Financial reporting quality

Financial Statement Analysis

1 A story: two report cards

- Honest card, poor marks
- Altered card, flattering marks
- Honest card, but one lucky exam
- An investor must tell these apart

IN THE LESSON

- Picture two students who both bring home poor report cards.
- The first student's card is honest.
- The marks are low, but they are exactly what the teacher recorded.
- The second student has quietly changed a few marks with a pen, so the card looks better than the truth.
- Both cards are disappointing, or flattering, in different ways.
- The first card is a faithful picture of a poor result.
- The second is an unfaithful picture.
- And there is a third kind of card, honest and excellent, but earned by one lucky exam that will not repeat.
- Investors face exactly these cases every time they open an annual report, and they must tell them apart.

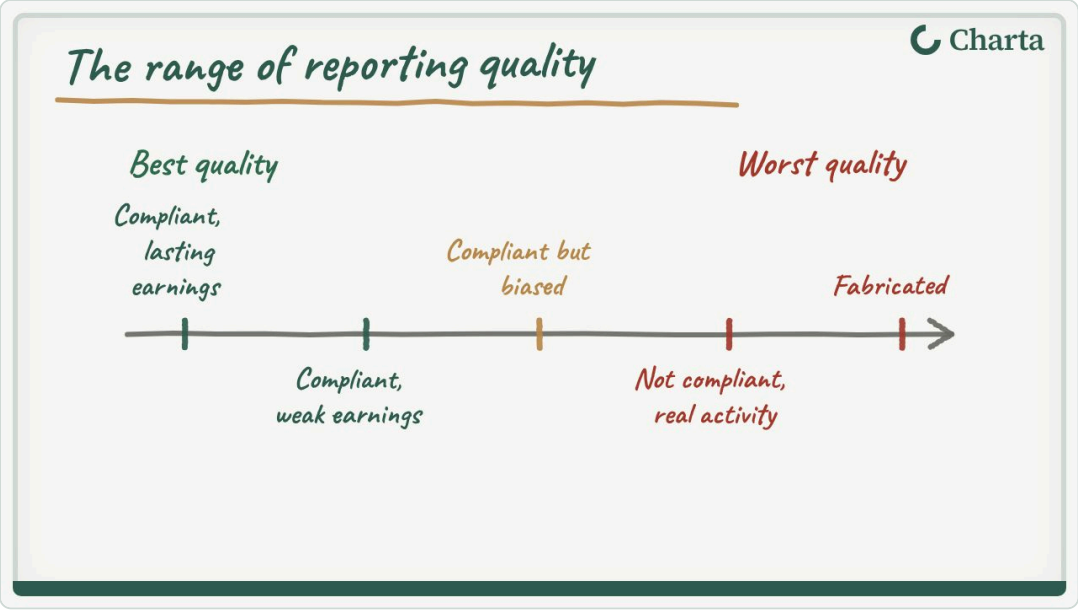
2 Two different questions

- Reporting quality: relevant and faithful to reality
- Earnings quality: sustainable and an adequate return
- Same ideas under IFRS and US GAAP
- Good reporting is needed to judge earnings at all

IN THE LESSON

- Analysts keep two ideas apart.
- Reporting quality asks whether the financial statements are useful for decisions.
- To be useful, they must be relevant, and they must faithfully represent what really happened, which means complete, neutral and free from error.
- That is reporting quality.
- Earnings quality is a different question.
- It asks whether the profit the company earned is sustainable and gives an adequate return.
- Sustainable means it is likely to repeat.
- Adequate means it is enough to reward the money invested.
- Under I F R S and under U S G A A P these ideas are the same, so you do not need to learn two versions.

3 The range of reporting quality



IN THE LESSON

- Now let us draw the range.
- Along the line, the best reporting sits on the left and the worst on the right.
- At the far left, the company follows the rules, the reports are useful, and the earnings are sustainable.
- Next, the company still follows the rules and reports faithfully, but its earnings are weak or will not last.
- Third, the reports follow the rules but the managers have leaned on their choices and estimates to make results look better, or sometimes worse.
- This is called biased reporting.
- Fourth, the company breaks the rules, though the numbers are based on real activity.
- Last, at the far right, the company simply makes up transactions and balances.
- That is fabrication, or fraud.

