Q3. What relationships will be established to study:
a. Inventory Turnover
b. Trade Receivables Turnover
c. Trade Payables Turnover
d. Working Capital Turnover
Solution:
a. Inventory Turnover Ratio: This ratio is computed to ascertain the competence with which the stock is used. This ratio is based on the relationship between cost of goods sold and average stock kept during the year.

$$\text{Inventory/Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Stock}}$$

Cost of Goods Sold = Opening Stock + Purchases + Direct Expenses - Closing Stock

Or, Cost of Goods Sold = Net Sales - Gross Profit

$$\text{Average Stock} = \frac{\text{Opening Stock} + \text{Closing Stock}}{2}$$

b. Debtors Turnover Ratio or Trade Receivables Turnover Ratio: This ratio is computed to ascertain the pace at which the amount is collected from debtors. It establishes the relationship between net credit sales and average accounts receivables.

$$\text{Debtors Turnover Ratio} = \frac{\text{Net Credit Sales}}{\text{Average Accounts Receivables}}$$

Net Credit Sales = Total Sales - Cash Sales

Average Accounts Receivebles

$$= \frac{(\text{Opening Debtors} + \text{Opening Bills Receivables}) + (\text{Closing Debtors} + \text{Closing Bills Receivables})}{2}$$

c. Trade Payables Turnover Ratio: It is also known as Creditors Turnover Ratio. It is computed to determine the pace at which the amount is paid to creditors. It determines the relationship between net credit purchases and average accounts payables.

$$\text{Payable Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Accounts Payable}}$$

Net Credit Purchases = Total Purchases - Cash Purchases

Average Accounts Payable =

$$\frac{(\text{Opening Creditors} + \text{Opening Bills Payables}) + (\text{Closing Creditors} + \text{Closing Bills Payables})}{2}$$

d. Working Capital Turnover Ratio: This ratio is computed to determine how competently the working capital is employed in making sales. It determines the relationship between net sales and working capital.

$$\text{Working Capital Turnover Ratio} = \frac{\text{Net Sales}}{\text{Working Capital}}$$

Net Sales = Total Sales - Sales Return

Working Capital = Current Assets - Current Liablities

*********** END **********