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BUSINESS SOLUTIONS

Key Performance Indicators (KPIs)

For Informed Business Decisions

You're likely aware of how insightful properly prepared financial statements can be — especially when they follow Generally Accepted Accounting Principles. *But how can you best extract these valuable insights?*

One way is to view your financial statements through a wide variety of "lenses" provided by key performance indicators (KPIs). These are calculations or formulas into which you can plug numbers from your financial statements and get results that enable you to make better business decisions. Outlined below are some useful KPIs that can help you reveal important trends and developments in your business, and ensure you are seeing the big picture.

Liquidity Ratios

Current Ratio: Measures current assets available to cover current liabilities, a test of near-term solvency.

Current Ratio = Current Assets / Current Liabilities

Quick Ratio: A more stringent version of the current ratio, indicating liquid assets available to cover current debt.

Quick Ratio = Cash + Accounts Receivable / Current Liabilities

Days Payable: Reflects the average number of days for each payable before payment is made.

Days Payable = 365 / (Cost of Sales/Accounts Payable)

Profitability Ratios

Gross Profit Margin: Measures a company's ability to cover direct cost of sales – a widely used ratio.

Gross Profit Margin = Profit After Direct Costs / Business Revenue

EBITDA / Business Revenue: A metric designed to eliminate the effect of finance and accounting decisions when comparing companies and industry benchmarks.

EBITDA / Business Revenue = (Earnings Before Interest, Taxes, Depreciation, and Amortization) / Business Revenue

Pre-tax Return on Assets (ROA): A critical indicator of profitability. Companies that use their assets efficiently tend to show a higher ratio than the industry norm.

Pre-tax Return on Assets = (ROA) (Pre-tax Profit / Total Assets)

Efficiency Ratios

Days Receivable: Reflects the number of days that receivables are outstanding. Higher than average ratios may indicate a problem in the collection process.

Days Receivable = 365 / (Business Revenue/Accounts Receivable)

Days Inventory: Reflects the number of times inventory is turned over during the year. High levels can indicate shortages in the ability to deliver on a timely basis.

Days Inventory = 365 / (Cost of Sales/Inventory)

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Efficiency Ratios, continued

Assets / Business Revenue: Indicates whether a company is handling a reasonable volume of business revenue in relation to investment. High ratios relative to industry norms might indicate overly conservative sales efforts or lagging sales management.

Assets / Business Revenue = (Total Assets / Business Revenue)

Sales per Employee: A basic efficiency measure developed outside of the formal financial statement, often reflecting relative value-added.

Sales per Employee = Business Revenue / FTE Employees

Debt Risk Ratios

Interest Coverage: Assesses financial stability by examining whether a company is profitable enough to pay interest on debt.

Interest Coverage = (EBITDA / Interest Expense)

Short-Term Debt Coverage: Reflects a level of capability to satisfy short-term debt. The larger the ratio to industry norms, the higher the risk and less security for creditors.

Short-term Debt Coverage = Current Liabilities / Net Worth

Long-Term Debt Coverage: A measure of debt coverage. This ratio measures the company's ability to satisfy long-term debt. The larger the ratio to industry norms, the higher the risk.

Long-term Debt Coverage = Long-term Liabilities / Net Worth

Total Debt Risk: This ratio helps to clarify the total risk impact of debt. Total liability levels should be comfortably less than net worth except in special circumstances. The most advantageous ratios are around or somewhat below industry norms.

Total Debt Risk = Total Liabilities / Net Worth

Running a successful business is challenging. With your hands in the day-to-day operations, it's sometimes difficult to see the big picture. Our **YeoConsults Business Solutions** offers fixed-fee programs tailored to meet your business's needs, goals and budget so you can focus on growing your business.

- **YeoConsults Outsourced Accounting**
- **YeoConsults Payroll Solutions**
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