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When one evaluates the companys liquidity position and whether it is liquid enough to meet its short-term obligations, financial ratios become vital. Two of the most popularly applied ratios to compute liquidity are the current ratio and quick ratio. The variation between the current ratio and quick ratio exists in what assets each counts. Both ratios measure the ability to meet short-term liabilities, but the current ratio takes into account all of the current assets, whereas the quick ratio excludes inventory, so it is a more conservative measure of liquidity. Download Difference Between Current Ratio and Quick Ratio PDF The current ratio is one of the fundamental financial metrics used by investors and analysts to gauge a companys ability to meet its short-term obligations. This ratio measures the total current assets relative to the current liabilities of a company, providing an overview of the companys short-term financial health. Simply put, it means that the current ratio will show if a company has enough cash-generating assets to settle its immediate liabilities. This is because it is a broad indicator as it incorporates all of those assets that are expected to be converted into cash within one year, including cash, accounts receivable, and inventory. The current ratio, though providing a general picture of the liquidity, may not always depict an accurate reflection of the ability of a company to pay off debts since it comprises assets that might not be as easily liquidated as others. The formula for calculating the current ratio is: Where: Current Assets are assets that can be converted into cash within a year (e.g., cash, accounts receivable, and inventory). Entities need to settle current liabilities within a year. (e.g., short-term debts, accounts payable). A current ratio of 1 or more usually means that the company has sufficient assets to pay off its short-term liabilities. However, a too-high ratio (say above 2) may imply inefficiency in using assets to generate revenue. To calculate the current ratio, follow these steps: Identify the companys current assets: Current assets generally consist of cash, accounts receivable, inventory, and short-term investments. Identify the companys current liabilities: Current liabilities may consist of accounts payable, short-term loans, and any other obligations due within one year. Apply the formula: Use the formula above to divide current assets by current liabilities. For example, if a company has current assets worth $500,000 and current liabilities worth $250,000, the current ratio would be: CurrentRatio=500,000/250,000=2 This means that for every dollar of liability, the company has $2 in current assets to cover it. The quick ratio is more stringent in measuring liquidity, often referred to as the acid-test ratio. The quick ratio gives a more accurate picture of how likely a company is to fulfill its short-term obligations through the sale of less liquid current assets. In the case of a current ratio, it excludes inventory and other less liquid current assets from the calculation, giving only the most liquid items, such as cash and marketable securities, with accounts receivable. People consider the quick ratio a more accurate measure of a companys short-term liquidity than the current ratio. It presumes that inventory may not be easily converted into cash in the short term, especially in industries where inventory may not be as liquid. The formula for calculating the current ratio is: Where: Quick assets include cash, marketable securities, and accounts receivable. Anything that you can quickly turn into cash within a short time frame. Current Liabilities remain the same as in the current ratio. Generally, experts consider a quick ratio of 1 or more to be a sign of good health for a company.This indicates that the company has adequate liquid assets to meet its short-term liabilities. If the quick ratio is less than 1, then the company may face difficulty in meeting its short-term obligations without liquidating the inventory or seeking further finance. To calculate the quick ratio, follow these steps: Identify quick assets: These include cash, cash equivalents, marketable securities, and receivables. Exclude inventory and prepaid expenses. Identify current liabilities: Current liabilities, as with the current ratio, are those due within one year. Apply the formula: Divide quick assets by current liabilities. For example, if a company has quick assets worth $400,000 and current liabilities worth $250,000, the quick ratio would be: QuickRatio=400,000/250,000=1.6 This implies that the company has $1.60 in liquid assets for every dollar of liability. The difference between the current ratio and quick ratio lies in the assets they include in their calculations and how they assess a companys short-term liquidity. Inclusion of Inventory: The key difference is that the current ratio includes inventory as a current asset, whereas the quick ratio excludes inventory and emphasizes more liquid assets. Conservatism: People consider the quick ratio a more conservative measure of liquidity because it removes inventory from the equation. Converting inventory into cash in the short term may not always be easy. Liquidity Focus: The current ratio gives a more general sense of liquidity by taking into account all current assets, while the quick ratio gives a more stringent test of the ability of a company to meet its short-term obligations without selling inventory. Proper Application: Industries apply the current ratio well when they can easily liquidate their inventory, such as in retail. However, the quick ratio is more proper in an industry wherein its inventory takes a longer time to sell or may not liquidate into cash, manufacturing for example. FactorCurrent RatioQuick RatioAssets IncludedIncludes all current assets, including inventoryExcludes inventory, only includes liquid assets like cash, receivablesFormulaCurrent Assets / Current LiabilitiesQuick Assets / Current LiabilitiesLiquidity MeasureGeneral measure of liquidityMore conservative, focuses on liquid assetsUse CaseUsed when inventory is liquid and easily converted to cashMore useful when inventory cannot be quickly soldRisk LevelHigher risk if the ratio is too high (inefficiency)More conservative, focus on liquid assets Download Difference Between Current Ratio and Quick Ratio PDF The difference between the current ratio and the quick ratio is important for financial analysis. The current ratio gives