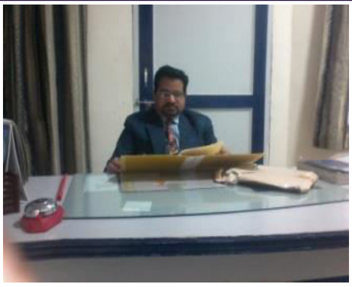

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(A): LIQUIDITY RATIOS

FICTITIOUS ASSETS [UNAMORTISED EXPENSES] [UB-VK-128]:

A.	Shares issue expenses
B.	Discount on issue of shares
C.	Loss on issue of debentures
D.	Underwriters Commissions

I **MEANING**

A. It refers to Ratio which measures short Term Solvency of Business

B. It refers to ratio which measures the ability of concern to meet the short-term obligation as and when they become due.

II **OTHER NAME[ALTERNATE NAMES] & FEATURES**

A. Short term solvency Ratio **[DKG-5.6]**

III **FEATURES:**

A. It also measures Margin of safety available during ***uncertainty of flow*** of funds

B. It indicates the Firm's ability to meet its current obligations ***out of current*** sources ***[DKG-5.3-E-2013]***

C. Short term payables are interested to know how promptly or readily the firm can meet its ***current obligations.***

D. When a firm wants to take short loans from the banks, the Bankers also study the liquidity Ratio of the firm in order to access the margin between current assets and current liabilities

III **TYPES/KINDS:**

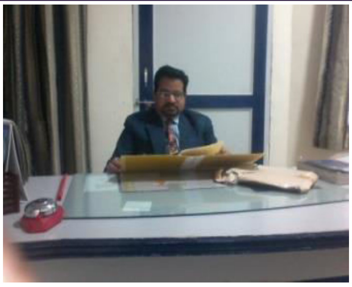
A. Current Ratio

B. Liquid Ratio

(B): CURRENT RATIOS (IMP)

I **MEANING**

A. It refers to Ratio which establishes relationship between current Assets and current Liabilities



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TEST 1

CURRENT RATIO

$$\frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{\text{(Cash + Acct. Recv. + Inventory)}}{\text{(Acct. Paybable + Fed. Income Tax Payable + Misc. Acct. Payable}}$$

A ratio of 2 to 1 is generally regarded as satisfactory.

B. It is a ratio Which express relationship between current Assets and current Liabilities

II **OBJECTIVE**

A. To measure Ability of company to meet short-term obligation

B. To express Short-term soundness of the Business

C. To measure Safety –Margin available for short term creditors

III **FORMULAE**

$$C.R = \frac{CURRENT\ ASSETS}{CURRENT\ LIABILITIES}$$

IV **POINTS FOR PROJECT [FOR DECISION MAKING]**

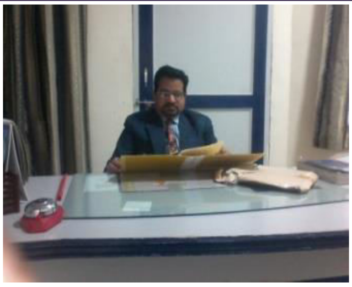
A. Ideal Ratio is 2:1 [It means Current Assets are twice of current liabilities]

B. ***HIGH C.R. RATIO*** reflect the following

1. Better capacity to meet current obligation
2. Availability of Idle funds
3. Lock-up amount in Debtors due to slack collection Policy

C. ***LOW RATIO*** reflect the following

1. Lack of Liquidity
2. Shortage of Working capital



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[C]: CBSE-PROBLEMS-CURRENT RATIO

V **SIGNIFICANCE

A. If C.R. is more than 2:1, it is beneficial to the short term creditors

B. If C.R. is less than 2:1 ,it indicates lack of liquidity and shortage of working capital

VI *DRAW BACKS [DEMERITS]:[DKG-5.8-E-2013]:

A. It is Susceptible to Window Dressing.

B. FOR INSTANCE:

1. If current Assets of Company are ₹ 2,25,000 and current Liabilities are 1.8:1

2. Suppose If Company pays off its trade payables by ₹ 25,000 the current ratio will be 2:1

Q1 **NCERT Q1:Pg 273

Following is the Balance Sheet of Rohit and Company as on March 31,2006

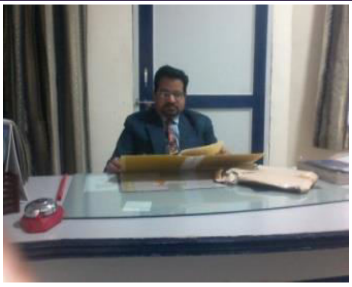
Share Capital	1,90,000	Fixed Assets	1,53,000
Reserves	1,25,000	Stock	55,800
P & L A/C	22,500	Debtors	28800
B/P	18,000	Cash	59400
Creditors	54,000		

