13: CREDIT ANALYSIS

1. Financial statements tell much about a borrower's _______ to repay a loan, but disclose little about the equally important __________ to repay.
2. If a company depends on raw materials provided by a subsidiary, there may be a(n) __________ presumption that it will stand behind the subsidiary's ____, even in the _________ of a(n) _______________.
3. Illiquidity manifests itself as an excess of current _______________, over __________________. The ________ ratio gauges the risk of this occurring by comparing the claims against the company that will become payable during the current _______________ (_______________) with the assets that are already in the form of cash or that will be converted to cash during the current _______________ (_____________).
4. The greater the amount by which asset values could deteriorate, the greater the "_________________," and the greater the creditor's sense of __________________. Equity is by definition _____________ minus _______________.
5. Aggressive ____________ frequently try to satisfy the letter of a(n) ____________ leverage limit imposed by lenders, without fulfilling the _____________ spirit behind it.
6. A firm that "zeros out" its ____________ at some point in each operating cycle can legitimately argue that its "true" leverage is represented by the permanent (___________) _____ on its balance sheet.
7. Current maturities of long-term debt should enter into the calculation of ___________, based on a conservative assumption that the company will replace maturing debt with new __________ borrowings.
8. Exposure to interest rate fluctuations can also arise from long-term ______________________. Companies can limit this risk by using __________________.

9. Public financial statements typically provide ____________ information about the extent to which the issuer has __________ its exposure to interest rate fluctuations through __________.
10. Analysts should remember that the ultimate objective is not to ______________ but to _______________.
11. In general, the credit analyst must recognize the heightened level of risk implied by the presence of preferred stock in the _____________. One formal way to take this risk into account is to calculate the ratio of _________ obligations to ____________.
12. In addition to including capital leases in the total debt calculation, analysts should also take into account the __________________ liabilities represented by contractual payments on _________________, which are reported as _____________ in the ______ to Financial Statements.
13. A corporation can employ leverage yet avoid showing debt on its consolidated balance sheet by entering ______________ or forming _______________ subsidiaries.
14. Under SFAS ______, balance sheet recognition is now given to pension liabilities related to employees' service to date. Similarly, SFAS ______ requires recognition of postretirement healthcare benefits as an on-balance sheet liability.
15. The precise formula for _____________ a ratio is less important than the assurance that it is _______________________ for all companies being evaluated.
16. In general, credit analysts should assume that the achievement of ___________ bond ratings is a(n) ______________ goal of corporate management.
17. The contemporary view is that profits are ultimately what sustain __________ and _____________. High profits keep plenty of cash flowing through the system and confirm the value of productive assets such as _____ and ___________.
18. The cumulative effect of a change in accounting procedures will appear "_____________," or after _____________ have already been deducted. The sum of net income and provision for income taxes will then differ from the ________________ that appears in the income statement.
19. Operating margin shows how well management has run the business __________ and _________ wisely, controlling ___________ and __________________ before taking into account financial policies, which largely determine ______________, and the ________, which is outside management's control.

20. Fixed-charge coverage is a(n) _______________ ratio of major interest to credit analysts. It measures the ability of a company's _________ to meet the ________________ on its debt, the lender's most direct concern. In its simplest form, the fixed-charge coverage ratio indicates the ___________ by which _________________ suffice to pay _________________.
21. Regardless of whether it is _________ or ____________, all interest accrued must be covered by ___________ and should therefore appear in the ______________ of the fixed-charge coverage calculation.
22. The two complications that arise in connection with incorporating operating lease payments into the fixed-charge coverage calculation are:
    a. ____
    b. ____
23. Companies sometimes argue that the denominator of the fixed-charge coverage ratio should include only ______________ expense, that is, the difference between _______________ and income derived from _________________, generally consisting of marketable securities.
24. Ratios related to sources and uses of funds measure credit quality at the most elemental level—a company's ability to ______________________ to ___ its ______.
25. Given corporations' general reluctance to sell new equity, a recurrent cash shortfall is likely to be made up with _______ financing, leading to a rise in the __________-to-__________ ratio.
26. A company that suffers a prolonged downtrend in its ratio of ________ to _______________ is likely to get more deeply into debt, and therefore become _______________ with each succeeding year.
27. Unlike earnings, ___________ is essentially a programmed item, a cash flow ensured by the accounting rules. The higher the percentage of cash flow derived from _____________, the higher is the _____________ of a company's cash flow, and the _______________ its financial flexibility on the vagaries of the marketplace.
28. Analysts cannot necessarily assume that all is well simply because capital expenditures consistently exceed depreciation. Among the issues to consider are:
    a. ____
    b. ____
    c. ____
    d. ____

