

Summary

This chapter covered two approaches to a firm's long-term debt-paying ability. One approach considers the firm's ability to carry debt as indicated by the income statement, and the other approach views it as indicated by the balance sheet. The ratios related to debt include the following:

$$\text{Times Interest Earned} = \frac{\text{Recurring Earnings, Excluding Interest Expense, Tax Expense, Equity Earnings, and Noncontrolling Interest}}{\text{Interest Expense, Including Capitalized Interest}}$$

$$\text{Fixed Charge Coverage} = \frac{\text{Recurring Earnings, Excluding Interest Expense, Tax Expense, Equity Earnings, and Noncontrolling Interest} + \text{Interest Portion of Rentals}}{\text{Interest Expense, Including Capitalized Interest} + \text{Interest Portion of Rentals}}$$

$$\text{Debt Ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

$$\text{Debt/Equity Ratio} = \frac{\text{Total Liabilities}}{\text{Shareholders' Equity}}$$

$$\text{Debt to Tangible Net Worth Ratio} = \frac{\text{Total Liabilities}}{\text{Shareholders' Equity} - \text{Intangible Assets}}$$