

Chapter 9 Problems

1. Bilbo Company has a current margin of 6% with operating income of \$6,000. What is the company's turnover, if the company has \$50,000 in operating assets?

$$\text{Turnover} = \text{Sales} / \text{OA}$$

$$\text{Margin} = \text{OI} / \text{Sales}$$

$$6\% = \$6,000 / X$$

$$6\% X = \$6,000$$

$$X = \$6,000 / 6\%$$

$$X = \$100,000$$

$$\text{Turnover} = \$100,000 / \$50,000 = 2$$

- a. 0.5
- b. 1.0
- c. **2.0**
- d. 3.0
- e. None of the above

2. Baggins Corporation would like to have a return of 12% on all of its investments. The Gold Division has current assets of \$1,500,000. The division has residual income of \$20,000. What is the division's margin if it has sales of \$800,000?

$$\text{Margin} = \text{OI} / \text{Sales}$$

$$\text{RI} = \text{OI} - (\text{OA} * \text{Desired ROI})$$

$$\$20,000 = \text{OI} - (\$1,500,000 * 12\%)$$

$$\$20,000 = \text{OI} - \$180,000$$

$$\text{OI} = \$200,000$$

$$\text{Margin} = \$200,000 / \$800,000 = 25\%$$

- a. **25%**
- b. 2.5%
- c. 53.3%
- d. 6.7%
- e. None of the above

3. The O'Donnell Company has several divisions. Paul is the manager of Division 1. Division 1 has current operating assets of \$10,000,000 with a return of 16%. The company's target is 12%. Because Paul has done such a good job managing Division 1, Paul's boss has asked him to accept a new investment project of \$3,000,000 that has a return of 14%. Should Paul accept the new investment?

To find change, calculate RI on new investment

$$\text{RI} = \text{OI} - (\text{OA} * \text{Desired ROI})$$

$$\text{OI} = \$3,000,000 * 14\% = \$420,000$$