POSTGRADUATE DIPLOMO IN HOSPITAL MANAGEMENT LAICO

FINANCIAL RATIOS – MANAGEMENT TOOL

Financial Ratios are the tools the management to measure the strength and weakness of the organization. This is the starting point for making future plans for expansion and development. The use of Ratios are required from various users.

The owners, creditors, Investors, lenders, Unions etc.

Trade creditors

The material suppliers may decide on their credit terms and also on the price based on the soundness of the firm. Considering the current ratio which shows the liquidity the creditors may supply at a lower rate for getting immediate payment.

Term Loan lenders

The Banks or other financing organizations would see the current ratio of the organization for the repayment period and in case of long term lending they will see the cash flow during that period.

Investors

To know the profitability of their investment the investors would be interested in knowing the profitability ratios. They will see the liquidity to payoff the investments. They will also like to see the profit earning capacity over a period.

Management

The management is very much interested in every aspect of the financial analysis.

Ratio is the relation between two accounting figures expressed mathematically.

Standards of comparison.

1.Past period ratios are necessary to compare.

2.Projected ratios based on the projections for expansion

3.Competitors ratio to compare

4.Industry ratio to know where the firm stands.

The analysis may be on:

1. Time series i.e., trend analysis
2. Performa analysis-By fixing projected ratio and comparing to that
3. Cross section analysis- To compare with the average ratio of the Industry

Types of Ratios

Profitability Ratios - Based on the Profit& loss account and Balance sheet

Liquidity Ratios - Based on the Balance sheet

Efficiency Ratio - Based on the Profit and loss account and Balance sheet

Glossary for Ratio Analysis

Current Assets - All movable assets which can be converted in to cash and with in one year.

Current liabilities - All dues payable to outsiders within one year.

Sales – The value of sales after Returns, discounts, rebates etc.

Working capital – Current Assets – current liabilities (Excluding short term bank loan)

Net working capital –current Assets-Current liabilities (Including short term bank loan)

Total Assets – The sum of Fixed and current Assets

Tangible Assets – The sum of Fixed and current assets (excluding intangible assets)

Cost of goods sold – Opening stock+ purchases+ sales expenses-closing stock

1. Liquid/ Quick Ratio =	Quick Assets / Quick liabilities	to measure the short term debt paying ability Norm-1:1
2. Current Ratio	Current Assets / Current liabilities	Measures short term debt paying ability Norm 2 : 1
3. W.C.Turnover Ratio	Sales / Working capital	The means to finance the sales norm 5 : 1
4. Ratio of Debt to net worth	Total Debt / Net worth	It is the ratio of owners fund to loan fund norm 0.5 : 1
5. G.P.Ratio	Gross profit / Net sales x 100	Efficiency of production/Trading operations
6. Net profit ratio	Net profit / Net sales x 100	Indicates net margin on sales
7. Operating expense Ratio	Operating cost / Net sales x 100	Shows magt. Ability to control level exp.to level of sales
8. Debt-Equity ratio	L.T.Debts / L.T.funds	A measure of the extent of trading on equity
9. Inventory turnover	Net sales / Average inventory	To assess fastness of moving and control on inventory
10. Debt collection ratio	Net credit sales debtors / Average receivable	To assess the effective collection of ---------
11. Return on Investment	net profit / Net worth	A measure of Return on investment
12. Return on Assets	Net profit / Total assets	To assess effectiveness of use of assets
13. Average collection Period	Receivable x 365 / net credit sales	To know the average debt colle ction period in days

14. Investment turnover	Net sales ------------------- Total Assets	effective use of assets to generate sales
15. Fixed assets to net worth	Fixed assets ------------------ Net worth	To know how much funds tied up in Fixed assets norm - not exceeding 0.75
16. Leverage ratio	Total Debt --------------- Capital employed	The ratio of debt to funds employed

ARUM&Co.MADURAI

TRADING ACCOUNT

For the year ending 31.3.2002

EXPENDITURE			INCOME			
To Opening stock	1	100000	Sales –Direct	1800000		
To purchases	2	4000000	**-Credit**	**5000000**		4
To Packing&forwarding	2a	300000		-----------		
To commission on sales	2b	80000		6800000		
			Less-Returns	20000	67**80000**	5
			Closing stock		200000	6
To Gross Profit c/d	3	**2500000**				
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		6980000			6980000	
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PROFIT OR LOSS ACCOUNT