29. A limitation of combination ratios that incorporate balance-sheet figures is that they have little meaning if __________ for _________ of years.
30. The underlying notion of a turnover ratio is that a company requires a certain level of _____________ and _____________ to support a given volume of sales.
31. A(n) _______________ is a possible explanation of declining inventory turnover. In this case, the inventory may not have suffered a severe reduction in value, but there are nevertheless unfavorable implications for ______________. Until the inventory glut can be worked off by ___________________________ to match the lower _____________, the company may have to borrow to finance its unusually high working capital, thereby increasing its _______________.
32. Fixed-charge coverage, too, has a weakness, for it is based on _______, which are subject to considerable manipulation.
33. Built from two comparatively hard numbers, the ratio of ___________ to ___________ provides one of the best single measures of ____________.
34. Expected _____________ have an important bearing on the decision to _________ or ______ credit, as well as on the _________ of debt securities.
35. Line of business is another basis for defining a(n) ____________.
36. Beyond a certain point, calculating and comparing companies on the basis of ___________ financial ratios contributes little _______________.
37. __________ or ____________ financial ratios can have different implications for different companies.
38. Quantitative models such as Zeta, as well as others that have been devised using various mathematical techniques, have several distinct benefits, such as:
    a. ____
    b. ____
    c. ____
39. Similar to the quantitative models consisting of ____________, the default risk models based on stock prices provide useful, but _________, signals.

CHAPTER 14: EQUITY ANALYSIS

1. In this chapter, the discussion focuses primarily on the use of financial statements in ____________ analysis.

2. Of the methods of fundamental common stock analysis, no other approach matches the intuitive appeal of regarding the stock price as the _______________ of expected ________ dividends. This approach is analogous to the _______________ calculation for a bond and therefore facilitates the comparison of different __________ of a single _______.
3. By thinking through the logic of the ___________ method, the analyst will find that value always comes back to __________.
4. The company's earnings growth rate may diverge from its sales growth due to changes in its _____________.
5. As a rule, a(n) ___________ company will not increase its dividend on a regular, annual basis.
6. Many analysts argue that _________, rather than ________, is the true determinant of dividend-paying capability.
7. Cash generated from ___________, which is generally more difficult for companies to manipulate than _________, can legitimately be viewed as the preferred measure of future _____________ capability.
8. The ability to vary the _______________, and therefore to assign a(n) _______ or _______ multiple to a company's earnings, is the equity analyst's defense against earnings ___________ by management.
9. It is appropriate to assign a(n) _______________ discount factor to the earnings of a company that competes against larger, better-capitalized firms. A small company may also suffer the ____________ of ______ of depth in management and concentration of its ___________ in _____ or ________.
10. A building-materials manufacturer may claim to be cushioned against fluctuations in housing starts because of a strong emphasis in its product line on the __________ and _______ markets.
11. Analysts should be especially wary of companies that have tended to jump on the bandwagon of "________" associated with the __________ of the moment.
12. Earnings per share will not grow merely because __________.
13. Leverage reaches a limit, since lenders will not continue advancing funds beyond a certain point as ________________.
14. One way to increase earnings per share is to _________ the ________ of ___________ outstanding.
15. To the extent that the company funds share buybacks with idle cash, the increase in _______________ is offset by a reduction arising from _________ income on __________.

16. Similar to most ratio analysis, the DuPont Formula is valuable not only for the _______ it ________ but also for the ___ ones it ______.
17. Besides introducing greater volatility into the ____________, adding debt to the balance sheet demonstrates no ___________ skill in ____________ operations.
18. Some companies have the potential to raise their share prices by _____________ their assets ______________________, while others can increase their value by ___________ their __________________.
19. Management's main adversaries in battles over "______________" were aggressive _______________.
20. At least in the early stages, before some raiders became overly aggressive in their financial forecast assumptions, it was feasible to extract value without creating undue bankruptcy risk, simply by ___________ the ratio of ____ to _________.
21. In future bear markets, when stocks again sell at depressed price-earnings multiples, investors will probably renew their focus on companies' ________ as _______________.
22. A leveraged buyout can bring about improved profitability for either of two reasons:
    a. ____
    b. ____
23. Today's ______________ may be a precursor of tomorrow's bankruptcy by a company that has economized its way to a(n) ____________ state.
24. A focus on ________________ multiples, the best-known form of fundamental analysis, is not the investor's _______________ to relying on technicians' stock charts.
25. For the investor who takes a longer view, __________________ provides an invaluable reference point for valuation.