COMMERCIAL BRIEFING - NO. 21

10 Financial Ratios

Every small business owner should understand ten numbers. Not to become an accountant, but to know whether the business is actually healthy before a problem becomes a crisis. This briefing explains each ratio in plain English, with the formula and a worked example.

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POWERED BY 3DMAI

IN SHORT

Most business owners focus on winning customers and building a brand. Businesses with strong sales still fail regularly, almost always because nobody was watching the numbers that determine profitability and survival. You do not need an accounting degree. You need ten numbers, checked monthly, and the discipline to act when one moves the wrong way. This briefing sets out each one in plain English with a worked example.

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1. GROSS MARGIN PERCENTAGE

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Gross Profit ÷ Sales × 100
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The most important ratio for any trading business. Sell £100,000, direct costs £60,000, gross profit £40,000, margin 40%. This is what is left to cover wages, rent, marketing and everything else. Poor gross margins cause businesses to struggle regardless of turnover.

2. MARK-UP PERCENTAGE

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Gross Profit ÷ Cost × 100
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Not the same as margin. Cost £100, sell £150, mark-up is 50% but margin is 33%. Confusing the two is one of the most common pricing mistakes in small business.

3. NET PROFIT MARGIN

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Net Profit ÷ Sales × 100
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A business turning over £1m but keeping £50,000 has a net margin of 5%. Gross margin measures product profitability. Net margin measures whether the whole business actually works.

4. CURRENT RATIO

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Current Assets ÷ Current Liabilities
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Above 1.2 generally indicates reasonable health. Approaching 2.0 suggests a stronger position. Tells you whether you can pay upcoming bills without a scramble.

5. DEBTOR DAYS

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Trade Debtors ÷ Annual Sales × 365
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How long customers actually take to pay. Many profitable businesses run into trouble simply because customers pay slowly. Covered in detail in a separate briefing.

6. CREDITOR DAYS

Trade Creditors ÷ Annual Purchases × 365

How long you take to pay suppliers. Managing payment terms effectively can significantly improve cashflow without increasing borrowing.

7. CASH CONVERSION CYCLE

Debtor Days + Stock Days – Creditor Days

A lower number is more efficient. Some businesses achieve a negative cycle, getting paid by customers before paying suppliers.

8. STOCK TURNOVER

Cost of Goods Sold ÷ Average Stock

Higher turnover means better efficiency and less working capital tied up in stock that has not sold yet.

9. OVERHEAD RATIO

Operating Expenses ÷ Sales × 100

Many businesses increase sales but not profit because overheads grow just as fast. Keeps growth honest.

10. BREAK-EVEN POINT

Fixed Costs ÷ Gross Margin %

Fixed costs £100,000, gross margin 40%, break-even sales £250,000. Every owner should know this number without opening a spreadsheet.

THE BONUS RATIO

Gross Profit ÷ Number of Employees

Gross Profit Per Employee reveals whether additional headcount is genuinely creating value or simply increasing overhead. Many businesses grow turnover while profit stagnates because this number quietly deteriorates unwatched.

BUILDING A SIMPLE DASHBOARD

A simple monthly dashboard tracking all eleven figures gives any business owner a clear picture of profitability, cashflow and efficiency, without becoming overwhelmed by financial reporting. What gets measured gets managed.

ABOUT MOOR & CO & 3DMAI

We help build the dashboard that makes these numbers visible.

Moor & Co provides senior commercial expertise working with small businesses across North Staffordshire and South Cheshire. Strategy, pricing, procurement, cashflow and reporting. Available short term, long term or project by project.

The intelligence platform behind the practice is **3DMAI**, built specifically for UK SMEs to make these numbers visible automatically.

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NOTE

This briefing explains commercial ratios and what they mean for decision making. It is not accounting, tax or financial advice. Your accountant is the right person to calculate these figures precisely from your accounts.