BizEquity's KPI Breakdown

Every BizEquity Valuation Report includes the following KPIs, or key performance indicators, calculated based on the analysis of company-specific data and various industry-specific averages. These KPIs can be used to measure the overall financial and operational health and growth potential of the business.

Return on Equity (ROE)

Compares profitability to the equity value of a company

It Means: The amount of net income generated as a percentage of shareholder's equity. Measures a company's profitability by depicting how much profit it generates with money shareholders have invested.

Why it Matters: ROE is a universal way to measure profitability against industry peers. It indicates the strength of the business model. High-growth companies tend to have high ROE.

For Example: An e-commerce company with an ROE of .48 generates 48 cents net income for every $1 of shareholder investment.

Affected By: Pre-tax income and total equity (equal to total assets – total liabilities)

Receivables (Conversion) Over Time

The time period in number of days it takes a company to collect accounts receivable.

It Means: How quickly a business is able to collect accounts receivable from customers. Faster collection makes cash available sooner to meet other business needs. Increases over time can signal difficulty in collecting from customers.

Why it Matters: Lower time periods indicate that a company relies mainly on cash or is efficient in collecting debts from imparted credit. A higher time period indicates collection inefficiency and may require a review of current credit and collections policies.

For Example: A receivables conversion of 24 days means it takes 24 days on average to collect account receivables. If credit terms are "net 30 days," this is a positive result.

Affected By: Accounts receivable and total revenues

Inventory Turnover

How long it takes to sell inventory on hand.

It Means: The turnover ratio addresses how efficiently goods are sold by calculating how many times a company's inventory is sold and replaced in a give time period.

Why it Matters: A lower ratio can indicate poor sales and excessive inventory, possibly due to pricing policies, while a higher ratio may indicate that product selection is too narrow. Keeping inventory balances to a minimum will reduce costs but may reduce sales volume.

For Example: A manufacturer with an inventory turnover of 5.7 sold all of its average inventory 5.7 times each year.

Affected By: Total revenues divided by inventory

Fixed Assets Turnover

Shows how productive a company's assets are.

It Means: This activity ratio shows the company's ability to generate net sales from investments in fixed assets.

Why it Matters: A higher ratio indicates productive fixed asset investment. This ratio is most vital to the manufacturing industry.

For Example: A manufacturing company with a fixed asset turnover of 3.8 generated sales worth $3.8 for every $1 of investment in fixed assets.

Affected By: Total revenues divided by fixed assets (book value as entered into balance sheet)

Debt-to-Equity over time

Shows the extent of the debt load compared with equity value

It Means: A function of the business's capital structure that provides a measure of financial leverage. It indicates the proportion of equity and liabilities being used to finance the business's asset base.

Why it Matters: A higher ratio indicates the business has been aggressively financing growth with debt and creditors are assuming a higher risk. A lower ratio indicates the business is "safer," but may also suggest overly cautious ownership.

For Example: If a company has a ratio of 2.8, this means that for every $1 owned by the shareholders, the company owes $2.8 to its creditors.

Affected By: Total liabilities divided by total equity (total equity = total assets - total liabilities)

Interest Coverage over time

Shows how much cushion a business has in paying its interest expenses (aka "times interest earned")

It Means: Equal to earnings before interest and taxes (EBIT) divided by interest expenses. It's used to determine the ease with which a company can pay interest on outstanding debt obligations.

Why it Matters: The higher the ratio, the easier it is for the company to repay current debts and take on additional debt if necessary. A lower ratio may cast doubt on the company's ability to meet ongoing principals and interest burdens.

For Example: An interest coverage ratio over 2x indicates that a company has the ability to meet interest payments two times over and may qualify for additional debt.

Affected By: Pre-tax income plus interest expense divided by interest expense

Cash-to-Debt over time

Shows a business's ability to pay off existing debts

It Means: Compares a company's operating cash balance to its total debt, providing an indication of the company's ability to cover total debt with operating cash holdings.

