

# ACCOUNTING RATIO CHEAT SHEET

## PART 1: THE LIQUIDITY RATIOS



Liquidity ratios are used to evaluate a business's ability to meet its short-term financial obligations.

CURRENT RATIO	HOW TO EVALUTE
$\text{CURRENT RATIO} = \frac{\text{CURRENT ASSETS}}{\text{CURRENT LIABILITIES}}$ <p><b>Current assets</b> are assets a company holds that should be fairly easy to convert into cash within a year's time. <b>Current liabilities</b> are short-term debts, usually payable within a year's time.</p>	<p>Look for a value of at least 1 but ideally 2. Any value below 1 means the company's short-term obligations exceed its short-term assets.</p>
QUICK RATIO	HOW TO EVALUTE
$\text{QUICK RATIO} = \frac{\text{CASH} + \text{AR} + \text{MARKETABLE SECURITIES}}{\text{CURRENT LIABILITIES}}$ <p><b>Cash</b>, <b>accounts receivable (AR)</b>, and <b>marketable securities</b> are all assets that can be liquidated quickly.</p>	<p>The quick ratio is similar to the current ratio but includes only highly liquid assets as opposed to all current assets. A quick ratio of at least 1 is therefore more assuring than a current ratio of the same value.</p>
CASH RATIO	HOW TO EVALUTE
$\text{CASH RATIO} = \frac{\text{CASH}}{\text{CURRENT LIABILITIES}}$	<p>The cash ratio is "quicker" than a quick ratio, as it only considers cash assets. A cash ratio of 1 is more assuring than a current or quick ratio of the same value.</p>
OPERATIONG CASH FLOW (OCF) RATIO	HOW TO EVALUTE
$\text{OPERATING CASH FLOW RATIO} = \frac{\text{INCOMING CASH FROM OPERATION}}{\text{CURRENT LIABILITIES}}$ <p><b>Operating Cash Flow</b> only includes cash obtained through regular company operations in the current time period.</p>	<p>A number lower than 1 on the OCF ratio is more easily forgiven than it would be on the Current, Quick, or Cash ratios. Nevertheless, just like with the other liquidity ratios, higher numbers are preferred over lower ones.</p>

## PART 2: DEBT, SOLVENCY, AND FREE CASH FLOW

NOTE



Whereas liquidity ratios assess a business's financial vitality in the short term, debt and solvency ratios can help clarify the business's longer-term financial strategy.

DEBT RATIO OR DEBT TO ASSETS RATIO	HOW TO EVALUATE
$\text{DEBT RATIO} = \frac{\text{TOTAL LIABILITIES}}{\text{TOTAL ASSETS}}$ <p><b>Total debt</b> includes both short- and long-term debt.</p>	<p>When a company's debt ratio is 1, it has just as many debts as it has assets. For some companies, a debt ratio of 1 may represent the verge of instability. Other companies can sustain or even benefit from greater debt levels.</p> <p>Conservative investors may prefer debt ratios of .25 or lower. If the debt ratio is close to .30 or above, then it is a good idea to investigate the company's overall debt strategy before investing.</p>
INTEREST COVERAGE RATIO	HOW TO EVALUATE
$\text{INTEREST COVERAGE RATIO} = \frac{\text{EBIT (EARNINGS BEFORE INTEREST \& TAXES)}}{\text{INTEREST EXPENSE}}$	<p>The interest coverage ratio is used to evaluate the relative expense of a business's debt. If the interest ratio is 1.5 or less, the business may be in significant debt trouble and may be unable to find new capital lenders.</p>
SOLVENCY RATIO	HOW TO EVALUATE
$\text{SOLVENCY RATIO} = \frac{\text{NET INCOME} + \text{DEPRECIATION}}{\text{SHORT-TERM LIABILITIES} + \text{LONG-TERM LIABILITIES}}$ <p><b>Net Income</b> (in this ratio) accounts only for income that can be readily converted into cash. <b>Depreciation</b> is the decline in asset value due to the passage of time or changing circumstances.</p> <p>The combination of both short- and long-term liabilities depicts the company's total debt levels.</p>	<p>The solvency ratio provides a solid, overall measurement of a business's ability to generate income sufficient to cover its debts.</p> <p>For normal businesses, a solvency ratio at 20% or above is (in most circumstances) considered healthy. Newer businesses may have lower-than-average solvency ratios, especially if they have yet to (or are just beginning to) turn a profit. The solvency ratio should steadily improve as the business matures.</p>
FREE CASH FLOW	HOW TO EVALUATE
$\text{NET CASH FLOW FROM OPERATIONS} - \text{CAPITAL EXPENDITURE} - \text{CASH DIVIDENDS} = \text{FREE CASH FLOW}$ <p>A company's <b>Free Cash Flow</b> measures the cash quantity remaining after essential expenditures.</p>	<p>A business with high levels of free cash flow may enjoy the privilege of throwing its financial weight around. Businesses may use free cash flow to pursue new expansions and acquisitions. They may also seek to profit from their own success by pursuing stock buybacks.</p>

## PART 3: EARNINGS PER SHARE



Earnings per Share (EPS) is useful for intracompany comparisons (evaluating the performance of one company across multiple different periods) usually on a year-by-year basis.

EARNINGS PER SHARE	HOW TO EVALUTE
<p><b>EARNINGS PER SHARE = <math>\frac{\text{NET INCOME} - \text{PREFERRED DIVIDENDS}}{\text{WEIGHTED AVERAGE OF OUTSTANDING COMMON STOCK SHARES}}</math></b></p> <p>Preferred Dividends are subtracted from net income because the numerator must only reflect income available to <b>common stock</b> holders. A weighted average is used because the quantity of outstanding common stock shares may fluctuate throughout a given evaluation period.</p>	<p>EPS is useful for making intracompany evaluations of C Corporations and S Corporations (entities that issue common stock).</p> <p>EPS is also effective at scaling relevant business data down to the stockholder level, allowing them a better grasp of their investment's performance.</p> <p>For other business entity types, such as sole proprietorships and LLCs, the simplest and most relevant intracompany comparison can be made by assessing net income or loss on a year-by-year basis.</p>