a broad view of liquidity, encompassing all current assets, whereas the quick ratio is more stringent, excluding inventory. Both ratios are important in assessing the ability of a company to meet its short-term obligations, but they serve different purposes and are useful in different contexts. By knowing these ratios, the investor, manager, and analyst can make better decisions about a companys financial health. What is the difference between current ratio and quick ratio? The difference between current ratio and quick ratio lies in the assets they include. The current ratio includes all current assets, including inventory, whereas the quick ratio excludes inventory and focuses only on more liquid assets, such as cash, accounts receivable, and marketable securities. Why is the quick ratio considered a more conservative measure than the current ratio?The quick ratio is more conservative because it excludes inventory, which may not be easily liquidated in the short term. This gives a more accurate picture of a companys ability to meet short-term obligations without relying on inventory sales. Which ratio is better for assessing a companys liquidity, current ratio or quick ratio? The best ratio depends on the industry and the companys financial structure. Businesses find the current ratio useful when they can easily convert inventory into cash, while industries find the quick ratio more useful when inventory is less liquid. What does a quick ratio below 1 indicate?A quick ratio below 1 indicates that a company may have insufficient liquid assets to cover its short-term liabilities without relying on inventory or external financing. It suggests potential liquidity issues. How does inventory affect the current ratio and quick ratio? Inventory inflates the current ratio since it is included in the calculation of current assets. However, the quick ratio excludes inventory, making it a more conservative indicator of liquidity. Free Online Accounting Lessons. We provide informative and up-to-date lessons on various topics to help you learn and become well-versed in accounting and finance. Start learning accounting with this accounting 101 basics course. This section serves as a primer for beginners and a refresher for those who already have background in accounting. Build and solidify your accounting foundation. Financial accounting is the branch that focuses on the preparation of financial statements. Guided by generally accepted accounting principles, it deals with historical data, turning them into financial reports. Managerial accounting focuses on providing information to be used by the management in decision-making. It deals with the needs of the management rather than strict compliance with generally accepted accounting principles. The current ratio is the proportion, quotient, or relationship between the amount of a companys current assets and the amount of its current liabilities. The current ratio is calculated by dividing the amount of current assets by the amount of current liabilities.Definition of Quick RatioThe quick ratio (or the acid test ratio) is more conservative than the current ratio in that the amount in inventories, supplies, and prepaid expenses is not included. These current assets are excluded because it is assumed that they will not be turning to cash quickly.The quick ratio is calculated by dividing the amount of quick assets by 2) the amount of current liabilities. The quick ratio assumes that only the following current assets are quick assets:CashCash equivalentsShort-term marketable securitiesAccounts receivableDifference between Current Ratio and Quick RatioTo illustrate the difference between the current ratio and the quick ratio, assume that a companys balance sheet reports current assets of $60,000 and current liabilities of $40,000. Its current assets include $35,000 of inventory and $1,000 of supplies and prepaid expenses. These amounts result in the following:Current ratio is 1.5 to 1 (1.5:1, or simply 1.5). This is the result of dividing $60,000 by $40,000.Quick ratio is 0.6 to 1. This is the result of dividing $24,000 (which is $60,000 $35,000 $1,000) by $40,000.AccountingCoach PRO has 24 blank forms to guide you in calculating and understanding financial ratios. Also included are 24 filled-in forms based on two financial statements. May 31, 2025 May 31, 2025/ Steven Bragg The current ratio and quick ratio are both designed to estimate the ability of a business to pay for its current liabilities. While they are fairly similar, there is one important difference in how they are calculated, which can lead to notably different outcomes. You should be aware of this difference, which we will cover in detail.What is the Current Ratio?The current ratio measures the ability of a business to pay for its current liabilities with its existing current assets. This means that the current ratio compares the current assets and current liabilities reported on a firms balance sheet. The formula for it is as follows:Current ratio = (Cash + Marketable securities + Receivables + Inventory) Current liabilitiesWhat is the Quick Ratio?The quick ratio is the same as the current ratio, except that inventory is not included in the current assets portion of the calculation. The reason for this exclusion is that inventory can be difficult to liquidate in the short term; some inventory items may require many months to sell, and possibly at reduced prices. The formula for the quick ratio is as follows:Quick ratio = (Cash + Marketable securities + Receivables) Current liabilitiesComparing the Current Ratio and Quick RatioThere are three key differences between the current ratio and the quick ratio, which are as follows:Time period orientation. The quick ratio focuses on the more liquid assets, and so gives a better view of how well a business can pay off its obligations. The current ratio is oriented toward a somewhat longer period of time (whatever is needed to sell off inventory), and so may not be the best option for judging the short-term liquidity of a business.Inventory treatment. The quick ratio does not include inventory in the numerator, while the current ratio includes it. Inventory is a questionable item to include in an analysis of the liquidity of a business, since it can be quite difficult to convert to cash in the short term. Even if it can be sold within a reasonably short period of time, it is now a receivable (if sold on credit), and so there is an additional wait until the buyer pays the receivable.Emphasis on liquidity. The quick