SPECIFIC-CASE

WORKSHEET 8 OF 9

Current Ratio Drops Below 1.0x Unexpectedly

Scenario: This quarter's balance sheet shows current ratio 0.93x — below 1.0x for the first time. The income statement still shows positive net profit. No payments are overdue. You do not know whether this is a one-time seasonal dip or the start of a structural decline. You need to diagnose the cause and decide whether to act immediately or monitor one more quarter.

Complementary worksheet for

Financial Ratio Analysis
by Ibrahim Anwar

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SECTION 1

What This Is For

A diagnostic framework for the specific moment when current ratio falls below 1.0x for the first time, with positive net income still showing on the income statement. This combination — current ratio below the bank's minimum alongside a profitable quarter — is precisely the situation that misleads most operators into waiting. The income statement says things are fine; the balance sheet says something else. This worksheet resolves that contradiction by identifying what caused the ratio to fall and whether the cause is seasonal or structural.

The worksheet is not a general liquidity tool. It is designed for the 72-hour window after the balance sheet is closed and the number appears below 1.0x. In that window, the operator needs to answer one question fast: is this a known seasonal pattern that will reverse, or is it the beginning of a structural deterioration that requires action within 90 days? The wrong answer costs 90 days.

SECTION 2

Benefits

What you get when you actually run this worksheet on a real situation:

- Separates the two possible causes of a current ratio decline — falling current assets versus rising current liabilities — which require completely different responses.
- Determines within one analysis session whether the drop is seasonal (compare same quarter last year) or structural (confirmed by three consecutive same-quarter readings).
- Identifies the specific asset or liability component responsible for the change, with the dollar amount.
- Provides a concrete decision framework: three conditions that must all hold for 'monitor one more quarter' to be the right call — if any one fails, the 90-day action is required.
- Calculates the cost of corrective action in concrete terms before the action is taken.

SECTION 3

Framework To Use

Side-of-Ratio Diagnostic

Current ratio = Current Assets / Current Liabilities. A ratio drop has one of two causes. The response depends entirely on which side moved.

CURRENT RATIO BELOW 1.0X — WHICH SIDE DROVE THE DROP?

SECTION 4

How To Use

Follow these steps in order. Each one builds on the previous.

1. Pull the balance sheet for this quarter, the prior quarter, and the same quarter last year. Three columns side by side.
2. Fill the diagnostic table: current assets total, current liabilities total, current ratio, quick ratio, then break into components: cash, receivables, inventory, trade payables, short-term bank debt.
3. Compare this quarter against prior quarter to find the immediate cause. Compare this quarter against same quarter last year to determine seasonal versus structural.
4. Identify which side moved: did current assets fall, or did current liabilities rise? By how many dollars? Which specific component is responsible? Write the dollar amount.
5. Apply the three-condition test: (1) is this drop consistent with the same quarter in the prior two years? (2) is quick ratio above 0.8x? (3) is same-quarter last year above 1.0x? If all three conditions hold, monitoring one more quarter is defensible. If any one condition fails, write the 90-day corrective action.
6. Calculate what the corrective action costs: in dollars, in days of delay, and in supplier or customer relationship impact if the action involves changing terms.

SECTION 5

Example Use

A building supplies distributor closes Q3 and current ratio shows 0.93x. Net profit for Q3 is $28,000 positive. No payments are overdue. Prior quarter (Q2) current ratio was 1.14x. Same quarter last year (Q3 prior year) was 1.08x. Quick ratio this quarter is 0.74x.

The owner fills the three-column diagnostic table.

Current assets this Q3: $312,000. Prior Q2: $358,000. Same Q3 prior year: $340,000.
Current liabilities this Q3: $335,000. Prior Q2: $314,000. Same Q3 prior year: $315,000.

Which side moved? Current liabilities rose from $314,000 to $335,000 — an increase of $21,000. Current assets fell from $358,000 to $312,000 — a decrease of $46,000. Both sides moved. Total effect: $67,000 swing in the ratio.

