

The Influence of Financial Ratio Factors on Financial Performance: A Literature Review in Financial Management

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ABSTRACT

Tinjauan pustaka ini bertujuan untuk mengidentifikasi dan meneliti faktor-faktor rasio keuangan inti yang secara signifikan memengaruhi kinerja laporan keuangan perusahaan, yang menawarkan wawasan penting untuk meningkatkan pengambilan keputusan manajerial dalam manajemen keuangan. Analisis difokuskan pada lima kategori utama rasio keuangan: likuiditas, solvabilitas, aktivitas, profitabilitas, dan investasi. Rasio-rasio ini berfungsi sebagai indikator penting untuk menilai kondisi keuangan dan efisiensi operasional perusahaan, dan umumnya digunakan oleh para pemangku kepentingan untuk mengevaluasi kesehatan keuangan dan memandu perencanaan strategis. Studi ini mensintesiskan temuan dari berbagai artikel penelitian sebelumnya untuk mengeksplorasi bagaimana setiap rasio memengaruhi berbagai dimensi kinerja keuangan, seperti pertumbuhan profitabilitas, pemanfaatan aset, pengelolaan utang, dan nilai pemegang saham. Dengan menyajikan pembahasan komprehensif tentang implikasi teoritis dan praktis dari analisis rasio keuangan, artikel ini berkontribusi pada pengembangan model konseptual yang menghubungkan indikator keuangan dengan metrik kinerja perusahaan. Tinjauan tersebut mengungkapkan bahwa: (1) terdapat korelasi kuat antara rasio keuangan dan kinerja perusahaan secara keseluruhan, khususnya dalam konteks efisiensi dan penciptaan nilai; (2) setiap rasio memberikan dampak yang berbeda pada hasil keuangan tergantung pada struktur operasional perusahaan; dan (3) penerapan analisis rasio keuangan yang konsisten mendukung keberlanjutan jangka panjang dan pertumbuhan perusahaan. Artikel ini diakhiri dengan menawarkan agenda penelitian untuk penyelidikan empiris di masa mendatang tentang peran strategis rasio keuangan dalam manajemen keuangan perusahaan.

This literature review aims to identify and examine the core financial ratio factors that significantly affect the performance of corporate financial statements, offering critical insights for enhancing managerial decision-making in financial management. The analysis focuses on five primary categories of financial ratios: liquidity, solvency, activity, profitability, and investment. These ratios serve as essential indicators for assessing a company's financial condition and operational efficiency, and they are commonly used by stakeholders to evaluate financial health and guide strategic planning. This study synthesizes findings from various previous research articles to explore how each ratio influences different dimensions of financial performance, such as profitability growth, asset utilization, debt management, and shareholder value. By presenting a comprehensive discussion on the theoretical and practical implications of financial ratio analysis, this article contributes to the development of a conceptual model that links financial indicators to company performance metrics. The review reveals that: (1) there is a strong correlation between financial ratios and overall company performance, particularly in the context of efficiency and value creation; (2) each ratio exerts a distinct impact

on financial outcomes depending on the firm's operational structure; and (3) a consistent application of financial ratio analysis supports long-term sustainability and corporate growth. The article concludes by offering a research agenda for future empirical investigations on the strategic role of financial ratios in corporate financial management.



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INTRODUCTION

In today's dynamic and highly competitive global business landscape, companies are increasingly challenged to maintain optimal financial performance to ensure sustainability, growth, and competitive advantage. Financial performance is widely recognized as one of the most critical indicators of a company's operational success and its ability to generate value for stakeholders in both the short and long term. Corporate financial performance is generally assessed through various financial metrics derived from the company's financial statements. Among the most widely used tools in this assessment is financial ratio analysis, which allows for the evaluation of financial efficiency, profitability, and risk. By analyzing financial ratios, stakeholders can gain a clearer picture of how well a company manages its resources, controls its liabilities, and generates returns.