ratio is a more conservative measure of liquidity, since it assumes that an entitys inventory holdings might not be sold quickly enough to cover its short-term obligations.Consequently, the more reliable measure of short-term liquidity is the quick ratio. The only exception is when a business has a history of high inventory turnover (such as a grocery store), where inventory is not only sold off with great rapidity, but also where the resulting sales are converted to cash very quickly.Related AccountingTools CoursesBusiness Ratios GuidebookThe Interpretation of Financial Statements As an example of the difference between the two ratios, a retailer reports the following information:Cash = $50,000Receivables = $250,000Inventory = $600,000Current liabilities = $300,000The current ratio of the business is 3:1, while its quick ratio is a much smaller 1:1. In this case, the presence of a large proportion of inventory is masking a relatively low level of liquidity, which could be a concern to a lender or supplier.Comparing Results Across the Current Ratio and Quick RatioWhen comparing the current ratio and quick ratio, it is important to assess how much of a companys short-term liquidity relies on less liquid current assets like inventory and prepaid expenses. The current ratio includes all current assets in relation to current liabilities, while the quick ratio excludes inventory and other less liquid items, focusing only on the most readily convertible assets, which are cash, marketable securities, and receivables. A large difference between the two ratios suggests a heavy reliance on inventory to meet short-term obligations, which may be a concern if inventory is slow-moving or hard to liquidate. Ideally, both ratios should be above 1, but a closer quick ratio indicates stronger immediate liquidity.Related ArticlesAcid-Test RatiosCash RatioDefensive Interval RatioDoomsday RatioLiquidity IndexLiquidity Ratios May 31, 2025/ Steven Bragg/ All BlogsFinancial Statement Analysis ResourcesCurrent Ratio vs Quick RatioSolvency RatiosInsolvency TestsInsolvency TestAltman Z ScoreBeneish M-ScoreSolvency RatiosBOOT CAMP - Financial Modeling (6 Hrs)Boot Camp: LEARN Financial Modeling in Just 6 Hours!Table Of ContentsAs an investor, if you want a quick review of how a company is doing financially, you must look at the company's current ratio. The current ratio means a company's ability to pay off short-term liabilities with its short-term assets. Usually, when the creditors are looking at a company, they look for a higher current ratio; because a higher current ratio will ensure that they will get repaid easily, and the certainty of payment would increase.So what current ratio is all about? First, we will look at the balance sheet of the company and then select the current assets and divide the current assets by the current liabilities of the company during the same period.If we get all we need to know as investors from the current ratio, why should we look at a quick ratio? Here's the catch.The quick ratio helps investors get to the bottom of things and discover whether the company can pay off its current obligations. There is only one thing that's different in the quick ratio than the current ratio. While calculating the quick ratio, we consider all the current assets except inventories. Many financial analysts feel that inventory takes time to turn itself into cash to pay off debt. We also exclude prepaid expenses to get to the quick ratio in some cases. Thus, the quick ratio is a better starting point to understand whether the company can pay off its short-term obligations. The quick ratio is also called the acid test ratio.As we saw earlier that Toll Brothers had a current ratio of 4.6x. This makes us believe that they are in the best position to meet their current liabilities. However, when we calculate the Quick ratio, we note that it's only 0.36x. This is due to high inventory levels in the balance sheet, as seen below.source: Toll Brothers SEC FilingsLet's look at the formula of the current ratio first.Current Ratio = Current Assets / Current Liabilities As you can see, the current ratio is simple. Go over to the company's balance sheet, select "current assets," and divide the sum by "current liabilities," and you get to know the ratio.But what do we include in the current assets?Current Assets: Under current assets, the company would include cash, including foreign currency, short term investments, accounts receivables, inventories, prepaid expenses, etc.Current liabilities: Current Liabilities are liabilities that are due in the next 12 months or less. Under current liabilities, the firms would include accounts payable, sales taxes payable, income taxes payable, interest payable, bank overdrafts, payroll taxes payable, customer deposits in advance, accrued expenses, short-term loans, current maturities of long term debt, etc.Now, let's look at the quick ratio. We look at the quick ratio in two ways.Quick Ratio = (Cash & Cash Equivalents + Short Term Investments + Accounts Receivables) / Current LiabilitiesHere, if you notice, everything is taken under current assets except inventories.Let's look at what we include in cash & cash equivalents, short term investments, and account receivables.Cash & Cash Equivalents: Under Cash, the firms include coins & paper money, un-deposited receipts, checking accounts, and money order. And under cash equivalent, the organizations take into account money market mutual funds, treasury securities preferred stocks which have the maturity of 90 days or less, bank certificates of deposits, and commercial paper.Short Term Investments: These investments are the short term that can be liquidated easily within a short period, usually within 90 days or less.Accounts Receivables: The sum of money that is yet to be received from the company's debtors is called accounts receivable; including accounts receivable is criticized by some analysts because there is less certainty in the liquidation of accounts receivable!Let's look at the second way of computing the quick ratio (acid test ratio) Quick Ratio = (Total current assets Inventory Prepaid Expenses) / Current Liabilities In this case, you can take the whole current assets from the balance sheet of the company and then simply deduct the inventories and prepaid expenses. Then divide the figure by current liabilities to get to the quick or acid test ratio.First, we will interpret the current ratio and then the quick ratio.e will interpret the current ratio and then the quick ratio.When creditors