4 The five points on the range

- 1. Rules followed, earnings lasting and adequate
- 2. Rules followed, earnings weak or one-off
- 3. Rules followed in form, choices biased
- 4. Rules broken, but the activity was real
- 5. Transactions and balances invented

IN THE LESSON

- Let us name each point clearly.
- Number one is the best: reporting follows the standards and the earnings are sustainable and adequate.
- Number two follows the standards honestly, yet the earnings are low or one off.
- Number three follows the standards in form, but management chose aggressive or conservative treatments to push profit up or down.
- Number four does not follow the standards, though the underlying business activity is real.
- Number five is fabricated.
- Notice the pattern.
- Moving along the line, first the earnings get worse, then the honesty gets worse, then the very existence of the transactions is in doubt.
- The further right, the less any number can be relied on.

5 Bias goes both ways

- Aggressive: profit and assets pushed up now
- Conservative: profit and assets pushed down now
- Cookie jar: hide profit in good years, release it later
- Smoothing: steady growth that real business rarely shows

IN THE LESSON

- Bias does not always flatter.
- Aggressive choices push profit and assets up now, for example by booking sales early or spreading a cost over many years.
- Conservative choices push them down now, for example by writing off assets quickly or setting aside large reserves.
- Why would a manager understate profit?
- Sometimes to build a cushion.
- In a good year the company hides profit in a reserve, and in a bad year it releases the reserve to cover the shortfall.
- Analysts call that a cookie jar.
- Managers may also smooth profit, so that earnings climb steadily instead of bouncing.
- Smooth results look comforting, but the smoothness itself is manufactured, and so the picture is biased either way.

6 Example 1: same profit, different quality

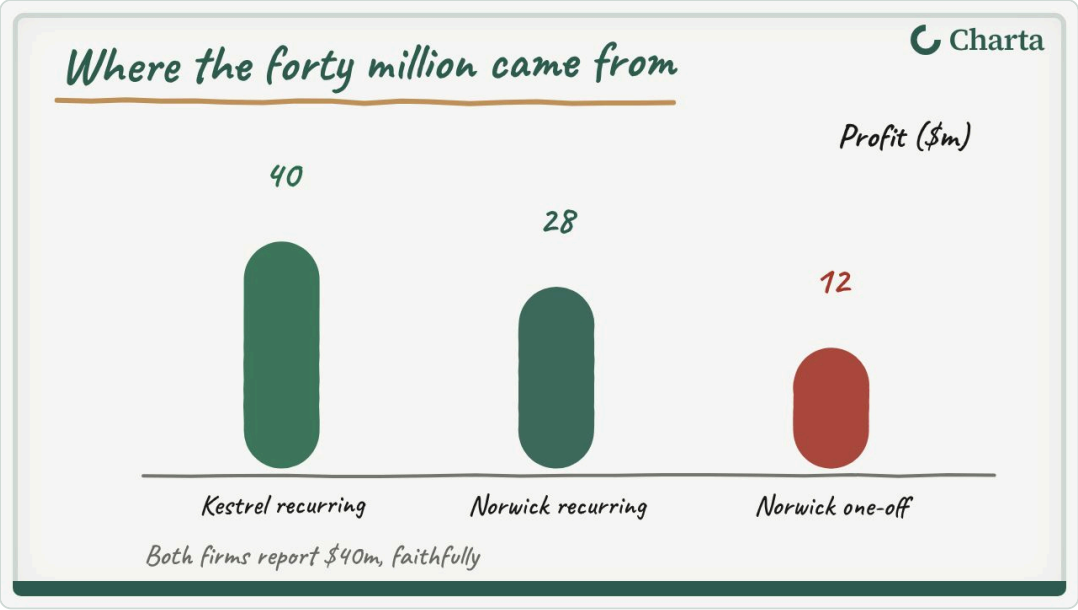
Norwick reports $40m, of which $12m is a one-off gain

Recurring profit	40 − 12	**$28m**
Share that will repeat	28 ÷ 40	**70%**
Share that was one-off	12 ÷ 40	**30%**
Next year, if nothing new	40 → 28	**−30%**

IN THE LESSON

- Example one.
- Kestrel earns forty million dollars in year one, and every dollar comes from selling components, which will go on next year.
- A rival, Norwick Parts, also reports forty million dollars, honestly and with full disclosure.
- But twelve million of it came from selling a spare warehouse.
- Subtract that and Norwick's recurring profit is twenty eight million.
- Divide twenty eight by forty and seventy per cent of the profit will repeat.
- The other thirty per cent, twelve over forty, was one off.
- If nothing new turns up next year, Norwick's profit falls from forty to twenty eight, a drop of thirty per cent.
- Both reports are high quality.
- Only Kestrel's earnings are.