Financial ratios are calculated by comparing specific figures from income statements, balance sheets, and cash flow statements. These include liquidity ratios, which assess the company's ability to meet short-term obligations; solvency ratios, which evaluate the long-term financial stability and risk of insolvency; activity ratios, which measure operational efficiency in managing assets; profitability ratios, which reveal the firm's ability to generate income relative to revenue, assets, or equity; and investment ratios, which reflect investor expectations and market performance. These ratios serve not only as tools for retrospective analysis but also as predictive indicators of future performance. For internal management, they assist in identifying weaknesses in financial practices and guiding strategic decisions. For external parties—such as investors, creditors, and regulatory authorities—they offer valuable insights for decision-making, benchmarking, and risk assessment.

A well-performing financial structure supports operational effectiveness and reflects managerial competence in utilizing assets, controlling costs, and achieving strategic objectives. As such, consistent analysis and monitoring of financial ratios are vital components of a company's financial management system. These tools contribute significantly to maintaining financial discipline and transparency in an organization. Understanding the relationship between financial ratios and financial performance can also help companies improve their financial planning processes. Firms that utilize financial ratios effectively are better positioned to detect early signs of financial distress and take proactive measures. Moreover, ratio analysis provides a framework for setting performance benchmarks and establishing financial goals aligned with strategic priorities.

Despite the widespread use of financial ratios in corporate settings, there is still a need to explore their influence through a systematic review of existing literature. This literature review aims to investigate how different types of financial ratios affect financial statement performance, offering both theoretical and practical insights into their implications in financial management. By consolidating findings from previous studies, this review seeks to build a robust theoretical foundation for further empirical research. It also aims to identify gaps in the current literature, propose hypotheses for future investigation, and support academic and managerial understanding of the strategic role of financial ratios in enhancing corporate performance.

This study focuses on five major categories of financial ratios liquidity, solvency, activity, profitability, and investment—and their impact on financial performance indicators. The outcomes are expected to enrich the knowledge base in financial management and contribute to improved corporate practices and academic discourse.

Literature review

1. Corporate Financial Performance

Corporate financial performance is a key indicator that reflects how effectively a company utilizes its financial resources to generate profits and sustain growth. It provides insights into the overall health of a company and is used as a benchmark for internal assessment and external evaluation by stakeholders, including investors, creditors, and regulators (Nuriasari, 2018; Aisyiah et al., 2013; Handayani & Handayani, 2022). Financial performance is typically measured through financial statements, which capture critical financial data such as income, expenditures, assets, liabilities, and equity flows.

Financial performance analysis allows firms to evaluate their adherence to sound financial management principles. Among the tools available, financial ratio analysis is widely used to translate financial data into actionable metrics. The ability of a company to manage its capital effectively is crucial in generating optimal performance. High financial performance is often associated with increased corporate value and investor confidence (Lumenta & Worang, 2019; Husna & Satria, 2019). A company with poor financial performance may exhibit signs such as excessive liquidity ratios relative to available cash and cash equivalents, which could signal ineffective cash or inventory management. Therefore, proper interpretation of financial ratios is critical for drawing accurate conclusions about financial performance.

2. Liquidity Ratios

Liquidity ratios are used to assess a company's ability to meet short-term obligations as they come due. These ratios evaluate the availability of current assets to pay off current liabilities, thereby indicating the firm's short-term financial health. A strong liquidity position enhances stakeholder confidence and increases the firm's credibility in the market (Nuriasari, 2018). Common liquidity ratios include the current ratio, quick ratio, and cash ratio (Handayani & Handayani, 2022). The current ratio compares current assets to current liabilities, indicating the firm's ability to meet short-term debts. The quick ratio excludes inventories from current assets, providing a stricter measure of liquidity. The cash ratio focuses solely on cash and marketable securities, offering the most conservative view of liquidity. It is important to note that a high current ratio does not necessarily reflect strong financial health. An excessively high current ratio may indicate inefficient working capital management. Hence, comparative benchmarking with industry standards is essential for accurate interpretation (Lumenta & Worang, 2019).

