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THE BUSINESS ENCYCLOPEDIA

Your guide to
General Business
Terminologies

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BUSINESS TERMINOLOGIES

Here are some of the key terms you would need to know and understand in business. When I first started I used some of these words interchangeably and had all my facts and figures wrong. The good news is you don't have to!

I have put this together with straightforward examples for you to understand and use to assess your business.

TERM	DEFINITION	EXAMPLE
REVENUE	The income generated from normal business operations, typically from the sale of goods and services.	A retail store makes $1 million in revenue from selling clothes over a year
NET PROFIT	The total profit of a company after all expenses and taxes have been deducted from total revenue.	A company earns $2 million in revenue, incurs $1.5 million in expenses, resulting in a net income of $500,000
PROFIT MARGIN	The percentage of revenue that exceeds the costs of production. It's an indicator of a company's profitability.	If a product sells for $50 and costs $30 to produce, the profit margin is 40%
ROI (RETURN ON INVESTMENT)	A measure of the profitability of an investment, calculated as the ratio of net profit to the original investment cost.	If a company invests $100,000 in a marketing campaign and generates $150,000 in additional revenue, the ROI is 50%.
CASH FLOW	The total amount of money being transferred into and out of a business, especially as affecting liquidity.	A company has $500,000 in sales revenue and $300,000 in expenses, resulting in a positive cash flow of $200,000.
MARKET SHARE	The portion of a market controlled by a particular company or product.	If a smartphone company sells 25 million units in a market of 100 million units, it has a 25% market share.

TERM	DEFINITION	EXAMPLE
SUPPLY CHAIN	The network between a company and its suppliers to produce and distribute a specific product to the final buyer.	The supply chain for a car manufacturer includes suppliers of raw materials, parts manufacturers, and dealerships.
EQUITY	The value of shares issued by a company, representing ownership interest.	If a company's total assets are worth $1 million and its liabilities amount to $400,000, the equity is $600,000.
LIABILITY	A company's legal financial debts or obligations that arise during business operations.	Loans, accounts payable, and mortgages are common liabilities.
ASSETS	Resources owned by a company that have economic value.	Buildings, machinery, patents, and cash are all assets
BREAK-EVEN POINT	The point at which total revenue equals total costs, resulting in no net loss or gain.	A business needs to sell 10,000 units of its product at $10 each to cover its fixed and variable costs, thus breaking even at $100,000.
SCALABILITY	The ability of a business to grow and manage increased demand.	A software company that can serve millions of users without degrading performance demonstrates high scalability.

TERM	DEFINITION	EXAMPLE
BRAND EQUITY	**The value a brand adds to a product or service based on consumer perception.**	**A well-known luxury car brand like Mercedes-Benz has high brand equity compared to lesser-known brands.**
DEPRECIATION	The reduction in value of an asset over time, due to wear and tear	A company buys machinery for $100,000 and depreciates it over 10 years, recognizing $10,000 as an annual depreciation expense.
INVENTORY TURNOVER	A measure of how many times inventory is sold and replaced over a period.	If a company has an annual cost of goods sold (COGS) of $500,000 and average inventory of $100,000, the inventory turnover is 5.
KPI (KEY PERFORMANCE INDICATOR)	**A measurable value that demonstrates how effectively a company is achieving key business objectives.**	**Monthly sales growth, customer acquisition cost, and employee turnover rate are common KPIs.**
MARKET SEGMENTATION	The process of dividing a market into distinct groups of buyers with different needs or behaviors.	A clothing retailer segments its market by age, offering different product lines for teenagers, young adults, and seniors.
ECONOMIES OF SCALE	The cost advantage that arises with increased output of a product.	A factory that produces large quantities of a single product can reduce costs per unit through bulk purchasing of materials.

TERM	DEFINITION	EXAMPLE
ACCOUNTS PAYABLE (AP)	Money owed by a company to its creditors.	A company needs to pay its supplier for raw materials received. The amount owed is recorded as accounts payable.
ACCOUNTS RECEIVABLE (AR)	Money owed to a company by its customers.	A company sells goods to a customer on credit. The amount the customer owes is recorded as accounts receivable.
BRAND EQUITY	The value that a brand adds to a product.	Apple has high brand equity, allowing it to charge premium prices for its products.
DIVIDEND	A portion of a company's earnings distributed to shareholders.	A company earning profits may decide to pay a dividend of $2 per share to its shareholders.
GROSS DOMESTIC PRODUCT (GDP)	The total value of all goods and services produced within a country during a specific period.	The GDP of the United States in 2020 was approximately $21 trillion.
INITIAL PUBLIC OFFERING (IPO)	The first time a company offers its stock for public sale.	When Facebook went public in 2012, it was an IPO.