7 Where the forty million came from



IN THE LESSON

- Here is the same example as bars.
- The vertical axis shows profit in millions of dollars.
- The first bar is Kestrel's recurring profit of forty, the whole of its result.
- The second bar is Norwick's recurring profit of twenty eight.
- The third, in red, is Norwick's one off gain of twelve.
- Add the second and third bars and you get forty, the same headline as Kestrel.
- That is the trap.
- Reported profit is a single number, so two firms can match on it and still be very different businesses.
- An analyst takes the headline apart before comparing, asking how much of the profit comes from the main business and how much from events that will not return.

8 Four combinations, and the trap

Two separate scales, not one

Reporting, then earnings	Verdict
Faithful report, lasting profit	Best
Faithful report, weak profit	Honest
Biased report, strong profit	Distrust
Poor report, any profit	Unknown

IN THE LESSON

- The most tested trap sits here.
- Reporting quality and earnings quality are two separate scales, so a company can score high on one and low on the other.
- Faithful report, sustainable profit is the best case.
- Faithful report, weak or one off profit is high reporting quality and low earnings quality at once, an honest report of a poor year.
- Take a shipping firm that reports faithfully, but whose profit came from a contract that has ended.
- Its reporting is fine.
- Its earnings are not.
- There is also an order of work.
- If the reporting is biased or not compliant, you cannot even judge the earnings, because you cannot trust the numbers.
- So assess reporting quality first, then earnings quality.

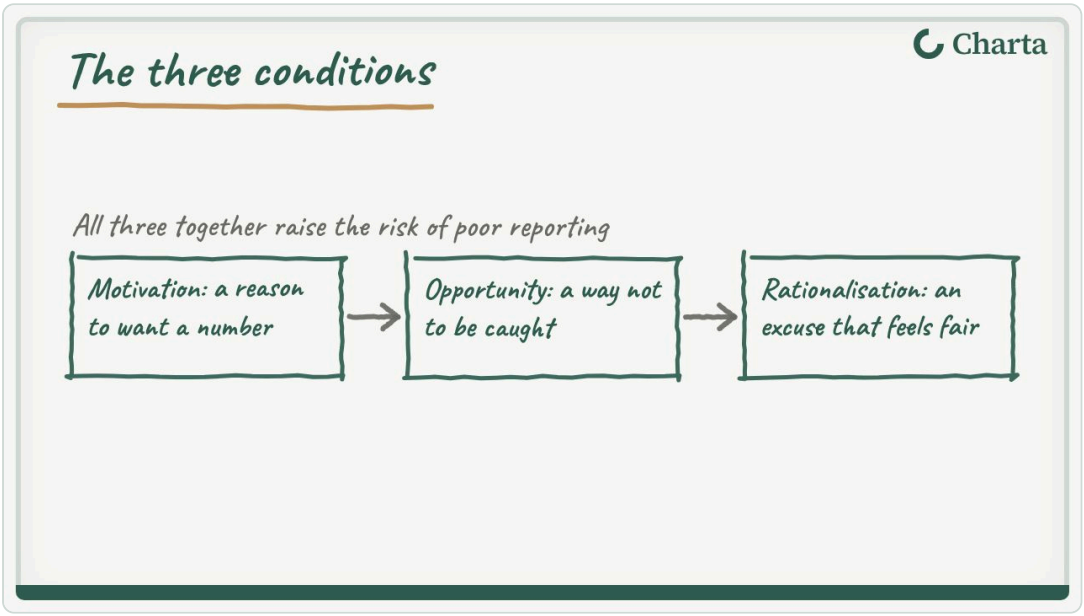
9 A story: what a fire needs

- A fire needs fuel, oxygen and heat together
- Misreporting needs three conditions together
- Reason, way, excuse: take one away, risk falls
- Ordinary people under pressure, not only villains

IN THE LESSON

- A fire needs three things at once: fuel, oxygen and heat.
- Take away any one and it goes out.
- Poor financial reporting works in a similar way.
- Researchers who study accounting misstatements keep finding that three conditions sit together, and the model is often called the fraud triangle.
- The first is a reason to want a different number.
- The second is a way to do it without being caught.
- The third is a story the person tells themselves so that the step feels acceptable.
- Most managers are not villains.
- Ordinary people, under pressure, with a gap in the controls and a comforting excuse, are the ones who tend to cross the line.
- That is why the problem recurs.

