Ratio Analysis

- **Current Ratio** = Current Assets/Current Liabilities
  (Ideal ratio = 2:1)
- **Liquid/Quick/Acid test Ratio** = Quick Assets/ Quick liabilities
  Ability to meet immediate liabilities.
- Quick assets = CA-stock-prepaid expenses.
- Quick liabilities = CL-overdraft-cash credit.
- Absolute cash ratio = Cash/Bank balance + Marketable securities/ Current liabilities
  Availability of cash to meet short term commitments.
- Interval measure = Quick assets/ Cash expenses per day.
  Ability to meet regular cash expenses.
- Base Balance sheet equation is Equity + Debt = FA+WC.

Equity Funds: Equity sh cap + Pref. sh cap + R&S – fictitious assets
From Assets side: Equity funds = FA+WC-Long term debt
Prepaid expenses is a fictitious asset.

Capital Structure Ratios (Indicates long term solvency)

- Equity to Total fund ratio = Equity fund/Total funds

Total funds = equity + debt
Indicates extent of own funds used in operations.

- Debt Equity ratio = Debt/Equity
  (Ideal ratio 2:1)
- Capital gearing ratio = Fixed charge bearing capital/Pure equity funds

  Fixed charge bearing capital = Long term debt + Pref. share capital

  Pure equity funds = Equity funds other than pref. share capital.
- Fixed Assets to Long term funds ratio = FA/Long term funds
  (Ideal ratio is less than 1)

  Long term funds = Equity + Debt
- Proprietary ratio = Proprietary fund/Total Assets
  Proprietary fund = Equity funds = Net worth
  Total Assets = FA+CA
- Gearing ratio = Equity capital/Pref. capital

Coverage Ratios (Indicates ability to serve fixed liabilities)

- Debt service coverage ratio = Earnings available for debt service / Instalment + Interest

  Earnings available for debt service = PAT + Interest + Non-cash expenses + Non-operating expenses& losses.

- Interest coverage ratio = EBIT/Interest

- Preference dividend coverage ratio = PAT/ Pref. dividend

Turnover/Activity/Performance ratios (Indicates operating efficiency)

- Capital Turnover ratio = Sales/ Capital employed

  Capital employed = Equity + Debt – Non trade investments.

  (or) Capital employed = FA+WC

- Fixed Assets Turnover ratio = sales/Fixed Assets

- Working capital Turnover ratio = Sales/Working capital

- Stock/Inventory Turnover ratio = Cost of goods sold/Average Stock

- Debtors Turnover ratio = Credit sales/Average Accounts Receivable
  Accounts receivable = Debtors + B/R

- Creditors Turnover ratio = Credit Purchases/Average accounts payable
  Accounts payable = Creditors +B/P

Profitability Ratios based on sales

- Gross Profit Ratio = Gross Profit/Sales*100
- Operating Profit Ratio = Operating Profit/Sales * 100
  Operating profit = EBIT + Non operating expenses & losses- Non operating Incomes & gains.

- Net profit ratio = Net profit/Sales *100
  Indicates overall profitability

- Contribution Ratio = Contribution/Saes*100
  Indicates profitability in marginal costing

Profitability Ratios from Ownership point of view

- Ratios Return on Capital/Investment = Return/Capital employed *100
  Return = Operating profit = EBIT + Non-operating expenses & losses – Non operating incomes & gains

  Capital employed = Equity + Debt – non trade investments
  (Or) Fixed Assets + Working capital

  Indicates overall profitability of business for capital employed

- Return on Equity funds = PAT/Net worth *100
  Indicates the profitability of equity funds invested in the business.

- Earnings per share = PAT-Preference dividend/ no. of equity shares
  Indicates return/income per share.

- Dividend per share = Total dividend/no. of equity shares

- Return on Assets = PAT/Average total assets/tangible assets/Fixed assets
  Indicates net income from investments in average fixed assets

- Price Earnings ratio = Market price/EPS
  Indicates market price per rupee of earnings

- Operating profit ratio = Operating profit/Sales*100

- Operating exp ratio = Operating exp/Sales *100
  Operating exp = P&L exp other than interest

- Operating ratio = Total operating cost/Sales*100
  Total operating cost = COGS + Operating exp.

- Dividend Yield = Dividend per share/Market price per share

- Rate of return to the investor, Y = F-P/P * 12/M * 100

  Where, Y = Yield
  M = Maturity period

- Preference dividend coverage ratio = PAT/Pref. dividend

- Equity dividend coverage = PAT-Pref. dividend/Equity dividend

- Average collection period = 365 days/Drs turnover ratio = Ans in days

- Stock velocity = 2 months
  Stock T.O ratio = 12/2 = 6 months

- Debtors Velocity = Sales/Drs
  Debtors = Credit Sales/Drs T.O ratio = Answer in amount.