FIN300: Financial Statement Analysis

TRAIN TO LEARN EFFECTIVELY: TIP SHEETS

Financial Analysis Ratios

- **Profitability ratios:** how profitable is the firm?
- **Liquidity ratios:** how fast you can turn assets into cash.
- **Asset Efficiency:** how assets are managed to generate revenue.
- **Working Capital Ratios:** are they being efficient at collecting?
- **Interest Coverage Ratio:** how easily can a company pay interest on outstanding debt?
- **Leverage Ratios:** is the company financed with more debt or equity?
- **Valuation Ratios:** useful for investing purposes (High = NOT GOOD/overvalued)
  - Price to Earnings $\frac{Market\ Capitalization}{Net\ Income}$

Profitability High=Good Gross margin, operating margin, net profit margin	Liquidity High=Good Current ratio, Quick ratio	Asset Efficiency High=Good Asset Turnover, Fixed Asset Turnover	Working Capital Ratios High=NOT GOOD Inventory Turnover, Accounts Receivable Days,	Interest Coverage High=Good	Leverage High= NOT GOOD Debt to Equity, Debt to Capital, Net debt
$\frac{Gross\ profit}{Total\ Sales}$	$\frac{Current\ Assets}{Current\ liabilities}$	$\frac{Sales}{Total\ Assets}$	$\frac{Accounts\ Rec.}{Daily\ sales}$	$\frac{EBIT}{Interest}$	$\frac{Total\ debt}{Total\ Equity}$
$\frac{Operating\ income}{Total\ Sales}$	$\frac{Current\ Assets - Inventory}{Current\ liabilities}$	$\frac{Sales}{Fixed\ Assets}$	$\frac{Cost\ of\ goods\ sold}{Avg.\ Inventory}$		$\frac{Total\ debt}{Total\ Equity + Total\ Debt}$
$\frac{Net\ Income}{Total\ Sales}$					$Total\ debt - excess\ cash$

Toronto Metropolitan University

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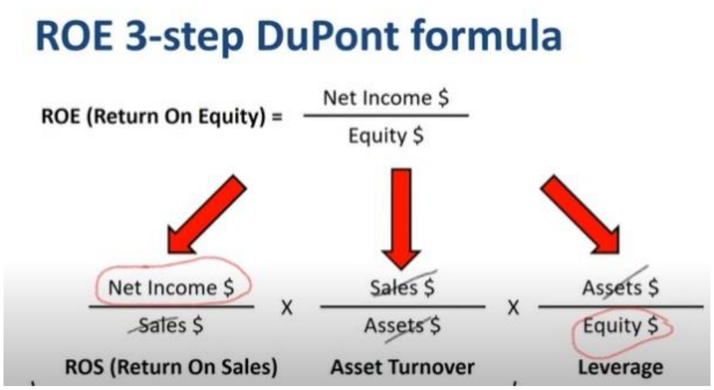
Dupont Analysis

- **Return on Equity (ROE) =** $\frac{Net\ Income}{Book\ Value\ of\ Equity}$ = Profit Margin × Asset Turnover × Financial Leverage
- **Profit Margin =** $\frac{Net\ Income}{Total\ Sales}$
- **Asset Turnover =** $\frac{Sales}{Total\ Assets}$
- **Financial Leverage (Equity Multiplier) =** $\frac{Total\ Assets}{Book\ Value\ of\ Equity}$



Return on Sales – indicator of profitability.

Asset Turnover – efficiency of working capital, which are current assets such as, Accounts Receivable, Accounts Payable and Inventory.

Financial Leverage – ability to sustain financial obligations using equity.