Breaking down assets: cash went from $87,000 to $62,000 (down $25,000 — the owner made a tax installment payment in August). Receivables went from $156,000 to $148,000 (down $8,000 — slightly faster collection). Inventory went from $115,000 to $102,000 (down $13,000 — Q3 is a slower season, stock was drawn down without replenishment yet).

Breaking down liabilities: trade payables rose from $198,000 to $224,000 (up $26,000 — the main supplier changed invoice terms from net-30 to net-45 effective Q3, shifting more payables into current). Bank installment unchanged.

Three-condition test: (1) Same Q3 last year had current ratio 1.08x — also below 1.2x but above 1.0x. Not the same pattern (last year was above 1.0x, this year below). Condition 1 partially fails — last year was not below 1.0x. (2) Quick ratio 0.74x — below 0.8x threshold. Condition 2 fails. (3) Same quarter last year 1.08x — above 1.0x. Condition 3 holds.

Two of three conditions fail. The 90-day action is required. Owner writes: accelerate two receivable collections above $15,000 each (representing $34,000 if collected within 30 days). Do not pay the next supplier invoice of $18,000 early — defer to due date to preserve cash. These two actions together would move current assets from $312,000 to approximately $346,000, and current liabilities would remain at $335,000, producing a current ratio of approximately 1.03x. Not ideal, but above the 1.0x floor before Q4 closes.

SECTION 6

The Worksheet

Tear this out, copy it onto a fresh sheet, or fill it in directly.

Current Ratio Drops Below 1.0x Unexpectedly

Scenario: This quarter's balance sheet shows current ratio 0.93x — below 1.0x for the first time. The income statement still shows positive net profit. No payments are overdue. You do not know whether this is a one-time seasonal dip or the start of a structural decline. You need to diagnose the cause and decide whether to act immediately or monitor one more quarter.

DIAGNOSTIC ITEM	THIS QUARTER	PRIOR QUARTER	SAME QUARTER LAST YEAR	SIGNAL

SECTION 6 (CONTINUED)

Reflection Prompts

After filling in the worksheet on the previous page, work through these.

1. Row labels: Current Assets ($) · Current Liabilities ($) · Current Ratio · Quick Ratio · Cash + Bank ($) · Receivables ($) · Inventory ($) · Trade Payables ($). Fill from this quarter, prior quarter, and same quarter last year. In the Signal column: write whether each row is better, worse, or consistent compared to same quarter last year.

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2. Identify which side of the ratio drove the drop: did current assets fall, or did current liabilities rise? Write the dollar amount of the change for each component. Which single component accounts for the largest portion of the ratio movement? Is that component under the operator's control (receivables, inventory management) or an external timing event (supplier invoice cycle, loan installment reclassification)?

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3. Three-condition test: write the result for each — (1) Is this Q consistent with the same Q in prior two years? (2) Is quick ratio above 0.8x? (3) Was same-quarter last year above 1.0x? If all three hold: monitor next quarter before acting. If any one fails: write the specific action to raise current ratio above 1.0x within 90 days — and calculate what the action costs in concrete terms ($, days of delay, counterparty relationship impact).

SECTION 7

Tips and Traps

TIPS

- Look at quick ratio alongside current ratio the moment current ratio drops below 1.0x. If quick ratio is also below 0.8x, the liquidity risk is more immediate — inventory speed cannot save the position.
- When current liabilities rose, check first whether it is the current portion of long-term debt. A large installment reclassified from long-term to current in this quarter is a timing event, not a deterioration — but it must still be managed.
- If the drop is confirmed as seasonal (same quarter consistently lower for three consecutive years), build that seasonal floor into your covenant headroom calculations before the next credit renewal. Banks expect seasonal businesses to show the pattern and explain it, not to hide it.
- The three-condition test is strict by design. One failed condition means acting — not asking more questions. The 90-day action window is the relevant constraint, not academic certainty about whether the cause is structural.

TRAPS

- Trusting positive net income to mean current ratio is fine. Net income does not appear in the current ratio calculation — it can be positive while current ratio deteriorates through receivable lengthening, inventory build, or new short-term borrowing.
- Waiting for the full quarter of data to confirm the trend before acting. If quick ratio is below 0.8x and same-quarter prior year was above 1.0x, the 90-day clock starts when the balance sheet is closed, not when the next quarter closes.
- Assuming the bank does not know. Banks calculate current ratio from the same quarterly financial statements the operator submits. A current ratio breach on a submitted statement triggers a review at the bank's credit monitoring team before the operator receives any notification.

