Valuation: Measuring and Managing the Value of Companies

Leases, Pensions, and Other Obligations

Chapter 27 Problems

1. Casher Industries leases a significant portion of its assets, expecting $25 million in rental expense next year. Casher Industries can borrow at 7 percent and the average life of leased asset is 7 years. Estimate the value of leased assets. If you misestimate the average life to be 10 years, how large will the valuation error be?

2. Casher Industries is expected to earn $25 million in operating profit next year. The company pays an operating tax rate of 30 percent and a marginal tax rate of 35 percent. What is the company's after-tax operating profit before and after the adjustment?

3. Many financial analysts estimate the value of operating leases by discounting rental payments provided in the annual report at the cost of debt. Is this method likely to overestimate or underestimate the value of leased assets? Why?

4. Many companies securitize their accounts receivable. Name two ways the cost for securitizing receivables is recognized. If you decide to recapitalize securitized receivable, when for which method is an expense adjustment required?

5. Using an Internet search tool, find Procter & Gamble's investor relations website. Under "Financial Reporting," you will find the company's 2009 annual report. In Note 8 of the annual report (which is titled postretirement benefits and employee stock ownership plan), P&G reports a breakout of its pension expense. Use this breakout to eliminate nonoperating income related to pensions from operating income reported in P&G's income statement.

6. Using an Internet search tool, find Procter & Gamble's investor relations website. Under "Financial Reporting," you will find the company's 2009 annual report. In the balance sheet, there is no report of prepaid pension assets or unfunded pension liabilities. Does this mean the P&G's pension plan is fully funded?