Why it Matters: A higher ratio indicates the company is better equipped to carry and service its total debt and may also suggest excess cash or excess net working capital. A low ratio may signal future difficulties serving debt or meeting payroll/vendor obligations.

For Example: If a business has a ratio of 74%, for every $1 of debt, it has 74 cents in liquid holdings that could be used to service that debt.

Affected By: Cash divided by total liabilities

Income-to-Revenue over time (pre-tax)

Pre-tax profitability ratio unaffected by a company's actual tax burden

It Means: Also known as return on sales, this profitability ratio indicates the relative profit margin of the company for each dollar of sales. A rising percentage will often lead to a higher valuation.

Why it Matters: A higher percentage ratio indicates a higher rate of relative profitability. Higher gross profits ad lower operating expenses coupled with higher revenues will bolster this important metric.

For Example: If a business has a percentage ratio of 17%, this means that for every $1 of revenue, it has a pre-tax income of 17 cents.

Affected By: Pre-tax income divided by total revenues

Cash Flow-to-Revenue over time

Key for analyzing a company's ability to grow without the assistance of outside capital

It Means: This multi-purpose ratio indicates a company's ability to convert sales revenue into spendable cash. A rising percentage will often lead to a higher valuation.

Why it Matters: A higher percentage ratio indicates that a company is able to turn a higher amount of revenue into cash flow.

For Example: If a business has a percentage ratio of 11%, it means that for every $1 in revenue, it generates around 11 cents in discretionary cash flow.

Affected By: Discretionary earnings* divided by total revenue

*Discretionary earnings equal the sum of pre-tax income + owner compensation + interest + depreciation and amortization expense OR EBITDA + owner compensation

Receivables-to-Income over time (pre-tax)

Affects a company's ability to maintain profit margin.

It Means: Provides an indication of the amount of credit being granted to the customer base relative to ongoing profits.

Why it Matters: If receivables are greater than pre-tax profit, it becomes more important to establish and maintain an effective and efficient credit, billing and collections process.

For Example: A company with $100K in receivables and $100K in pre-tax profit must collect all receivables to maintain the profit margin.

Affected By: Total accounts receivable divided by pretax income

Inventory-to-Income over time (pre-tax)

Indicates a company's ability to use inventory to improve profitability. Total inventory div

It Means: This ratio illustrates the relative importance of inventory holdings to company profitability.

Why it Matters: For retail and manufacturing companies, sourcing and managing inventory properly can improve profitability and maximize operational efficiencies.

For Example: A company with a goal of decreasing this ratio would aim to generate higher pre-tax profit with lower average inventory holdings.

Affected By: Total inventory divided by pretax income

Fixed Assets-to-Income over time (pre-tax)

Should be reviewed both over time and against industry norms.

It Means: This ratio provides insight into a company's profitability relative to its stock of fixed assets (furniture, fixtures, equipment and vehicles).

Why it Matters: Everything else being equal, companies seek higher pre-tax profits for each dollar invested in fixed assets. As the ratio declines, a company is generating higher profits per dollar of fixed assets.

For Example: A ratio greater than one suggests that more money has been invested into capital assets than profits have been generated.

Affected By: Total fixed assets (book value) divided by pretax profits

Total Debt-to-Income over time (pre-tax)

Businesses with lower debt, higher profit will be worth more than businesses with higher debts, lower profits

It Means: Illustrates the relationship between total company obligations at any point in time (short- and long-term debt

Why it Matters: Companies with high debts relative to pre-tax profits are often riskier than those with lower total debts, although some companies rely on the use of debt to grow and enhance profit margins (when the ROI of borrowed funds is greater than the cost of borrowing).

For Example: If a company's total debts are $100K and total pre-tax profits are $50K, it will take two years to pay off debts out of ongoing profits.

Affected By: Total inventory divided by pretax income

Questions?
Contact support@hardstone.com