look at the current ratio, it's usually because they want to ensure the certainty of repayment. If a company has less than one as its current ratio, then the creditors can understand that the company will not be able to pay off its short-term obligations easily. And if the current ratio of the company is more than 1, then they are in a better position to liquidate their current assets to pay off the short-term liabilities. But what if the current ratio of a company is too higher? For example, let's say that Company A has a current ratio of 5 in a given year, what would be the possible interpretation? There are two ways of looking at it. First, they are doing exceptionally well to liquidate their current assets very well and pay off debts faster. Second, the company cannot utilize its assets well, and thus, the current assets are much more than the current liabilities of the company.Now, let's have a look at a quick ratio.Many financial analysts believe that a quick ratio is a better way to understand a company's financial affairs than the current ratio. Their argument is inventoried shouldn't be included in the expectation of paying off current liabilities because no-one knows how long it would take to liquidate inventories. It is similar to prepaid expenses. A prepaid expense is an amount paid in advance for goods and services to be received in the future. As it is something that is already paid, it can't be used to pay off the further obligation. So we also deduct the prepaid expense from the current assets while computing the quick ratio. In In the case of the quick ratio, if the ratio is more than 1, creditors believe the company is doing well and vice versa.We will discuss two examples to try to understand the current ratio and quick ratio.Let's have a look.X (in US $)Y (in US $)Cash 100003000Cash Equivalent1000500Accounts Receivable10005000Inventories5006000Accounts Payable40003000Current Taxes Payable50006000Current Long-term Liabilities110009000Compute "Current Ratio" and "Quick Ratio."First, let's start with the current ratio.Here's what we will include in current assets X (in US $)Y (in US $)Cash 100003000Cash Equivalent1000500Accounts Receivable10005000Inventories5006000Total Current Assets1250014500We will look at current liabilities now X (in US $)Y (in US $)Accounts Payable40003000Current Taxes Payable50006000Current Long-term Liabilities110009000Total Current Liabilities2000018000Now we can easily calculate the current ratio.The current ratio of X & Y would be X (in US $)Y (in US $)Total Current Assets (A)1250014500Total Current Liabilities (B)2000018000Current Ratio (A / B)0.630.81From the above, it can be easily said that both X & Y need to improve their current ratio to be able to pay off their short term obligations.Let's look at the quick ratio now.To calculate the quick ratio, we need to exclude "inventories" as no "prepaid expenses" are given.X (in US $)Y (in US $)Cash 100003000Cash Equivalent1000500Accounts Receivable10005000Total Current Assets (Except "Inventories")120008500Now the quick ratio would be X (in US $)Y (in US $)Total Current Assets (M)120008500Total Current Liabilities (N)2000018000Current Ratio (M / N)0.600.47One thing noticeable here. There is not much difference in the quick ratio for X because of excluding inventories. But in the case of Y, there is a vast difference. That means inventories can inflate the ratio and give creditors more hope in getting paid.Paul started a clothing store a few years back. Paul wants to expand his business and needs to take a loan from the bank to do so. Bank asks for a balance sheet to understand the quick ratio of Paul's clothing store. Here are the details below Cash: US $15,000Accounts Receivable: US $3,000Inventory: US $4,000Stock Investments: US $4,000Prepaid taxes: US $1500Current Liabilities: US $20,000Compute "Quick Ratio" on behalf of the bank.As we know that "inventory" and "prepaid taxes" wouldn't be included in the quick ratio, we will get the current assets as follows.(Cash + Accounts Receivable + Stock Investments) = US $(15,000 + 3,000 + 4,000) = US $22,000.And the current liabilities are mentioned, i.e., US $20,000.Then, the quick ratio would be = 22,000 / 20,000 = 1.1.A quick ratio of more than 1 is good enough for the bank to start. The bank will now look at more ratios to think over whether to lend a loan to Paul to expand his business.In this example, let us look at how to calculate the Current Ratio and Quick Ratio of Colgate. If you wish to get access to the calculation excel sheet, then you can download the samehere - Ratio Analysis in ExcelBelow is the snapshot of Colgate's Balance Sheet for years from 2010 - 2013.Current Ratio is easy to calculate = Current Assets of Colgate divided by Current Liability of Colgate.For example, in 2011, Current Assetswas$4,402 million, and Current Liability was $3,716 million.Colgate Current Ratio (2011) = 4,402/3,716 = 1.18xLikewise, we can calculate the current ratio for all other years.The following observations can be made with regards to Colgate Current Ratios The current ratio increased from1.00x in 2010 to 1.22x in the year 2012. Colgate's current ratio increased due to an increase in cash and cash equivalentsand other assets from 2010 to 2012. In addition, we saw that the current liabilities were more or less stagnant at around $3,700 million for these three years. The current ratio dipped to 1.08x in 2013 due to an increase in current liabilities caused by the current portion of long-term debt to $895 million.Now that we have calculated the Current Ratio, we calculate the Quick Ratio of Colgate. The quick ratio only considers receivables and cash and cash equivalents in the numerator.Now that we know the current ratio calculation and quick ratio let us compare the two for Apple (product company). The below graph depicts Apple's Current Ratio and Quick Ratio for the past ten years.source: ychartsWe notethe following from the above graph -The Current Ratio of Apple currently is 1.35x, while its Quick Ratio is 1.22x. These two ratios are very close to each other. There is not much difference between these two ratios. We note that historically, they have stayed very close to each other The key reason for this is that Apple has most of its current assets as Cash & Cash Equivalents, Marketable Securities, and Receivables. Inventory as a percentage of Current Assets is insignificant (less than 2%), as seen from the balance sheet below.source: Apple SEC filingsNow that we have seen Apple's comparison, it is easy to guess