QB365 Question Bank Software Study Materials

Ratio Analysis Important 2 Marks Questions With Answers (Book Back and Creative)

12th Standard

Accountancy

Total Marks : 40

2 Marks

20 x 2 = 40

1) What is meant by accounting ratios?

Answer : (i) Ratio is a mathematical expression of relationship between two related or interdependent items.

(ii) It is the numerical or quantitative relationship between two items

(iii) It is calculated by dividing one item by the other related item.

(iv) When ratios are calculated on the basis of accounting information, these are called 'accounting ratios'.

2) What is meant by debt equity ratio?

Answer : (i) Debt equity ratio is calculated to assess the long term solvency position of a business concern.

(ii) Debt equity ratio expresses the relationship between long term debt and shareholders' funds.

(iii) It is computed as follows:

Debt enquity ratio = $\frac{Long\ term\ debt}{Shareholders\ funds}$

Long term debt = Debentures, bonds, long term loans, other long term borrowing. Share holder's fund = Equity share capital + Preference share capital + reserves and surplus

3) What does return on investment ratio indicate?

Answer : (i) Return on investment shows the proportion of net profit. before interest and tax to capital employed (shareholders' funds and long term debts).

(ii) This ratio measures how efficiently the capital employed is used in the business.

(iii) It is an overall measure of profitability of a business concern.

(iv) It is computed as below: Return on Investment (ROI)

= $\frac{Net\ profit\ before\ interest\ and\ tax}{Capital\ employed}$ x 100

Capital employed = Share holder's fund + Non currebt liablities greater the return on investment better is the profitability of a business and vice versa

4) Calculate the current ratio from the following information.

PARTICULARS	RS.	PARTICULARS	RS.
Current investments	40,000	Fixed assets	5,00,000
Inventories	2,00,000	Trade creditors	80,000
Trade debtors	1,20,000	Bills payable	50,000
Bills receivable	80,000	Expenses payable	20,000
Cash and cash equivalents	10,000	Non-current liability	3,00,000

Answer : Current ratio = $\frac{Current\ assets}{Current\ liabilities}$

Current assets = Current investments + Inventories + Bills receivables + Trade debtors + Cash and cash equivalents

= Rs.40,000 + Rs.2,00,000 + Rs.1,20,000 + Rs. 80,000 + Rs.10,000

= Rs.4,50,000

Current liabilities = Trade creditors + Bills payable + Expenses payable

= Rs.80,000 + Rs.50,000 + Rs.20,000 = Rs.1,50,000

Current ratio = $\frac{4,50,000}{1,50,000}$ = 3:1

5) Calculate quick ratio: Total current liabilities Rs. 2,40,000; Total current assets Rs. 4,50,000; Inventories Rs. 70,000; Prepaid expenses Rs. 20,000.

Answer : Quick ratio = $\frac{Quick\quad assets}{Current\quad liabilities}$

Quick assets = Current assets - Inventories - Prepaid expenses

= Rs.4,50,00 + Rs.70,000 - Rs.20,000

= Rs.3,60,000

Quick ratio = $\frac{3,60,000}{2,40,000}$ = 1:5:1

6) From the following information of Geetha Ltd., calculate fixed assets turnover ratio

(i) Revenue from operations during the year were Rs. 55,00,000.

(ii) Fixed assets at the end of the year Rs. 5,00,000.

Answer : Fixed assets turnover ratio = $\frac{\textit{Revenue from operations}}{\textit{Average fixed assets}}$

= $\frac{55,00,000}{5,00,000}$ = 11 times

7) Calculate gross profit ratio from the following:

Revenue from operations Rs. 2,50,000, Cost of revenue from operations Rs. 2,10,000 and Purchases Rs. 1,80,000.

Answer : Gross profit ratio = $\frac{\textit{Gross profit}}{\textit{Revenue from operations}} \times 100$

Gross profit = Revenue from operations - Cost of revenue from operations

= Rs.2,50,000 - Rs.2,10,000

= Rs.40,000

∴ Gross profit ratio = $\frac{40,000}{2,50,000} \times 100$ = 16%

8) Calculate quick ratio of Ananth Constructions Ltd from the information given below.

PARTICULARS	RS.
Total current liabilities	1,00,000
Total current assets	2,50,000
Inventories	50,000
Prepaid expenses	15,000

Answer : Quick ratio = $\frac{\textit{Quick assets}}{\textit{Current liabilities}} = \frac{1,85,000}{1,00,000}$ = 1.85:1

Quick assets = Current assets – Inventories – Prepaid expenses

= 2,50,000 – 50,000 – 15,000

= Rs.1,85,000

9) Calculate gross profit ratio from the following:

Revenue from operations Rs.1,00,000, Cost of revenue from operations Rs.80,000 and purchases Rs. 62,500

Answer : $Gross\ profit\ ratio = \frac{Gross\ profit}{Revenue\ from\ operators} \times 100$

= $\frac{20,000}{1,00,000} \times 100 = 20\%$

Gross profit = Revenue from operations – Cost of revenue from operations

= 1,00,000 – 80,000 = Rs.20,000

(ii) Operating cost ratio

Operating cost ratio is the proportion of operating cost to revenue from operations.

