Measuring Liquidity

You need to be able to learn and use liquidity ratios to help you draw conclusions on the performance of an organisation.

The ratios that you need to learn are;

Current Ratio

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

This shows the level of current assets compared to current liabilities. It is expressed as a ratio. For example 2:1 means that for every £1 in current liabilities the organisation has £2 in current assets.

This means that the organisation can pay all of their current liabilities if payment was demanded quickly. The ideal industry standard for this figure is between £1.50 and £2 in current assets for every £1 of current liabilities.

Liquid Capital Ratio (Acid Test)

$$\frac{\text{(Current Assets – Inventory)}}{\text{Current Liabilities}}$$

This shows the level of current assets excluding inventories, compared to current liabilities. This ratio takes the view that stock needs to be sold and isn't so quickly turned into cash. It will depreciate in value over time and if sold quickly then the value of this asset will be reduced.

It is expressed as a ratio. For example 0.5:1 means that for every £1 in current liabilities the organisation has £0.50 in liquid assets. This means that the organisation could not meet all of their current liabilities in this example. The ideal industry standard for this figure is between £0.75 and £1 in current assets for every £1 of current liabilities.

Supermarket Sweep

You are going to conduct some liquidity ratio analysis on 4 different well known UK supermarkets. All of the financial information that you will need will be included in the annual reports.

You can find the annual reports for each of these organisations in in the F3 section of this page; http://www.beebusinessbee.co.uk/index.php/business-qualifications/btec-nationals-business-level-3/btec-nationals-2016

You should focus your ratios on **one year** for each organisation and keep this the same for all organisations once selected.

You should use this information to complete the table below.

Chosen Year:

Organisation	Current Ratio	Liquid Capital Ratio
Tesco		
Sainsbury's		
Morrison's		
Marks and Spencer		

Now that you have completed this ratio analysis.

Evaluate in your option which supermarket is performing the best when focusing on liquidity?