BUSN3049 Corporate Finance
Tutorial 9

1. Your portfolio is 200 shares of Callahan, Inc. The stock currently sells for \$93 per share. the company has announced a dividend of \$1.43 per share with an ex-dividend date of April 19. Assuming no taxes, how much will your stock be worth on April 19?

   Answer

   With no taxes we would expect the share price to drop by exactly the amount of the dividend, so the new share price will be

   $$P_{New} = 93 - 1.43 = 91.57$$

   Your total share investment will be worth

   $$V_{New} = 200 \times 91.57 = 18,314$$

2. The balance sheet for Tempest, Inc., is shown here in market value terms. There are 19,000 shares of stock outstanding.

   Market Value Balance Sheet (\$)

Cash	120,000		
Fixed Assets	476,600	Equity	596,600
Total	**596,600**		**596,600**

   The company has declared a dividend of \$1.15 per share. The stock goes ex dividend tomorrow. Ignoring any tax effects, what is the stock selling for today? What will it sell for tomorrow? What will the balance sheet look like after dividends are paid?

   Answer

   The share price is the total market value of equity divided by the shares outstanding, so

   $$P_0 = \frac{596,600}{19,000} = 31.40$$

   per share.

   Ignoring tax effects, the share price will drop by the amount of the dividend, so

   $$P_1 = 31.40 - 1.15 = 30.25$$

   The total dividends paid will be

   $$1.15(19,000) = 21,850.$$

   The equity and cash accounts will both decline by \$21,850. The new statement of financial position will be

Market Value Balance Sheet ($)			
Cash	98,150		
Non-current Assets	476,600	Equity	574,750
Total	**574,750**		**574,750**

3. Taco Time Corporation is evaluating an extra dividend versus a share purchase. In either case, $7,095 would be spent. Current earnings are $2.70 per share, and the stock currently sells for $59 per share. There are 4,300 shares outstanding. Ignoring the taxes and other imperfections, evaluate the two alternatives in terms of the effect on the price per share of the stock and shareholder wealth.

   Answer

   If the company makes a dividend payment, we can calculate the wealth of a shareholder as

   $$Dividend\ per\ Sahre = \frac{7,095}{4,300} = 1.65$$

   The share price after the dividend payment will be

   $$P_X = 59 - 1.65 = 57,35$$

   The shareholder will have a share worth $57.35 and a $1.65 dividend for a total wealth of $59. If the company makes a repurchase, the company will repurchase

   $$Shares\ Repurchased = \frac{7,095}{59} = 120.25$$

   share.

   If the shareholder lets their shares be repurchased, they will have $59 in cash. If the shareholder keeps their shares, they're still worth $59.