Ratio analysis of tcs wipro infosys essay

CURRENT RATIO It is a liquidity ratio that measures a company’s ability to pay short-term obligations. Also known as “ liquidity ratio”, “ cash asset ratio” and “ cash ratio”. By putting to test a company’s financial strength, deduces company’s ability to pay back its short-term liabilities (debt and payables) with its short-term assets (cash, inventory, receivables).

The higher the current ratio, the more capable the company is of paying its obligations. An acceptable current ratio varies by industry. Generally, the more liquid the current assets, the smaller the current ratio can be without cause for concern. For most companies, 1. 5 is an acceptable current ratio.

A ratio under 1 suggests that the company would be unable to pay off its obligations if they came due at that point. As the number approaches or falls below 1 (which means the company has a negative working capital), investors and stakeholders need to take a close look at the business and make sure there are no liquidity issues. Companies that have ratios around or below 1 should only be those which have inventories that can immediately be converted into cash. On the other hand a very high current ratio means that firm has much cash on hand, and that the management may be doing a poor job of investing it. As seen in services industries, ITES companies generally tend to have a very high current ratio (2+) due to less debts and more retained incomes.

While all the three companies show high current ratios of over 2, Infosys has the highest current ratio of 3. 28. DEBT TO ASSETS RATIO Long term financial strength or soundness of a firm is measured in terms of its ability to pay interest regularly or repay principal on due dates or at the time of maturity taking into account its assets. The debt/asset ratio shows the proportion of a company’s assets which are financed through debt. If the ratio is less than one, most of the company’s assets are financed through equity.

If the ratio is greater than one, most of the company’s assets are financed through debt. Companies with high debt/asset ratios are said to be “ highly leveraged,” and could be in danger if creditors start to demand repayment of debt. Generally a low debt to assets ratio is desirable. Companies with high ratios place themselves at risk, especially in an increasing interest rate market. Creditors are bound to get worried if the company is exposed to a large amount of debt and may demand that the company pay some of it back. As we see in the case of the ITES companies, the amount of debt taken is very less and their repayments can be easily covered by their assets as shown by their low debt to assets ratio.

Infosys has zero debt and thus can be said to have the best asset financing system of the three. EQUITY RATIO = NETWORTH/TOTAL ASSET The Equity Ratio is a good indicator of the level of leverage used by a company. The Equity ratio measures the proportion of the total assets that are financed by stockholders and not creditors. Generally a high equity ratio is desirable as it implies excess of equity financing over debt. A low equity ratio can also produce good results for stockholders as long as the company earns a rate of return on assets that is greater than the interest rate paid to creditors. All the three companies have high equity ratios.

Infosys with no debts has an equity ratio of 1. 22 INTEREST COVERAGE RATIO A ratio used to determine how easily a company can pay interest on outstanding debt. Alternatively, the interest coverage ratio is a measurement of the number of times a company could make its interest payments with its earnings before interest and taxes. Higher the interest coverage ratio better is the firm’s ability to meet its interest burden whereas the lower the ratio, the higher the company’s debt burden. Generally, a firm should try to have an interest coverage ratio of more than 1.

5. An interest coverage ratio below 1. 0 indicates the business is having difficulties generating the cash necessary to pay its interest obligations. Both wipro and TCS maintain very high interest coverage ratio of approx 30 and 1463 respectively. Infosys as mentioned earlier has no debt. Return On Total Assets An indicator of how profitable a company is relative to its total assets.

ROA gives an idea as to how efficient management is at using its assets to generate earnings. The greater a company’s earnings in proportion to its assets (and the greater the coefficient from this calculation), the more effectively that company is said to be using its assets. ITES companies being asset-light firms should generally have a very high ROTA. Both TCS and Infosys have good ROTAs of 0. 454 and 0.

463 respectively. However Wipro has a comparatively lower ROTA of 0. 225. Earning Per Share (EPS) EPS indicates the portion of a company’s profit allocated to each outstanding share of common stock.

EPS serves as an indicator of a company's profitability. A high EPS can contribute to rise in share price of the firm and attract more investors. All the three companies TCS, Infosys and Wipro have High EPS of 46, 17. and 29.

7 respectively. Return On Equity (ROE) It is a measure of a company's profitability that reveals how much profit a company generates with the money shareholders have invested. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. Since it directly links the performance of a firm with the money it raised from its shareholders, a high ROE is desired by all firms to maintain the trust of the shareholders.

Both TCS and Infosys show high ROEs of 0. 41 and 0. 3 while wipro maintains a good ROE of 0. 264 (Comparatively low ROE of wipro can be attributed to its high equity financing). PAT Margin It shows the marginal change in the profit after taxes as compared to the same of previous financial year.

PAT margin reflects directly the success of all managerial strategies and decisions taken during the year. A high PAT margin would imply successful decisions and strategies implemented by the management of the firm whereas a negative or a lower than average margin would indicate a failure of company strategies. PAT margins however could also be influenced by systematic changes like a downturn in the economy, changes made in the taxation policy by the government etc EBIT Margin It shows the marginal change in the profit before interest and taxes as compared to the same of previous financial year. Similar to PAT margin. EBIT margins also reflect the success of all managerial strategies and decisions taken during the year.

EBIT margins are also influenced by systematic changes like emergence of a new technology etc.