

[Issued in March 2025]

## Background

Financial ratios are used by CARE Ratings Limited (CareEdge Ratings) to make a holistic assessment of the financial performance of an entity, and in evaluating the entity's performance vis-à-vis its peers within the industry. Financial ratios are not an 'end' by themselves but a 'means' to understanding the fundamentals of an entity. This document provides a general list of ratios used by CareEdge Ratings in its credit risk assessment for manufacturing, trading and service sector entities. These ratios are applied on the past financial statements of entities as well as for future projections. In addition to ratios mentioned in this document, various other sector-specific ratios are used, or certain adjustments are made to financial ratios of entities belonging to certain sectors like real estate, construction, infrastructure etc., for evaluating entities in these sectors. CareEdge Ratings' sector-specific rating methodologies are available on its website [www.careratings.com](http://www.careratings.com).

Financial ratios commonly used by CareEdge Ratings can be categorised into the following four types:

- Growth ratios
- Profitability ratios
- Leverage and coverage ratios
- Turnover and liquidity ratios

These are given in detail below:

### A. Growth ratios

Trends in the growth rates in income and profitability of an entity vis-à-vis the industry reflect its ability to sustain its market share, profitability and operating efficiency. In this regard, CareEdge Ratings focuses on growth in income, profit before interest, lease rentals, depreciation and tax (PBILDT) and profit after tax (PAT). Growth ratios considered by CareEdge Ratings include the following ('t' refers to the current period while 't-1' refers to the immediately preceding period):

Ratio	Formula
Growth in Net Sales	$\frac{[(\text{Net Sales}_t \times 12 / \text{No. of Months}) - (\text{Net Sales}_{t-1} \times 12 / \text{No. of Months})] \times 100}{[\text{Net Sales}_{t-1} \times 12 / \text{No. of Months}]}$
Growth in Total Operating Income (TOI)	$\frac{[(\text{TOI}_t \times 12 / \text{No. of Months}) - (\text{TOI}_{t-1} \times 12 / \text{No. of Months})] \times 100}{[\text{TOI}_{t-1} \times 12 / \text{No. of Months}]}$
Growth in PBILDT	$\frac{[(\text{PBILDT}_t \times 12 / \text{No. of Months}) - (\text{PBILDT}_{t-1} \times 12 / \text{No. of Months})] \times 100}{[\text{PBILDT}_{t-1} \times 12 / \text{No. of Months}]}$
Growth in PAT	$\frac{[(\text{PAT}_t \times 12 / \text{No. of Months}) - (\text{PAT}_{t-1} \times 12 / \text{No. of Months})] \times 100}{[\text{PAT}_{t-1} \times 12 / \text{No. of Months}]}$

- **TOI** - For computing the TOI, CareEdge Ratings considers the **entire operating income** of the entity. For arriving at the core sales figure, the indirect tax expenses incurred by the entity (like Goods and Services Tax [GST], excise duty, sales tax, service tax, etc.) are netted-off from the gross sales. CareEdge Ratings also includes some **other income related to the core operations** like income derived from job work done by the

entity, any royalty / technical knowhow / commission received in relation to the core operations, refund of indirect taxes, sale of scrap, cash discount received, duty drawback and other export incentives received by the entity and exchange rate gain (not related to debt). Non-core income items do not form part of the TOI.

CareEdge Ratings considers interest income, dividend income, rental income, etc., as non-operating income as these are non-core income items, even though these items may be **recurring in nature**.

- **PBILDT** - To arrive at the PBILDT, all operating expenses are deducted from the TOI. Operating expenses include raw material cost, cost of traded goods purchased, stores and spares, power and fuel, employee costs, selling and distribution expenses and administrative and general expenses, and include royalty / technical knowhow / commission incurred, insurance cost, directors' fees, exchange rate loss (not related to debt), bad debts, etc.
- **PAT** - PAT is arrived at by deducting (-) / adding (+) the following from / to the PBILDT:

(-) Interest and finance charges net of capitalised interest cost. This includes all the finance charges incurred by the entity, including interest on term loans, interest on working capital borrowings, interest on unsecured loans from the promoters / group entities, interest on lease liability, premium on redemption of bonds and preference shares, gains / losses arising out of exchange rate fluctuation on debt, etc.

