**Problem 12-03. AFN Equation**

Baxter Video Products' sales are expected to increase by 20% from $5 million in 2010 to $6 million in 2011. Its assets totaled $4 million at the end of 2010. Baxter is already at full capacity, so its assets must grow at the same rate as projected sales. At the end of 2010, current liabilities were $1 million, consisting of $250,000 of accounts payable, $500,000 of notes payable, and $250,000 of accruals. The after-tax profit margin is forecasted to be 5%, and the forecasted payout ratio is 55%. Assume that the company pays no dividends. Under these assumptions, what would be the additional funds needed for the coming year? Round your answer to the nearest dollar.
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Why is this AFN different from the one when the company pays dividends?

**I.** Under this scenario the company would have a higher level of retained earnings but this would have no effect on the amount of additional funds needed.
**II.** Under this scenario the company would have a lower level of retained earnings which would reduce the amount of additional funds needed.
**III.** Under this scenario the company would have a lower level of retained earnings but this would have no effect on the amount of additional funds needed.
**IV.** Under this scenario the company would have a higher level of retained earnings which would reduce the amount of additional funds needed.
**V.** Under this scenario the company would have a higher level of retained earnings which would increase the amount of additional funds needed.

**Problem 12-02. AFN Equation**

Baxter Video Products' sales are expected to increase by 20% from $5 million in 2010 to $6 million in 2011. Its assets totaled $4 million at the end of 2010. Baxter is already at full capacity, so its assets must grow at the same rate as projected sales. At the end of 2010, current liabilities were $1 million, consisting of $250,000 of accounts payable, $500,000 of notes payable, and $250,000 of accruals. The after-tax profit margin is forecasted to be 7%, and the forecasted payout ratio is 60%. What would be the additional funds needed if the company's year-end 2010 assets had been $4 million? Assume that the company is operating at full capacity. Round your answer to the nearest dollar.
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What would be the additional funds needed if the company's year-end 2010 assets had been $3 million? Is the company's "capital intensity" ratio the same or different?

**I.** The capital intensity ratio is measured as A\*/S0. This firm's capital intensity ratio is higher than that of the firm with $3 million year-end 2010 assets; therefore, this firm is more capital intensive - it would require a large increase in total assets to support the increase in sales.
**II.** The capital intensity ratio is measured as A\*/S0. This firm's capital intensity ratio is lower than that of the firm with $3 million year-end 2010 assets; therefore, this firm is more capital intensive - it would require a large increase in total assets to support the increase in sales.
**III.** The capital intensity ratio is measured as A\*/S0. This firm's capital intensity ratio is higher than that of the firm with $3 million year-end 2010 assets; therefore, this firm is less capital intensive - it would require a smaller increase in total assets to support the increase in sales.
**IV.** The capital intensity ratio is measured as A\*/S0. This firm's capital intensity ratio is lower than that of the firm with $3 million year-end 2010 assets; therefore, this firm is more capital intensive - it would require a smaller increase in total assets to support the increase in sales.