

A-Level Business Studies Financial Ratio Cheat Sheet

Master Financial Performance Analysis

GCSE • A-Level • AQA • Edexcel • OCR

Profitability Ratios

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Ratio	Formula	What it Measures	Good Sign	Poor Sign
Gross Profit Margin	$\text{Gross Profit} \div \text{Revenue} \times 100$	Efficiency of production and pricing	Increasing	Falling margins
Operating Profit Margin	$\text{Operating Profit} \div \text{Revenue} \times 100$	Overall operational efficiency	Higher than competitors	Rising costs reducing profit
Profit for the Year Margin (Net Profit Margin)	$\text{Profit for the Year} \div \text{Revenue} \times 100$	Final profitability after all expenses	Increasing over time	Falling profitability

Examiner Tip

Always explain **why** the ratio changed.

Instead of:

Gross profit increased.

Write:

Gross profit margin increased from 38% to 44%, suggesting improved cost control or greater pricing power, which should strengthen profitability if maintained.

Liquidity Ratios

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Ratio	Formula	Ideal Range	What it Shows
Current Ratio	$\text{Current Assets} \div \text{Current Liabilities}$	1.2–2.0	Ability to pay short-term debts
Acid Test Ratio	$(\text{Current Assets} - \text{Inventory}) \div \text{Current Liabilities}$	Around 1	Immediate liquidity excluding stock

Interpretation

High Current Ratio

✓ Good liquidity

X Too much idle cash

Low Current Ratio

✓ Efficient working capital

X Possible cash flow problems

Efficiency Ratios

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Ratio	Formula	Better Direction
Inventory Turnover	$\text{Cost of Sales} \div \text{Average Inventory}$	Higher generally better
Inventory Turnover Period	$\text{Average Inventory} \div \text{Cost of Sales} \times 365$	Lower generally better
Receivables Days	$\text{Trade Receivables} \div \text{Revenue} \times 365$	Lower
Payables Days	$\text{Trade Payables} \div \text{Cost of Sales} \times 365$	Higher (within supplier terms)
Asset Turnover	$\text{Revenue} \div \text{Capital Employed}$	Higher

What They Mean

Inventory too high

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Cash tied up

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Higher storage costs

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Lower profitability

Receivables too high

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Customers paying late

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Poor cash flow

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Potential bad debts

Payables increasing

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Improves cash flow

BUT

↓

May damage supplier relationships

Investment Ratios

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Ratio	Formula	Interpretation
Return on Capital Employed (ROCE)	$\text{Operating Profit} \div \text{Capital Employed} \times 100$	Overall efficiency of invested capital

ROCE Analysis

High ROCE

✓ Business using assets efficiently

✓ Strong investment performance

Low ROCE

X Weak returns

X Possible overinvestment

Financial Ratio Comparison

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Ratio Type	Measures
Profitability	Profit generation
Liquidity	Ability to pay debts
Efficiency	Use of resources
Investment	Return to investors

Examiner Analysis Framework

Never stop at calculating the ratio.

Use this structure:

Step 1

State the figure.

ROCE increased from 12% to 17%.

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Step 2

Interpret.

This suggests capital is being used more efficiently.

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Step 3

Explain why.

The business may have increased sales while controlling operating costs.

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Step 4

Evaluate.

However, this may only be temporary if demand falls next year.

This four-step structure is what earns higher-level analysis marks.

Common Evaluation Points

Every ratio has limitations.

Always consider:

✓ Industry averages

✓ Previous years

✓ Competitor performance

✓ Economic conditions

✓ Seasonal effects

✓ One-off events

Common Exam Mistakes

- ✗ Calculating but not interpreting
 - ✗ Ignoring trends
 - ✗ Comparing unrelated industries
 - ✗ No judgement
 - ✗ Confusing liquidity with profitability
 - ✗ Using the wrong denominator
 - ✗ Forgetting percentages
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Ratio Memory Tricks

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Ratio	Remember
Gross Margin	Production efficiency
Operating Margin	Running the business
Current Ratio	Can we pay today's bills?
Acid Test	Can we pay immediately?
ROCE	Are investors getting good returns?
Receivables Days	How quickly customers pay
Payables Days	How long we take to pay suppliers
Inventory Turnover	How quickly stock sells

30-Second Exam Checklist

Before moving on, ask yourself:

- ☐ Have I calculated the ratio correctly?
- ☐ Have I interpreted it?

- ☐ Have I explained the reason?
- ☐ Have I linked it to the case study?
- ☐ Have I evaluated the result?
- ☐ Have I reached a judgement?