Table 17.2	Ratios and Formulae at a Glance

Ratio	*Formula*
1. Liquidity Ratios	
(a) Current ratio (Standard 2:1)	Current assets/Current liabilities
(b) Quick ratio or Acid test ratio (Standard 1:1)	Quick Assets/Current liabilities where Quick assets = Current assets – (closing stock + Prepaid expenses)
2. Activity Ratios	
(a) Inventory turnover ratio$^{\phi}$	(Cost of goods sold/Average inventory)
(b) Debtors' turnover ratio$^{\phi}$	(Credit sales/Average debtors)
(c) Creditors' turnover ratio$^{\phi}$	(Credit purchases/Average creditors)
3. Solvency Ratios	
(a) Debt-Equity ratio (standard 1:1)	(Outsiders' funds/Insiders' funds)
(b) Interest coverage ratio$^{\phi}$	(EBIT/Fixed interest charges)
(c) Proprietors' funds to total assets ratio (0.5:1)	(Proprietors' funds/Total assets)
(i) Ratio of fixed assets to proprietors' funds (65%)	(Tangible fixed assets/proprietors' funds) × 100
(ii) Ratio of current assets to proprietors' funds (35%)	(Current assets/Proprietors' funds) × 100
4. Profitability Ratios	
(a) Gross profit Ratio$^{\phi}$	(Gross profit/Sales) × 100
(b) Net profit ratio$^{\phi}$	(Net profit/Sales) × 100
(c) Operating ratio$^{\blacklozenge}$	(Operating expenses/Net sales) × 100
(d) Return on investment (ROI)$^{\phi}$	(Net profit after taxes/Total investment)
(i) Return on assetsf	(Net profit after taxes/Total tangible assets
(ii) Return on capital employed$^{\phi}$	(Adjusted net profits/Capital employed)
(e) Earnings per share (EPS)$^{\phi}$	(Net profit after Taxes/No. of shares outstanding)
(f) Dividend yield$^{\phi}$	$\dfrac{\text{Nominal value of share}}{\text{Market prie of the share}} \times$ Dividend per share (%)
(g) Price/earnings ratio (P/E ratio)$^{\phi}$	(Market price /Earnings per share)
(i) Earning power$^{\phi}$	Net profit margin × Investment turnover

$^{\phi}$ Should be as high as possible

$^{\blacklozenge}$ Should be as low as possible