**11.12**

**Analysis of selected liquidity, activity, financial leverage, and profitability measures of Microsoft Corp.**

Presented here are summarized data from the balance sheets and income statements of Microsoft Corp, a computer software company.

**Condensed income statements and other data for the years ended June 30, 2006 and 2005**

**(in millions, except earnings per share)**

 **2006 2005**

Revenue……………………………………………………………………… $44,282 $39,788

**Operating expenses:**

 Cost of revenue…………………………………………………….. 7,650 6,031

 Research and development…………………………………… 6,584 6,097

 Sales and marketing………………………………………………. 9,818 8,563

 General and administrative……………………………………. 3,758 4,536

 Total operating expenses……………………………….. $27,810 $25,227

Operating income……………………………………………………….. $16,472 $14,561

Investment income and other…………………………………….. 1,790 2,067

Income before income taxes……………………………………….. $18,262 $16,628

Provision for income taxes…………………………………………… 5,663 4,374

Net income………………………………………………………………….. $12,599 $12,252

Earnings per share:

 Basic…………………………………………………………………………. $ 1.21 $ 1.13

 Diluted……………………………………………………………………… $ 1.20 $ 1.12

Market price per share at year-end……………………………… $23.08 $24.26

**Condensed balance sheets June 30, 2006 and 2005 (in millions, except per share)**

 **2006 2005**

**Assets**

Current assets:

 Cash and equivalents………………………………………… $6,714 $4,851

 Short-term investments……………………………………. 24,447 32,900

 Total cash and short-term investments…………. $34,161 $37,751

 Accounts receivable, net…………………………………… 9,316 7,180

 Inventories, net………………………………………………… 1,478 491

 Deferred income taxes……………………………………… 1,940 1,701

 Other………………………………………………………………… 2,115 1,614

 Total current assets……………………………………….. $49,010 $48,737

 Property and equipment, net……………………………. 3,044 2,346

 Equity and other investments……………………………. 9,232 11,004

 Goodwill and intangible assets, net…………………… 4,405 3,808

 Deferred income taxes………………………………………. 2,611 3,621

 Other long-term assets………………………………………. 1,295 1,299

 Total assets……………………………………………. $69,597 $70,815

**Liabilities and stockholders’ equity**

Current liabilities:

 Accounts payable……………………………………………….. $2,909 $2,086

 Accrued compensation……………………………………….. 1,938 1,662

 Income taxes………………………………………………………. 1,557 2,020

 Short-term unearned revenue……………………………. 9,138 7,502

 Other…………………………………………………………………… 6,900 3,607

 **Total current liabilities………………………... $22,442 $16,877**

Long-term unearned revenue………………………………………….. 1,764 1,665

Other long-term liabilities………………………………………………… 5,287 4,158

Stockholders’ equity:

 Common stock and paid-in-capital-shares

 Authorized 24,000; shares issued and

 Outstanding 10,062 and 10,710…………………………. $59,005 $60,413

Retained earnings (deficit), including accumulated

Other comprehensive income of $1,229 and $1,426……….(18,901) (12,298)

Total stockholders’ equity……………………………………………….. $40,104 $48,115

 Total liabilities and stockholders’ equity……………….**$69,597** **$70,815**

At June 30, 2004, total assets were $92,389, total liabilities were $17,564. And total stockholders’ equity was $74,825 (in millions)

1. Calculate Microsoft’s working capital, current ratio, and acid-test ratio at June 30, 2006 and at June 30, 2005.
2. Calculate Microsoft’s ROE for the years ended June 30, 2006 and 2005.
3. Calculate Microsoft’s ROI showing margin and turnover, for the years ended June 30, 2006 and 2005.
4. Calculate Microsoft’s price/earnings ratio at June 30, 2006 and 2005.
5. Calculate the following activity measures for Microsoft for the year ended June 30, 2006:
6. Accounts receivable turnover
7. Number of days’ sales in accounts receivable.
8. Calculate the following financial leverage measures for Microsoft at June 30, 2006 and 2005:
9. Debt ratio.
10. Debt/equity ratio.
11. 1. For the first time in the company’s history, Microsoft paid cash dividends on its common stock in 2003 ($0.08 per share, for a total of $857 million) in fiscal 2004, dividends were increased to $0.16 per share, for a total of $1,729 million. What do you think was the primary reason for Microsoft’s “no dividends” policy prior to 2003, and why would the company have changed this policy?

2) in fiscal 2005, dividends totaled $36,968, which included a special dividend of $3.00 per share ($32,640 million) in addition to a regular quarterly dividend of $0.08 per share. In fiscal 2006, dividends totaled $3,594 million. What do you think was the primary reason for Microsoft’s unusually large special dividend in 2004?

h. write a conclusion about the appropriateness of an investment in the common stock of Microsoft Corp. for a young, single professional with funds to invest in common stock.