

Profitability ratios: short term liquidity essay sample

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Planning is very important to companies and firms, they need to analyze their various ratios and from that they are able to draw conclusions and make predictions for the long run. Financial planning is a process where accountants estimate the capital needed and they determine who their competition is. There are various ratios that are needed in order to determine how a company is doing financially. These include the following: profitability ratio, short term liquidity & efficiency ratio, working capital, long term solvency and shareholder ratios. This report will focus on the long-term solvency and shareholder ratios for Asos Ltd. Since there was a lack of data it was impossible to calculate the gearing ratio, interest cover, return of equity and the dividend payout ratio. Therefore this report will discuss what the terms mean and why the ratios are missing.

Many companies need to borrow money in order to have an appropriate amount of funds to expand their company, because they need to invest in new apparatus and machinery. Sometimes the investment can be funded from profits that have been made or it can come from issued share, however it is most likely to be borrowed. The more interest they pay then the more money needs to be borrowed. However borrowing money is always a risk since the company has to pay the interest even if the investment is successful or not. If they are making losses they will still have to pay interest. The more capital the company borrows the bigger the risk is. When one looks at the different accounts they would want to analyze how big the risk is and in order to do this one must use the gearing ratio.

What does Gearing Ratio mean?

The gearing ratio is a term that is used to describe a financial ratio that <https://assignbuster.com/profitability-ratios-short-term-liquidity-essay-sample/>

compares the owner's equity or capital that comes from borrowed funds.

Gearing is essentially a measure of financial leverage, it demonstrates the amount to which a firm's activities are funded by the owner's funds against the creditor's funds.

As outsiders looking at a set of accounts we therefore want to assess how big that risk is, and to do this we use another ratio. This ratio is known as the **GEARING RATIO**.