



ANVCA ANNUAL MEETING
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Hilton Anchorage Hotel

THE BASICS: READING AND UNDERSTANDING FINANCIAL STATEMENTS

OVERVIEW

Financial Statements Consist of:

1. Balance Sheet
2. Income Statement (Also called P&L for profit and loss)
3. Statement of Cash Flow
4. Statement of Shareholders' Equity and Comprehensive Income

OVERVIEW – cont.

In order to get a feel of the financial well-being of a company, you need to review **ALL** components:

- Balance Sheet
- Income Statement
- Statement of Cash Flow
- Statements of Shareholders' Equity

Balance Sheet

It shows the assets, liabilities, and equity (or net worth) of the company at a particular point in time.

The basic formula is: $\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}$

Balance Sheet Key Items

- Cash
- Accounts Receivables
- Investments
- Debt
- Shareholders' Equity

CONSOLIDATED BALANCE SHEETS
(dollars in millions except share amounts)

	30-Jan-10	31-Jan-09
ASSETS		
Current assets:		
Cash and cash equivalents	37.0	53.6
Merchandise inventories	873.8	915.2
Accounts receivable and other current assets	76.5	102.4
Deferred income taxes	1.0	
Total current assets	988.3	1,071.2
Property and equipment net	392.8	494.2
Other assets	39.9	39.4
Deferred income taxes	3.9	4.0
Goodwill	0.3	0.2
total assets	1,425.2	1,609.0
Liabilities and Stockholders' Equity		
Current liabilities:		
Short-term borrowings and current portion of long-term debt	275.4	329.8
Trade accounts payable	350.8	350.0
Accrued payroll and other liabilities	257.4	279.8
Taxes, including income taxes	44.1	30.1
Deferred income taxes		4.0
Total current liabilities	927.7	993.7
Long-term debt	6.6	6.4
Other long-term liabilities	332.6	354.8
Contingencies (Note8)		
total liabilities	1,266.9	1,354.9
Stockholders equity		
Common stock 300,000,000 share authorized: 59,869,384 and 59,903,232 shares issued and outstanding at January 30, 2010 and January 31, 2009, respectively	187.2	187.4
Accumulated other comprehensive income	16.7	11.9
Retained earnings (deficit)	(45.6)	63.8
Total stockholders' equity	158.3	263.1
Total liabilities and stockholders' equity	1,425.2	1,618.0

**The basic formula of the balance sheet is:
Assets = Liabilities + Shareholder's Equity**

Income Statement

It shows the company's revenue, expenses, and net income (i.e., the bottom line). The income statement is also commonly referred to as the P&L (profit and loss).

Income Statement Key Items

- Sources of revenues
- Sources of expenses
- Earnings from joint ventures
- Gains/Losses from sale of business interests or assets
- Income before taxes
- Net Income

Profitability

- The Income Statement tells you if a company had a profit (net income) or a loss (net loss).
- Profitability Ratio:
 - $\text{Net Income} / \text{Total Revenue}$
- Compare the profit ratio to peers

CONSOLIDATED STATEMENTS OF OPERATIONS

(dollars in millions except per share data)

	30-Jan-10	31-Jan-09	2-Feb-08
Sales	2,791.1	3,242.1	3,555.1
Other Revenue	32.8	33.3	42.3
Total Revenue	2,823.9	3,275.4	3,597.4
Cost of Merchandise sold (includes cost of goods sold)	2,191.3	2,484.8	2,668.3
Gross Margin	632.6	790.6	929.1
Selling general and administrative expenses	711.3	842.4	912.0
Goodwill Impairment		40.3	
Asset impairments and other writedowns	16.2	57.1	13.0
Operating income (loss)	(94.9)	(149.2)	4.1
Interest expense	24.1	45.4	43.1
Warrant/put expense (income)	20.7	(40.1)	
Total interest expense	44.8	5.3	43.1
Loss before income tax	(139.7)	(154.5)	(39.0)
Income tax provision (benefit)	(29.5)	30.2	(19.1)
Loss from continuing operations	(110.2)	(184.7)	(19.9)
Loss from operations of discontinued operations		(1.7)	(8.7)
Gain (loss) from disposal of discontinued operations	0.8	(0.3)	(128.8)
Gain (loss) from discontinued operations (net of tax)	0.8	(2.0)	(137.5)
Net loss	(109.4)	(186.7)	(157.4)
Loss per common share data (note 2)			
Basic:			
Loss from continuing operations per common share	(1.83)	(3.07)	(0.34)
Gain (loss) from discontinued operations per common share	0.01	(0.03)	(2.34)
Net loss per common share	(1.82)	(3.10)	(2.68)
Weighted-average common shares outstanding (in Millions)	60.1	60.2	58.7

Look
for
trends

The
bottom
line

Statements of Cash Flow

A company may have an impressive amount of assets and equity on the balance sheet, an impressive amount of revenue and net income on the income statement, but the cash flow statement tells you about your cash situation.

Cash is King

Profitability on the income statement is great, but how much was actually received and put to use.

