# Liquidity ratios

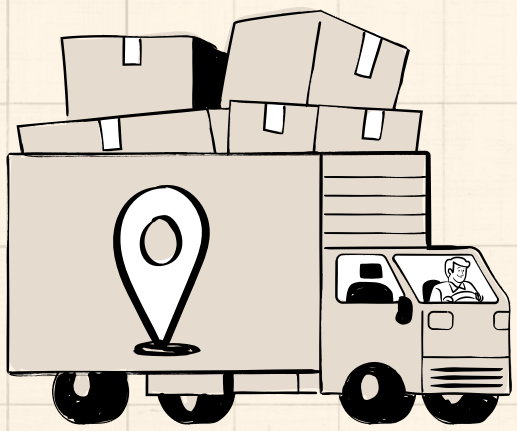
*Jyoti Barik*

# Current Ratio

This ratio measures a company's ability to pay its short-term liabilities(payable within one year) with its overall current assets, such as cash, accounts receivable, inventories, etc.

A ratio above 1 indicates the company can cover its obligations.

$$\textit{Current Ratio} = \frac{\textit{Current Assets}}{\textit{Current Liabilities}}$$



# Quick Ratio
# (Acid-Test Ratio)

The quick ratio provides a more conservative view of company's ability to meet its short-term obligations with its most liquid  assets, thus excluding inventories from the current assets.

$$Quick\ Ratio = \frac{Current\ Assets - Inventory}{Current\ Liabilities}$$

# Cash Ratio
# (Absolute liquid ratio)

The absolute liquid / cash ratio is the most conservative liquidity ratio. It only considers cash and cash equivalents against current liabilities.

Generally, the higher the ratio, the better equipped the firm is to face disastrous events. However, a very high ratio may suggest the company is holding too much cash and could be missing out on investment opportunities.

$$\textit{Cash Ratio} = \frac{\textit{Cash/bank + Marketable securities}}{\textit{Current Liabilities}}$$

Liquidity ratios indicate financial flexibility and cash flow strength—higher ratios suggest strong solvency, while lower ones may signal liquidity stress.

Therefore, liquidity ratios must be interpreted in context — alongside industry standards, company size, and trend analysis — to draw meaningful conclusions about short-term financial strength and working capital efficiency.

*Jyoti Barik*