Tutorial 6

#1:
A substantial percentage of the companies listed on the NYSE and NASDAQ don't pay dividends, but investors are nonetheless willing to buy shares in them. How is this possible?

#2:
Suppose a company has a preferred stock issue and a common stock issue. Both have just paid a $2 dividend. Which do you think will have a higher price, a share of the preferred or a share of the common?

#3:
The Jackson-Timberlake Wardrobe Co. just paid a dividend of $1.95 per share on its stock. The dividends are expected to grow at a constant rate of 6 percent per year, indefinitely. If investors require an 11 percent return on The Jackson-Timberlake Wardrobe Co. stock, what is the current price? What will the price be in three years? In 15 years?

#4:
Great Pumpkin Farms (GPF) just paid a dividend of $3.50 on its stock. The growth rate in dividends is expected to be a constant 5 percent per year, indefinitely. Investors require a 14% return on the stock for the first three years, a 12 percent return for the next three years, and then a 10 percent return thereafter. What is the current share price?

#5:
Far Side Corporation is expected to pay the following dividends over the next four years: $11, $8, $5, and $2. Afterwards, the company pledges to maintain a constant 5 percent growth rate in dividends, forever. If the required return on the stock is 12 percent, what is the current share price?

#6:
Antiques R Us is a manufacturing firm. The company just paid a $10.46 dividend, but management expects to reduce the payout by 4 percent per year indefinitely. If you require an 11.5 percent return on this stock, what will you pay for a share today?

#7:
Consider four different stocks, all of which have a required return of 19 percent and a most recent dividend of $4.50 per share. Stocks W, X, and Y are expected to maintain constant growth rates in dividends for the foreseeable future of 10 percent, 0 percent, and -5 percent per year, respectively. Stock Z is a growth stock that will increase its dividend by 20 percent for the next two years and then maintain a constant 12 percent growth rate, thereafter. What is the dividend yield for each of these four stocks? What is the expected capital gains yield? Discuss the relationship among the various returns that you find for each of these stocks.

#8:
The risk-free rate is an annual rate of 6 percent, and the market return is an annual rate of 12 percent. Stock A is expected to generate a constant dividend of $5.20 per share. A toxic spill results in a lawsuit and potential fines, and the beta of the stock increases by 25%. Consequently, the equilibrium price of the stock falls by 12%. Assume that dividends remain unchanged, what is the new equilibrium price of the Stock A?