ANSWERS:

CA= 144000 ; CL= 72,000 ; C.R = 2:1 which is Ideal

Q2 **NCERT-Q3-PG-273:QUESTION-3:

Current Ratio is 3:5. Working Capital is Rs 9,00,000. Calculate the amount



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of Current Assets and Current Liabilities.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{or, } 3.5 = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

or,

$$\frac{\textit{CURRENT ASSETS}}{\textit{CURRENT LIABILITIES}} = 3.5$$

WORKING CAPITAL = CURRENT ASSETS – CURRENT LIABILITIES
WORKING CAPITAL = 90,000
CURRENT ASSETS–CURRENT LIABILITIES=90,000
3.5 CURRENT LIABILITIES – CURRENT LIABILITIES = 90,000
OR, 2.5 CURRENT LIABILITIES = 90,000

$$\text{or, Current Liabilities} = \frac{90{,}000}{2.5} = 36{,}000$$

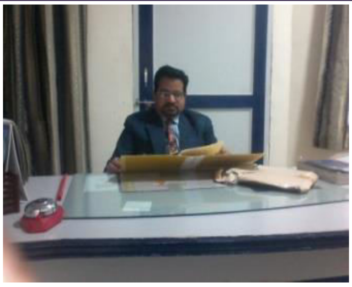
$$\begin{aligned}\text{or, Current Assets} &= 3.5 \text{ Current Liabilities}\\ &= 3.5 \times 36{,}000\\ &= 1{,}26{,}000\end{aligned}$$

Q3 *****CBSE-1999C,2003; TW-306***

Explain briefly the meaning and significance of current Ratio

Q4 ****CBSE-2004; TW-306**

Give any two Example of each of current Assets and Current Liabilities



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(D): LIQUID RATIO(IMP)

TEST 2
ACID-TEST RATIO
Cash + Net receivables + Current Marketable Securities
————————————
Current Liabilities
A ratio of 1 to 1 is generally regarded as satisfactory.

[UB-VK-128]

QUICK ASSETS INCLUDES FOLLOWINGS: UB-VK-31

A.	Current investments
B.	Trade receivables
C.	Cash & cash equivalents
D.	Short term Loans and Advances
E.	Other current assets

Q5 **CBSE: 2002, TW-292

A firm has current Ratio of 4:1 and Quick Ratio of 2.5 : 1. Assuming inventories are Rs 22,500. Find out total Current Assets and Total Current Liabilities

Ans: C.L = 15000; C.A=60,000

I **MEANING:

A. It refers to ratio which express relationship between Liquid Assets and Current Liabilities (XID-68)

B. It is a ratio expressing relationship between Liquid Assets and Current Liabilities

C. According to Soloman J.Frink ," Liquidity is the ability of the Firm to meet its Current Obligations as they fall due" [SAS-664-E-2012]:

II **OTHER NAME:

A. Acid Test Ratio

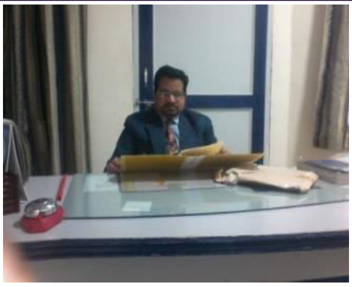
B. Quick Ratio

III **OBJECTIVES

A. To measure the ability of the Firm to meet the short term obligation as and when due relying upon realization of stock

IV **FORMULAE

$$\text{Liquid Ratio} = \frac{\text{LIQUID RATIOS}}{\text{CURRENT LIABILITIES}}$$



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FOLLOWING ARE NOT QUICK ASSETS UB-VK-132:

- A. Raw Materials
- B. Work-in-progress
- C. Finished Assets
- D. Stock-in-trade [in respect of goods acquired for trading]
- E. Stores & spares
- F. Loose Tools
- G. Fictitious assets

V ****POINTS FOR CONCLUSION/DECESION**

A. Ideal Quick Ratio is 1:1

B. 1:1 Ratio indicates the 100% availability of funds to meet liabilities.

C. It is calculated at particular date(not for particular Period)

D. It shows very Short Term Liquidity or Capacity of the Business to meet its Obligation at Short Notice [Ordinarilly within one months] [SAS-665-E-2012]

