

Ratio	Method of Calculation	Significance of each ratio
<b><u>Profitability Ratios</u></b>		
Return on total assets	$\frac{\text{Operating Profit before Tax + Interest Expense}}{\text{Average Total Assets}}$	Measures the rate of return earned through operating total assets provided by both creditors and owners.
Profit Margin	$\frac{\text{Operating Profit}}{\text{Net Sales}}$	Measures net profitability of each dollar of sales.
<b><u>Liquidity Ratios</u></b>		
Current ratio	$\frac{\text{Current Assets}}{\text{Current Liabilities}}$	A measure of short-term liquidity.
Quick ratio	$\frac{\text{Cash at Bank + Marketable Security + Net Receivables}}{\text{Current Liabilities}}$	A more rigorous measure of short-term liquidity.
Receivables turnover	$\frac{\text{Net Sales}}{\text{Average Receivables Balance}}$	Measures the effectiveness of collections.
Average collection period	$\frac{\text{Average Receivables} \times 365}{\text{Net Sales}}$	Measures the average number of days taken to collect receivables.
Inventory turnover	$\frac{\text{Cost of Goods Sold}}{\text{Average Inventory Balance}}$	Indicates the liquidity of inventory. Measures the number of times inventory was sold on average during the period.
<b><u>Financial Stability Ratios</u></b>		
Debt Ratio	$\frac{\text{Total Liabilities}}{\text{Total Assets}}$	Measures percentage of assets provided by creditors.
Equity Ratio	$\frac{\text{Total Owner Equity}}{\text{Total Assets}}$	Measures percentage of assets provided by the owner.
Asset Turnover Ratio	$\frac{\text{Net Sales}}{\text{Average Total Assets}}$	Measures the effectiveness of the business use of assets during the period
Times Interest Earned	$\frac{\text{Operating Profit before Tax + Interest Expense}}{\text{Interest Expense}}$	Measures the ability of the business to meet its interest payments.

Brought to you by:

[www.how-to-start-a-small-business.com](http://www.how-to-start-a-small-business.com)