SECTION 8

Appendixes

Appendix A — 90-Day Current Ratio Recovery Actions (Ranked by Speed)

Speed = how quickly the action converts to an improved current ratio.

1. Accelerate receivable collections (highest speed):
   Contact top 5 customers with balances > 30 days. Collect $X this week.
   Impact: current assets increase by amount collected.
   Timeline: 1-4 weeks.

2. Defer non-urgent payables (high speed):
   Identify payables not yet due. Request a 15-day extension from suppliers.
   Impact: current liabilities reduced by deferred amount.
   Timeline: immediate, subject to supplier agreement.

3. Sell slow-moving inventory at breakeven (medium speed):
   Converts inventory (lower liquidity) to cash (higher liquidity).
   Impact: current assets composition improves (cash vs inventory).
   Current ratio total may stay the same; quick ratio improves.
   Timeline: 2-8 weeks depending on product and buyer.

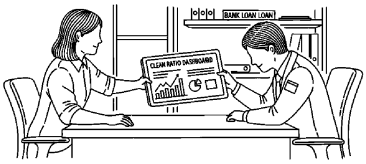
4. Negotiate short-term overdraft to buffer (low speed — last resort):
   Adds current liabilities, which worsens current ratio further unless
   cash drawn is used to pay down a larger current liability simultaneously.
   Use only if none of the above options close the gap within the window.

Appendix B — Seasonal Current Ratio Pattern Documentation

Build this table from three years of same-quarter data:

Quarter	Year N-2	Year N-1	Year N	Seasonal low? (Y/N)
Q1				
Q2				
Q3				
Q4				

A quarter marked seasonal low in all three years is a predictable pattern,
not a deterioration signal. Document it and build covenant headroom calculations
around the seasonal low, not the peak quarter.



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Financial Ratio Analysis

Read Your Own Financial Statements Before the Bank Reads Them for You

by Ibrahim Anwar

This worksheet is one of nine in the *Financial Ratio Analysis* companion worksheet pack. The full pack is grouped into three categories: high-volume worksheets you can run weekly, niche-search worksheets for rare but high-value situations, and specific-case worksheets that walk you through a single concrete scenario.

Every framework, decision filter, and figure used in these worksheets is drawn from the chapters of the source book. The book sets the diagnosis, the worksheets give you the form to act on it.

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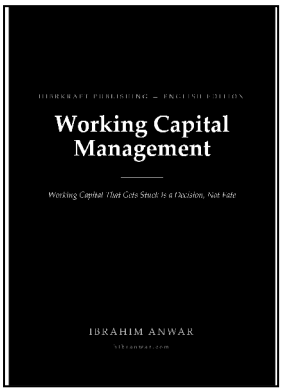

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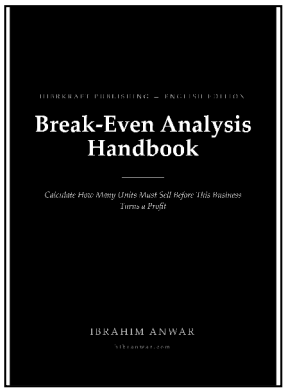

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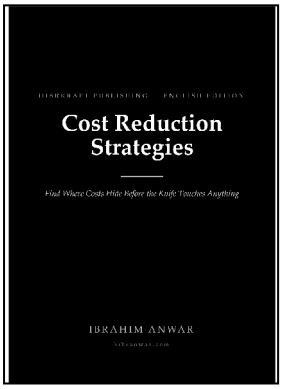

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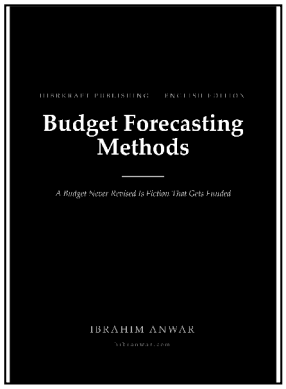

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