the graph of Microsoft's Current Ratio vs. Quick Ratio.The below chart plots Microsoft's Quick and Current ratio for the past 10 years.source: ychartsWe note the following -The Current Ratio is currently at 2.35x, while the quick ratio is at 2.21x. This is again a narrow range, just like Apple. The key reason for this is that Inventory is a minuscule part of the total current assets. Current assets primarily consist of Cash and Cash Equivalents, Short Term Investments, and receivables.source: Microsoft SEC FilingsLet us now look at sector-specific Current Ratio and Quick Ratio Comparisons. First, we note that Software applications companies have a narrow range of current and Quick Ratios.Below is a list of top Software Application companies -source: ychartsSAP has a current ratio of 1.24x, while its quick ratio is 1.18x. Likewise, Adobe Systems has a current ratio of 2.08 vs. a quick ratio of 1.99x. Software companies are not dependent on inventory, and hence, their contribution to current assets is significantly less. We note from the table above that (Inventories + Prepaid)/Current Assets is meager.In contrast to software companies, Steel companies are capital intensive sector and is heavily dependent on Inventories.Below is a list of top Steel companies -source: ychartsWe note that ArcelorMittal Current Ratio is 1.24x, while its Quick Ratio is 0.42 Likewise, for ThyssenKrupp, the current ratio is at 1.13 vs. Quick ratio of 0.59 We note that the range (Current ratio quick ratio) is relatively broad here. This is because, for such companies, inventories and prepaid contribute a considerable percentage of Current Assets (as seen from above, the contribution is greater than 30% in these companies)Another example that we see here is of Tobacco Sector. We note that this is a fairly capital intensive sector and depends on a lot on storing raw material, WIP, and finished goods inventories. Therefore, the Tobacco sector also shows a broad difference between the Current Ratio and the Quick Ratio.Below is the table showing these differences and the contribution of inventory and prepaid expenses to Current Assets.source: ychartsLet's discuss the disadvantages of both of these ratios.Here are the disadvantages of the current ratio First of all, the only current ratio would not give an investor a clear picture of a company's liquidity position. The investor needs to look at other ratios like quick and cash ratios. The current ratio includes inventories and other current assets, which may inflate the figure. Thus, the current ratio doesn't always give the right idea about a company's liquidity. If sales depend on seasons for any particular company or industry, the then-current ratio may vary over the year. The way inventory is valued will impact the current ratio as it includes inventory in its calculation.The quick ratio is a better way to look at the company's liquidity. But it still has some demerits. Let's have a look First of all, no investor and creditor should depend on an acid test or quick ratio only to understand the liquidity position. They also need to compare the cash and current ratios. And they also should check out how much the company depends on its inventory. The quick ratio includes accounts receivables that may not get liquidated quickly. And as a result, it may not give an accurate picture. The quick ratio excludes inventories on all occasions. But in the case of inventory-intensive industries like supermarkets, a quick ratio cannot provide an accurate picture due to the exclusion of inventories from the current assets.To be clear about a company's liquidity position, only the current ratio and quick ratio are not enough; the investors and creditors should look at the cash ratio as well. And they need to find out which industry and company they are calculating for; on every occasion, the same ratio wouldn't give an accurate picture. As a whole, they should look at all the liquidity ratios before drawing any conclusions. Current ratio and quick ratio are two key liquidity ratios that provide complementary perspectives on a companys short-term financial health. Both ratios assess a companys short-term cash position and its ability to handle immediate financial needs and obligations.Liquidity ratios, such as the current and quick ratios, assess a companys ability to convert assets into cash quickly and cost-effectively. These ratios help analysts, investors, and company leadership understand whether a business can meet its short-term obligations without disrupting operations.The difference between the current ratio and quick ratio lies in what liquid assets are included in each ratios calculation and how each ratio is interpreted.Source: CFIs Financial Analysis Fundamentals courseWhat is the Current Ratio?The current ratio, also known as the working capital ratio, measures a businesss ability to meet its short-term obligations that are due within a year. This ratio compares total current assets to total current liabilities. It also looks at how a company can maximize the liquidity of its current assets to settle its liabilities and debt obligations.The current ratio is calculated by dividing total current assets by total current liabilities:Current Ratio = Current Assets Current LiabilitiesWhat is the Quick Ratio?The quick ratio, also known as the Acid Test Ratio, measures the ability of a business to pay its short-term liabilities. But unlike the current ratio, the quick ratio limits assets to cash or other assets that a company can swiftly convert into cash. Therefore, the quick ratio excludes accounts like inventory and prepaid expenses.The quick ratio is usually calculated by subtracting inventory from the total current assets and dividing the result by total current liabilities:Quick Ratio = (Current Assets Inventory) Current LiabilitiesWhat are the Differences Between the Current Ratio and the Quick Ratio?The current ratio is more comprehensive than the quick ratio, as it includes all current assets from the balance sheet cash, marketable securities, accounts receivable, and inventory.Another way to understand the difference is that a quick ratio only looks at the most liquid assets, which is a stricter assessment of a companys immediate liquidity. For example, inventory is a company asset that relies on sales to generate cash. Depending on sales cycles, it may take time for inventory to sell, i.e., convert into cash, thus making it less quick than other current assets.Source: CFIs Accounting Fundamentals courseCurrent Ratio Formula and