10 The three conditions



IN THE LESSON

- Here are the three conditions, drawn as a chain.
- Read left to right.
- Motivation comes first: management has a reason to want a different number.
- Examples are meeting analysts' forecasts, earning a bonus, keeping a loan agreement from being breached, or lifting the share price before the company sells shares.
- Opportunity comes next: weak controls, a board or audit committee that does not push back, or accounting that depends on estimates nobody can easily check.
- Rationalisation comes last: the belief that the treatment is defensible, or that a shortfall will be made up next year.
- When all three meet, a misstatement becomes much more likely.
- It is a warning of risk, not a proof that it happened.

11 Two numbers that create pressure

EPS = net income ÷ shares
Leverage = debt ÷ EBITDA

Net income	Profit for the owners
Shares	Number of shares in issue
Debt	Borrowing owed to lenders
EBITDA	Operating profit plus depreciation

IN THE LESSON

- Two ratios explain much of the motivation.
- Earnings per share is net income divided by the number of shares.
- Analysts publish a forecast of it, and a company that misses the forecast is often punished in the share price.
- So managers feel a pull toward just meeting it.
- Leverage, here debt divided by E B I T D A, is the second.
- E B I T D A is profit before interest, tax, depreciation and amortisation, a rough measure of operating cash earnings.
- Many loan agreements contain a covenant, a promise to keep that ratio below a limit.
- Breaking it can let the lender demand repayment.
- Both ratios are tied to a single figure the manager can influence, which is exactly what creates the temptation.

12 Example 2: hitting the forecast

Forecast EPS $2.00. 30m shares. Equipment $400m. Tax 25%.

Depreciation, 8-year life	400 ÷ 8	**$50m**
Depreciation, 10-year life	400 ÷ 10	**$40m**
Profit boost after tax	(50 − 40) × 0.75	**$7.5m**
EPS on old lives	52.5 ÷ 30	**$1.75**
EPS as reported	60 ÷ 30	**$2.00**

IN THE LESSON

- Example two.
- Kestrel has thirty million shares, and analysts forecast earnings per share of two dollars.
- Kestrel owns four hundred million dollars of equipment.
- Under its old policy it depreciated that over eight years, a charge of fifty million a year.
- Management lengthens the life to ten years, which makes the charge forty million.
- A change in an estimate like this is applied from now on under both I F R S and U S G A A P, and it needs a sound reason.
- Pre tax profit rises by ten million, and after twenty five per cent tax that is seven and a half million.
- Profit becomes sixty, so earnings per share is exactly two dollars.
- On the old lives it was fifty two and a half, or one dollar seventy five, a miss.

13 Example 3: staying inside a covenant

Debt $400m. Covenant: debt ÷ EBITDA at most 3.0 times.

Leverage as it stands	400 ÷ 130	**3.08x**
Cost moved to an asset	8 not expensed	**+$8m**
EBITDA afterwards	130 + 8	**$138m**
Leverage afterwards	400 ÷ 138	**2.90x**
Covenant limit	maximum	**3.0x**

IN THE LESSON

- Example three is a different pressure.
- Suppose Kestrel's loan agreement says debt divided by E B I T D A must stay at or below three times.
- Kestrel owes four hundred million, and its E B I T D A is one hundred and thirty million.
- Four hundred over one hundred and thirty is three point zero eight times, a breach.
- Now suppose management decides eight million of costs that it would normally expense can be capitalised, meaning recorded as an asset instead.
- That is the treatment of development costs I F R S allows once strict conditions are met, and U S G A A P mostly does not.
- E B I T D A rises to one hundred and thirty eight, and the ratio falls to two point nine times, just inside the limit.

14 Opportunity: where the rules give room

- Judgement: asset lives, bad debts, contract values
- Development costs: IFRS may capitalise, US GAAP expenses
- Revaluing property up: IFRS allows, US GAAP does not
- Room is not wrong. Room can be misused.

IN THE LESSON

- Motivation alone is not enough.
- A manager also needs opportunity, and some of it is built into the rules.
- Every set of standards asks for judgement, such as how long an asset lasts, how many customers will not pay, or what a contract is worth.
- Both frameworks also allow certain choices.
- Development costs may be capitalised under I F R S once criteria are met, while U S G A A P generally expenses them.
- I F R S allows property to be revalued upward, U S G A A P does not.
- I F R S allows a written down inventory value to be reversed later, U S G A A P does not.
- None of these choices is wrong in itself.
- They are room, and room can be used well or badly.
- You will meet them again in other lessons.