VI ****SIGNIFICANCE:**

A. 1:1 Ratio indicates availability of funds to meet the liability 100%

VII ****(NCERT-273,Q2)**

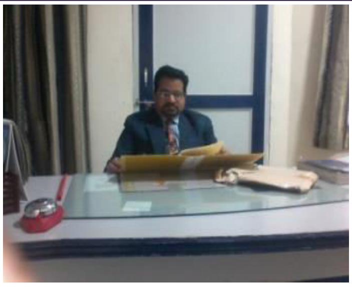
Following is the Balance Sheet of Title Machine Ltd as on March 31,2006

Equity Share Capital	24,000	Building	45,000
8% Debenture	9,000	Stock	12,000
P & L A/C	6,000	Debtors	9,000
Bank O/D	6,000	Cash	2280
Creditors	23,400	Prepaid	
Prov. For Tax	600	Expenses	720

Calculate current Ratio and Liquid Ratio

ANSWER:

Quick Assets = 11280; Current Liabilities =30,000; Quick Ratio = 0.376



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VIII

**NCERT-Q11-PG-274☹(PART-IV)

From the following information calculate:

A. Gross Profit Ratio

B. Inventory Turnover Ratio

C. Current Ratio

D. Liquid Ratio

E. Net Profit Ratio

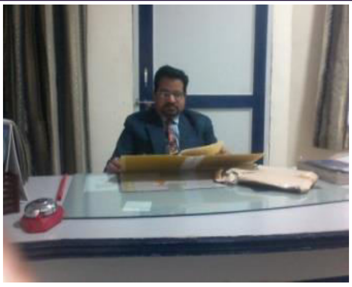
F. Working capital Ratio:

	Rs
Sales	25,20,000
Net Profit	3,60,000
Cast of Sales	19,20,000
Long-term Debts	9,00,000
Creditors	2,00,000
Average Inventory	8,00,000
Current Assets	7,60,000
Fixed Assets	14,40,000
Current Liabilities	6,00,000
Net Profit before Interest and Tax	8,00,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\begin{aligned}\text{Current Asset } &= \text{Liquid Assets} + \text{Stock}\\ &= 7,60,000 + 8,00,000\\ &= 15,60,000\end{aligned}$$

$$\text{Current Ratio} = \frac{15,60,000}{6,00,000} = \frac{2.6}{1} = 2.6:1$$



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$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}} = \frac{7,60,000}{6,00,000} = \frac{1.27}{1} = 1.27.$$

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Net Sales}} \times 100 = \frac{3,60,000}{25,20,000} \times 100 = 14.28\%$$

(E) : LIQUID ASSETS

I **MEANING**

A. It refers to those Assets which can be converted into cash quickly or without much loss of time.

B. It implies current Assets minus closing Stock and prepaid Expenses

II **OTHER NAME**

A. Quick Assets

III **INSTANCES**

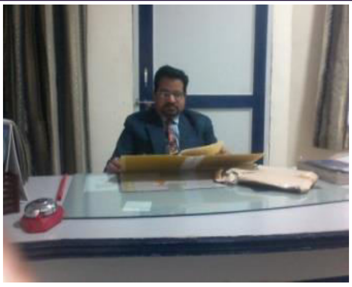
A. Cash and Bank

B. Debtors less Provisions

C. Advances & Deposits

IV **FORMULA**

LIQUID ASSETS = Current Assets – Prepaid Exp- Stock



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(E) : CURRENT ASSETS

CURRENT INVESTMENT[TSG-IA-9-OLD] [CONVERTIBLE INTO CASH WITHIN 12MONTHS]

A. Investment in Equity Instrument	X
B. Investment In Pref. Shares	X
C. Investment in Govt Or Trust Securities	X
D. Investment In Mutual Funds	X
E. Investment In Partnership Firm	X
F. Investment in Debenture Or Bonds	X
G. Other Investment [Convertible into cash within 12 months]	X

INVENTORIES-LIST[TSG-IA-9-OL]

A. Stock in Trade	XX
B. Raw Material	XX
C. Work in Progress	XX
D. Finished	XX
E. Stores & Spares ×	XX
F. Loose Tools ×	XX
G. Others	XX

NOTES

Inventories donot include Loose Tools and spares and stores for the calculation of ratios

I **MEANING

A. It refers to those Assets which are either in form of cash or can be converted into cash within one year

B. It refers to Assets which can be converted into cash within one year

C. It refers to those Assets which can be converted into cash or cash Equivalents within short period of time [Usually one year]

II **PARTS/COMPONENTS

A. Most liquid or Quick Assets

B. *PLUS LESS* Liquid Assets

C. Although bank Overdraft, cash and bank are CASH AND CASH EQUIVALENT it is included in current liabilities for calculations of accounting ratio [V.IMP] [DKG-5.7-E-2013]

