## 5.06 Analysis of Inventories

**Question 1**
An automotive parts company manufactures specialty engine pistons and presents its financial statements using US GAAP. Due to manufacturing improvements, it estimates that its inventory is worth less than its carrying value. The relevant per-unit information for 20X8 is shown below:

| *(US $)* | |
|---|---|
| Original cost | 105 |
| Selling price | 150 |
| Replacement cost | 90 |
| Net realizable value | 100 |
| Normal profit margin | 7 |

If this company uses LIFO, the per-unit cost for its 20X8 ending inventory is *closest* to:
A. $90
B. $93
C. $100

**Question 2**
In a period of increasing inventory costs, a company using FIFO instead of LIFO will *most likely* experience a lower:
A. current ratio.
B. gross profit margin.
C. inventory turnover ratio.

**Question 3**
An analyst gathers the following data on two companies:

**Selected financial information**

| In EUR (*millions*) | Company A | Company B |
|---|---|---|
| Inventory valuation method | LIFO | FIFO |
| Revenue (20X9) | 1,300 | 2,200 |
| COGS (20X9) | 800 | 1,500 |
| Gross profit (20X9) | 500 | 700 |
| Inventory (20X9) | 145 | 280 |
| Inventory (20X8) | 115 | 265 |
| LIFO reserve (20X9) | 20 | |
| LIFO reserve (20X8) | 35 | |

Neither company has reported inventory shortages or write-downs. After the appropriate adjustments are made to compare the companies' financial data, Company A's inventory turnover is *most likely*:
A. less than Company B's.
B. the same as Company B's.
C. greater than Company B's.

**Question 4**
A clothing retailer reporting under IFRS purchased merchandise for £500,000 at the beginning of the year. Normally, the retailer could sell this inventory for £700,000, but now the estimated selling price is £510,000. The cost of selling the inventory is £15,000. Based on this information,
the retailer's reported carrying value of inventory (in £ thousands) is *closest* to:
A. 485
B. 495
C. 500

**Question 5**
.A company reporting under US GAAP and using FIFO assesses its inventory's net realizable value as being €200,000 less than its carrying value. The company records a write-down and increases COGS by €200,000. In the subsequent period, a new assessment of the inventory's net realizable value is €250,000 higher than its revised carrying value. The company's *most appropriate* action is to reduce COGS by:

A. €0
B. €200,000
C. €250,000

**Question 6**
A company that reports under US GAAP decides to change its inventory accounting from FIFO to LIFO. The change on its financial statements is *most appropriately* disclosed:
A. retroactively, including a restatement of prior years' financial statements.
B. retroactively, without restating prior financial statements but disclosing the impact of the change to prior years' statements in footnotes.
C. prospectively, without restating prior financial statements but disclosing the impact of the change to prior years' statements in footnotes.

**Question 7**
A manager collects information on a company's inventory for a period:

| Per-Unit Inventory | USD |
|---|---|
| Original cost | 105 |
| Selling price | 140 |
| Selling cost | 10 |
| Completion cost | 30 |
| Replacement cost | 96 |
| Normal profit margin | 7 |

The company uses LIFO to calculate COGS. Based on only this information, under US GAAP, the per-unit value (in USD) for the existing inventory is *closest* to:
A. 96
B. 100
C. 105

**Question 8**
In 20X7, a company wrote down its inventory from £30 million to £28.7 million. In 20X8, a global shortage of this product results in the inventory having a net realizable value of £35 million. Under IFRS, the company's revaluation of inventory to reflect its increased value is *closest* to:
A. £0
B. £1.3 million
C. £6.3 million

**Question 9**
When inventory costs are declining, a company using FIFO will *most likely* experience:
A. a lower current ratio.
B. a higher gross profit margin.
C. an increase in working capital.

**Question 10**
An engineering company manufactures high-end automotive accessories. It reports under US GAAP and uses LIFO. The company is replacing its inventory for the coming year and has determined that its existing inventory has become obsolete. An analyst gathers the following Information:

| Per-Unit Inventory | USD |
|---|---|
| Original cost | 105 |
| Selling price | 150 |
| Replacement cost | 96 |
| Net realizable value | 100 |
| Normal profit margin | 7 |

The per-unit value that the company reports for the existing inventory is *closest* to:
A. $96
B. $100
C. $110

**Question 11**
A company that reports under IFRS is valuing its year-end inventory. It has collected the following information (in CHF millions):

| | |
|---|---|
| Historic cost | 175 |
| Replacement cost | 165 |
| Selling price | 240 |
| Cost to sell inventory | 60 |

Based on this data, the inventory value (in CHF millions) reported on its balance sheet is *closest* to:
A. 165
B. 175
C. 180

**Question 12**
Which of the following types of ratio will *most likely* be positively affected by an inventory write-down?
A. Activity
B. Liquidity
C. Profitability

**Question 13**
A manufacturing company that uses LIFO under US GAAP shows the following inventory-related information at the end of 20X8:

| Selected Data ($ *millions*) | |
|---|---|
| Cost of ending inventory | 100 |
| Selling price | 110 |
| Completing cost | 15 |
| Nomal profit margin | 20 |
| Replacement cost | 70 |

Based on this data, the inventory amount reported on the balance sheet (in $ millions) is *closest* to:
A. 70
B. 75
C. 95

**Question 14**
Unlike companies that comply with US GAAP, a company reporting under IFRS can disclose in its financial statements the amount of:
A. LIFO reserves.
B. an inventory write-down.
C. a reversal of an inventory write-down.

**Question 15**
A company reporting under US GAAP has both increasing inventory levels and increasing inventory unit costs. Which inventory valuation method *most likely* results in the lowest days of inventory on hand?
A. LIFO
B. FIFO
C. Weighted average cost