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1. Describe the 3 main categories of ratios and provide a specific example of a ratio that is used in each category. For each of the 3 ratios you selected, describe how it is used in managerial decision-making.

By definition, a ratio is an outcome that is obtained when the financial account balance of one account is divided by the account balance of another account (Liang, Lu, Tsai & Shih, 2015). One of the categories of ratios is liquidity ratios. With liquidity ratios, the ability of the organization to pay both short or long-term obligations can be deduced (Liang, Lu, Tsai & Shih, 2015). Normally, for an organization to be able to meet its short and long term commitments, it has to have some degree of liquidity. There are various examples of liquidity ratio however, the current ratio is the most common one. With the current ratio, the ability of the organization to meet its short goals. Therefore, the current ratio will be important for managers in making decisions on how the organization can effectively pay its current obligations.

Profitability ratios are the second category of ratios. With the profitability ratios, the organization's performance in utilizing the available resources and make a profit can be determined (Liang, Lu, Tsai & Shih, 2015). The profitability ratios consist of the measurement metrics that show the ability of the organization to generate revenue. Return on assets is one of the examples of profitability ratios. With return on assets, the profitability of an organization can be assessed with regard to the cost and expenses before being compared to the assets (Liang, Lu, Tsai & Shih, 2015). Therefore, the management can use the return on assets to measure how the organization is performing in relation to its assets.

Leverage ratios are the third category of ratios. With the leverage ratios, the debt that the organization has incurred against its income statement is measured. It indicates how the organization finances its assets using equity. The debt to asset ratio is an example of this

category of ratios. Debt to asset ratio highlights all the assets financed by the creditors as opposed to investors in the organization. the creditors and investors normally use the debt to asset ratio to analyze the financial health of an organization.

Reference

- Liang, D., Lu, C. C., Tsai, C. F., & Shih, G. A. (2016). Financial ratios and corporate governance indicators in bankruptcy prediction: A comprehensive study. *European Journal of Operational Research*, 252(2), 561-572.

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