(-) depreciation / amortisation on assets, including depreciation on right-to-use assets.

(+/-) non-operating income / expense (including non-core income / expenses and profit / loss on sale of assets and investments).

(+/-) prior period items (including income tax).

(-) tax expense (both current and deferred taxes).

- **Gross cash accruals (GCA)** - GCA is computed by adding all inherently non-cash expenditure (like depreciation and amortisation, excluding depreciation on right-to-use assets created pursuant to adoption of INDAS 116), provision for deferred tax, write-offs, etc. to the PAT. However, the expenditures which are not inherently non-cash from an accrual accounting perspective such as provision for bad debts, doubtful debts or warranties are usually not added back.

## B. Profitability and return ratios

Ability of an entity to earn profit determines its positioning in the value chain. Profitability reflects the final result of the business operations. Important measures of profitability are PBILDT margin, PAT margin, return on capital employed (ROCE) and return on networth (RONW). Profitability ratios are not regarded in isolation but are seen in conjunction with the peers and the industry segment(s) in which the entity operates. Profitability ratios considered by CareEdge Ratings include:

Ratio	Formula		Significance in the Analysis
PBILDT Margin	PBILDT / TOI	× 100	A key indicator of operating efficiency in any manufacturing / trading / service activity without considering the financing mix and the tax expenditure of the entity.
PAT Margin	PAT / TOI	× 100	Considers both business risk and financial risk. This is the margin available for the distribution to the equity shareholders.
ROCE	$\frac{[(\text{PBIT} \pm \text{Non-Operating Income} / \text{Expenses} \pm \text{Extraordinary Income} / \text{Expenses} \pm \text{Other Comprehensive Income}) \times (12 / \text{No. of Months})]}{[\text{Avg. (TCE}_t, \text{TCE}_{t-1})]}$ <p>TCE: Total Capital Employed = Tangible Network + Total Debt + Net Deferred Tax Liabilities / (Assets) (OR) Net Fixed Assets + Net Working Capital</p>	× 100	ROCE reflects the earnings capacity of assets deployed, ignoring the taxation and the financing mix. It is an important tool for comparison of performance of entities within the industry.
RONW	$\frac{[(\text{PAT} \pm \text{Other Comprehensive Income}) \times (12 / \text{No. of Months})]}{[\text{Avg. (Tangible Network}_t, \text{Tangible Network}_{t-1})]}$	× 100	RONW reflects the return to the equity shareholders.

- **Tangible network** of the entity includes equity share capital, all reserves and surplus (excluding revaluation reserve), unsecured loans from the promoters / group entities which are subordinated to the outside loans, equity share warrants, share application money, employee stock ownership plan (ESOPs) outstanding and minority interest (in case of consolidated financials). Other considerations while calculating the tangible network are highlighted below:
  - Miscellaneous expenditure not written-off and accumulated losses - Both miscellaneous expenditure not written-off and accumulated losses are deducted from the above to arrive at the tangible network.
  - Revaluation reserves - Revaluation reserves arising out of revaluation of fixed assets are not treated as a part of the tangible network of the entity.
  - Treatment of intangible assets - An intangible asset is an asset which is not physical in nature. Examples of intangible assets include computer software, patents, copyrights, licenses, intellectual property, trademark (including brands and publishing titles), customer lists, mortgage servicing rights, import quotas, franchises, customer or supplier relationships, customer loyalty, market share, marketing rights, goodwill, etc.

Generally, intangible assets are excluded from the tangible network of the entity (e.g., software, internally generated goodwill, goodwill on consolidation). However, in case an intangible asset is critical to the core operations of the entity, CareEdge Ratings considers the same as a part of the tangible network of the entity. Examples of such intangible assets include:

- Telecom license fees paid by the telecom operators to the Government of India.
- Surface rights paid by the miners to undertake mining activity in India.

