Explanation of Financial Indicators

LIQUIDITY

Financial ratios in this category measure the company's capacity to pay its debts as they come due.

Ratios included in the Fintel® Benchmark Analysis Report

Quick Ratio

Definition:	The ratio between all assets quickly convertible into cash and all current liabilities. Specifically excludes inventory.
Calculation: (x:y)	Current Assets less Inventory/Current Liabilities
Analysis:	Indicates the extent to which you could pay current liabilities without relying on the sale of inventory -- how quickly you can pay your bills. Generally, a ratio of 1:1 is good and indicates you don't have to rely on the sale of inventory to pay the bills.
	Although a little better than the Current ratio, the Quick ratio still ignores timing of receipts and payments.

Current Ratio

Definition:	The ratio between all current assets and all current liabilities; another way of expressing liquidity.
Calculation: (x:y)	Current Assets/Current Liabilities
Analysis:	1:1 current ratio means; the company has \$1.00 in current assets to cover each \$1.00 in current liabilities. Look for a current ratio above 1:1 and as close to 2:1 as possible.
	One problem with the current ratio is that it ignores timing of cash received and paid out. For example, if all the bills are due this week, and inventory is the only current asset, but won't be sold until the end of the month, the current ratio tells very little about the company's ability to survive.

Current Liabilities to Networth

Definition:	This ratio is a measure of the return or earnings on the money invested in your firm.
Calculation: (%)	Current Liabilities/Net Worth(or Equity)
Analysis:	This return must be high enough to provide owners with an adequate return for the risk that is being assumed by keeping investments in the firm.
	A low return will also make it difficult to attract additional investment capital in the future and this measure should be compared to similar size firms in your industry.

Current Liabilities to Inventory

Definition:	This ratio provides an indication of the ability of your firm's inventory sales to generate the cash needed to meet the short-term obligation of creditors.
Calculation: (%)	Current Liabilities/Inventory
Analysis:	A ratio that is low usually indicates that your firm will be able to meet short term obligations and a high ratio may be cause for concern and signal of a potential cash shortage.

Total Liabilities to Net Worth

Definition:	This expresses the relationship between the capital contributed by creditors and the capital contributed to your firm by owners.
Calculation: (%)	Total Liabilities/Net Worth(or Equity)
Analysis:	This provides an indication of the ability of a firm to meet creditor obligations and the lower the ratio the better financial condition the firm is thought to be in.
	A high ratio may signal potential cash shortage and a low ratio firm usually has greater ability to borrow debt in the future.

Some information taken from the SBA (Small Business Administration)

Explanation of Financial Indicators

EFFICIENCY	*Also called Asset Management ratios. Indicator of how efficiently the company manages its assets*
Collection Period (Days in Receivables)	
Definition:	This calculation shows the average number of days it takes to collect your accounts receivable (number of days of sales in receivables).
Calculation: (days)	(Accounts Receivable/Sales)x365
Analysis: ↓	Look for trends that indicate a change in your customers' payment habits. Compare the calculated days in receivables to your stated terms. Compare to industry standards.
	Review an Aging of Receivables and be familiar with your customers payment habits and watch for any changes that might indicate a problem.
	A long collection period usually signals high delinquencies and the potential for cash shortages.
Inventory Turnover (Days in Inventory)	
Definition:	This calculation shows the average number of days it will take to sell your inventory
Calculation: (x:y)	(Inventory/Cost of Goods Sold)x365
Analysis: ↓	Look for trends that indicate a change in your inventory levels.
	Compare the calculated days in inventory to your inventory cycle.
	Compare to industry standards.
Assets to Sales	
Definition:	This ratio is a measure of your firm's productive use of assets and a low percentage compared to the average for your industry usually indicates high asset use efficiency.
Calculation: (%)	Total Assets/Sales
Analysis: ↑	If you are more highly labor intensive than most in your industry, or if your fixed assets are largely depreciated, your ratio may be distorted and falsely indicate higher asset efficiency than is the case.
Sales to Net Working Capital	
Definition:	This ratio measure how efficiently working capital is being used by your firm.
Calculation: (x:y)	Sales/(Current Assets-Current Liabilities)
Analysis: ↑	A low ratio may indicate inefficient use of working capital while a high ratio may signal potential cash shortages and risk of not being able to pay creditors.
Accounts Payable to Sales	
Definition:	Indicates how efficiently your business generates sales on each dollar of assets.
Calculation: (%)	Accounts Payable/Sales
Analysis: ↑	A low percentage may indicate an over reliance on supplier credit to support sales.