Statements of Cash Flow Key Items

- Cash provided by operations
- Cash used in investing activities
- Cash used in financing activities
- Increase or Decrease in Cash

Cash Flow Statement Process

- Start with Net Income from the Income Statement
- Make adjustment for non-cash items, which gives you cash from operations
- Reflect investing activities (buying/selling securities, capital purchases, buying/selling business interests)
- Reflect financing activities (dividends paid, borrowing money, paying down debt)

Non-Cash Items

- Depreciation and amortization
- Unrealized gains/losses for investment trading accounts
- Revenues recorded, but have not yet been collected (Accounts Receivables)
- Expenses recorded, but have not yet been paid (Accounts Payable and Accrued Expenses)

CONSOLIDATED STATEMENTS OF CASH FLOWS

Cash flow calculates the cash position by starting with net income

Jan 30 2010 Jan 31 2009 Feb 2 2008

Cash provided by (used for)			
Net loss	(109.4)	(186.7)	(157.4)
Net income (loss) from discontinued operations	0.8	(2.0)	(137.5)
Loss from continuing operations	(110.2)	(184.7)	(19.9)
Operations			
Adjustments to reconcile loss from operations to operating cash flow			
Depreciation	98.8		
Loss on disposal of assets	3.8		
Stock-based compensation cost (income)	(0.3)		
Increase in warrant liability	8.8		
(Increase) decrease in deferred income taxes	(4.8)		
Decrease in other long-term assets	0.2		
(Decrease) increase in other long-term liabilities	(22.5)		
Goodwill impairment			
Write-off intangible asset	16.2		
Asset impairments and other writedowns	16.2		
Cash provided by (used for) current assets and current liabilities			
Decrease in inventories	43.9		
Decrease in accounts receivable	10.4		
Decrease (increase) in prepaid expenses	3.9		
Increase (decrease) in accounts payable	0.2		
Increase (decrease) in taxes payable	13.4		
Increase (decrease) in accrued payroll and other liabilities	(21.9)		
Net cash provided by operating activities of continuing operations	56.1		
Investing			
Capital expenditures	(17.9)		
Investment in Paperchase			
Proceeds from the sale of discontinued operation			
Net cash provided by (used for) investing activities	(17.9)		
Financing			
Proceeds from the excess tax benefit of options exercised			
Net funding from (repayment of) credit facility	(54.5)		
Funding from short-term note financing		42.5	
Issuance of long-term debt		1.2	0.4
Repayment of long-term debt	(0.3)	(1.4)	
Repayment of long-term capital lease obligations	(1.2)	(0.4)	(0.4)
Issuance of common stock	0.1	(0.4)	3.1
Repurchase of common stock		(0.2)	(0.6)
Payment of cash dividends		(6.5)	(19.4)
Net cash provided by (used for) financing activities	(55.9)	(226.4)	27.4
Effect of exchange rates on cash and cash equivalents	0.3	(0.9)	0.8
Net cash provided by (used for) provided by operations	0.8	(21.3)	(0.7)
Net cash used for investing activities of discontinued operations		(6.5)	(17.8)
Net cash used for by financing activities of discontinued operations			(41.9)
Effect of exchange rates on cash and cash equivalents of discontinued operations		2.8	(0.2)
Net cash provided by (used for) discontinued operations	0.8	(25.0)	(60.6)
Net decrease in cash and cash equivalents	(16.6)	(4.9)	(39.1)
Cash and cash equivalents at beginnings of year	53.6	58.5	97.6
Cash and cash equivalents at end of year	37.0	53.6	58.5
Supplemental cash flow disclosures			
Interest paid	16.6	36.3	43.8
Net income taxes (received) paid	(42.5)	(34.6)	12.4

and then making adjustments for:

- (1) non-cash items
- (2) investing activities that reflect the purchases and sales of investments (marketable securities and other assets)
- (3) financing activities

Paid dividends are not reflected in the income statement or balance sheet

The cash flow statement will then show a net increase or decrease in cash.

Statements of Shareholder Equity

It shows a detailed view of the equity in a company. Equity increases from profitable operations. It decreases from losses from operations and dividends declared/paid.

Key Items To Look For:

- Dividends declared/paid
- Other comprehensive income

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	shares	amount	other comprehen	earnings (deficit)	Total
Balance at February 3, 2007	58,476,306	177.5	28.5	438.0	644.0
Net Loss				(157.4)	(157.4)
Discontinued operations currency translation adjustment			8.7		8.7
Foreign currency translation adjustments			5.2		5.2
Comprehensive income				(143.5)	(143.5)
Adoption of FIN 48				(4.2)	(4.2)
Cash dividends declared (\$0.41 per common share)				(25.9)	(25.9)
Issuance of common stock					8.4
Repurchase and retirement of common stock	(132,937)	(0.6)			(0.6)
Tax benefit of equity comprnsation		0.9			0.9
Balance at February 2, 2008	58,794,224	186.2	42.4	250.5	479.1
Net Loss				(186.7)	(186.7)
Discontinued operations currency translation adjustment			(17.1)		(17.1)
Foreign currency translation adjustments			(13.4)		(13.4)
Comprehensive income				(217.2)	(217.2)
Issuance of common stock	1,787,776	0.9			0.9
Repurchase and retirement of common stock	(678,768)	(0.2)			(0.2)
Tax benefit of equity comprnsation		0.5	0.5		0.5
Balance at January 31, 2009	59,903,232	187.4	11.9	63.8	263.1
Net Loss				(109.4)	(109.4)
Foreign currency translation adjustments			4.8		4.8
Comprehensive income				(104.6)	(104.6)
Issuance of common stock	908,210	3.1			3.1
Repurchase and retirement of common stock	(942,058)	(3.3)			(3.3)
Balance at January 30, 2010	59,869,384	187.2	16.7	(45.6)	158.3

Dividends
declared and to
be paid.

The shareholders' equity is
the amount that would go
to the shareholders if the
company were dissolved.

Highlights of Sample Financial Statements

- The financials show a declining trend in revenue and gross margin; consecutive net losses
- The financials show a negative cash flow and decreasing balance sheet
- The financials show a cessation of paying dividends
- The financial statements are for Borders, which filed for bankruptcy in Feb. 2011

Summary

- Need to read all components of the financial statements
- Look for trends
- Cash is King
- Read the footnotes
- Ask questions