For the year ending 31.03.2002

EXPENDITURE			INCOME	
			By Gross profit B/d	2500000
To Periodicals		5000	By Miscellaneous income	5000
To R& M		60000		
To vehicles Maintenance		50000		
To Salary & wages		1500000		
To Electricity charges		200000		
To Postage&Telegram		5000		
To Telephones		15000		
To printing & stationery		7000		
To Rent		36000		
To Welfare expenses		3000		
To Entertainment expenses		1000		
To Miscellaneous expenses		15000		
Depreciation		50000		
NET PROFIT	7	**558000**		
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		2505000		2505000
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BALANCE SHEET AS AT 31.03.2002

LIABILITIES		ASSETS		
7a.Share capital	500000	18.**Fixed Assets**	1200000	
8. Reserves&surplus	200000	19.less-depreciation 200000		1000000
9. Profit&loss a/c	558000	**Current Assets**		
10. SBI-LT Loan a/c	500000	20.Investments		600000
Sundry creditors		21.Stock in trade	200000	
11. Bank overdraft	200000	22.Deposits/ Advances	158000	
12. Deposits &advances	50000	23.Debtors/Receivables	200000	
13. Creditors for purchases	100000	24.Cash & Bank Balances	50000	
14. Creditors for expenses	50000	**Non current assets**		
Provisions		25.Goodwill	100000	
15. Prov. for gratuity	50000	26.Defrd.Rev.Expend.	50000	
16. Prov. For Bonus	100000			
17. Prov. For contingency	50000			
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	2358000	27	2358000	
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Base figures:

1. Gross profit	Item 3
2. Net profit	Item 7
3. Total Assets	Item 27
4. Tangible Assets	Item 27 minus items 25 and 26
5. Intangible Assets	Items 25+26
6. Equity/capital	Item 7a
7. Capital employed	Item 7a to 10-(25+26)
8. Current Assets	items21 to 24
9. Current liabilities	Items 11 to 17
10. Quick/liquid assets	Items 22 to 24
11. Net sales	Item 5
12. Credit sales	Item 4
13. Net worth	Item (18 to 24)-(10 to 17) or 7a to 9-(25+26)
14. Average inventory	Item (1+6)/2
15. Average purchase	Item (1+2-6)/12
16. Quick liabilities	Item 11+12+ 13+14
17. Cost of goods sold	Items 1 to 2b- 6

NATURE OF RATIO	FORMULA	FIGURES	RATIO
Gross profit Ratio	Gross profitx100/Net sales	2900000 x 100/6780000	42.77 %
Net Profit Ratio	Net Profitx100/ Net sales	558000 x 100/6780000	8.23 %
Operating cost ratio	Operating costsx100/net sales	1947000x100/6780000	28.72 %
Net profit to total Assets or Return on Assets	Net profitx100/total assets	558000x100/2358000	23.66 %
Inventory turnover ratio	Net sales/Average inventory	6780000/150000	45.20
Quick/liquid ratio	Quick assets/ quick liabilities	318500/187500	1.70
Current Ratio	Current Assets/current liabilities	608000/600000	1.01
Working capital Turnover ratio	Sales / Working capital	6780000/608000	11.15
Debt to Net worth	Total Debt/net worth	700000/1108000	0.63
Debt equity ratio	Debts/Equity capital	700000/500000	1.40
Debt collection Ratio	Net credit sales/Average receivable	5000000/200000	25
Average collection period or debtors velocity	Receivable x 365/net credit sales	200000 x 365/5000000	15 days
Average credit days for purchases	Payable x 365/monthly average purchase	100000 x 365/4000000	9 days
Return on investment	Net profit/ net worth	558000/1108000	0.50
Investment turnover	Netsales / Total assets	6780000/2358000	2.87
Fixed Assets to net worth	Fixed Assets/net worth	1000000/1108000	0.90
Leverage Ratio or capital gearing	Total debt/capital employed	700000/1608000	0.43
Fixed assets to Proprietor’s fund	Fixed assets/proprietor fund	1000000/500000	2
Proprietary Ratio	Proprietors fund/Total assets	500000/2358000	0.21