TERM	DEFINITION	EXAMPLE
TARGET MARKET	**A particular group of consumers identified as the recipients of a specific marketing campaign or product.**	**A company launching a new line of eco-friendly products may target environmentally conscious consumers.**
WORKING CAPITAL	The difference between a company's current assets and current liabilities.	If a company has $200,000 in current assets and $150,000 in current liabilities, its working capital is $50,000.
INCOME STATEMENT	A financial statement that shows a company's revenue and expenses over a specific period, typically a fiscal quarter or year.	It indicates how the revenue is transformed into the net income or net profit.
MARKET CAPITALIZATION (MARKET CAP)	The total market value of a company's outstanding shares of stock.	If a company has 1 million shares outstanding, and each share is worth $50, the market cap is $50 million.
LIQUIDITY	The ease with which an asset can be converted into cash without affecting its market price.	Cash is the most liquid asset, while real estate is less liquid.
CAPITAL EXPENDITURE (CAPEX)	Funds used by a company to acquire, upgrade, and maintain physical assets such as property, industrial buildings, or equipment.	Spending $1 million on new machinery for a factory.

OPERATING EXPENSE (OPEX)	The ongoing costs for running a product, business, or system.	Rent, utilities, payroll, and insurance are common operating expenses.
AMORTIZATION	The gradual write-off of the initial cost of an intangible asset over a period.	The cost of a patent being expensed over its useful life.
BENCHMARKING	Comparing business processes and performance metrics to industry bests and best practices from other companies.	A company may benchmark its customer service performance against the industry leader.

SOME PROFIT & LOSS/INCOME STATEMENT TERMINOLOGIES

TERM	DEFINITION	EXAMPLE
COST OF GOODS SOLD (COGS)	The direct costs attributable to the production of the goods sold by a company.	If the company spends $20,000 on raw materials and labor to produce the goods sold, the COGS is $20,000.
OPERATING PROFIT (OPERATING INCOME)	The profit earned from the core business operations, excluding deductions of interest and taxes.	Operating Profit = Gross Profit - Operating Expenses If the gross profit is $30,000 and the operating expenses are $15,000, the operating profit is $15,000.
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION, AND AMORTIZATION (EBITDA)	A measure of a company's overall financial performance and is used as an alternative to net income in some circumstances.	EBITDA = Operating Profit + Depreciation + Amortization If the operating profit is $15,000, depreciation is $1,000, and amortization is $500, the EBITDA is $16,500.
INTEREST EXPENSE	The cost incurred by an entity for borrowed funds.	If a company has a loan on which it pays $2,000 in interest annually, the interest expense is $2,000.
TAX EXPENSE	The amount of expense that a business recognizes in an accounting period for the government tax related to its taxable profit.	If the taxable profit is $13,000 and the tax rate is 10%, the tax expense is $1,300.
NON-OPERATING INCOME/EXPENSES	Revenues and expenses that are not related to the core operations of the business, such as income from investments or loss from the sale of assets.	If a company earns $2,000 from the sale of an old machine, this amount is considered non-operating income.
RETAINED EARNINGS	The portion of net income which is retained by the corporation rather than distributed to its owners as dividends.	If a company has a net profit of $12,000 and decides to pay $2,000 as dividends, the retained earnings will be $10,000.

SOME BALANCE SHEET TERMINOLOGIES

CURRENT ASSETS	**Assets that can be converted into cash or used with a year**	**Cash, accounts receivables, inventory, pre-paid expenses**
NON-CURRENT ASSETS	Assets that are expected to provide economic benefits for more than one year	Property, plant, equipment, long term investments etc
CURRENT LIABILITIES	Debts/obligation that companies are expected to pay within a year	Accounts payable, short- term loans, accrued expenses
NON-CURRENT LIABILITIES	Debts/obligations that are to be settled in more than a year	Long term loan, bonds, payable
INTANGLE ASSETS	Non-physical assets that have economic value	Patents, trademarks, goodwill.

BUSINESS TERMINOLOGIES (Ratios)

Below is a list of some key business terminologies, their meanings, formulas and examples!