- Media rights like movie rights, audio rights, video rights, broadcasting rights, television rights, theatrical rights, satellite rights, music rights, digital rights, overseas rights, copyrights, etc.
- Intellectual property rights (IPRs) - Intellectual property (IP) is a non-physical property created by the intellect of human mind. Examples of IPs include patents, copyrights, trademarks, designs, etc. IPRs are generally seen in the information technology (IT) and pharmaceutical sectors.

### C. Leverage and coverage ratios

Financial leverage refers to the use of debt finance in the overall funding mix. Leverage ratios help in assessing the risk arising from the use of debt capital whereas coverage ratios show the relationship between debt servicing obligations and cash flow sources available for meeting these obligations. CareEdge Ratings uses ratios like long-term debt-equity, overall gearing, total outside liabilities to networth, interest coverage, total debt as a proportion of cash accruals, PBILDT and cash flow from operations (CFO) and debt service coverage ratio (DSCR) to measure the degree of leverage used and the level of coverage available with the entity for debt servicing.

Leverage and coverage ratios considered by CareEdge Ratings include:

Ratio	Formula	Significance in the Analysis
Long-term Debt Equity	$\frac{\text{Total Long-term Debt (Including Current Portion of Long-term Debt)}}{\text{Tangible Network}}$	<ul style="list-style-type: none"> <li>Debt equity, overall gearing and total outside liabilities to networth ratios indicate the extent of financial leverage in the entity and are a measure of financial risk. Though a higher leverage would indicate higher returns to the equity shareholders, the degree of risk increases for the debt holders in case of uncertainty or volatility of earnings.</li> <li>While calculating debt equity ratio, only long-term debt (including the current portion of long-term debt) is considered.</li> </ul>
Overall Gearing (Including Acceptances / Creditors on Letter of Credit (LC))	$\frac{\text{Total Debt (Including Acceptances / Creditors on LC)}}{\text{Tangible Network}}$	
Total Outside Liabilities to Networth	$\frac{\text{Total Outside Liabilities}}{\text{Tangible Network}}$	<ul style="list-style-type: none"> <li>Both debt equity and overall gearing ratios are adjusted for the exposure to group entities and the analysis is done in conjunction with the performance of group entities.</li> <li>CareEdge Ratings also considers the impact of non-fund-based limits (availed by the entity) on the leverage of the entity.</li> <li>Total outside liabilities include total debt, other long-term liabilities and provisions, net of deferred tax liabilities / assets.</li> </ul>
Interest Coverage	$\frac{\text{PBILDT}}{\text{(Total Interest and Finance Charges – Amortisation of Premium on Debentures (if any) – Interest Capitalised)}}$	It indicates the extent of cover available to meet interest payments. It is a simple indicator of profitability and cushion available to the secured creditors.
Term Debt / GCA	$\frac{\text{Total Long-term Debt (Including Current Portion of Long-term Debt)}}{\text{GCA}}$	<ul style="list-style-type: none"> <li>Term debt / GCA and total debt / GCA indicate the number of years that would be required for repayment of long-term debt and total debt, respectively, considering the current level of GCA.</li> <li>Term debt / PBILDT and total debt / PBILDT indicate the number of years that would be required to repay long-term debt and total debt considering the current level of</li> </ul>
Total Debt / GCA	$\frac{\text{Total Debt (Including Acceptances / Creditors on LC)}}{\text{GCA}}$	
Term Debt / PBILDT	$\frac{\text{Total Long-term Debt (Including Current Portion of Long-term Debt)}}{\text{PBILDT}}$	

