Academy for Lease & Finance Professionals
Credit Example

Balance Sheet

Cash	$1,000,000	**Accounts Payable**	$1,300,000
Accounts Receivable	$1,500,000	**Current Portion of Long Term Debt**	$1,000,000
Fixed Assets	$6,000,000	**Long Term Debt**	$3,500,000
Other Assets	$80,000	**Total Liabilities**	$5,800,000
		Net Worth	$2,780,000
Total Assets	$8,580,000	**Total Liabilities & Net Worth**	$8,580,000

Income Statement

Revenue	$18,000,000
Cost of Sales	$15,000,000
G & A	$1,800,000
Total Expenses	$16,800,000
Income (before tax)	$1,200,000
Income taxes	$480,000
Income (after tax)	$720,000

ABC Company has come to you to lease a $1,250,000 machine tool over a seven-year period.

Review the following condensed financial information, then calculate the following ratios.
a. Debt to equity
b. Current ratio
c. Return on equity
d. Gross profit margin

ANSWERS:

a. Debt to equity = (Total Liabilities / Net Worth)
Debts divided by equity

$\frac{\$5,800,000}{\$2,780,000}$ = **2.086:1**

A ratio of 2:1 is pretty good; every $2 of debt you take one, you have a $1 worth of equity.

b. Current ratio = ((Cash + Accounts Receivable) / (Accounts Payable + Current Portion of LT Debt))
Current assets divided by current liabilities

$\frac{\$2,500,000}{\$2,300,000}$ = **1.086:1**

Generally, a ratio of more than 1.25:1 is preferred.

c. Return on equity = (Income after tax) / Net worth)
Income after tax divided by equity

$\frac{\$720,000}{\$2,780,000}$ = **25.9%**

If you were to invest in this company, for every $1, you'll get a $0.26 return. This is a good ratio.

d. Gross profit margin = ((Revenues - Costs of Goods Sold))/Net Sales)
Gross profit on Sales divided by net sales
$\frac{\$3,000,000}{\$18,000,000}$ = **16.67%**