15 Opportunity: weak watchers, hard estimates

- Weak internal controls inside the company
- Board and audit committee that do not push back
- Auditors give an opinion, not a guarantee
- Hard-to-verify estimates: long contracts, model values

IN THE LESSON

- Opportunity also comes from weak watchers.
- Internal controls are the checks inside the company, such as approval limits and separate people for recording and paying.
- If they are poor, errors and manipulation survive.
- The board and its audit committee are meant to challenge management.
- If they are dominated by the chief executive or lack accounting expertise, they will not.
- The external auditor gives an opinion on whether the statements are fairly presented, but an audit is a sample, not a guarantee.
- Regulators and the market also watch.
- Finally, the business model matters.
- Revenue recognised over long contracts, or assets valued by models with no market price, rest on estimates that outsiders cannot easily verify, and that is opportunity by its very nature.

16 Rationalisation: the story people tell

- "Everyone in our industry does it"
- "It is allowed by the rules"
- "We will make it up next year"
- Small first steps grow into large ones

IN THE LESSON

- The third condition is the hardest to see, because it lives in a person's head.
- Rationalisation is the reasoning that lets someone take a step while still thinking of themselves as honest.
- A manager may say that competitors do the same, that the treatment is allowed in the rules, or that this is only a temporary timing shift and next year will put it right.
- Each excuse sounds reasonable, and that is its power.
- This is why it is a separate condition from motivation.
- Motivation explains why someone wants the result, rationalisation explains how an honest person gets there.
- It also explains why small first steps tend to grow: next year the gap is larger, and the same excuse is needed again.

17 Four mistakes to avoid so far

- 1. Reporting quality and earnings quality are separate
- 2. Compliant with the rules is not the same as unbiased
- 3. Bias can lower profit as well as raise it
- 4. The three conditions show risk, not proof

IN THE LESSON

- Before the warning signs, here are the mistakes learners most often make.
- First, treating reporting quality and earnings quality as one scale.
- They are separate, so honest reporting of a bad year is high on one and low on the other.
- Second, thinking that compliant means good.
- Reports can follow the rules and still be biased in the choices they use.
- Third, believing that bias always inflates profit.
- It can be conservative, as with the cookie jar.
- Fourth, treating the three conditions as proof.
- Having motivation, opportunity and rationalisation raises the risk of misstatement.
- It does not mean anything has happened.
- Hold these four in your head, because questions like each of them.

18 A story: the smoke detector

- A detector signals, it does not prove
- Compare figures that should move together
- One flag: investigate. A cluster: be alarmed
- Flags tell you where to look

IN THE LESSON

- A smoke detector does not prove a house is on fire.
- It might be burnt toast.
- But when the alarm sounds, you go and look, and if three detectors in different rooms sound together, you leave the house.
- Red flags in financial statements work in the same way.
- They do not prove poor reporting.
- They tell the analyst where to look more closely.
- The most useful flags are relative, not absolute.
- A receivables balance of one hundred is neither good nor bad on its own.
- What matters is how it moves compared with revenue, or compared with cash.
- The analyst's habit is to set two figures side by side and ask why they are not moving together.

19 Two days that expose growth

DSO = receivables ÷ revenue × 365
DIO = inventory ÷ COGS × 365

Receivables	Owed by customers, year end
Revenue	Sales for the year
Inventory	Stock on hand, year end
Cost of goods sold	Cost of what was sold

IN THE LESSON

- Two simple ratios turn the idea into numbers.
- Days sales outstanding, or D S O, is receivables divided by revenue, times three hundred and sixty five.
- It tells you the average number of days customers take to pay.
- Days inventory outstanding, or D I O, is inventory divided by cost of goods sold, times three hundred and sixty five.
- It tells you how many days of sales the stock on the shelf represents.
- Note that for this lesson we use year end balances, because we are tracing a trend and want a quick, clean comparison.
- In other lessons the ratios use the average of the start and end of the year, which gives a smoother figure.
- The direction of the movement is what we watch.