Ratio	Formula	Significance in the Analysis
Total Debt / PBILDT	Total Debt (Including Acceptances / Creditors on LC) / PBILDT	operating profit. • Total debt / CFO indicates the number of years that would be required to repay total debt considering the current level of CFO. CFO is cash generated from operations after adjusting for working capital changes.
Total Debt / CFO	Total Debt (Including Acceptances / Creditors on LC) / CFO	
DSCR	$\frac{\text{GCA} + \text{Interest and Finance Charges} - \text{Internal Accruals Committed for Capex or Investment}}{\text{Gross Long-term Debt Repayable in the Year} + \text{Standalone CP} + \text{Short-term Debt Repayment} + \text{Interest and Finance Charges}}$ <p>CP: Commercial Paper</p>	DSCR indicates adequacy of cash accruals to meet debt obligations. This ratio is seen in conjunction with the cumulative DSCR (given below) which incorporates prior period cash accruals. Though DSCR is an important indicator of the entity's repayment ability, CareEdge Ratings also considers the available liquidity, financial flexibility, or refinancing ability of the entity (including due to group strength).
Cash DSCR	$\frac{\text{GCA} + \text{Interest and Finance Charges} - \text{Internal Accruals Committed for Capex or Investment} - 25\% \text{ Increase in Working Capital}}{\text{Gross Long-term Debt Repayable in the Year} + \text{Standalone CP} + \text{Short-term Debt Repayment} + \text{Interest and Finance Charges}}$	Cash DSCR is computed by deducting the margin money for working capital (25% of the incremental working capital) from the funds available for debt servicing on the assumption that it will be met out of the GCA and hence, will not be available for debt servicing. The balance 75% of the incremental working capital is assumed to be met through working capital borrowings.
Cumulative / Average DSCR		It indicates running position of the average DSCR every year. Cumulative DSCR for the last year of the projections would be equivalent to the average DSCR for the tenure of the facility / instrument.

- **Total debt** - In total debt, CareEdge Ratings considers all forms of short-term and long-term debt, including redeemable preference share capital, optionally convertible debentures, interest free loans, foreign currency loans, vehicle loans, fixed deposits, unsecured loans, CP, inter-corporate borrowings, borrowings from the promoters, associates, other group entities and bills discounted. Apart from these, CareEdge Ratings also considers acceptances / creditors on LC (including capex LCs), lease liability and mobilisation advances backed by financial bank guarantees (generally in case of construction entities) as a part of total debt of the entity. Any corporate guarantee given to the lenders of the subsidiaries or other group entities is added to debt to calculate adjusted leverage ratios.

However, if any part of the borrowings from the promoters / related parties are subordinated to the loans from the outsiders, the same is treated as a part of the tangible network. Nevertheless, interest expense on a subordinated debt is treated as a normal interest expense of the entity.

If a debt is fully backed by dedicated / lien-marked fixed deposits / cash margin, CareEdge Ratings excludes the same from total debt.

- **Treatment of hybrid instruments** - Hybrid instruments are the instruments which have the characteristics of both, debt and equity. Examples of such instruments include redeemable preference shares, compulsorily convertible instruments, optionally convertible instruments, including foreign currency convertible bonds

(FCCBs), perpetual debt, etc. These instruments normally carry a fixed rate of coupon / dividend. At times, the coupon / dividend may be deferrable, thus giving the issuer the flexibility to conserve cash in times of stress.

- Redeemable preference shares - Preference shares have a fixed tenure at the end of which they have to be redeemed by the issuer. Further, they also carry a fixed rate of dividend. Hence, preference share capital typically has the characteristics of debt and is treated as such by CareEdge Ratings in its analysis. However, if preference shares are issued to the promoters of the entity and are redeemable after repayment of outstanding term debt of the entity, they assume the nature of long-term funding from the promoters and hence, CareEdge Ratings treat them as quasi equity.
- Compulsorily convertible instruments - Sometimes the instrument could be compulsorily convertible into equity shares at the end of a certain time frame. Hence, the entity does not have to redeem the instrument at the end of the tenure and as such there is no credit risk. In all such cases where the terms of preference shares / debentures give it equity-like characteristics, CareEdge Ratings treats them as quasi equity and consider it as a part of the tangible networth of the entity. However, if the terms of compulsorily convertible instruments are such that the investors have an exit option on the entity or the conversion to equity shares is conditional, CareEdge Ratings treats these instruments as debt.
- Optionally convertible instruments - At times, entities also issue optionally convertible instruments (typically optionally convertible preference shares (OCPS) / optionally convertible debentures (OCDs)). Here, the investor has the option to convert the instrument into equity shares at the end of a certain time frame at a pre-determined price. In this case, the alternative of redemption of the instrument cannot be ruled out till the time it is actually converted into equity. The instrument thus has debt-like characteristics till conversion into equity. Thus, CareEdge Ratings generally treats optionally convertible instruments as debt in its analysis.

