Probability / Liquidity

Sunday, 28 April 2024 4:58 PM

P Gross Profit Margin: $\frac{\text{Gross P}}{\text{NSR}} \times 100\%$

P Mark-up on Cost: $\frac{\text{Gross P}}{\text{COS}} \times 100\%$

P Profit Margin: $\frac{\text{Profit}}{\text{NSR}} \times 100\%$

P Return on Equity: $\frac{\text{Profit}}{\text{avg eq}} \times 100\%$

Average Equity: $\frac{\text{Equity (St)} + \text{Equity (En)}}{2}$

L Working Capital: Current Assets − Current Liabilities

L Current ratio: $\frac{\text{Current Ass}}{\text{Current Lia}}$

L Quick Ratio: $\frac{\text{Cash + receivables}}{\text{Current Lia}}$

Rate of Inv Turnover: $\frac{\text{Cost of Sales}}{\text{Avg Inv}}$

Avg Inv: $\frac{\text{Inv (St)} + \text{Inv (En)}}{2}$

Days sales in inventory: $\frac{\text{Avg Inv}}{\text{COS}} \times 365$

Rate of Inv turnover: $\frac{\text{Net Credit Sales / Service Fee Rev}}{\text{Avg Net TR}}$

Avg Net TR: $\frac{\text{Net TR (St)} + \text{Net TR (En)}}{2}$

Net TR: TR − Allowance for impairment loss

TR Collect Period: $\frac{\text{Avg Net TR}}{\text{Net Cr Sales Rev / Serv}} \times 365$ / $\frac{1}{\text{rate TR Turnover}} \times 365$

Profitability

The ability of the business to generate excess income to cover its expenses

Why Business needs to be profitable?

To gain competitive advantage over competitors

Profit can be reinvested into the business

What is return on equity?

Amount of P business earns for every dollar of equity invested into business

How to improve Profitability

- Sell goods at higher price
- Buy goods at lower price
- Increases sources of other income
- Reduce operating expenses

Liquidity

The ability of a business to convert current assets into cash to pay for current liabilities.

'Working Capital' means?

Excess current asset over current liability

Why working capital is important?

- Business needs to have enough CA to settle liabilities when due
- Needs enough CA to pay daily operating exp
- Easier for business to obtain short-term loan from lenders

Quick Ratio vs Current Ratio

Current Ratio: ability to pay short term debts with CA

Quick Ratio: ability to pay debts using quick assets, excluding inv & prepayments

Improve liquidity?

- increase sources of cash
- Manage cash outflow

low liquidity? − low on cash

- eventual shutdown
- cant negotiate for better credit terms w/ supplier
- unable to obtain bank loan

Why liquidity change when profit same

Liquidity: CA & CL

Profit: income & exp

- may buy goods on credit
- customers pay at diff time
  ↳ only selling to same grp of customers