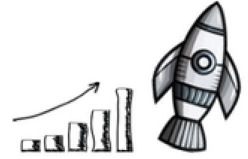

Cash Ratio

The cash ratio is a good way for investors to measure a company's current liquidity. The ratio tells investors the ability of a company to cover all of its short-term obligations with cash held on the balance sheet. The measurement for this ratio takes the company's current cash and marketable securities and divides them by the current liabilities. Investors would want this ratio to be greater than one, showing that the company can cover all its current liabilities with cash. If the ratio is less than one, it could show investors and creditors that there is a risk that the company may not be able to fulfill all of its current debt obligations.

Let's give an example of a company with a high cash ratio.

Monster Beverage Corporation's (MNST) most recent balance sheet is as follows (In Millions):

Cash and Short Term Investments: $2,732.43
Current Liabilities: $1,044.36
The cash ratio for MNST is 2,732.43/1,044.36= 2.62

A 2.62 cash ratio for MNST shows investors that the company will have no problem with its liabilities in the short term, as it can cover more than double that amount with cash on hand.

And now, here is an example of a company with a low cash ratio.

Best Buy's (BBY) most recent balance sheet is as follows (In Millions):

Cash and Cash Equivalents: $940
Current Liabilities: $8,635
The cash ratio for BBY is 940/8,635= 0.11

A 0.11 cash ratio means investors should look further into the balance sheet to see how the company would fund its liabilities moving forward.

A high cash ratio is not always great for a company, as the management team could be utilizing the cash on the balance sheet for investments back into the company to fuel future growth. Cash could also be distributed back to shareholders as a dividend or share repurchase.