IDAL
INVEST IN LEBANON

UNDERSTAND YOUR FINANCIALS

DIFFERENT FINANCIAL RATIOS & THEIR ANALYSIS

BSU BUSINESS SUPPORT UNIT

CALCULATING YOUR GROSS PROFIT

Gross profit is what's left when the cost of goods sold are subtracted from sales. It is the difference between what you bought your product for and what you sold it for, and can indicate whether you are pricing your product or service correctly.

Calculating your gross profit is part of completing your profit and loss statement.

Gross profit = Total Sales minus Cost of Goods Sold.

Calculating your gross profit margin is important as it shows that your sales are sufficient to cover your costs. The gross profit margin ratio shows the proportion of profit for each sales dollar before expenses have been paid.

Gross profit margin = Gross Profit / Sales: 1.0

An acceptable gross profit margin ratio varies from industry to industry but in general the higher the margin the better. To improve your gross profit margin, you can increase your prices or reduce the costs of producing or acquiring your goods (or both). Increasing your prices can impact your sales revenue however, so you need to consider this carefully.

LIQUIDITY RATIOS

Liquidity ratios measure a company's ability to meet its maturing short-term obligations. In other words, can a company quickly convert its assets to cash without a loss in value if necessary to meet its short-term obligations?

Current Ratio
Current Assets / Current Liabilities
This ratio reflects the number of times short-term assets cover short-term liabilities and is a fairly accurate indication of a company›s ability to service its current obligations. A high number indicates a strong ability to service short-term obligations.

Quick Ratio
(Cash + Marketable Securities + Trade Accounts Receivable) / Current Liabilities
This ratio, also known as the acid test ratio, measures immediate liquidity - the number of times cash, accounts receivable, and marketable securities cover short-term obligations. A high number suggests a company has a strong ability to service short-term obligations.

Accounts Receivable to Working Capital
Trade Accounts Receivable / (Current Assets - Current Liabilities)
This ratio measures the dependency of working capital on the collection of receivables. A low number indicates that a company has a satisfactory level of working capital and accounts receivable makes up an appropriate portion of current assets.

Inventory to Working Capital
Inventory / (Current Assets - Current Liabilities)
This ratio measures the dependency of working capital on inventory. A low number for this ratio is preferred indicating that a company has a satisfactory level of working capital and inventory makes up a reasonable portion of current assets.

Long Term Liabilities to Working Capital
Long Term Liabilities / (Current Assets - Current Liabilities)
This ratio measures the degree to which a company's long-term debt has been used to replenish working capital versus fixed asset acquisition.

Sales to Working Capital
Sales / (Current Assets - Current Liabilities)
This ratio measures a company's ability to finance current operations. Working capital (current assets - current liabilities) is another measure of liquidity and the ability to cover short-term obligations. A low number is indicates that a company has a satisfactory level of working capital.

ACTIVITY RATIOS

Activity ratios provide a useful gauge of a company's operations by determining, for example, the average number of days it takes to collect on customer accounts and the average number of days to pay vendors.

Accounts Receivable Turnover
Sales / Trade Accounts Receivable
This ratio measures the number of times receivables turn over in a year and reveals how successful a company is in collecting its outstanding receivables.

Days Sales in Receivables
Trade Accounts Receivable / (Sales / Days)
This ratio measures the average number of days a company's receivables are outstanding. A lower number of days is desired. Companies should attempt to reduce the number of days sales in receivables in order to increase cash flow. The general rule used is that the time allowed for payment by the selling terms should not be exceeded by more than 10 or 15 days.

Operating Cycle Days
(Inventory / (Cost of Sales / Days)) + (Trade Accounts Receivable / (Sales / Days))
This ratio calculates the total conversion period for a company, or in other words, the average number of days it takes to convert inventory into cash from sales. It is calculated by adding together the days cost of sales in inventory to the days sales in receivables.

Sales to Assets
Sales / Total Assets
This ratio measures a company's ability to produce sales in relation to total assets to determine the effectiveness of the company's asset base in producing sales. A high number indicates that a company is using its assets to successfully generate sales.