#### D. Turnover and liquidity ratios

Turnover ratios, also referred to as activity ratios or asset turnover ratios, measure the extent of efficiency of assets deployed and utilised by the entity. These ratios are based on the relationship between the level of activity, represented by sales or cost of goods sold, and the level of various assets, including inventories and fixed assets. Liquidity ratios such as current ratio and quick ratio are broad indicators of the liquidity level and are important ratios for the rating of short-term instruments. The analysis of cash flow statement is also important for liquidity assessment. Turnover and liquidity ratios considered by CareEdge Ratings include:

Ratio	Formula	Significance in the Analysis
Avg. Inventory Period	$\frac{[\text{Avg. (INV}_t, \text{INV}_{t-1}) \times 30 \times \text{No. of Months}]}{[\text{Costs of Sales} - \text{Selling Expenses}]}$ INV:Total Inventory	<p>This indicates the turnaround time of inventory. A high average inventory period may indicate high levels of obsolescence of inventory, while a low level of inventory may be inadequate to meet any exigencies.</p> <p>This ratio is compared with the normal inventory holding policy of the entity and the industry practice. CareEdge Ratings also looks at the average raw material inventory period, average work-in-progress (WIP) inventory period and the average finished goods inventory period.</p>
Avg. Collection Period	$\frac{[\text{Avg. (REC}_t, \text{REC}_{t-1}) \times 30 \times \text{No. of Months}]}{[\text{Gross Sales} + \text{Traded Goods Sales} + \text{Job Work Income} + \text{Scrap Sales}]}$	<p>This ratio indicates the quality of debtors. A very low figure may indicate strict trade terms resulting into possible loss of sales whereas a very high average collection period may indicate slow realisation of debtors and in turn may be an indicator of a stressed</p>

Ratio	Formula	Significance in the Analysis
	REC: Total Receivables	liquidity position. It is compared with the normal ('stated') credit period extended to the customers and the industry norms.
Avg. Creditors Period	$\frac{[\text{Avg. (CRED}_t, \text{CRED}_{t-1}) \times 30 \times \text{No. of Months}] / [\text{Cost of Sales} - \text{Misc. Expenditure Written Off}]}{\text{CRED: Total Creditors}}$	It is compared with the normal credit period enjoyed by the entity and the industry norms. A very high figure may indicate possible delays in payments to the creditors, which would ultimately reflect in high cost of raw material, as 'interest' on 'delayed' payments normally gets loaded to the raw material cost.
Working Capital Cycle	Avg. Inventory Period + Avg. Collection Period – Avg. Creditors Period	The effect of all the above-mentioned ratios is reflected in the working capital cycle.
Fixed Assets Turnover Ratio	$\frac{[(\text{TOI}) \times (12 / \text{No. of Months})] / [\text{Avg. (Gross Block}_t, \text{Gross Block}_{t-1})]}{\text{Gross Block: Net of Intangible Assets such as Goodwill etc.}}$	In general, higher the ratio, higher the efficiency of asset / capital utilisation. However, a very high figure can indicate old assets requiring large outlay on modernisation going forward. Hence, this ratio has to be looked at in conjunction with the industry average.
Working Capital Turnover Ratio	$\frac{[(\text{TOI}) \times (12 / \text{No. of Months})] / [\text{Avg. (NWC}_t, \text{NWC}_{t-1})]}{\text{NWC: Net Working Capital} = \text{Total Current Assets} - [\text{Total Current Liabilities Related to Operations} - \text{Creditors for Capital Goods}]}$	In general, higher the ratio, higher is the efficiency. A very high figure can, however, indicate low levels of inventory, which may be inadequate to meet any exigencies.
Current Ratio	Total Current Assets / [Total Short-term Debt (Including Current Portion of Long-term Debt / Fixed Deposits and Bills Discounted) + Total Current Liabilities and Provisions]	This indicates short-term liquidity position. CareEdge Ratings compares the same with the industry trends and also the banking norms.
Quick Ratio	[Total Current Assets – Total Inventories] / [Total Short-term Debt (including Current Portion of Long-term Debt / Fixed Deposits and Bills Discounted) + Total Current Liabilities and Provisions]	This indicates capacity to meet short-term obligations using near-liquid assets. CareEdge Ratings compares the same with the industry trends and also the banking norms.

