

Ratios

Liquidity Ratios →

Chapter	Ratio	Formula	What the Ratio Measures	Desired Result
2	Working capital	Current assets – Current liabilities	Short-term debt-paying ability	Higher
2	Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$	Short-term debt-paying ability	Higher
13	Cash current debt coverage	$\frac{\text{Net cash provided (used) by operating activities}}{\text{Average current liabilities}}$	Short-term debt-paying ability (cash basis)	Higher
8	Receivables turnover	$\frac{\text{Net credit sales}}{\text{Average gross accounts receivable}}$	Liquidity of receivables	Higher
8	Average collection period	$\frac{365 \text{ days}}{\text{Receivables turnover}}$	Number of days receivables are outstanding	Lower
6	Inventory turnover	$\frac{\text{Cost of goods sold}}{\text{Average inventory}}$	Liquidity of inventory	Higher
6	Days in inventory	$\frac{365 \text{ days}}{\text{Inventory turnover}}$	Number of days inventory is on hand	Lower

Solvency Ratios →

Chapter	Ratio	Formula	What the Ratio Measures	Desired Result
2, 10	Debt to total assets	$\frac{\text{Total liabilities}}{\text{Total assets}}$	Percentage of total assets provided by creditors	Lower
10	Times interest earned	$\frac{\text{Profit} + \text{Interest expense} + \text{Income tax expense (EBIT)}}{\text{Interest expense}}$	Ability to meet interest payments	Higher
13	Cash total debt coverage	$\frac{\text{Net cash provided (used) by operating activities}}{\text{Average total liabilities}}$	Long-term debt-paying ability (cash basis)	Higher
13	Free cash flow	Net cash provided (used) by operating activities – Net capital expenditures – Dividends paid	Cash available from operating activities for discretionary purposes	Higher

Profitability Ratios →

Chapter	Ratio	Formula	What the Ratio Measures	Desired Result
11	Return on common shareholders' equity	$\frac{\text{Profit} - \text{Preferred dividends}}{\text{Average common shareholders' equity}}$	Profitability of shareholders' investment	Higher
9	Return on assets	$\frac{\text{Profit}}{\text{Average total assets}}$	Overall profitability of assets	Higher
5	Profit margin	$\frac{\text{Profit}}{\text{Net sales}}$	Profit generated by each dollar of sales	Higher
9	Asset turnover	$\frac{\text{Net sales}}{\text{Average total assets}}$	How efficiently assets are used to generate sales	Higher
5	Gross profit margin	$\frac{\text{Gross profit}}{\text{Net sales}}$	Margin between selling price and cost of goods sold	Higher
2, 11	Earnings per share	$\frac{\text{Profit} - \text{Preferred dividends}}{\text{Weighted average number of common shares}}$	Profit earned on each common share	Higher
2	Price-earnings ratio	$\frac{\text{Market price per share}}{\text{Earnings per share}}$	Relationship between market price per share and earnings per share	Higher
11	Payout ratio	$\frac{\text{Cash dividends}}{\text{Profit}}$	Percentage of profit distributed as cash dividends	Higher
11	Dividend yield	$\frac{\text{Dividend per share}}{\text{Market price per share}}$	Income generated for the shareholder by each share, based on the market price per share	Higher