Financial Ratio Formulas Checklist

General Notes

Key financial ratios help you to interpret financial information in a way that gives you a valuable insight how well an organization is managed at the highest level. To perform the calculations you will need to have access to:

- Income Statements
- Balance Sheets
- Cash Flow statements
- Statements of Retained Earnings

Performance Financial Ratios - there are several ratios that you can use to measure how an organization is performing in terms of both profitability and efficiency. You will use the details from the balance sheet.

Gearing

= Total Borrowings *divided by* Net Worth

No. of Days Credit Granted

= Sum of (Trade Debtors *divided by* Annual Sales) *multiplied by* 365 days

No. of Days Credit Taken

= Sum of (Trade Creditors *divided by* Annual Purchases) *multiplied by* 365 days

Stock Turnover

= Cost of Goods Sold *divided by* Average Stock Value

Operating Expenses as a % of Turnover

= Operating Expenses *divided by* Net Profit

Solvency Financial Ratios - you will use the balance sheet details to assess the ‘liquidity’ of an organization by looking at the relationship between current assets and current liabilities. Current in this instance means within twelve months.

Current Ratio

= Current Assets *divided by* Current Liabilities

Quick Ratio or Acid Test Ratio

= Sum of (Current Assets *less* Stock) *divided by* Current Liabilities

PROFITABILITY FINANCIAL RATIOS – you will use the income statement details to assess profitability by comparing profit as a percentage of sales or assets.

Gross Profit Margin

= Gross Profit *divided by* Turnover

Net Profit Margin

= Net Profit *divided by* Total Sales

Return on Assets

= Net Assets *divided by* Net Profit

INVESTMENT POTENTIAL FINANCIAL RATIOS - They are concerned with the return on investment for shareholders, and with the relationship between return and the value of an investment in a company's shares.

Price to Earnings Ratio or P/E Ratio

= Current Share Price *divided by* Earnings per Share (EPS)

Price-to-Book Ratio or P/B Ratio

= Stock Price *divided by* Book Value of Equity

Price/Earnings to Growth or PEG Ratio

= Price /Earnings ratio *divided by* Annual Earnings per Share (EPS) growth

Dividend Yield

= Dividend per Share *divided by* Price per Share

NOTE:

Whilst you can compare the ratios of organizations in different industries is usually of limited value because of differences in market conditions, capital requirements and competition.

The trend over time is often more revealing than one figure in isolation and that comparisons between industries may not be very useful.

You must have a clear understanding of what the organization actually does and the industry it operates in before you draw any conclusions from these ratios.