CalculationSuppose youre analyzing a company that holds the following assets and liabilities on its balance sheet:AssetsCash = $15 millionMarketable securities = $20 millionInventory = $25 millionLiabilitiesShort-term debt = $15 millionAccounts payables = $15 millionUsing the current ratio formula (Current Ratio = Current Assets Current Liabilities), you perform the following calculation:Current assets = 15 + 20 + 25 = $60 millionCurrent liabilities = 15 + 15 = $30 millionCurrent ratio = $60 million / $30 million = 2.0 (or expressed as a multiple as 2x)Typically, a current ratio greater than 1.0 suggests financial well-being for a company. A current ratio of 2.0 means that the company could pay off its current liabilities twice with its current assets.Source: CFIs Financial Analysis Fundamentals courseQuick Ratio Formula and CalculationNow suppose you want to assess the same companys liquidity position with a more conservative measurement the quick ratio.In contrast with the current ratio, the Quick Ratio excludes inventory from current assets before dividing by current liabilities:Quick Ratio = (Current Assets Inventory) Current LiabilitiesYou calculate the companys current ratio as follows:Current Assets Inventory = 60 25 = $35 millionCurrent liabilities = $30 millionQuick ratio = $35 million / $30 million = 1.17 (or expressed as a multiple as 1.17x)The quick ratio of 1.17 indicates the company can pay off its current liabilities 1.17 times using only its most liquid assets, without relying on inventory sales.For an even more conservative liquidity ratio, analysts sometimes subtract prepaid expenses, or future expenses paid in advance, as well as inventory from current assets. To calculate a quick ratio with this approach, use the following formula:Quick Ratio = [Current Assets Inventory Prepaid Expenses] Current LiabilitiesSource: CFIs Financial Analysis Fundamentals courseHow to Interpret the Current Ratio vs. Quick RatioWhat the Current Ratio RevealsA strong current ratio signals flexibility. It shows the company has enough accessible resources to cover near-term financial obligations and maybe even some breathing room. But too much of a cushion can raise questions about underutilized capital.A current ratio above 1.0 means the company holds more current assets than current liabilities.A ratio of 2.0 suggests it could pay off its short-term liabilities twice over.Analysts often consider a range between 1.5 and 3.0 healthy, but that depends on the business:Retailers may operate well with ratios around 0.90, thanks to quick inventory turnover.Manufacturers tend to target higher ratios due to slower-moving inventory.A very high ratio can sometimes signal inefficiency, such as cash sitting idle instead of being reinvested for growth.What the Quick Ratio RevealsThe quick ratio helps you gauge how easily a company could respond to immediate financial pressure without relying on inventory or other assets that take time to liquidate. Its a more conservative read on liquidity, especially useful when speed matters.A quick ratio above 1.0 typically indicates that the company can meet short-term obligations using its most liquid assets.The sweet spot for many businesses falls between 1.0 and 1.5, though expectations vary by industry:Retailers may function well with ratios as low as 0.30, given predictable cash inflows.A ratio below 1.0 could mean the company is vulnerable if sales slow down or credit tightens.On the other hand, a very high quick ratio might indicate excess liquidity that could be put to better use.Comparing Results Across Both RatiosLooking at both ratios side by side helps you understand how much the company depends on inventory to stay liquid.A wide gap between the two often signals heavy reliance on inventory. For instance, a current ratio of 2.0 and a quick ratio of 0.7 suggest that inventory makes up a large portion of current assets.That might be perfectly reasonable for a retail business but it could raise red flags in sectors like tech, where inventory can become obsolete quickly.Bottom line: Neither ratio tells the full story on its own. Use them together to spot patterns, assess risk, and benchmark against industry norms. Thats how you turn numbers into insight.Source: CFIs Financial Analysis Fundamentals courseCurrent Ratio vs Quick Ratio: Which Should You Use for Your Financial Analysis?When it comes to the current ratio and quick ratio, both measures provide essential perspectives on a companys liquidity position. Rather than choosing between them, use both ratios as complementary measures that provide a fuller picture. Track these two ratios over time to identify trends and always compare them against industry benchmarks for meaningful context.Financial ratio analysis, including these liquidity metrics, is covered in depth in CFIs Financial Analysis Fundamentals course, a core requirement in the FMVA certification program.CFIs Financial Modeling & Valuation Analyst (FMVA) certification is one of the most recognized programs for learning financial modeling skills. Its designed for professionals pursuing careers in investment banking, equity research, FP&A, corporate finance, and related fields. Over 75% of CFI learners report significant career advancement within months of program completion.The FMVA program provides the structured path and hands-on training you need to build real-world modeling skills and apply them with confidence in any corporate finance environment.Earn Your Certification!Additional ResourcesFinancial Ratios Definitive GuideROA vs. ROE: Differences, Formulas, and Uses in Financial AnalysisNegative Working Capital: Strength or a Warning Sign?Essential Guide to Accounting for Financial AnalystsSee all Accounting resourcesSee all Financial Modeling resources The Current Ratio and Quick Ratio are both financial ratios used to assess a company's liquidity and ability to meet short-term obligations. However, they differ in terms of the assets included in the calculation. The Current Ratio measures a company's ability to pay off its current liabilities using its current assets, including both liquid and illiquid assets. On the other hand, the Quick Ratio, also known as the Acid-Test Ratio, focuses only on the most liquid assets, such as cash, marketable securities, and accounts receivable. This ratio provides a more conservative measure of a company's liquidity as it excludes inventory and prepaid expenses. While both ratios provide insights into a company's short-term financial health, the Quick Ratio is considered a more