**[For the previous version, please refer to 'Financial Ratios - Non-Financial Sector' issued in [March 2023](#)]**

## CARE Ratings Limited

Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022  
Phone : +91 - 22 - 6754 3456 | CIN: L67190MH1993PLC071691

Connect :



Locations: Ahmedabad | Andheri-Mumbai | Bengaluru | Chennai | Coimbatore | Hyderabad | Kolkata | Noida | Pune

### About:

CareEdge is a knowledge-based analytical group offering services in Credit Ratings, Analytics, Consulting and Sustainability. Established in 1993, the parent company CARE Ratings Ltd (CareEdge Ratings) is India's second-largest rating agency, with a credible track record of rating companies across diverse sectors and holding leadership positions in high-growth sectors such as BFSI and Infra. The wholly-owned subsidiaries of CareEdge Ratings are (I) CARE Analytics & Advisory Private Ltd (previously known as CARE Risk Solutions Pvt Ltd), (II) CARE ESG Ratings Ltd, (previously known as CARE Advisory Research and Training Ltd) and (III) CareEdge Global IFSC Ltd. CareEdge Ratings' other international subsidiary entities include CARE Ratings (Africa) Private Ltd in Mauritius, CARE Ratings South Africa (Pty) Ltd, and CARE Ratings Nepal Ltd. For more information: [www.careedge.in](http://www.careedge.in).

### Disclaimer:

This disclaimer pertains to the ratings issued and content published by CARE Ratings Limited ("CareEdge Ratings"). Ratings are opinions on the likelihood of timely payment of the obligations under the rated instrument and are not recommendations to sanction, renew, disburse, or recall the concerned bank facilities or to buy, sell, or hold any security. Any opinions expressed herein are in good faith and are subject to change without notice. The rating reflects the opinions as on the date of the rating. A rating does not convey suitability or price for the investor. The rating agency does not conduct an audit on the rated entity or an independent verification of any information it receives and/or relies on for the rating exercise. CareEdge Ratings has based its ratings/outlook on the information obtained from reliable and credible sources. CareEdge Ratings does not, however, guarantee the accuracy, adequacy, or completeness of any information and is not responsible for any errors or omissions and the results obtained from the use of such information. The users of the rating should rely on their own judgment and may take professional advice while using the rating in any way. CareEdge Ratings shall not be liable for any losses that user may incur or any financial liability whatsoever to the user of the rating. The use or access of the rating does not create a client relationship between CARE and the user.

CareEdge Ratings disclaims warranty of any kind, express, implied or other warranties or conditions, to the extent permitted by applicable laws, including warranties of merchantability, accuracy, completeness, error-free, non-infringement, non-interruption, satisfactory quality, fitness for a particular purpose or intended usage.

Most entities whose bank facilities/instruments are rated by CareEdge Ratings have paid a credit rating fee, based on the amount and type of bank facilities/instruments. CareEdge Ratings or its subsidiaries/associates may also be involved with other commercial transactions with the entity. CareEdge Ratings does not act as a fiduciary by providing the rating. The ratings are intended for use only within the jurisdiction of India. The ratings of CareEdge Ratings do not factor in any rating-related trigger clauses as per the terms of the facilities/instruments, which may involve acceleration of payments in case of rating downgrades. However, if any such clauses are introduced and triggered, the ratings may see volatility and sharp downgrades. CareEdge Ratings has established policies and procedures as required under applicable laws and regulations which are available on its website.

Privacy Policy applies. For Privacy Policy please refer to [https://www.careratings.com/privacy\\_policy](https://www.careratings.com/privacy_policy)

© 2025, CARE Ratings Limited. All Rights Reserved.

This content is being published for the purpose of dissemination of information. Any use or reference to the contents herein on an "as-is" basis is permitted with due acknowledgement to CARE Ratings. Reproduction or retransmission in whole or in part is prohibited except with prior written consent from CARE Ratings.