# Ratios

**Profitability ratios:** Compares net profit from revenue employed.
**Liquidity ratios:** Investigate short term financial viability.
**Gearing:** Extent to which a firm is dependent on borrowing.
**Shareholder ratios:** Returns for shareholders.
**Financial efficiency ratios:** Analyse how well a firm uses its assets and liabilities.

**Profitability ratios:**

**Gross profit margin = (gross profit / revenue) x100**
- Higher is better
- Need to compare with figures from other years.

**Return on capital employed = (operating profit / capital employed) x100**
- Higher is better.
- Need to compare with other years or other firms.
- Annual return on money invested as a %.



**Liquidity ratios:**

**Current ratio (liquidity ratio) = current assets : current liabilities**
- Ideal is 1.5 : 1
- Higher means many resources not being used.
- Too low and struggle to pay debts.

**Acid test ratio = (current assets - stock) : current liabilities**
- Also known as quick ratio or liquid ratio.
- Ideal is 1 : 1.
- Can pay debts without stock.
- Supermarkets are an exception.

**Gearing = (long term loans / capital employed) x100**
- 50% optimum.
- Above is highly geared.
- High gearing = more risky investment.
- Low gearing = timidity in good economic times.