Foundational financial ratios

Use the below guide as a reference when working on your financial risk assessment or analyzing performance. Consider comparing your yearly numbers to a three-to-five-year average. You may not need all the ratios, but monitor what's important for your current project.

Indicator	Financial Performance	Ratio	What it measures
Performance	Liquidity Can you access cash when you need it? Will current liabilities be paid?	**Current Ratio** Current assets/Current liabilities	• Dollar amount of current assets available to service each dollar of current liabilities
		Working Capital Current assets – Current liabilities	• Dollar amount available to operate the business after current liabilities have been paid • If there's enough cash or cash equivalents to pay off the current debts and cover upcoming expenses
	Solvency Can you meet your long-term financial obligations?	**Net Worth** Total assets – Total liabilities (To calculate adjusted net worth, remove postponed or subordinated shareholder loans from total liabilities.)	• Financial worth of a business (Can provide limited information alone and must be considered along with the net worth ratio.)
		Net Worth Ratio Net worth/Total assets x 100 (To calculate adjusted net worth ratio, use adjusted net worth.)	• Net worth (equity) in proportion to the assets
		Debt-to-Equity Total liabilities/Total equity	• Use of debt to acquire additional assets or increase profits generated through business operations • How the assets and business operations are financed, either through debt or equity • Can help to determine your commitment based on how much of their finances the customer invests in the operation
		Total liabilities Postponed or Subordinated debt/ Total assets – (Total liabilities – Postponed or Subordinated debt)	• Extent to which creditors have financed your business as compared to you, adjusting for debt owing to creditors or shareholders

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Indicator	Financial Performance	Ratio	What it measures
Performance	Efficiency How efficient are you at making money?	**Operating Expense Ratio** Operating expenses/Gross revenue (x 100 for %) - Operating expenses: Gross expenses – Fixed expenses. - Fixed expenses = interest, depreciation, land rent, property taxes.	• Amount of each dollar of revenue that goes towards paying operating expenses • Extent to which a business uses its resources to produce earnings
	Profitability Are you making money?	**Gross margin/ Gross profit** Revenue Gross profit = Revenue - COGS COGS = Total variable expenses	• How well a business uses its assets to generate profit • Compares the percentage of gross profit to each sales dollar of revenue • Degree to which a business yields profit or financial gain
Coverage	Debt Coverage What portion of your income is required to service debt?	**Debt Exposure Ratio** Farm revenue + Off-farm income + Other income ――――――――――――― Current + Term liabilities	• Debt coverage • Total income as a percentage of total debt • Portion of income is required to service debt
	Is the amount of cash available to service debt impacting the ability of an operation to meet its debt payments?	**Debt Service Capacity** Net farm income after tax + Interest + Depreciation – Drawings + Contributions	• Dollar amount available to make term debt payments, including principal and interest
		Adjusted Debt Service Capacity Debt service capacity – Gain on disposal + Loss on disposal – Extraordinary income + Extraordinary expenses + Deferred income tax	• Reflects an operation's ability to service debt by removing items that may not portray a typical year • Removes gain/loss on disposal, adjusts for extraordinary income/ expenses and adds deferred income because these items either are not a cash transaction or are not expected to occur in future years
		EBITDA (Earnings Before Interest, Income Taxes, Depreciation and Amortization) Net income before tax + Interest + Depreciation + Amortization	• Provides a snapshot of operational efficiency • Provides a base number to help determine if there are enough funds available to pay debt obligations
		Adjusted Debt Service Coverage Ratio Adjusted debt service capacity/Debt service requirements Debt service requirements = Principal, Interest and Capital lease payments from the future period	• Dollar amount that your operation has available for payments compared to the dollar amount of payments due • Ability of the operation to pay debts within a specific period
		Residual after-debt servicing Debt service capacity – Debt service requirements	• Funds remaining after all debt service requirements for the period have been paid in dollars (Should be considered together with debt service coverage to understand how large the residual is as compared to Debt service requirements)