## Quick Revision Notes

### ACCOUNTING RATIOS

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<th>I. LIQUIDITY RATIOS</th>
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<tr>
<td><strong>A. Current Ratio</strong></td>
<td><strong>A. Debt to Equity Ratio</strong></td>
<td><strong>A. Inventory Turnover Ratio</strong></td>
<td><strong>A. Gross Profit Ratio</strong></td>
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<tr>
<td>Current Assets</td>
<td>Long Term Debt</td>
<td>Cost of Good Sold</td>
<td>Gross Profit X100</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>Shareholders’ Fund</td>
<td>Average Inventory (at cost)</td>
<td>Net Sales</td>
</tr>
<tr>
<td>Current assets are</td>
<td>Long term loans refer to</td>
<td>Cost of Goods Sold = Opening Stock + All Direct Expenses i.e. (Purchases +</td>
<td>Gross Profit = Net Sales</td>
</tr>
<tr>
<td>those which can be converted into cash</td>
<td>Long term obligations which have to be paid after 1 Year.</td>
<td>Carriage + Wages + Other Direct Expenses) – Closing Stock.</td>
<td>Cost of Goods Sold</td>
</tr>
<tr>
<td>Within one year.</td>
<td>Long Term Debt = Debentures + Mortgage Loan + Bank Loan + Loan</td>
<td>Average Stock / Inventory</td>
<td>Cost of Goods Sold = Opening Stock + Purchases + All Direct Expenses – Closing Stock</td>
</tr>
<tr>
<td>Current Assets = Cash + Bank + Stock (Raw Material + Work in Progress + Finished Goods)</td>
<td>From financial institution + Public Deposit</td>
<td>= Opening Stock + Closing Stock/2</td>
<td>Higher the ratio, better it is, as it implies efficient Management of Inventories.</td>
</tr>
<tr>
<td>+ Debtors (Less Provision)</td>
<td>Shareholder’s Funds = Equity Share Capital + Preference Share Capital + Share Premium + Capital Reserve + General Reserve + Other Reserves</td>
<td>Higher the ratio, better it is, as it implies efficient Management of Inventories.</td>
<td><strong>B. Operating Ratio</strong></td>
</tr>
<tr>
<td>+ Bills Receivable + Short Term Investments (Marketable Securities)</td>
<td>+ Profit and Loss A/c (Credit Balance) - Accumulated Losses - Fictitious Assets.</td>
<td><strong>B. Debtors Turnover Ratio</strong></td>
<td>Operating Cost &amp; Operating Expenses X100</td>
</tr>
<tr>
<td>+ Prepaid Expenses</td>
<td>Or Shareholders’ Funds = Total assets – Total debt.</td>
<td>Net Credit Sales / Average Debtors + Average Receivables</td>
<td>Net Sales</td>
</tr>
<tr>
<td>+ Loans &amp; Advances + Accrued Incomes</td>
<td>Or Shareholders fund = Capital employed – Long Term debt</td>
<td>Higher the ratio, better it is, since it indicates that Debts are being collected more quickly</td>
<td></td>
</tr>
<tr>
<td>Note: Debtors due within six months are to be included</td>
<td></td>
<td><strong>C. Creditors Turnover Ratio</strong></td>
<td>Cost of Goods Sold + Operating Expenses X100</td>
</tr>
<tr>
<td>In current assets. Current Liabilities = Creditors + Bills Payable + Outstanding Expenses</td>
<td></td>
<td>Net Credit Purchases = Average Payables + Average Creditors</td>
<td>Net Sales</td>
</tr>
<tr>
<td>+ Bank Overdraft</td>
<td></td>
<td></td>
<td>Operating expenses includes all administrative expenses.</td>
</tr>
<tr>
<td>+ Accrued Expenses</td>
<td></td>
<td></td>
<td>Lower the ratio, better it is, which leaves a high margin of profit to meet other non operating expenses.</td>
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<tr>
<td>+ Provisions for Taxation</td>
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</tbody>
</table>
# I. LIQUIDITY RATIOS

- A year + Un-expired Income.
- Current Ratio of 2:1 is considered an ideal ratio.

### B. Liquid Ratio

**LIQUID Assets**

Current Liabilities

Liquid Assets = Cash + Bank + Debtors + Bill Receivable + Short term Investment + marketable Securities and Short term Loans and advances

Or

Liquid Assets = Current Assets – Stock – Prepaid Expenses

Liquid ratio of 1:1 is said to be satisfactory.

# II. SOLVENCY RATIO

- Debt Equity Ratio of 2:1 is considered safe.
- **B. Total Assets to Debt Ratio**
  - Total Assets
  - Long Term Loan
  - Total Assets or Fixed Assets are net of Depreciation.
  - Higher are ratio, Better it is, which implies profitable situation of a business concern.

# III. ACTIVITY RATIOS

- **C. Proprietary Ratio**
  - Shareholders’ Funds
  - Total Assets
  - It shall be taken as safe if it is above 50 percent.
  - Total Assets = Net fixed assets + Investment + current assets
  - Or = Debts + Shareholders’ fund + current liabilities
  - Or = Capital employed + current liabilities

- **D. Working Capital Turnover Ratio**
  - Net Working Capital
  - Working capital is the Excess of current assets Over current liabilities. Higher the ratio, better it Is. As it shows that Working capital is being Utilized efficiently in Making sales.

- **E. Fixed Assets Turnover Ratio**
  - Net Sales
  - = Net Fixed Assets
  - Higher the ratio, better it is,
  - It shows that fixed assets are being utilized efficiently In making sales.

- **F. Current Assets Turnover Ratio**
  - Net Sales
  - = Current Assets
  - Higher the ratio, better it is,
  - As it indicates optimum Utilization of Current Assets.

# IV. PROFITABILITY RATIO

- **C. Net Profit Ratio**
  - Net Profit
  - = x 100
  - Net Sales
  - Higher the ratio, better it is,
  - As it indicates efficiency of the business enterprise.

- **D. Return on Investment**
  - Profit Before Interest, Tax and Dividend
  - X100
  - Capital Employed
  - Higher the ratio, better it is,
  - As it indicates how Economically and Efficiently funds are being Utilized by the business Enterprise.

- **E. Earning Per Share**
  - Net Profit after interest Tax & Preference dividend
  - Number of Equity Shares
  - Higher the ratio better it is.

- **F. Dividend Per Share**
  - Dividend Paid to Equity Shareholders
  - Number of Equity Shares
  - Higher the ratio, better it is.

- **G. Price Earning Ratio**
  - Market Price Per Share
  - Earning Per Share
  - Higher the ratio, better it is,
I. LIQUIDITY RATIO
II. SOLVENCY RATIO
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As it indicates growth and Good earning of the Company.

H. Earning Yield Earning Per Share Market Price Per Share Higher the ratio better it is.