

all accounting ratios formulas

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All Accounting Ratios Formulas: A Complete Guide for Finance Professionals

In today's fast moving business environment, financial analysis is more critical than ever. Whether you're a seasoned CFO, a budding analyst, or a student preparing for an exam, you'll quickly discover that a deep understanding of accounting ratios is essential for making informed decisions. This article will walk you through **all accounting ratios formulas**, breaking them down into digestible categories, explaining how to calculate them, and highlighting what each metric tells you about a company's financial health.

We'll cover the most widely used ratios—liquidity, solvency, profitability, efficiency, and market performance—along with the formulas you need to master. By the end, you'll be able to build a robust financial model, benchmark a company against peers, and spot potential red flags before they become crises.

Why Ratios Matter: The Power of Numbers

Ratios condense complex financial statements into single, actionable numbers. They provide a snapshot of a company's performance, allowing investors, creditors, and managers to compare companies of different sizes, industries, and time periods. While each ratio offers unique insights, together they paint a comprehensive picture of financial stability, operational efficiency, and profitability.

Liquidity Ratios: Measuring Short Term Health

Liquidity ratios assess a company's ability to meet its short term obligations. These ratios are especially important for creditors and investors evaluating a firm's risk profile.

Current Ratio

The current ratio measures the ability to cover short term liabilities with short term assets.

Formula: $\text{Current Ratio} = \text{Current Assets} \div \text{Current Liabilities}$

Example: If a company has \$500,000 in current assets and \$300,000 in current liabilities, its current ratio is 1.67.

Quick Ratio (Acid Test Ratio)

Also known as the acid test ratio, it refines the current ratio by excluding inventory, which may not be quickly liquidated.

Formula: $\text{Quick Ratio} = (\text{Current Assets} - \text{Inventory}) \div \text{Current Liabilities}$

Example: With \$500,000 in current assets, \$200,000 in inventory, and \$300,000 in current liabilities, the quick ratio is 1.00.

Cash Ratio

The most conservative liquidity metric, it only considers cash and cash equivalents.

Formula: $\text{Cash Ratio} = \text{Cash \& Cash Equivalents} \div \text{Current Liabilities}$

Example: If a firm holds \$150,000 in cash and has \$300,000 in current liabilities, the cash ratio is 0.50.

Solvency Ratios: Evaluating Long Term Viability

Solvency ratios gauge a company's capacity to meet long term obligations and assess financial leverage.

Debt to Equity Ratio

Measures the proportion of debt used to finance assets relative to shareholders' equity.

Formula: *Debt to Equity Ratio = Total Debt ÷ Total Equity*

Example: With \$800,000 in debt and \$400,000 in equity, the ratio is 2.0.

Debt Ratio

Shows the percentage of assets financed by debt.

Formula: *Debt Ratio = Total Debt ÷ Total Assets*

Example: If total assets are \$1,200,000 and debt is \$800,000, the debt ratio is 0.67.

Interest Coverage Ratio

Assesses a company's ability to pay interest on its debt.

Formula: *Interest Coverage Ratio = EBIT ÷ Interest Expense*

Example: EBIT of \$250,000 and interest expense of \$50,000 yields a ratio of 5.0.

Profitability Ratios: Measuring Earnings Power

Profitability ratios reveal how effectively a company generates profit from its revenue, assets, and equity.

Gross Profit Margin

Shows the percentage of revenue remaining after deducting the cost of goods sold.

Formula: *Gross Profit Margin = (Revenue – Cost of Goods Sold) ÷ Revenue*

Example: Revenue of \$1,000,000 and COGS of \$600,000 gives a margin of 0.40 (40%).

Operating Profit Margin

Measures earnings before interest and taxes (EBIT) as a percentage of revenue.

Formula: *Operating Profit Margin = EBIT ÷ Revenue*

Example: EBIT of \$200,000 on \$1,000,000 revenue equals 0.20 (20%).

Net Profit Margin

Shows the percentage of revenue that turns into net income.

Formula: *Net Profit Margin = Net Income ÷ Revenue*

Example: Net income of \$120,000 on \$1,000,000 revenue equals 0.12 (12%).

Return on Assets (ROA)

Assesses how efficiently a company uses its assets to generate profit.

Formula: $ROA = \text{Net Income} \div \text{Total Assets}$

Example: Net income of \$120,000 and assets of \$1,200,000 equals 0.10 (10%).

Return on Equity (ROE)

Measures the return on shareholders' capital.