PROFITABILITY RATIOS – These tell you the company's ability to generate profit

TERM	MEANING/FORMULA	EXAMPLE
GROSS PROFIT MARGIN	**Measures the proportion of revenue that exceeds the cost of goods sold (COGS).** **(Revenue - COGS) / Revenue**	**If a company has $1,000,000 in revenue and $600,000 in COGS, the gross profit margin is 40%** **[($1,000,000 - $600,000) / $1,000,000]**
OPERATING PROFIT MARGIN	**Measures the proportion of revenue that remains after paying for variable costs of production.** **Operating Income / Revenue**	If a company has $1,000,000 in revenue and $700,000 in operating expenses, the operating profit margin is 30% **($300,000 / $1,000,000).**
NET PROFIT MARGIN	**Measures the proportion of profit a company makes for every dollar of revenue.** **Net Income / Revenue**	If a company has $1,000,000 in revenue and $200,000 in net income, the net profit margin is 20%. **($200,000 / $1,000,000).**
RETURN ON ASSETS (ROA)	**Measures how efficiently a company uses its assets to generate profit.** **Net Income / Total Assets**	If a company has $200,000 in net income and $1,000,000 in total assets, the ROA is 20% **($200,000 / $1,000,000).**
RETURN ON EQUITY (ROE)	**Measures the return generated on shareholders' equity.** **Net Income / Shareholders' Equity**	If a company has $200,000 in net income and $500,000 in shareholders' equity, the ROE is 40%. **($200,000 / $500,000).**

LIQUIDITY RATIOS – These tell you the company's ability to meet its short term obligation (bills)

TERM	MEANING/FORMULA	EXAMPLE
CURRENT RATIO	**Measures a company's ability to pay short-term obligations with its current assets.** **Current Assets / Current Liabilities**	**If a company has $500,000 in current assets and $250,000 in current liabilities, the current ratio is 2.0:** **($500,000 / $250,000).**
QUICK RATIO (ACID-TEST RATIO)	Measures a company's ability to meet short-term obligations with its most liquid assets. **(Current Assets - Inventory) / Current Liabilities**	If a company has $500,000 in current assets, $100,000 in inventory, and $250,000 in current liabilities, the quick ratio is 1.6: **[($500,000 - $100,000) / $250,000].**
CASH RATIO	Measures a company's ability to pay off short-term debt with cash and cash equivalents. **Cash and Cash Equivalents / Current Liabilities**	If a company has $200,000 in cash and cash equivalents and $250,000 in current liabilities, the cash ratio is 0.8. **($200,000 / $250,000).**

SOLVENCY RATIOS – These tell you the company's ability to meet long term obligations (debts)

TERM	MEANING/FORMULA	EXAMPLE
DEBT TO EQUITY RATIO	Measures a company's financial leverage and the proportion of debt used to finance assets relative to equity. **Total Debt / Total Equity**	**If a company has $1,000,000 in total debt and $500,000 in total equity, the debt to equity ratio is 2.0** **($1,000,000 / $500,000)**
DEBT RATIO	Indicates the proportion of a company's assets that are financed by debt. **Total Debt / Total Assets**	If a company has $1,000,000 in total debt and $2,000,000 in total assets, the debt ratio is 0.5 **($1,000,000 / $2,000,000)**
INTEREST COVERAGE RATIO	Measures a company's ability to pay interest on its debt. **Earnings Before Interest and Taxes (EBIT) / Interest Expense**	If a company has an EBIT of $300,000 and an interest expense of $50,000, the interest coverage ratio is 6.0 **($300,000 / $50,000)**

MARKET VALUE RATIOS – these tell you the measure stock prices

TERM	MEANING/FORMULA	EXAMPLE
EARNINGS PER SHARE (EPS)	**Measures the portion of a company's profit allocated to each outstanding share of common stock.** **Net Income / Average Outstanding Shares**	**If a company has $200,000 in net income and 50,000 outstanding shares, the EPS is $4.00** **($200,000 / 50,000)**
PRICE TO EARNINGS (P/E) RATIO	Measures a company's current share price relative to its per-share earnings. **Market Price per Share / Earnings per Share (EPS)**	If a company's share price is $40 and its EPS is $4.00, the P/E ratio is 10 **($40 / $4.00)**
DIVIDEND YIELD	Measures the dividend income per share relative to the share price. **Annual Dividends per Share / Market Price per Share**	If a company pays an annual dividend of $2.00 per share and the share price is $40, the dividend yield is 5% **($2.00 / $40)**
RETURN ON INVESTMENT (ROI)	Measures the gain or loss generated on an investment relative to its cost. **(Net Profit / Cost of Investment) x 100**	If an investment cost $10,000 and the net profit is $2,000, the ROI is 20% **[($2,000 / $10,000) x 100]**

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