Appendix A: Definition of Financial Ratios

Ratio	Computation method	Significance
Liquidity:		
Current	Current assets/Current liabilities	Measures the farm business' ability to pay its debts as they come due.
Quick	Current assets-Inventory/Current liabilities	Eliminates source of likely loss from current ratio.
Net capital	Total assets/Total liabilities	Measures the farm business' ability to cover all debt.
Farm business debt service coverage	Net farm income+interest/ Interest+principal payment	Measures the farm business' ability to repay both interest and principal.
Debt servicing	Interest+principal payments/ Gross cash farm income	Measures the share of the farm business' gross income needed to service debt.
Times interest	Net farm income before interest and taxes/Interest payments	Measures the farm business' ability to to service debt out of net income earned.
Efficiency:		
Gross	Cash operating expenses/ Gross cash farm income	Measures the proportion of gross cash farm income absorbed by cash operating expenses.
Fixed	Total fixed expenses/ Gross cash farm income	Measures the proportion of gross cash farm income absorbed by fixed expenses.
Interest to gross cash income	Interest/Gross cash farm income	Measures the share of gross cash farm income committed to interest payments.
Asset turnover	Gross cash farm income/ Farm business assets	Measures the gross farm income generated per dollar of farm business assets.
Debt-burden	Net cash farm income/ Farm business debt	Measures the burden placed on net cash farm income to retire outstanding debt.
Leverage	Total liabilities/Net worth	Measures the proportion to which debt is used, as related to equity capital, to finance the total farm business.
Solvency:		
Debt to assets	Farm business debt/ Farm business assets	Measures debt pledged against farm business assets, indicating overall financial risk.
Debt to equity	Farm business debt/ Farm business equity	Measures the relative proportion of funds invested by creditors and owners.

Profitability:

Rate of return on assets Current income	Returns to farm assets from current income/ Farm business assets	Measures how efficiently the farm business uses its assets; the per-dollar return on farm assets.
Rate of return on equity Current income	Returns to farm assets from current income-interest/ Farm business equity	Measures the returns to equity capital employed in the farm business from current income.
Profit margin	Net farm income/ Gross cash farm income	Measures profits earned per dollar of the value of farm production.
Economic profit margin	Net farm income minus an imputed value for non-operator unpaid labor and a return to owned assets/ Gross cash farm income	Measures ‘net’ profits earned per dollar of the value of farm production.