III **QUICK ASSETS (MOST LIQUID ASSETS)

A. Cash & Bank

B. Debtors less Provisions

C. B/R less Provision

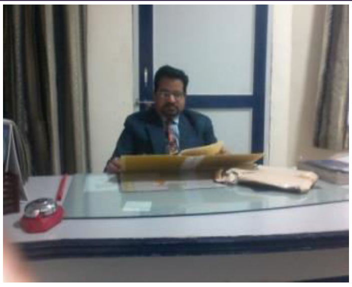
D. Marketable Securities at realizable Value

E. SHORT TERM INVESTMENT[DKG-5.7-E-2013]

IV OTHER LESS LIQUID ASSETS BUT CURRENT ASSETS:

A. Prepaid Expenses

B. Advance Payments



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C. Advance Income Tax paid [PCT-12.95]

D. Stock, Merchandise

E. Current Investment

(G): CURRENT LIABILITY

I **MEANING

A. It refers to Liability which are to be paid within a year

B. It refers to Liabilities which are expected to be matured within one year

ADDITIONAL FORMULAE

CURRENT LIABILITY = TOTAL DEBT – L.T. DEBT
CURRENT ALIABILITY = CURRENT ASSETS – WORKING CAPITAL

II **CURRENT LIABILITIES[LISTS]

A. Creditors

B. Bills Payable

C. Bank O/D

D. Accrued Interest but not due on Debentures

E. Advances Received from Customers

(G): NCERT-BOOK QUESTIONS

Q1 **NCERT-Q3-PG-273:QUESTION-3:

Current Ratio is 3:5. Working Capital is Rs 9,00,000. Calculate the amount of Current Assets and Current Liabilities.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{or, } 3.5 = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

or, Current Assets = 3.5 ; Current Liabilities (**1**)

Working Capital = Current Assets – Current Liabilities

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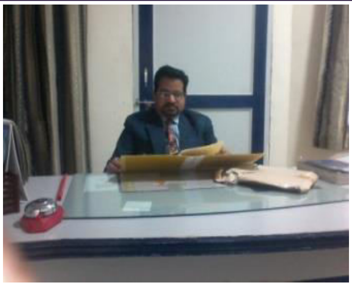


Working Capital = 90,000
or, Current Assets – Current Liabilities = 90,000
or, 3.5 Current Liabilities – Current Liabilities = 90,000 (from **1**)
or, 2.5 Current Liabilities = 90,000

$$\text{or, Current Liabilities} = \frac{90{,}000}{2.5} = 36{,}000$$

$$\begin{aligned}\text{or, Current Assets} &= 3.5 \text{ Current Liabilities} \\ &= 3.5 \times 36{,}000 \\ &= 1{,}26{,}000\end{aligned}$$

Q2 ***NCERT-Q4-PG-273***

Shine Limited has a current ratio 4.5:1 and quick ratio 3:1; if the stock is 36,000, calculate current liabilities and current assets.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\frac{4.5}{1} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

or, 4.5 Current Liabilities = Current Assets

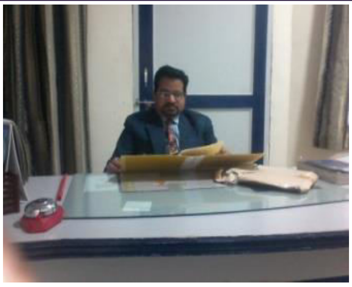
$$\text{Quick ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}}$$

$$3:1 = \frac{\text{Quick Assets}}{\text{Current Liabilities}}$$

or, 3 Current Liabilities = Quick Assets

$$\begin{aligned}\text{Quick Assets} &= \text{Current Assets} - \text{Stock} \\ &= \text{Current Assets} - 36{,}000\end{aligned}$$

or, 4.5 Current Liabilities – 3 Current Liabilities = 36,000



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or, 1.5 Current Liabilities = 36,000
or, Current Liabilities = 24,000
Current Assets = 4.5 Current Liabilities

$$\text{or, Current Assets} = 4.5 \times 24{,}000$$
$$= 1{,}08{,}000$$

Q3 ***NCERT-Q5:-PG-27***

Current liabilities of a company are Rs 75,000. If current ratio is 4:1 and liquid ratio is 1:1, calculate value of current assets, liquid assets and stock.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$
$$\text{or, } 4 = \frac{\text{Current Assets}}{75{,}000}$$

or, 4 × 75,000 = Current Assets
or, Current Assets = 3,00,000

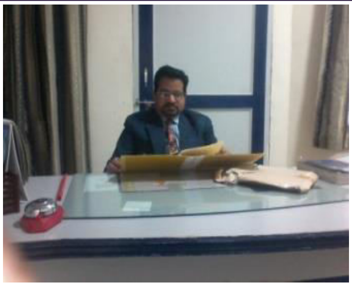
$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

or, $1 = \frac{\text{Liquid Assets}}{75{,}000}$

Liquid Assets = 75,000

$$\text{Stock} = \text{Current Assets} - \text{Liquid Assets}$$
$$= 3{,}00{,}000 - 75{,}000$$
$$= 2{,}25{,}000$$

Q4 ***NCERT-Q6-PG-273:***
Handa Ltd.has stock of Rs 20,000. Total liquid assets are Rs 1,00,000 and quick ratio is 2:1. Calculate current ratio.