Ratios included in the Fintel® Benchmark Analysis Report

Some information taken from the SBA (Small Business Administration)

Explanation of Financial Indicators

EFFICIENCY	*Also called Asset Management ratios. Indicator of how efficiently the company manages its assets*
Sales to Total Assets	
Definition:	Indicates how efficiently your business generates sales on each dollar of assets.
Calculation: (%)	Sales/Total Assets
Analysis: ↑	A volume indicator that can be used to measure efficiency of your business from year to year.
Accounts Receivable Turnover	
Definition:	Number of times that trade receivables turnover during the year.
Calculation: (x:y)	Sales/Accounts Receivable
Analysis: ↑	The higher the turnover, the shorter the time between sales and collecting cash.
	Compare to industry standards.
Days in Accounts Payable	
Definition:	This calculation shows the average length of time your trade payables are outstanding before they are paid. (number of days sales @ cost in payables).
Calculation: (days)	(Accounts Payable/Cost of Goods Sold)x365
Analysis: ↑	Look for trends that indicate a change in your payment habits.
	Compare the calculated days in payables to the terms offered by your suppliers.
	Compare to industry standards.
	Review an Aging of Payables and be familiar with the terms offered by your suppliers.
Accounts Payable Turnover	
Definition:	The number of times trade payables turnover during the year.
Calculation: (x:y)	Cost of Goods Sold/Accounts Payable
Analysis: ↓	The higher the turnover, the shorter the time between purchase and payment.
	A low turnover may indicate that there is a shortage of cash to pay your bills or some other reason for a delay in payment.
Inventory Turnover	
Definition:	Number of times that you turn over (or sell) inventory during the year.
Calculation: (x:y)	Cost of Goods Sold/Inventory
Analysis: ↑	Generally, a high inventory turnover is an indicator of good inventory management.
	But a high ratio can also mean there is a shortage of inventory.
	A low turnover may indicate overstocking, or obsolete inventory.
	Compare to industry standards.
Gross Margin Return on Fixed Assets	
Definition:	Indicates how efficiently you used your fixed assets.
Calculation: (%)	Gross Profit/Net Fixed Assets
Analysis: ↑	Shows amount of gross profit dollars generated by every dollar of fixed assets (net of depreciation).
	Caution: Major fixed asset purchases can appear to have a negative impact on a current year.

Some information taken from the SBA (Small Business Administration)

Explanation of Financial Indicators

PROFITABILITY

The ratios in this section measure the ability of the business to make a profit.

Return on Sales (Net Profit Margin)

Definition:	This ratio shows the percentage profit earned on sales by your firm and it is important to compare your performance with that of similar size firms in your industry.
Calculation: (%)	Net Profit/Sales
Analysis: ↑	Compare to other businesses in the same industry to see if your business is operating as profitably as it should be.
	Are you generating enough sales to leave an acceptable profit? Look at the trend from month to month. Is it staying the same? Improving? Deteriorating?
	Trend from month to month can show how well you are managing your operating or overhead costs.
	This ratio should increase as the volume of sales grows because fixed costs are spread over more units of sales.

Return on Assets

Definition:	This ratio provides you with a measure of the return on your total investment in assets including those financed with debt as well as equity.
Calculation: (%)	Net Profit/Total Assets
Analysis: ↑	ROA shows the amount of income for every dollar tied up in assets.
	Year to year trends may be an indicator ... but watch out for changes in the total asset figure as you depreciate your assets (a decrease or increase in the denominator can effect the ratio and doesn't necessarily mean the business is improving or declining.) This is an important measure that should be compared with similar size firms in your industry.

Return on Net Worth

Definition:	This ratio provides you with a measure of the return on your total investment in assets including those financed with debt as well as equity.
Calculation: (%)	Net Profit/Net Worth (Equity)
Analysis: ↑	Compare the return on equity to other investment alternatives, such as a savings account, stock or bond.
	A low return will also make it difficult to attract additional investment capital in the future and this measure should be compared to similar size firms in your industry.