stringent measure of liquidity. When it comes to analyzing a company's financial health, there are several ratios that investors and analysts use. Two commonly used ratios are the Current Ratio and the Quick Ratio. These ratios provide insights into a company's ability to meet its short-term obligations. While both ratios serve a similar purpose, they differ in terms of the components they consider and the level of liquidity they measure. In this article, we will explore the attributes of both ratios and discuss their strengths and limitations.Current RatioThe Current Ratio is a liquidity ratio that measures a company's ability to pay off its short-term liabilities using its short-term assets. It is calculated by dividing the total current assets by the total current liabilities. The formula for the Current Ratio is as follows:Current Ratio = Total Current Assets / Total Current LiabilitiesThe Current Ratio provides an indication of a company's short-term liquidity position. A ratio greater than 1 indicates that a company has more current assets than current liabilities, suggesting that it can cover its short-term obligations. However, a ratio significantly higher than 1 may indicate that a company is not efficiently utilizing its assets or has excess inventory or receivables.One of the advantages of the Current Ratio is that it considers all current assets, including cash, accounts receivable, and inventory. This makes it a comprehensive measure of a company's liquidity. Additionally, the Current Ratio is easy to calculate and widely used, making it a popular tool for financial analysis.Quick RatioThe Quick Ratio, also known as the Acid-Test Ratio, is a more stringent measure of liquidity compared to the Current Ratio. It excludes inventory from the current assets, as inventory may not be easily converted into cash in the short term. The Quick Ratio is calculated by dividing the sum of cash, cash equivalents, short-term investments, and accounts receivable by the total current liabilities. The formula for the Quick Ratio is as follows:Quick Ratio = (Cash + Cash Equivalents + Short-term Investments + Accounts Receivable) / Total Current LiabilitiesThe Quick Ratio provides a more conservative assessment of a company's ability to meet its short-term obligations. By excluding inventory, it focuses on the most liquid assets that can be readily converted into cash. A higher Quick Ratio indicates a stronger liquidity position, as the company has a greater ability to pay off its current liabilities without relying on inventory sales.One of the limitations of the Quick Ratio is that it may not be suitable for companies with significant inventory holdings. For example, retail companies often have high inventory levels, and excluding inventory from the ratio may not accurately reflect their liquidity position. However, for service-based companies or those with minimal inventory, the Quick Ratio can provide a more accurate measure of liquidity.ComparisonNow that we have discussed the attributes of both the Current Ratio and the Quick Ratio, let's compare them in terms of their strengths and limitations:1. Liquidity AssessmentThe Current Ratio provides a broader assessment of a company's liquidity position by considering all current assets. It gives a more comprehensive view of the company's ability to meet its short-term obligations. On the other hand, the Quick Ratio focuses on the most liquid assets, excluding inventory. This makes it a more conservative measure of liquidity, as it considers only the assets that can be quickly converted into cash.2. Inventory ConsiderationThe Current Ratio includes inventory as part of the current assets. This is beneficial for companies with significant inventory holdings, as it reflects their ability to convert inventory into cash. However, for companies with slow-moving or obsolete inventory, the inclusion of inventory in the Current Ratio may overstate their liquidity position. The Quick Ratio, on the other hand, excludes inventory, providing a more accurate measure of liquidity for companies with minimal inventory or those where inventory is not easily converted into cash.3. Calculation ComplexityThe Current Ratio is relatively simple to calculate, as it only requires the total current assets and total current liabilities. This makes it a widely used ratio in financial analysis. On the other hand, the Quick Ratio involves a more detailed calculation, as it requires the identification and exclusion of inventory from the current assets. This additional complexity may make the Quick Ratio less commonly used compared to the Current Ratio.4. Industry ConsiderationsBoth ratios have their strengths and limitations depending on the industry in which a company operates. For example, retail companies with high inventory turnover may find the Quick Ratio more useful, as it provides a clearer picture of their liquidity position. On the other hand, service-based companies or those with minimal inventory may rely more on the Current Ratio to assess their liquidity. It is important to consider the nature of the business and industry-specific factors when choosing between the two ratios.5. Time SensitivityBoth the Current Ratio and the Quick Ratio provide a snapshot of a company's liquidity position at a specific point in time. Changes in the composition of current assets or liabilities can significantly impact the ratios. Therefore, it is important to analyze these ratios in conjunction with other financial indicators and trends to gain a more comprehensive understanding of a company's financial health.ConclusionThe Current Ratio and the Quick Ratio are both valuable tools for assessing a company's liquidity position. While the Current Ratio provides a broader view of liquidity by considering all current assets, the Quick Ratio focuses on the most liquid assets, excluding inventory. The choice between the two ratios depends on the industry, the nature of the business, and the specific circumstances of the company being analyzed. It is important to consider these factors and analyze the ratios in conjunction with other financial indicators to gain a comprehensive understanding of a company's financial health. Comparisons may contain inaccurate information about people, places, or facts. Please report any issues. This website uses cookies to provide better user experience and user's session management. By continuing visiting this website you consent the use of these cookies. In this article 4 Mins Share Financial ratios are important indicators