RFHHA MANAGEMENT TIP OF THE DAY FOR HOSPITAL ADMINISTRATORS 1302

What is the Quick Ratio?

The Quick Ratio method is a model for measuring the liquidity of a company. It is calculated by taking all assets which are quickly convertible into cash, and to divide the result by all current liabilities. It specifically excludes inventory. It is an indicator of the extent to which a company can pay current liabilities without having to rely on the sale of inventory.

Typically, a Quick Ratio of 1:1 or higher is good, and indicates a company does not have to rely on the sale of inventory to pay the bills.

Calculation of the Quick Ratio.
Formula
For the Quick Ratio formula

This ratio is also known as the **Acid-test Ratio**.

A thing to remember when we use the Quick Ratio is that this model ignores timing of both cash received and cash paid out.

Take the example of a company with no bills due today, but lots of bills which are due tomorrow. This company may show a good Quick Ratio, but cannot be considered as having a good liquidity.

The quick ratio is an indicator of a company's short-term liquidity position and measures a company's ability to meet its short-term obligations with its most liquid assets. Since it indicates the company's ability to instantly use its near-cash assets (assets that can be converted quickly to cash) to pay down its current liabilities, it is also called the acid test ratio. An acid test is a quick test designed to produce instant results—hence, the name.

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