**Ratio Analysis**

All ratios are indexed to the company’s industry and strategic place in the market—whether it is small, mid-sized, or large company.

Retail

* Gross Margin Ratio (Profitability)
	+ Net Sales – Cost of Goods Sold/Net Sales or Gross Profit/Net Sales
		- Demonstrates the percentage of sales remaining to pay all expenses after cost of goods sold
* Profit Margin Ratio (Profitability)
	+ Net Income/Net Sales
	+ 
		- Demonstrates the percentage of sales that is profit
		- Net income in each sales dollar

Inventory

* Inventory Turnover (Liquidity and Efficiency)
	+ Cost of Goods Sold/Average Inventory (Average inventory is calculated as beginning inventory plus ending inventory divided by 2)
	+ 
		- Demonstrates how often inventory turns into sales during a specific period
		- Efficiency of inventory management
		- How long a company holds inventory before selling it
* Days’ Sales in Inventory (Liquidity and Efficiency)
	+ Ending Inventory/Cost of Goods Sold. This ratio is then multiplied by 365
	+ 
		- Is there adequate inventory on hand to meet sales demand?
		- Liquidity of inventory – Is inventory turning into sales and eventually cash?

Accounts Receivable

* Accounts Receivable Turnover (Liquidity and Efficiency)
	+ Net Sales/Average Net Accounts Receivable (Average net accounts receivable is calculated as beginning net accounts receivable plus ending net accounts divided by 2)
	+ 
		- Demonstrates the number of times accounts receivable are collected in a period--how efficiently are accounts receivable collected. A high ratio indicates quick collection.
		- Efficiency of collection
* Average Collection Period or Days’ Sales in AR (Liquidity and Efficiency)
	+ 365 divided by the Accounts Receivable Turnover Ratio
		- Demonstrates the number of days it takes to collect on AR.

Assets

* Return on Total Assets Ratio or Return on Assets (Profitability)
	+ **Net income**/Average total assets (Average total assets is calculated as beginning total assets plus ending total assets divided by 2)
	+ 
		- Demonstrates how well assets are employed to generate profit.
		- Overall profitability of assets
* Total Asset Turnover (Liquidity and Efficiency)
	+ **Net Sales**/Average total assets (Average total assets is calculated as beginning total assets plus ending total assets divided by 2)
	+ 
		- Demonstrates how well assets are employed to generate sales
		- Efficiency of assets in producing sales

Equity

* Payout Ratio (Profitability)
	+ Common Stock Cash Dividends/Net Income
		- A lower payout ratio indicates that a company is retaining more of its earnings to fuel its growth, whereas a higher payout ratio indicates that a company is sharing more of its earnings with stockholders. A payout ratio of more than 100% means that a company's dividend payments are exceeding its net income.
* Return on Common Stockholders’ Equity or Return on Equity (Profitability)
	+ Net Income – Preferred Dividends/Average Common Stockholders’ Equity (Average common stockholders’ equity is calculated as beginning common stockholders’ equity plus ending common stockholders’ equity divided by 2)
	+ 
		- Demonstrates how well equity is employed to generate profit.
		- Profitability of owner investment

