Current Ratio

The current ratio is a liquidity ratio that investors can calculate when looking to invest in a company. This ratio takes the company's current assets and divides them by the current liabilities to tell investors how well a company could pay their liabilities due within 12 months. The current ratio should be used to compare similar companies to one another to see if there is any distress in one of the companies you are looking to invest in. With everything constant, investors should look for higher current ratios that demonstrate a more vital ability to pay off the company's current liabilities going forward. All the information needed to calculate the current ratio can be found in the balance sheet of the financial statements.

Now let's give an example of how to calculate the current ratio with Home Depot's latest quarterly release:

Total Current Assets (In Millions)= $33,867
Total Current Liabilities (In Millions)= $30,387
Total Current Ratio= 33,867/30,387= 1.11

This current ratio shows that HD is in a good financial position to pay off all of its current liabilities in the next 12 months, with its current assets on its balance sheet.

As a comparison, LOW (Lowe's) has a current ratio of 1.17, which shows that they are in a slightly better position than HD on the balance sheet. If LOW had a current ratio of 0.6 while HD had a ratio of 1.11, then the investor may have to ask questions regarding the risk LOW could have with their liabilities going forward.