CONCEPT: RATIOS – WORKING CAPITAL AND THE CURRENT RATIO

● The concepts of working capital and the current ratio are very similar, so we will study them together

□ The current ratio is the most common ________________ ratio

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

Analysis: The current ratio tells us how many dollars of current assets are available for each dollar of current liabilities

Red Flag: A current ratio below ________ is generally a sign of liquidity problems.

□ Working capital is not technically a ratio, but still a helpful financial analysis tool

$$Working\ Capital = Current\ Assets - Current\ Liabilities$$

Analysis: Positive working capital indicates short-term financial stability.

Red Flag: Negative working capital generally indicates short-term financial problems.
Also, abnormally high working capital could indicate inefficient management of assets.

EXAMPLE: Super Liquid Company has current assets totaling $450,000 and current liabilities totaling $315,000. Calculate the current ratio and working capital for SLC.

PRACTICE: The following table contains selected financial information for Tougher Question, Inc.

Cash	$45,000		Inventory	$25,000
Machinery	$80,000		Accounts Payable	$30,000
Accounts Receivable	$10,000		Common Stock	$50,000
Short Term Debt	$40,000		Bonds Payable	$100,000
Land	$60,000		Prepaid Expenses	$15,000
Accrued Expenses	$35,000		Retained Earnings	$20,000

Calculate the current ratio and working capital for TQ, Inc.