3. Solvency Ratios

Solvency ratios measure a company's ability to meet its long-term obligations and indicate financial leverage. These ratios reveal the extent to which a company is financed by debt relative to its assets or equity. A high solvency ratio implies greater reliance on debt financing, which may increase financial risk (Aziz & Rahman, 2017; Tjandra, 2022). Key solvency ratios include the Debt to Asset Ratio, Debt to Equity Ratio, Long-Term Debt to Equity Ratio, Times Interest Earned, and Fixed Charge Coverage. These ratios assess the firm's long-term financial structure, ability to service debt, and sustainability in adverse financial conditions (Shintia & Novi, 2017). For example, the Debt to Equity Ratio indicates how much financing is provided by creditors compared to shareholders. A high ratio may suggest financial vulnerability, whereas a lower ratio indicates a more conservative financing structure.

4. Activity Ratios

Activity ratios evaluate how efficiently a company utilizes its resources to generate revenue. These ratios assess the turnover of assets, inventory, receivables, and payables, which are essential in operational performance analysis (Omuemu & Okoye, 2021). Types of activity ratios include the Inventory Turnover Ratio, Accounts Receivable Turnover Ratio, Asset Turnover Ratio, Credit Turnover Ratio, and Working Capital Turnover Ratio. A high turnover ratio typically reflects efficient resource management and rapid asset utilization (Indah & Tyas, 2020; Ratningsih & Alawiyah, 2017). Each of these ratios plays a role in understanding how well a company transforms its operational inputs into financial outputs. For instance, low inventory turnover might indicate overstocking or sluggish sales, whereas high receivable turnover could reflect effective credit policies.

5. Profitability Ratios

Profitability ratios measure a company's ability to generate profit relative to sales, assets, or equity. These ratios are vital in assessing the firm's operational success and long-term sustainability.

The broader and more detailed the profitability indicators, the better the insight into financial health (Ali, 2020). Common profitability ratios include Return on Assets (ROA), Return on Equity (ROE), Net Profit Margin, and Gross Profit Margin. These indicators provide information on how effectively a company turns investments and operations into earnings. Profitability analysis also assists in determining whether a company is above or below industry standards (Perusahaan, 2011). Companies with strong profitability often exhibit effective cost management and strategic decision-making, resulting in higher returns and market confidence.

6. Investment Ratios

Investment ratios are used to evaluate the performance and attractiveness of investments. These ratios measure the return generated from invested capital and guide decision-makers in choosing the most efficient investment options (Rao, 2005; Kartono, 2019). Examples of investment ratios include Return on Investment (ROI), Net Present Value (NPV), and Internal Rate of Return (IRR). These ratios are commonly used to assess the effectiveness of corporate investments and whether they align with long-term financial goals. By evaluating investment outcomes, companies can optimize capital allocation and ensure that projects contribute positively to shareholder wealth.

7. Summary of Previous Research

To contextualize this literature review, previous studies have been compared in terms of scope, variables used, and methodology. For instance (Nuriasari, 2018). found a significant effect of liquidity ratios on financial performance, while (Handayani & Handayani, 2022) confirmed the relevance of liquidity metrics in evaluating BUMN firms. However, these studies employed quantitative methods, whereas this review adopts a qualitative synthesis approach. Similarly, research by (Tjandra (2022), Shintia & Novi (2017) analyzed solvency ratios using specific debt metrics. This literature review, however, provides a broader conceptual framework, offering theoretical grounding for multiple financial ratio categories in one unified study.