Sales Per Employee

Definition:	Dollar amount of sales for each full-time employee.This is a measure of the productivity of employees and can give you an indication of appropriate staffing levels when compared to similar firms in you industry. In addition, this is a measure of how capital or labor intensive a firm is.
Calculation: ($)	Sales/# of Employees
Analysis: ↑	This is a measure of the productivity of employees and can give you an indication of appropriate staffing levels when compared to similar firms in you industry. In addition, this is a measure of how capital or labor intensive a firm is.
	Shows amount of sales generated per employee

Profit Per Employee

Definition:	Dollar amount of profit for each full-time employee.This is a measure of the profits your firm is generating for each employee working for you.
Calculation: ($)	Profit/# of Employees
Analysis: ↑	You want to maximize your profit per employee.The management of labor resources is important to the success of your business and you should carefully compare both sales and profits per employee for your firm with similar firms in your industry.
	Shows amount of profit generated per employee

Ratios included in the Fintel® Benchmark Analysis Report

Some information taken from the SBA (Small Business Administration)

ALIGNING ENERGIES
ALIGNMENT DYNAMICS, INC.
FOCUSED FOR RESULTS

Explanation of Financial Indicators

PROFITABILITY

The ratios in this section measure the ability of the business to make a profit.

Return on Sales (Gross Profit Margin)

Definition:	Indicator of how much profit is earned on your products without consideration of selling and administration costs.
Calculation: (%)	Gross Profit/Sales
Analysis: ↑	Compare to other businesses in the same industry to see if your business is operating as profitably as it should be.
	Look at the trend from month to month. Is it staying the same? Improving? Deteriorating?
	Is there enough gross profit in the business to cover your operating costs?
	Is there a positive gross margin on all your products?

COGS to Sales

Definition:	Percentage of sales used to pay for expenses which vary directly with sales.
Calculation: (%)	Cost of Goods Sold/Sales
Analysis: ↓	Look for a stable ratio as an indicator that the company is controlling its gross margins.
	Compare to other businesses in the same industry to see if your business is controlling production costs.

SG&A to Sales

Definition:	Percentage of selling, general and administrative costs to sales.
Calculation: (%)	General & Administrative Expenses/Sales
Analysis: ↓	Look for a steady or decreasing percentage indicating that the company is controlling its overhead expenses.

Owner's Discretionary Profit Dollars

Definition:	How much income generated by the company is available for the owner
Calculation: ($)	Officer Salaries+Net Income+Income Tax
Analysis: ↑	Obviously, we want this to be as high a number as possible to provide ownership with ample dollars as well as ample opportunities.

Owner's Discretionary Profit Percentage

Definition	Percentage of profits to sales before paying owner compensation or income taxes
Calculation: (%)	(Officer Salaries+Net Income+Income Tax)/Sales
Analysis: ↑	Look for steady or increasing percentages from year to year.
	The company should be able to pay the owner as well as produce a profit to continue operations.

Some information taken from the SBA (Small Business Administration)

Explanation of Financial Indicators

SAFETY	*Indicator of the businesses' vulnerability to risk. These ratios are often used by creditors to determine the ability of the business to repay loans.*
Debt to Equity	
Definition:	Shows the ratio between capital invested by the owners and the funds provided by lenders.
Calculation:	Total Liabilities/Total Equity (Loans to shareholders are treated as equity)
Analysis:	Comparison of how much of the business was financed through debt and how much was financed through equity. For this calculation it is common practice to include loans from owners in equity rather than in debt.
	The higher the ratio, the greater the risk to a present or future creditor.
	Look for a debt to equity ratio in the range of 1:1 to 4:1
	Most lenders have credit guidelines and limits for the debt to equity ratio (2:1 is a commonly used as an upper limit for small business loans).
	Too much debt can put your business at risk... but too little debt may mean you are not realizing the full potential of your business -- and may actually hurt your overall profitability. This is particularly true for larger companies where shareholders want a higher reward (dividend rate) than lenders (interest rate). If you think that you might be in this situation, talk to your accountant or financial advisor.
Debt coverage ratio	
Definition:	Indicates how well your cash flow covers debt and the capacity of the business to take on additional debt.
Calculation:	EBITIDA/Current Portion of Debt+Interest
Analysis:	Shows how much of your cash profits are available to repay debt.
	Lenders look at this ratio to determine if there is adequate cash to make loan payments.
	Look for a number above 1.

Some information taken from the SBA (Small Business Administration)