**Financial Condition Analysis**

Questions:

17.1

**a. Modern Medical Devices has a current ratio of 0.5. Which of the following actions would improve**

(i.e., increase) this ratio?

- Use cash to pay off current liabilities.

- Collect some of the current accounts receivable.

- Use cash to pay off some long-term debt.

- Purchase additional inventory on credit (i.e., accounts payable).

- Sell some of the existing inventory at cost.

b. **Assume that the company has a current ratio of 1.2. Now, which of the above actions would improve this ratio?**

17.5

**For each ratio calculated in parts a and b, in question 17.1, Be sure to provide an assessment of how Green Valley is doing in comparison to industry averages.**

Consider the following financial statements for Green Valley Nursing Home, Inc. a for profit long-term care facility:

Green Valley Nursing Home Inc.

Statement of Income and Retained Earnings

Year Ended December 31, 2011

**Revenue:**

Net patient service revenue $3,163,258

Other revenue 106,146

Total Revenue $3,269,404

Expenses:

Salaries and benefits $1,515,438

Medical supplies and drugs 966,781

Insurance and other 296,357

Provision for bad debts 110,000

Depreciation 85,000

Interest 206,780

Total expenses $3,180,356

Operating Income $89,048

Provision for income tax 31,167

Net Income $57,881

Retained earnings, beginning of year $199,961

Retained earnings, end of year $257,842

Green Valley Nursing Home Inc.

Balance Sheet

December 31, 2011

**Assets**

Current assets:

Cash $105,737

Marketable securities 200,000

Net patient accounts receivables 215,600

Supplies 87,655

Total current assets $608,992

Property and equipment $2,250,000

Less accumulated depreciation 356,000

Net property and equipment $1,894,000

**Total assets** $2,502,992

**Liabilities and Shareholder’s Equity**

**Current liabilities:**

Accounts payable $72,250

Accrued expenses 192,900

Notes payable 100,000

Current portion of long-term debt 80,000

Total current liabilities $445,150

Long term debt $1,700,000

**Shareholders’ Equity:**

Common stock, $10 par value $100,000

Retained earnings 257,842

Total shareholder’s equity $357,842

Total liabilities and shareholders’ equity $2,502,992

Additional Questions

**A. Perform a Du Pont analysis on Green Valley. Assume that the industry average ratios are as follows:**

Total margin 3.5%

Total asset turnover 1.5

Equity multiplier 2.5

Return on equity 13.1%

**B. Calculate and interpret the following ratios:** **Industry Average**

Return on assets (ROA) 5.2%

Current ratio 2.0

Days cash on hand 22

Average collection period 19 days

Debt ratio 71%

Debt to equity ratio 2.5

Times interest earned **(TIE)** ratio 2.6

Fixed asset turnover ratio 1.4

**c. Assume that there are 10,000 shares of Green Valley’s stock outstanding and that some recently sold for $45 per share.**

- What is the firm’s price/earnings ratio?

- What is its market/book ratio?

17.5.1

**d. Refer back to Textbook Problem 17.5.  Recast the financial statements for Green Valley into common size financial statements.  Describe at least two advantages of a common size presentation of financial statements.**