METHODOLOGY

This study adopts a qualitative research approach utilizing a literature review (library research) method. The aim is to explore and synthesize existing theoretical frameworks and empirical findings concerning the influence of financial ratios on corporate financial performance. This method is appropriate for identifying patterns, gaps, and theoretical linkages among key variables, based on comprehensive examination of scholarly literature, books, academic journals, and reputable digital sources. The data used in this study were collected through secondary sources, including peer-reviewed journal articles, textbooks, and official publications accessed through online academic databases such as Google Scholar, Mendeley, ScienceDirect, and other digital journal repositories. Additionally, physical resources from university libraries were used to ensure a comprehensive and balanced review of the literature.

According to Creswell (2008), qualitative research is a method of inquiry aimed at exploring and understanding a central phenomenon through non-numeric data, often presented in descriptive or interpretative formats. The qualitative method is particularly useful in this context, as it allows for an in-depth understanding of the theoretical constructs and relationships among variables such as liquidity, solvency, activity, profitability, and investment ratios and their effects on financial statement performance. The rationale for employing a qualitative literature review lies in its ability to capture the complexity and multidimensionality of financial performance within organizations. Financial statement analysis involves diverse stakeholders and operational contexts; thus, a qualitative synthesis facilitates a broader interpretation of how financial ratios are understood and applied in various organizational settings. Through the application of qualitative content analysis, this study identifies, organizes, and discusses findings from prior research to develop a conceptual framework for understanding the interdependence between financial ratio indicators and the effectiveness of financial reporting. The findings are expected to inform future empirical studies and offer theoretical foundations for hypothesis development.

RESULTS AND DISCUSSION

Based on the theoretical framework and prior relevant studies, this discussion section explores the influence of key financial ratios on the performance of corporate financial statements, within the concentration of financial management.

Liquidity Ratios and Financial Performance

Liquidity ratios represent a firm's capacity to meet short-term obligations by utilizing liquid assets. Key measures such as the current ratio, quick ratio, and cash ratio are used to assess how efficiently a company can convert its assets into cash to satisfy liabilities. High liquidity ratios typically indicate strong financial health and are positively associated with enhanced financial performance, as they suggest the organization can meet its short-term financial commitments (Nuriasari, 2018). Financial performance is frequently assessed through financial statements, including the balance sheet, income statement, and cash flow statement. Liquidity management is essential in ensuring smooth operational activities and mitigating insolvency risks (Handayani & Handayani, 2022). However, excessively high liquidity might indicate underutilized assets, while low liquidity may reflect a company's potential inability to meet liabilities, thereby impairing profitability. A good liquidity position attracts investors and creditors and enhances the firm's valuation. Hence, the liquidity ratio is a fundamental indicator in strategic decision-making, allowing companies to evaluate asset utilization and liability structures to maintain or improve financial performance (Lumenta & Worang, 2019).

Solvency Ratios and Financial Performance

Solvency ratios, such as the debt-to-equity ratio and the debt-to-asset ratio, evaluate a company's long-term financial stability and its capacity to fulfill long-term obligations. A high solvency ratio may imply excessive reliance on debt financing, increasing financial risk, while a lower ratio indicates a strong equity base and financial independence (Tjandra, 2022). Solvency analysis helps stakeholders understand how much of the firm's capital structure is composed of debt and how much is covered by internal financing. These metrics also measure how well a firm can manage its debt obligations and the sustainability of its capital structure. Consequently, solvency ratios are crucial in assessing the firm's creditworthiness and long-term financial performance (Shintia & Novi, 2017).

Activity Ratios and Financial Performance

Activity ratios measure how efficiently a company utilizes its assets to generate revenue. Key indicators include inventory turnover, receivable turnover, and total asset turnover. These ratios are highly sensitive to changes in sales volumes and asset levels. For instance, higher inventory turnover implies effective inventory management, whereas lower asset turnover may suggest underutilization of resources. Based on PT. Bata Tbk's financial data from 2013–2016, significant fluctuations were observed in activity ratios, impacting profitability trends. While inventory turnover remained relatively stable, total asset turnover declined, indicating reduced efficiency in asset utilization. Overall, positive activity ratio trends correlate with better operational and financial outcomes, guiding managerial strategies for asset optimization.

