Ratio analysis—the foundation of fundamental analysis—helps to gain a deeper insight into the financial health and the current and probable performance of the company being studied. For this insight, the analysts use the quantitative method where the information recorded in the company’s financial statements are compared and analyzed. And there are certain formulae that are used for the same.

Liquidity Ratios

Also known as Solvency Ratios, and as the name indicates, it focuses on a company’s current assets and liabilities to assess if it can pay the short-term debts. The three common liquidity ratios used are current ratio, quick ratio, and burn rate. Among the three, current ratio comes in handy to analyze the liquidity and solvency of the start-ups.

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| --- | --- | --- |
| **S. No.** | **RATIOS** | **FORMULAS** |
| 1 | Current Ratio | Current Assets/Current Liabilities |
| 2 | Quick Ratio | Liquid Assets/Current Liabilities |
| 3 | Absolute Liquid Ratio | Absolute Liquid Assets/Current Liabilities |

Profitability Ratios

These ratios analyze another key aspect of a company and that is how it uses its assets and how effectively it generates the profit from the assets and equities. This also then gives the analyst information on the effectiveness of the use of the company’s operations.

|  |  |  |
| --- | --- | --- |
| **S. No.** | **RATIOS** | **FORMULAS** |
| 1 | Gross Profit Ratio | Gross Profit/Net Sales X 100 |
| 2 | Operating Cost Ratio | Operating Cost/Net Sales X 100 |
| 3 | Operating Profit ratio | Operating Profit/Net Sales X 100 |
| 4 | Net Profit Ratio | Operating Profit/Net Sales X 100 |
| 5 | Return on Investment Ratio | Net Profit After Interest  And Taxes/ Shareholders Funds or Investments  X 100 |
| 6 | Return on Capital Employed Ratio | Net Profit after Taxes/ Gross Capital Employed X 100 |
| 7 | Earnings Per Share Ratio | Net Profit After Tax & Preference Dividend /No of Equity Shares |
| 8 | Dividend Pay Out Ratio | Dividend Per Equity Share/Earning Per Equity Share X 100 |
| 9 | Earning Per Equity Share | Net Profit after Tax & Preference Dividend / No. of Equity Share |
| 10 | Dividend Yield Ratio | Dividend Per Share/ Market Value Per Share X 100 |
| 11 | Price Earnings Ratio | Market Price Per Share Equity Share/ Earning Per Share X 100 |
| 12 | Net Profit to Net Worth Ratio | Net Profit after Taxes / Shareholders Net Worth X 100 |

Working Capital Ratios

Like the Liquidity ratios, it also analyses if the company can pay off the current debts or liabilities using the current assets. This ratio is crucial for the creditors to establish the liquidity of a company, and how quickly a company converts its assets to bring in cash for resolving the debts.

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| --- | --- | --- |
| **S. No.** | **RATIOS** | **FORMULAS** |
| 1 | Inventory Ratio | Net Sales / Inventory |
| 2 | Debtors Turnover Ratio | Total Sales /  Account Receivables |
| 3 | Debt Collection Ratio | Receivables  x Months or days in a year / Net Credit Sales for the year |
| 4 | Creditors Turnover Ratio | Net Credit Purchases / Average Accounts Payable |
| 5 | Average Payment Period | Average Trade Creditors / Net Credit Purchases X 100 |
| 6 | Working Capital Turnover Ratio | Net Sales / Working Capital |
| 7 | Fixed Assets Turnover Ratio | Cost of goods Sold / Total Fixed Assets |
| 8 | Capital Turnover Ratio | Cost of Sales / Capital Employed |

Capital Structure Ratios

Each firm or company has capital or funds to finance its operations. These ratios, i.e., the Capital Structure Ratios, analyze how structurally a firm uses the capital or funds.

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| --- | --- | --- |
| **S. No.** | **RATIOS** | **FORMULAS** |
| 1 | Debt Equity Ratio | Total Long Term Debts / Shareholders Fund |
| 2 | Proprietary Ratio | Shareholders Fund/ Total Assets |
| 3 | Capital Gearing ratio | Equity Share Capital / Fixed Interest Bearing Funds |
| 4 | Debt Service Ratio | Net profit Before Interest & Taxes / Fixed Interest Charges |

Overall Profitability Ratio

True to its name, these ratios measure how profitable a particular firm or company is, or how it can turn its assets and capital into profits for future use.

|  |  |  |
| --- | --- | --- |
| **S. No.** | **RATIOS** | **FORMULAS** |
| 1 | Overall Profit Ability Ratio | Net Profit / Total Assets |

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