Sales to Net Fixed Assets
Sales / (Property and Equipment - Accumulated Depreciation)
This ratio measures a company's ability to effectively utilize its fixed assets to generate sales. This ratio is similar to the sales to assets ratio, but it excludes current assets, long-term investments, intangible assets, and other non-current assets. A high number indicates that a company productively uses its fixed assets to produce sales.

Net Fixed Assets to Equity
(Property and Equipment - Accumulated Depreciation) / Total Equity
This ratio measures the extent to which investors' capital was used to finance productive assets. A lower ratio indicates a proportionally smaller investment in fixed assets in relation to net worth, which is desired by creditors in case of liquidation.

PROFITABILITY RATIOS

Profitability ratios measure a company's ability to use its capital or assets to generate profits. Improving profitability is a constant challenge for all companies and their management.

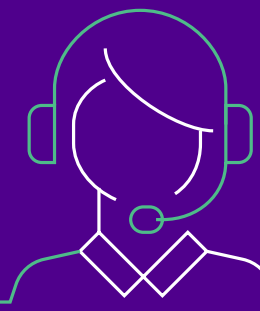
COVERAGE RATIOS

Coverage ratios assess a company's ability to meet its long-term obligations, remain solvent, and avoid bankruptcy. It measures how well a company's cash flow covers its short-term financial obligations.

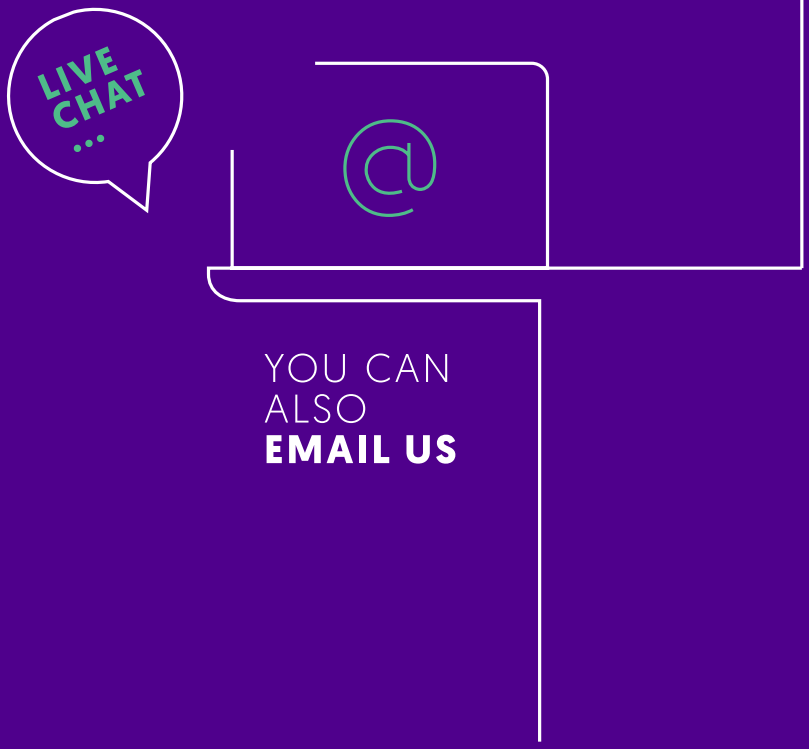
Debt to Total Assets Total Liabilities / Total Assets
This ratio measures what proportion of debt a company is carrying relative to its assets. A ratio value greater than one indicates a company has more debt than assets. Naturally, companies and creditors prefer a lower number.

Debt to Equity
Total Liabilities / Total Equity
This ratio measures the financial leverage of a company by indicating what proportion of debt and equity a company is using to finance its assets. A lower number suggests there is both a lower risk involved for creditors and strong, long-term, financial security for a company.

CONTACT US



THROUGH OUR **BSU COORDINATOR**



YOU CAN ALSO **EMAIL US**

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