

COMMONLY USED FINANCIAL RATIOS

These are the 15 most commonly used financial ratios and concepts, along with the formulas for calculating them, how they are used, and examples of good performance. This tool is particularly useful for leaders who do not have a financial background but need to understand financial yardsticks.

| Ratio | Formula | Comments |
|----------------------------------|---|---|
| Current | current assets/ current liabilities | Measures cash reserves; 2 is solid; varies by industry. |
| Quick | current assets minus inventory/ current liabilities | Indicates what a company can realize in cash right away; 1 is solid. |
| EBITA | earnings minus interest, taxes and amortization. | Indicates underlying financial performance by stripping away non-revenue based factors. |
| Debt to assets | long-term debt/total assets | Measures relative security of current debt; .33 is good. |
| Debt to equity | total debt/total equity | Provides insight into company's financial strategy. |
| Leverage | total assets/ stockholders equity | Shows how many assets each dollar of equity supports. |
| Inventory turnover | total sales/ total value of inventory | Measures how much money is tied up in inventory. |
| Average collection period | accounts receivable/ sales per day | Use to assess collection policies and procedures; if terms are net 30, then 30 to 40 is good. |
| Sales to fixed assets | sales/assets | Shows sales efficiency; must be compared to industry average. |

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| Profit margin on sales | net income/total sales | Shows profit efficiency; must be compared to industry average. |
| Return on Equity | net income/ stockholders equity | Shows yield to investors; 15 percent considered good. |
| Return on total assets | a) net income/total assets b) net income + after tax interest/total assets | Shows yield on assets; second formula (b) perhaps more accurate because total assets include debt. |
| Return on investment | net income/ shareholders equity | Same as return on equity. |
| Price to cash flow | stock price per share/ cash flow per share | Evaluates stock performance; sum of net income and depreciation can be used to compute cash flow. |
| Price/earnings ratio (also known as P/E) | price per share/ earnings per share | Evaluates stock performance; must be compared with industry, stock market, and company history. |