Ratio Analysis Wrap-up!

So Many Ratios!

LIQUIDITY

Current Ratio

Quick Ratio

WORKING CAPITAL

Days Sales Outstanding

Inventory Turnover Ratio

FINANCIAL LEVERAGE

Debt Ratio

Debt / Equity Ratio

Interest Coverage Ratio

Times-Interest-Earned Ratio

PROFITABILITY

Gross Margin

Operating Margin

Net Margin

INVESTMENT-BASED

Return on Equity

Return on Assets

Return on Invested Capital

Revenues per Employee

MARKET VALUE

Earnings per Share

Price to Earnings Ratio

Book Value

Market to Book Ratio

Here are 4 Important Ones for a Quick Look…

LIQUIDITY

Current Ratio

Quick Ratio

WORKING CAPITAL

Days Sales Outstanding

Inventory Turnover Ratio

FINANCIAL LEVERAGE

Debt Ratio

Debt / Equity Ratio

Interest Coverage Ratio

Times-Interest-Earned Ratio

PROFITABILITY

Gross Margin

Operating Margin

Net Margin

INVESTMENT-BASED

Return on Equity

Return on Assets

Return on Invested Capital

Revenues per Employee

MARKET VALUE

Earnings per Share

Price to Earnings Ratio

Book Value

Market to Book Ratio

Here are 4 Important Ones for a Quick Look…

LIQUIDITY ***Current Ratio***	*If greater than 1, the company is in good shape in handling its near-term debt payments.*
WORKING CAPITAL ***Days Sales Outstanding***	*If consistently less than the payment terms (30 or 60 days), the company is collecting on its Accounts Receivables (e.g., customers are paying on time).*
FINANCIAL LEVERAGE ***Debt / Equity Ratio***	*If consistently less than ratio less than 1 indicates the company is not over-leveraged; it is using its debt effectively without relying on too much of it.*
PROFITABILITY ***Gross Margin***	*If gross margins are better than industry averages and increasing, the company is improving manufacturing efficiency and/or able to charge a higher price than the competition.*

Financial Ratio Analysis…

What should you really do with all of these?

Comparison: evaluate the ratios from one financial period to the next (quarter to quarter, year to year).

- Is the ratio increasing? Decreasing? Why?
- What is the trend over time? Increasing? Decreasing? Why?
- The answer is usually in the 10-K Filing, buried in the fine print.

Benchmarking: evaluate the ratios for one company, then compare them to the company's competitors.

- Is the ratio higher? Lower? Why?
- The answer is this one is much harder to find and often based on your own assessment of what is happening in each company.

Main Takeaways…

There are many ratios (so many!); understanding what they mean and how they characterize a company’s financial performance enables managers to pinpoint what needs attention, and they allow investors to determine whether the company is indeed a good investment or not.

Financial ratios are grouped into several categories:

- ✓ Liquidity Ratios – can the company pay the bills?
- ✓ Working Capital Management Ratios – how well does the company manage its operations?
- ✓ Profitability Ratios - is the company making enough money?
- ✓ Financial Leverage Ratios - is the company carrying too much debt?
- ✓ Investment Ratios - is the company achieving a good return on its investments?
- ✓ Market Value Ratios - is the company a good investment?

We can learn a lot about a company by comparing these financial ratios from one year to the next, and by comparing the company’s ratios to others in its industry.

Next Time…

Budgeting and Forecasting

Credits & References

Slide 1: Ratio Analysis – Statistics/Business. Laptop in the office with term on the Screen by MQ-Illustrations, Adobe Stock (331061495.jpeg).

Slide 8: Budget Planning by onephoto, Adobe Stock (112904496.jpeg).