20 Example 4: receivables outrun sales

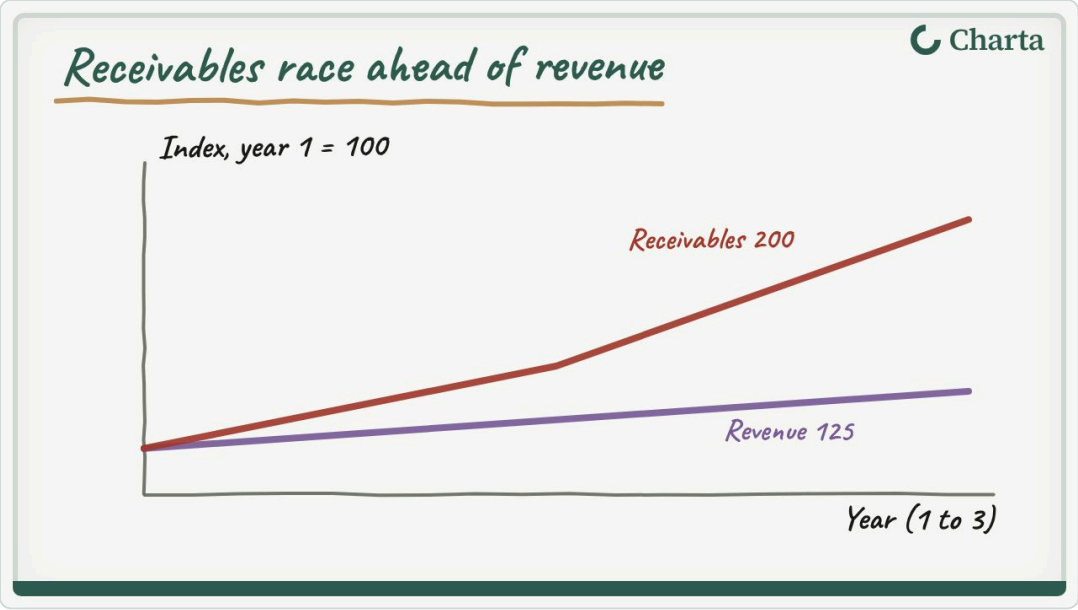
Kestrel: revenue and receivables, $m, year ends

Revenue growth, year 3	500 ÷ 450 − 1	**11.1%**
Receivables growth, year 3	100 ÷ 68 − 1	**47.1%**
DSO, year 1	50 ÷ 400 × 365	**45.6 days**
DSO, year 3	100 ÷ 500 × 365	**73.0 days**
Customers now slower by	73.0 − 45.6	**27.4 days**

IN THE LESSON

- Example four.
- Over two years Kestrel's revenue climbs from four hundred to five hundred million.
- Receivables climb from fifty to one hundred million.
- Revenue grew twelve and a half per cent, then eleven per cent, a steady pace.
- Now look at receivables in the last year alone.
- They went from sixty eight to one hundred, a rise of forty seven per cent, more than four times as fast as sales.
- Convert to days.
- In year one, customers took forty five point six days to pay.
- In year three they take seventy three.
- That is twenty seven more days.
- Either customers have become slow, or Kestrel is booking sales early, shipping goods before customers have agreed to take them.

21 Receivables race ahead of revenue



IN THE LESSON

- Here is the same story as a picture.
- The horizontal axis is the three years.
- The vertical axis is an index, where year one is set to one hundred, so we can compare growth on equal terms.
- The lower line is revenue.
- It climbs gently to one hundred and twenty five.
- The upper line is receivables.
- It starts at the same place but rises to two hundred, doubling in two years.
- The gap between the lines is the warning.
- Healthy growth would keep the lines close together, since more sales bring more receivables in proportion.
- When the second line pulls away, sales are being recorded that the cash has not caught up with.
- Inventory shows a similar pattern in the next example.

22 Example 5: stock piling up

Kestrel: inventory and cost of goods sold, $m

Inventory growth, years 1 to 3	114 ÷ 62 − 1	**84%**
COGS growth, years 1 to 3	300 ÷ 240 − 1	**25%**
DIO, year 1	62 ÷ 240 × 365	**94.3 days**
DIO, year 3	114 ÷ 300 × 365	**138.7 days**
Extra days of stock	138.7 − 94.3	**44.4 days**

IN THE LESSON

- Example five is the same test on inventory.
- Compare it with cost of goods sold, the cost of the goods that were sold.
- Kestrel's inventory rose from sixty two to one hundred and fourteen million, up eighty four per cent.
- Cost of goods sold rose from two hundred and forty to three hundred, up only twenty five per cent.
- In days, year one held ninety four point three days of stock.
- Year three holds one hundred and thirty eight point seven days, about forty four days more.
- Possible reasons are innocent, such as stocking up for a big launch.
- But stock that is not selling may be obsolete, and old stock that is not written down overstates both assets and profit.
- The analyst asks management which explanation is true.

23 Profit against cash

Accruals = NI − CFO − CFI
Accruals ratio = Accruals ÷ average NOA

Net income	Profit on the income statement
Operating cash flow	Cash from running the business
Investing cash flow	Cash spent on or from investing
Net operating assets	Operating assets − liabilities

IN THE LESSON

- The second great comparison is profit against cash, and it is measured as accruals.
- Net income includes accruals, which are revenues and expenses recorded before the cash moves.
- There are two formal ways to count them.
- The cash flow approach is net income minus operating cash flow minus investing cash flow.
- Investing cash flow comes off as well, because items such as depreciation and gains on asset sales sit in profit without being operating cash.
- The balance sheet approach is the change in net operating assets: operating assets, meaning total assets less cash and short term investments, minus operating liabilities, meaning total liabilities less borrowings.
- To compare firms of different size, divide accruals by average net operating assets to get the accruals ratio.
- A higher or rising ratio means lower earnings quality.
- A very negative ratio means high quality.