Formula: $ROE = \text{Net Income} \div \text{Shareholders' Equity}$

Example: Net income of \$120,000 and equity of \$400,000 yields 0.30 (30%).

Return on Capital Employed (ROCE)

Evaluates profitability relative to all capital invested (debt and equity).

Formula: $ROCE = EBIT \div (\text{Total Assets} - \text{Current Liabilities})$

Example: EBIT of \$200,000 and net assets of \$800,000 gives 0.25 (25%).

Efficiency Ratios: Assessing Operational Effectiveness

Efficiency ratios examine how well a company uses its resources and manages its operations.

Inventory Turnover

Indicates how many times inventory is sold and replaced during a period.

Formula: $\text{Inventory Turnover} = \text{Cost of Goods Sold} \div \text{Average Inventory}$

Example: COGS of \$600,000 and average inventory of \$120,000 equals 5.0.

Days Inventory Outstanding (DIO)

Shows the average number of days inventory is held before sale.

Formula: $DIO = 365 \div \text{Inventory Turnover}$

Example: Inventory turnover of 5.0 results in 73 days.

Accounts Receivable Turnover

Measures how quickly a company collects cash from credit sales.

Formula: $\text{Accounts Receivable Turnover} = \text{Net Credit Sales} \div \text{Average Accounts Receivable}$

Example: Net credit sales of \$800,000 and average receivables of \$80,000 yields 10.0.

Days Sales Outstanding (DSO)

Average number of days to collect receivables.

Formula: $DSO = 365 \div \text{Accounts Receivable Turnover}$

Example: Turnover of 10.0 results in 36.5 days.

Accounts Payable Turnover

Shows how quickly a company pays its suppliers.

Formula: $\text{Accounts Payable Turnover} = \text{COGS} \div \text{Average Accounts Payable}$

Example: COGS of \$600,000 and average payables of \$60,000 yields 10.0.

Days Payable Outstanding (DPO)

Average number of days the company takes to pay its suppliers.

Formula: $DPO = 365 \div \text{Accounts Payable Turnover}$

Example: Turnover of 10.0 gives 36.5 days.

Asset Turnover

Assesses how efficiently a company uses its assets to generate revenue.

Formula: $\text{Asset Turnover} = \text{Revenue} \div \text{Average Total Assets}$

Example: Revenue of \$1,000,000 and average assets of \$1,200,000 yields 0.83.

Market Ratios: Gauging Investor Perceptions

Market ratios are used by investors to evaluate a company's market value relative to its financial performance.

Earnings Per Share (EPS)

Net income divided by the number of outstanding shares.

Formula: $EPS = \text{Net Income} \div \text{Shares Outstanding}$

Example: Net income of \$120,000 and 50,000 shares yields \$2.40 per share.

Price to Earnings (P/E) Ratio

Shows how much investors are willing to pay per dollar of earnings.

Formula: $P/E \text{ Ratio} = \text{Market Price per Share} \div EPS$

Example: Stock price of \$48 and EPS of \$2.40 gives a P/E of 20.

Price to Book (P/B) Ratio

Compares market value to book value.

Formula: $P/B \text{ Ratio} = \text{Market Price per Share} \div \text{Book Value per Share}$

Example: Market price of \$48 and book value of \$12 per share results in 4.0.

Dividend Yield

Shows the return on investment from dividends.

Formula: $\text{Dividend Yield} = \text{Annual Dividends per Share} \div \text{Market Price per Share}$

Example: Dividends of \$1.20 and price of \$48 yield 0.025 (2.5%).

Return on Market Value (ROMV)

Measures how well the market capitalizes on company earnings.

Formula: $ROMV = (\text{Annual Dividends} + \text{Change in Stock Price}) \div \text{Market Capitalization}$

Example: Annual dividends of \$1.20, price change of \$3.00, and market cap of \$2,400,000 gives 0.0025 (0.25%).

Putting It All Together: A Practical Example

Let's walk through a real world scenario. Suppose you're analyzing a mid size manufacturing firm, *Acme Industries*, with the following key figures:

- Current Assets: \$1,200,000
- Current Liabilities: \$800,000
- Inventory: \$300,000
- Cash & Cash Equivalents: \$200,000
- Total Debt: \$1,000,000
- Total Equity: \$600,000
- Total Assets: \$1,800,000
- Revenue: \$3,000,000
- Cost of Goods Sold: \$1,800,000
- Operating Income (EBIT): \$600,000

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