This ratio is a test of the operational efficiency of the business. It is calculated as under.

$$Operating\ cost\ ratio = \frac{Operating\ cost}{Revenue\ from\ operations} \times 100$$

Operating cost is the cost which is associated with the operating activities of the business.

Operating cost = Cost of revenue from operations + Operating expenses

Operating expenses = Employee benefit expenses + Depreciation + Other expenses related to office and administration, selling and distribution

A lower operating ratio indicates better profitability. Lesser the operating cost ratio, higher is the margin available for payment of non operating expenses such as interest on loans, loss on sale of fixed assets, etc

10) From the following information calculate capital gearing ratio:

PARTICULARS	RS.
I EQUITY AND LIABILITIES	
1. Shareholders' funds	
(a) Share capital	
Equity share capital	2,00,000
6% Preference share capital	1,00,000
(b) Reserves and surplus	

PARTICULARS	RS.
General reserve	1,25,000
Surplus	75,000
2. Non-current liabilities	
Long-term borrowings (8% Debentures)	2,00,000
3. Current liabilities	
Trade payables	1,50,000
Provision for tax	50,000
Total	9,00,000

Balance Sheet (Extract) as on 31.03.2018

Answer : Capital gearing ratio = $\frac{Funds\ bearing\ fixed\ interest\ and\ fixed\ dividend}{Equity\ shareholders'\ funds}$

= $\frac{3,00,000}{4,00,000}$ = 0.75:1

Funds bearing fixed interest and dividend = 6% Preference share capital + 8% Debentures

= 1,00,000 + 2,00,000 = Rs.3,00,000

Equity shareholder's funds = Equity share capital + General reserve + Surplus

= 2,00,000 + 1,25,000 + 75,000 = Rs.4,00,000

11) Definition of ratio analysis.

Answer : According to Myers, "Ratio analysis is a study of relationship among various financial factors in a business':

12) What is current ratio?

Answer : Current ratio gives the proportion of current assets to current liabilities of a business concern. It is computed by dividing current assets by current liabilities. It is calculated as follows:

Current ratio = $\frac{Currentassets}{Currentliabilities}$.

13) What does high total assets to debt ratio indicates?

Answer : High total assets to debt ratio indicates that assets have been mainly financed by owner's funds and the long-term debt is adequately covered by assets.

14) Quick ratio of a company is 1.5: 1.State giving reason, whether the ratio will improve, decline or not change on payment of divided by the company.

Answer : Ratio will increases as both the quick assets and current liabilities i.e., cash and creditors, will decreases by the same amount.

15) How does ratio analysis become less effective due to does ratio changes?

Answer : Accounting ratio are calculated from financial statements which are drawn on the basis of historical costs as recorded in the books of accounts. Thus. these ratios ignore the change in price level and they do not reflect the actual analysis.

16) The liquidity of a business firm is measured by its ability to satisfy its long-term obligations as they become due. Comments.

Answer : Yes, it is true that the liquidity of a business firm is measured by its ability to pay its long-term obligations as they become due. Here, the longterm obligation means payment of principal amount on the due date and payment of interest on the regular basis.

For measuring the long term solvency of any business, we calculate the following ratio.

(i) Debt equity ratio

(ii) Proprietary ratio

17) Give any two reasons.of increase in gross profit.

Answer : (i) Selling price· may have increased without the same increase in the price of materials and wages.

(ii) Gross profit may be hi

18) What is meant by Tradional classification of ratio?

Answer : Tradional classification of ratios is done on the basis of the financial Statements from which the ratios are calculated. Under the tradional Classification: the ratios are classified

(i) Balance sheet ratio

(ii) Income statement ratios and

(iii) Inter statement ratio

19) What is meant by liquidity ratios?

Answer : It means capability of being converted into Cash. Liquidity ratios help to access the ability of a business concern, to meet its short term financial obligations. It includes

(i) Current ratio

(ii) Quick ratio

20) What is the meaning of current Ratio?

Answer : Current ratio gives the proportion of Current assets to current liabilities, of a business . concern. It ·is computed by dividing current assets by current liabilities. It indicates the ability of an entity to meet its Current. liabilities, as and when they are due for payment

$$\text{Current Ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$