24 Example 6: profit up, cash down

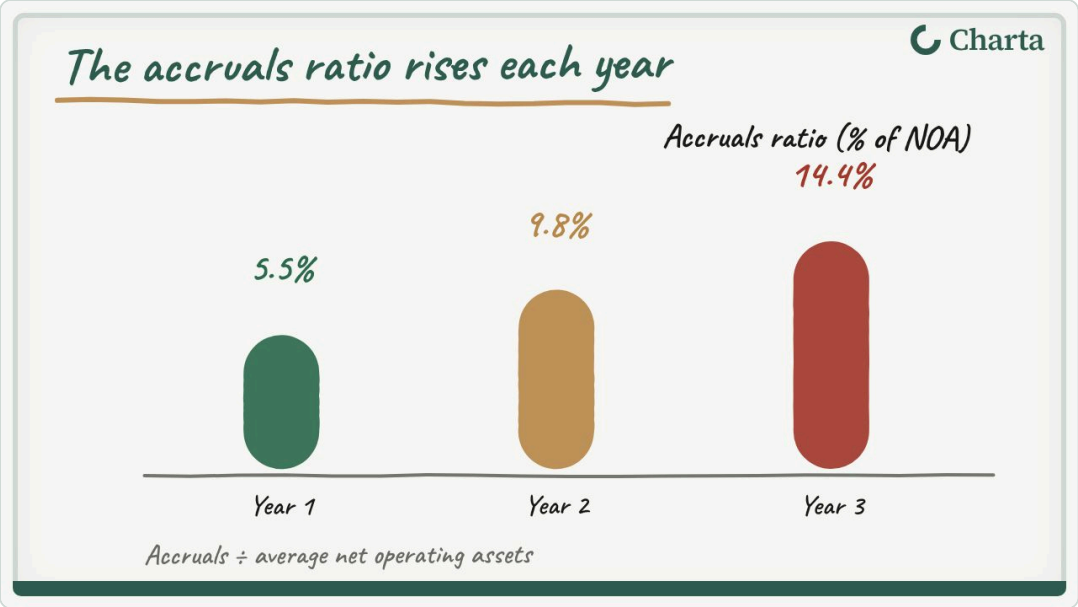
Kestrel: accruals by the cash flow approach, $m

Year 1 accruals	40 − 38 + 20	**$22m**
Year 2 accruals	50 − 30 + 24	**$44m**
Year 3 accruals	60 − 14 + 26	**$72m**
Year 1 accruals ratio	22 ÷ 400	**5.5%**
Year 3 accruals ratio	72 ÷ 500	**14.4%**

IN THE LESSON

- Example six.
- Kestrel's net income climbs each year: forty, fifty, sixty million.
- Operating cash flow goes the other way: thirty eight, thirty, fourteen.
- Investing cash flow is minus twenty, minus twenty four and minus twenty six.
- By the cash flow approach, accruals are net income minus operating cash flow minus investing cash flow: twenty two million in year one, forty four in year two and seventy two in year three.
- Average net operating assets are four hundred, four hundred and fifty and five hundred million, so the accruals ratio rises from five point five to nine point eight to fourteen point four per cent.
- Cash conversion, operating cash flow over net income, tells the same story: ninety five per cent in year one and twenty three in year three.
- A company can show rising profits for a while through accruals, but it cannot pay wages and suppliers with them.

25 The accruals ratio rises each year



IN THE LESSON

- Here is the accruals ratio as bars.
- The vertical axis shows accruals as a percentage of average net operating assets.
- In year one the bar is five point five per cent, a normal figure.
- In year two it is nine point eight, nearly twice as big.
- In year three it reaches fourteen point four, and the colours move from green to red to show the danger growing.
- This is the picture an analyst wants to see before trusting a rising profit line.
- Note what the picture does not say.
- It does not say Kestrel is fraudulent.
- A fast growing firm can legitimately have a widening gap.
- But the direction and the speed demand an explanation, and the explanation must come with evidence from the notes.

