







Plug-n-chug

- The plug-n-chug problems are the easiest.
- Such a problem is one where all but one item in a ratio is given to you, and all you have to do is solve for the remaining one.

Example:

Your firm had net income of \$1,000,000 last year and had total assets of \$5,000,000. What was the firm's return on assets?

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The only ratio mentioned is return on assets so we write that formula. (ROA is what we are finding.)

ROA = (net income) / (total assets)

We next identify what we know.

Net income=\$1,000,000 Total assets=\$5,000,000

This is a plug-n-chug problem since we know all entries for the ratio except the ROA which we can solve for.

ROA = (1,000,000) / (5,000,000) = .20 = 20%













After we know all present information, we can focus on the future information.

We know that the target current ratio is 3.0. To change to CR=3.0 from CR=4.0 we must change the CL and/or CA accounts (we will be either adding or subtracting).

In this case the problem says we are increasing CA by using CL. Thus, however much CL goes up is the same amount CA goes up.

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We must start with the current balances for CA and CL and determine the change. $CR = CA / CL \qquad \text{target CR} = 3.0$ $3 = \frac{10 + x}{2.5 + x}$ 3 (2.5 + x) = 10 + x 7.5 + 3 x = 10 + x 2x = 2.5 X = 1.25

CHECK: CR = (10 + 1.25) / (2.5 + 1.25) = 3

OVERALL

- Always remember to write the formulas down first, and then identify what you are looking for, what you have, and the type of problem you are facing.
- If you follow these steps, the problem are much easier.

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