for gauging a companys financial health. They show the financial position of the company, including its profitability and liquidity position. The two important ratios for measuring a companys ability to pay short term obligations and liquidity are the current and quick ratios. This article covers the current ratio, quick ratio and current vs quick ratio in detail. The following table summarizes the key differences between quick ratio and current ratio: Basis of DifferenceCurrent RatioQuick RatioRatioCurrent Assets to Current LiabilitiesHighly Liquid Assets to Current LiabilitiesApproachRelaxed approach to determine A companys debt repayment capacity.A stringent approach to determine a companys debt repayment capacity.ConsiderationConsiders assets that are easily convertible to cash within a year.Considers assets that are easily convertible to cash in 90 days or earlier.InventoryIncludesExcludesIdeal Result2:11:1 The current ratio is a liquidity ratio that computes the proportion of a companys current assets to its current liabilities. On the other hand, quick ratio is also a liquidity ratio that computes the proportion of a companys highly liquid assets to its current liabilities. The current ratio is comparatively a relaxed approach to determine a companys debt repayment capacity. On the other hand, the quick ratio is a stringent and conservative approach to determine a companys debt repayment capacity. The current ratio considers assets that are easily convertible to cash within a year. While quick ratio considers assets that are easily convertible to cash in 90 days or earlier. The current ratio includes inventory. Also, the current ratio is naturally high for firms with a strong stock of inventory. On the other hand, the quick ratio excludes inventory. Also, the quick ratio is low for firms with a strong stock of inventory. The ideal current ratio is 2:1. However, anything above 1 is good. On the other hand, the ideal quick ratio is 1:1. The current ratio is a liquidity ratio that investors and analysts use to understand the debt repayment capacity of the company. It measures if the company is able to pay off all its current liabilities using its current assets. All obligations that have to be paid off within one year are current liabilities. On the other hand, all the assets that can be converted into cash within one year are current assets. Current Ratio Formula Current Ratio = Current Assets / Current Liabilities The quick ratio is also a liquidity ratio that individuals use to estimate the debt repayment capacity of a company. However, the quick ratio considers only highly liquid assets rather than current assets. Thus, this is a major difference between current ratio and quick ratio. Quick ratio measures if the company is able to pay off all its current liabilities using its highly liquid assets. Highly liquid assets are current assets that can be liquidated in less than 90 days. Quick Ratio Formula Quick Ratio = (Cash + Cash Equivalents + Current Receivables + Short Term Investments) / Current Liabilities Discover More Courses > Management Accounting > Financial Ratios Checked for updates, April 2022. Accountingverse.com The current ratio is one of the most common measures of liquidity. It refers to the ratio of current assets to current liabilities.Current Ratio FormulaThe formula for current ratio is:Current ratio = Current assets Current liabilitiesCurrent assets include cash and cash equivalents, marketable securities, short-term receivables, inventories, and prepayments. Current liabilities include trade payables, current tax payable, accrued expenses, and other short-term obligations. Current assets refer to cash and other resources that can be converted into cash in the short-term (within 1 year or the company's normal operating cycle, whichever is longer).Current liabilities are obligations that are to be settled within 1 year or the normal operating cycle. ExampleXYZ Company had the following figures extracted from its books of accounts. Current assets: Cash and cash equivalents $ 83,000 Marketable securities 142,000 Trade and other receivables 167,000 Inventories 330,000 Prepayments 60,000 Total current assets $ 782,000 Non-current assets: Long-term investments $ 300,000 Fixed assets 1,000,000 Total current assets $ 1,300,000 TOTAL ASSETS $ 2,082,000 Current liabilities $ 337,000 Non-current liabilities 1,100,000 Stockholders' equity 645,000 TOTAL LIABILITIES & EQUITY $ 2,082,000 Computation of current ratio: Current ratio = Current assets Current liabilities = $782,000 $337,000 Current ratio = 2.32 If the current ratio computation results in an amount greater than 1, it means that the company has adequate current assets to settle its current liabilities. In the above example, XYZ Company has current assets 2.32 times larger than current liabilities. In other words, for every $1 of current liability, the company has $2.32 of current assets available to pay for it.A high current ratio is generally considered a favorable sign for the company. Creditors are more willing to extend credit to those who can show that they have the resources to pay obligations. However, a current ratio that is too high might indicate that the company is missing out on more rewarding opportunities. Instead of keeping current assets (which are idle assets), the company could have invested in more productive assets such as long-term investments and plant assets.The ideal current ratio is proportional to the operating cycle. Companies with shorter operating cycles, such as retail stores, can survive with a lower current ratio than, say for example, a ship-building company. The current ratio should be compared with standards -- which are often based on past performance, industry leaders, and industry average. Key TakeawaysThe current ratio is a very common financial ratio to measure liquidity.Current ratio is equal to total current assets divided by total current liabilities.A ratio greater than 1 means that the company has sufficient current assets to pay off short-term liabilities.A high ratio implies that the company has a thick liquidity cushion. Web link APA formatCurrent ratio (2022). Accountingverse. Next LessonPrevious LessonChapter OutlineFinancial Statement Analysis

What is a good current and quick ratio. When to use quick ratio vs current ratio. Difference between current ratio and quick ratio. Quick ratio higher. Current quick ratio. Difference between current assets and quick ratio. Current ratio and quick ratio analysis. Quick ratio vs current ratio.