26 More red flags to know

- Falling bad-debt allowance: too little set aside
- Longer asset lives: lower charge, higher profit
- Capitalising costs peers expense: cost moved to assets
- Big fourth-quarter adjustment: year tidied at the end
- Changing auditor or CFO, repeated one-off charges

IN THE LESSON

- There are more signs to know.
- A falling allowance for doubtful accounts while receivables rise suggests too little is set aside for customers who will not pay.
- Longer depreciation lives, as in example two, lift profit without any real change in the business.
- Capitalising costs that peers expense moves cost out of profit, but it also moves cash out of operating cash flow into investing.
- A large adjustment in the fourth quarter suggests the year was tidied up at the last minute.
- Frequent changes of auditor or chief financial officer suggest disagreement.
- And serial one off charges, such as a restructuring cost every year, hide recurring costs under a one off label.

27 Example 7: put the flags together

Year 3 pre-tax $80m, tax 25%, 30m shares

Remove longer-life boost	80 − 10	**$70m**
Allowance shortfall	5.0 − 3.0	**$2m**
Adjusted pre-tax profit	70 − 2	**$68m**
Adjusted net income	68 × 0.75	**$51m**
Adjusted EPS	51 ÷ 30	**$1.70**

IN THE LESSON

- Example seven turns the flags into a rough adjustment.
- Kestrel's year three profit before tax is eighty million.
- First, the depreciation change of example two added ten million to profit, so take it off.
- Second, the bad debt allowance.
- In year two it was five per cent of receivables, three point four over sixty eight.
- Apply the same cover to one hundred of receivables and the allowance should be five, but Kestrel holds three, a shortfall of two.
- Take that off as well.
- Adjusted pre tax profit is sixty eight million.
- After twenty five per cent tax it is fifty one million, or one dollar seventy per share, against the two dollars reported.
- The reported figure was flattered: the adjusted figure is about fifteen per cent below it.

28 Clusters, not single signs

- Each sign alone has an innocent reading
- Several together are much stronger evidence
- Read notes, compare peers, question management
- Adjust the numbers, and size the risk

IN THE LESSON

- The key idea is the cluster.
- Each sign on its own has an innocent explanation.
- Receivables may grow because Kestrel won a large customer who asked for longer terms.
- Stock may build before a launch.
- A chief financial officer may leave for a better job.
- But when receivables race ahead, stock piles up, profit pulls away from cash, the allowance falls and the depreciation lives lengthen, all in the same company, the innocent explanations run out.
- So the analyst steps up the work: read the notes on policies and estimates, compare with peers, ask management, and adjust the numbers as we did.
- A cluster raises the probability of a problem.
- It still does not prove it.

29 Recap: three ideas to carry away

- Range: lasting, weak, biased, not compliant, fabricated
- Two scales: reporting quality first, then earnings
- Motivation, opportunity, rationalisation: risk, not proof
- Flags are relative to sales and cash. Look for clusters.

IN THE LESSON

- Let us pull it together.
- Idea one: the range of reporting quality runs from compliant with lasting earnings, through compliant with weak earnings, compliant but biased, not compliant, to fabricated.
- Reporting quality and earnings quality are separate scales, so an honest report of a poor year is high on one and low on the other, and reporting quality must be judged first.
- Idea two: poor reporting needs motivation, opportunity and rationalisation together, which show risk but not proof.
- Idea three: red flags are relative.
- Receivables or inventory outrunning sales, accruals outrunning cash, a falling allowance, longer lives, capitalised costs, late adjustments, changing auditors, and repeated one off charges.
- A cluster is stronger than one.

30 Try three quick questions

1. A firm reports a poor year fully and faithfully. Reporting and earnings quality?
   Answer: High reporting quality, low earnings quality.
2. Name the three conditions usually present together when reporting is poor.
   Answer: Motivation, opportunity and rationalisation.
3. Net income 60, CFO 14, CFI −20, average NOA 400. Accruals ratio?
   Answer: 60 − 14 + 20 = 66. 66 ÷ 400 = 16.5%.

IN THE LESSON

- Now try three quick questions yourself.
- Pause after each one.
- Question one.
- A firm reports a poor year fully and faithfully.
- What are its reporting quality and its earnings quality?
- High reporting quality, low earnings quality.
- Question two.
- Name the three conditions usually present together when reporting is poor.
- Motivation, opportunity and rationalisation.
- Question three.
- Net income is sixty, operating cash flow is fourteen, investing cash flow is minus twenty, and average net operating assets are four hundred.
- What is the accruals ratio?
- Accruals are sixty minus fourteen plus twenty, which is sixty-six.
- Sixty-six divided by four hundred is sixteen point five per cent.
- Well done.