Accounting Analysis and Ratio Tools

**Analysis tools**

Students may use the following ratios for analysis of financial information:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Name | | Calculation | | Expressed as |
| Profitability (Return)  For all entities:  Return on equity | |  | | % |
| Return on total assets | |  | | % |
| Profit margin | |  | | % |
| Expense | |  | | % |
| Gross profit margin | |  | | % |
| For companies:  Earnings per ordinary share | |  | | $ |
| Earnings yield | |  | | % |
| Dividend per ordinary share | |  | | $ |
| Dividend yield | |  | | % |
| Financial Stability (Risk)  Short Term (Liquidity)  Quick ratio (acid test) | |  | | ratio |
| Working capital (current ratio) | |  | | ratio |
| Debtors’ turnover | |  | | times |
| Inventory turnover | |  | | times |
| Name | Calculation | | | Expressed as |
| Financial Stability (Risk), continued  Long Term (Solvency)  Debt ratio |  | | % | |
| Debt/equity |  | | % | |
| Times interest earned |  | | times | |

\* Averages are used for these values. However, the availability of information may necessitate the use of opening or closing values.

† Net sales should be used, except in the case where a business only provides service.

Accounting reports

| Report and purpose | Information |
| --- | --- |
| Income statement  The measurement of profit or loss | * Components: revenue and expenses * Classification of the components for service and trading entities |
| Balance sheet  Statement of financial position | * Components: assets, liabilities, and owner’s equity * The accounting equation * The concept of duality, showing the effects of transactions on the balance sheet * Classification of the components: current and non-current assets, liabilities, and owner’s equity |
| Statement of changes in equity | * Components: opening and closing capital, capital contributions, drawings, profit or loss. |
| Statement of cash flows  Sources of cash inflows and outflows | * Components: cash (sources and uses) * Differences between net profit and net cash flows in an accrual accounting system |

Links between accounting reports

| Reports | Links |
| --- | --- |
| Income statement *and* statement of changes in equity | Calculation of profit |
| Income statement *and* balance sheet | Impact of profit on the entity’s equity position |
| Income statement *and* statement of cash flows | Cash versus accrual representation of periodic flows (especially from operations) |
| Balance sheet *and* statement of changes in equity | End of period equity position of the entity |
| Balance sheet *and* statement of cash flows | Flow analysis of change in cash position over a period |