5.12 Introduction to Financial Statement Modeling

Question 1
A credit card provider conducts a consumer preference survey, which reveals that "Clients are likely to replace their credit cards with digital wallets or cryptocurrencies, which are more versatile and affordable." Based only on this survey result, which of Porter's five forces is *most likely* to weaken the company's pricing power?
A. Threat of substitutes
B. Threat of new entrants
C. Bargaining power of customers

Question 2
Three manufacturers dominate the canned fruit market and buy fruits from a fragmented market of many farmers. However, a large agricultural distributor enters the fruit market, sourcing the fruits from the farmers, which forces the manufacturers to buy directly from the distributor. Based only on this information and on Porter's framework, which of the following forces is *most likely* weakening the manufacturers' competitive position?
A. Threat of new entrants
B. Rivalry among incumbents
C. Bargaining power of suppliers

Question 3
At the beginning of the fiscal year, a CEO provides optimistic annual EPS guidance, citing strong government-sector demand. Throughout the year, unforeseen tariffs significantly increase raw material costs. The CEO declines to revise forecasts, stating that the company's solid fundamentals should be able to offset gross margin compression. Based only on this information, which of the following biases does the CEO *least likely* exhibit?
A. Conservatism bias
B. Illusion of control bias
C. Representativeness bias

Question 4
A surge in the price of cotton and labor costs is increasing input costs in the apparel industry. While most competitors decide to adjust their prices by the full increase in costs, one company decides to pass on only a portion of that increase. As a result, the company would *most likely* incur a decrease to its:
A. revenues.
B. sales volume.
C. gross margin percentage.

Question 5
Country A is currently in an inflationary environment. A multinational corporation that sources most of its inputs from Country A increases its global prices based on the change in Country A's general consumer price index (CPI). All else equal, this strategy will *most likely* reduce:

A. revenues if demand is highly price inelastic.
B. market share if competitors in other countries raise prices by a higher rate.
C. gross margin percentage if input costs increase more than Country A's CPI.

Question 6
A buy-side analyst of a large-cap mutual fund is evaluating an apparel company's stock as a possible addition to the fund. The analyst decides to create a valuation model with a five-year forecast horizon. Which of the following factors would *best justify* the analyst's decision?
A. The horizon is greater than the industry's business cycle.
B. The average annual portfolio turnover of the large-cap fund is 20%.
C. The apparel company expects to make a major acquisition in the next five years.

Question 7
A financial controller believes that the firm will have poor cash flow performance next year and asks an analyst to forecast free cash flows.
While reviewing the analyst's underlying assumptions, the controller focuses on unfavorable factors such as large replacement capital expenditure requirements while ignoring favorable factors such as high sales growth and improved working capital management.
This financial controller's behavior when reviewing the analyst's forecast is *most accurately* described as:
A. confirmation bias.
B. overconfidence bias.
C. representativeness bias.

Question 8
A global clothing company reports the following 20X1 financial results for one of its business units:

in € millions	20X1
Revenue	100.00
COGS	30.00
Gross profit	70.00
SG&A	50.00
EBIT	20.00

A forecast of 20X3 operating profits (EBIT) for this business unit assumes that:
- Volume will contribute 7% to annual sales growth each year.
- Price/mix will contribute 3% to annual sales growth each year.
- Net foreign currency fluctuation is expected to reduce annual sales growth by 1% each year.
- COGS is expected to be 30% of revenue each year.
- SG&A is expected to be 50% of revenue each year.

- Sales growth is calculated geometrically.

Using these assumptions, the 20X3 EBIT forecast (in € millions) for the business unit is *closest* to:
A. 21.82
B. 23.76
C. 23.81

Question 9
A company has annual revenues of $1.5 billion. An analyst forecasting next year's revenues expects volume growth of 6%, a positive forex impact of $90 million, and a positive impact of $111 million from an acquisition. If the analyst expects total revenue growth of 30%, organic growth is *closest* to:
A. 10.0%
B. 16.6%
C. 22.6%

Question 10
Due to a deflationary environment, a company is benefitting from a reduction in the cost of its main inputs. Since the company is in a competitive industry, which of the following strategies would *most likely* increase sales volume in the short run?
A. Keeping prices unchanged
B. Reducing prices by a smaller percentage than industry rivals
C. Passing cost variation to customers faster than its competitors

Question 11
A company had revenues of €500 million and a gross profit margin of 40% in Year 1. An analyst forecasting revenues for Year 2 estimates an increase of 7% in the average price and sales volume growth of 10%. The analyst also assumes that the company will experience a 2% inflation rate on COGS. The forecasted gross profit (€ million) in Year 2 is *closest* to:
A. 249.0
B. 251.9
C. 282.5

Question 12
A supervisor revises the forecasts of her team of analysts. She notices that one of the analysts builds excessively complex financial models, relying on numerous specific assumptions, and seeks the opinions of an uncommonly large number of experts. The analyst *most likely* displays which of the following behavioral biases?
A. Confirmation
B. Illusion of control
C. Representativeness