CONCEPT: RATIOS – AVERAGE COLLECTION PERIOD (DAYS' SALES OUTSTANDING)

- The ***Average Collection Period*** helps analyze how long a dollar sits in accounts receivable before being ____________
  - □ The Average Collection Period ratio is a common ________________ ratio
  - □ Extending credit ties up money (i.e. cash unavailable until collected from customer; can't repurchase inventory)
  - □ Average Collection Period is related to the AR Turnover Ratio, which we will review here:

$$AR\ Turnover = \frac{Net\ (Credit)\ Sales}{Average\ Net\ AR\ Balance} = \frac{Net\ (Credit)\ Sales}{(Beginning\ AR + Ending\ AR) \div 2}$$

$$Average\ Collection\ Period = \frac{365}{AR\ Turnover}$$

Analysis: The Average Collection Period tells us how many *days* a dollar sits in AR before being collected

Comparison: Different industries have different reasonable collection periods, use ***benchmarking***
______________ collection periods imply a more efficient use of AR (extending credit)

EXAMPLE: XYZ Company had net sales of $500,000 and COGS of $320,000. If the beginning balance of AR was $75,000 and the ending balance in AR was $25,000, what is the average collection period?

a) 101 days
b) 55 days
c) 37 days
d) 18 days

PRACTICE: ABC Company had $200,000 in Net Sales and Gross Profit of $80,000. If AR had a balance of $16,000, what are the days' sales outstanding?

a) 73 days
b) 49 days
c) 29 days
d) Not enough information