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$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilties}}$$

$$2 = \frac{1,00,000}{\text{Current Liabilities}}$$

$$\text{or, Current Liabilities} = \frac{1,00,000}{2}$$

$$= 50,000$$

$$\text{Current Assets} = \text{Liquid Assets} + \text{Stock}$$

$$= 1,00,000 + 20,000$$

$$= 1,20,000.$$

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilties}}$$

$$= \frac{1,20,000}{50,000}$$

$$= \frac{2.4}{1} = 2.4:1$$

Q5 **NCERT-Q8-PG-274:

Calculate Current Ratio if:Stock is Rs 6,00,000; Liquid Assets Rs 24,00,000; Quick Ratio 2:1.

$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilties}}$$

$$2 = \frac{24,00,000}{\text{Current Liabilities}}$$

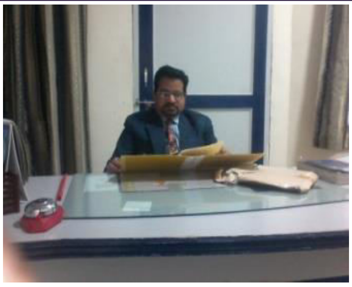
$$\text{Current Liabilities} = \frac{24,00,000}{2}$$

$$= 12,00,000$$

$$\text{Current Assets} = \text{Liquid Assets} + \text{Stock}$$

$$= 24,00,000 + 6,00,000$$

$$= 30,00,000.$$



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$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$= \frac{30,00,000}{12,00,000} = \frac{2.5}{1} = 2.5:1$$

Q6 **NCERT-Q10-PG-274-(PART-I AND II)

Calculate following ratios from the following information:

A. Current ratio

B. Acid test ratio

C. Operating Ratio

D. Gross Profit Ratio

	Rs
Current Assets	35,000
Current Liabilities	17,500
Stock	15,000
Operating Expenses	20,000
Sales	60,000
Cost of Goods Sold	30,000

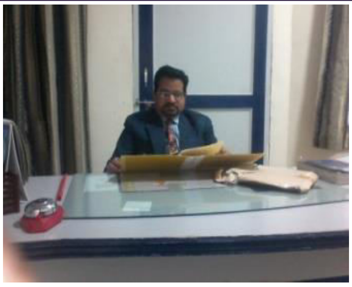
$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Current Ratio} = \frac{35,000}{17,500} = 2:1$$

$$\text{Acid Test Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$\begin{aligned}\text{Liquid Assets} &= \text{Current Assets} - \text{Stock}\\ &= 35,000 - 15,000\\ &= 20,000\end{aligned}$$

$$\text{Acid Test Ratio} = \frac{20,000}{17,500} = \frac{1.143}{1} = 1.143:1$$



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Q7 **NCERT-Q11-PG-274(PART(III):

From the following information calculate:

A. Gross Profit Ratio

B. Inventory Turnover Ratio

C. Current Ratio

D. Liquid Ratio

E. Net Profit Ratio

F. Working capital Ratio:

	Rs
Sales	25,20,000
Net Profit	3,60,000
Cast of Sales	19,20,000
Long-term Debts	9,00,000
Creditors	2,00,000
Average Inventory	8,00,000
Current Assets	7,60,000
Fixed Assets	14,40,000
Current Liabilities	6,00,000
Net Profit before Interest and Tax	8,00,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\begin{aligned}\text{Current Asset} &= \text{Liquid Assets} + \text{Stock}\\ &= 7,60,000 + 8,00,000\\ &= 15,60,000\end{aligned}$$

$$\text{Current Ratio} = \frac{15,60,000}{6,00,000} = \frac{2.6}{1} = 2.6:1$$

$$\begin{aligned}\text{Liquid Ratio} &= \frac{\text{Liquid Assets}}{\text{Current Liabilities}}\\ &= \frac{7,60,000}{6,00,000}\\ &= \frac{1.27}{1}\\ &= 1.27.\end{aligned}$$