Profitability Ratios and Financial Performance

Profitability ratios assess a firm's ability to generate profit relative to its revenues, assets, or equity. Common metrics include return on assets (ROA), return on equity (ROE), and net profit margin. High profitability ratios reflect effective cost management and strong revenue generation, positively influencing investor perceptions and stock performance (Internasional et al., 2021). Profitability also determines a firm's internal financing capacity for future investments and operational expansion. It is a key determinant of firm value, influencing investor decisions and capital market responses. Thus, maintaining robust profitability ratios is essential for financial sustainability and competitive positioning (Bank & KC, n.d).

Investment Ratios and Financial Performance

Investment ratios evaluate the effectiveness of capital investments, helping firms determine if returns justify the costs. Key measures include Return on Investment (ROI), Net Present Value (NPV), and Internal Rate of Return (IRR). High investment ratios indicate successful capital allocation and potential for enhanced future earnings (Kartono, 2019). Investment ratios also serve as tools to measure and mitigate financial risks. When appropriately applied, they guide firms in selecting profitable projects and avoiding inefficient capital allocation. However, investment ratios must be interpreted alongside

operational, managerial, and market factors to derive a comprehensive view of performance (Mulyani, 2013).

CONCLUSION

This study synthesizes findings from theoretical and empirical literature to evaluate the impact of key financial ratios Liquidity, Solvency, Activity, Profitability, and Investment on corporate financial performance. The analysis reveals that:

1. Liquidity ratios are essential in ensuring that companies maintain sufficient short-term assets to meet immediate obligations, thereby contributing to overall financial stability and operational efficiency.
2. Solvency ratios provide insights into a firm's long-term financial sustainability by indicating the balance between debt and equity financing. These ratios are critical for assessing financial risk and creditworthiness.
3. Activity ratios highlight the efficiency of asset utilization in generating revenue. They reflect the effectiveness of management strategies in optimizing operational processes.
4. Profitability ratios demonstrate a firm's ability to generate earnings from its operations and are vital indicators of financial success, shareholder value, and investment attractiveness.
5. Investment ratios evaluate the returns generated from capital allocations. They serve as a measure of strategic investment effectiveness and are useful for future planning and performance forecasting.

Overall, financial ratios serve as comprehensive diagnostic tools for assessing various dimensions of corporate performance. The integration of these indicators allows firms to make informed financial decisions and enhance their competitive positioning in dynamic market environments.

Based on the findings and analysis, the following recommendations are proposed:

1. Strategic Ratio Monitoring: Companies should regularly monitor and analyze financial ratios as part of their strategic management and financial planning processes. Integrating ratio analysis into routine performance reviews will help identify inefficiencies and areas for improvement.
2. Balanced Capital Structure: Firms should aim to maintain a healthy balance between debt and equity to optimize solvency ratios. Excessive debt can increase financial risk, while a conservative approach may limit growth opportunities.
3. Operational Efficiency: Improving inventory management and asset turnover can significantly enhance activity ratios. Firms should invest in technology and process improvements that facilitate efficient resource utilization.
4. Profit Maximization Strategy: Management should prioritize cost control and revenue enhancement initiatives to sustain high profitability ratios. Benchmarking against industry leaders can provide insights into best practices.
5. Investment Appraisal: Before committing capital, companies should employ rigorous investment appraisal techniques such as ROI, NPV, and IRR to ensure that investments align with strategic objectives and yield favorable returns.
6. Holistic Financial Evaluation: While individual ratios provide valuable insights, decision-makers should adopt a comprehensive approach by evaluating financial ratios in conjunction with qualitative factors such as market trends, management competency, and regulatory developments.

Future research may extend this study by incorporating sector-specific analysis, macroeconomic indicators, and case studies to validate and enrich the understanding of financial ratio implications on firm performance.

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