

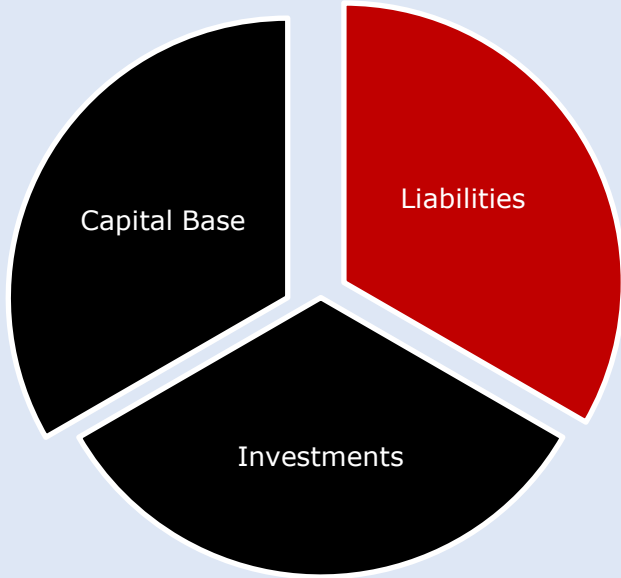
# ENGINEUNITY TUTORIAL



## Gearing Ratio



# Gearing Ratio



The **gearing ratio** is the ratio of the company's liabilities, when the cash account is overdrawn, to its assets, and indicates the **debt burden** of the company.

- 0 indicates no liabilities (debt)
- 1 indicates serious debt problems



# Gearing Ratio

Financial Performance

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Management consultants report

Graphical analysis

OPERATIONAL

SHAREHOLDERS

INVESTMENTS

Summary

Assets and liabilities

Per	Status	Year/qtr	Cash account			Capital base			Investments			Gearing ratio	Company value		
			Start period	% change	End period	Start period	% change	End period	Start period	% change	End period		Start period	% change	End period
1	History	2023 (Q1)	1,000,000	-13.06 %	869,420	4,000,000	-0.63 %	3,975,000	0	0.00 %	0	0.000	5,000,000	-3.11 %	4,844,420
2	History	2023 (Q2)	869,420	-19.96 %	695,898	3,975,000	-0.63 %	3,950,156	0	0.00 %	0	0.000	4,844,420	-4.09 %	4,646,054
3	History	2023 (Q3)	695,898	-29.47 %	490,823	3,950,156	5.34 %	4,160,995	0	100.00 %	102,400	0.000	4,646,054	2.33 %	4,754,218
4	History	2023 (Q4)	490,823	-150.91 %	-249,890	4,160,995	5.34 %	4,383,088	102,400	602.90 %	719,767	0.049	4,754,218	2.08 %	4,852,965
5	Early Years	2024 (Q1)	-249,890	-14.26 %	-285,536	4,383,088	5.34 %	4,617,035	719,767	-0.11 %	718,999	0.054	4,852,965	4.07 %	5,050,498
6	Early Years	2024 (Q2)	-285,536	1.02 %	-282,624	4,617,035	3.89 %	4,796,866	718,999	-7.25 %	666,866	0.052	5,050,498	2.59 %	5,181,108
7	Early Years	2024 (Q3)	-282,624	10.58 %	-252,725	4,796,866	2.90 %	4,935,823	666,866	2.39 %	682,795	0.045	5,181,108	3.57 %	5,365,893
8	Early Years	2024 (Q4)	-252,725	105.62 %	14,201	4,935,823	4.41 %	5,153,412	682,795	2.25 %	699,000	0.000	5,365,893	9.32 %	5,865,802

In the example shown, at the end of period 6, the gearing ratio is the :-

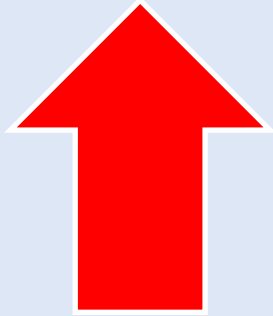
$$\begin{aligned} & \text{Absolute value of the Cash Account} / (\text{Capital Base} + \text{Investments}) \\ & 282,624 / (4,796,866 + 666,866) \\ & = 0.052 \end{aligned}$$

**How does the gearing ratio affect the company ?**



## Gearing Ratio

**INCREASES**



The company will be viewed as being vulnerable to both interest rate rises, and its ability to service its debts from its future profit flows. Consequently, this will have a **depressing affect on the company share price.**

**REDUCES**



Conversely, if the gearing ratio decreases then the company will be viewed as being more financially sound, and the **company share price will increase.**



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8	Early Years	2024 (Q4)	-252,725	105.62 %	14,201	4,935,823	4.41 %	5,153,412	682,795	2.25 %	698,189	0.000	5,365,893	9.32 %	5,865,802

- During period 5 the increasing gearing ratio had a **negative effect on the company share price, reducing it**
- During periods 6,7 and 8 the falling gearing ratio had a **positive effect on the company share price, increasing it**

## KEY POINTS

Whilst the company is growing a **certain level of gearing is usually necessary** to make full use of the cash account overdraft to expand the capital base and diversify through investments.