Universidad de Barcelona

3rd course: Financial Management ***Professor: Altina Sebastián González***

Exercises 2: External Equity Financing

1. Which of the following characteristics is proper of a preferred share:
   a. It pays a dividend set at the discretion of the Corporation Board and approved by the General Assembly
   b. It has voting rights
   c. It is entitled to receive a fixed dividend payment
   d. Its missed out payment dividends can never be carried forward

2. Sunny shares have a par value of $1, an issue price of $5 and a market value of $4. The company paid a dividend of $.20/share. Calculate the surplus and the dividend yield of Sunny shares.
   a. Surplus =$3; dividend return = 5%
   b. Surplus =$4; dividend return = 5%
   c. Surplus =$3; dividend return = 4%
   d. None of the previous answers is correct

3. With the information of the following table, fill in the blank spaces

Confort Plus

Share Price	30 €
eps	?
Total Outstanding shares	250.000
Total earnings	500.000 €
PER	?

   a. eps = 2€; PER = 6,67%
   b. eps = 2€; PER = 15
   c. We need more information
   d. None of the previous answers is correct

4. The Confort Plus charter sets in 1.000.000 the authorized shares. Calculate how many shares can Confort Plus issue without changing its charter as well as the present market value (MV) of the company.
   a. 750.000 new shares and MV = 30.000.000€
   b. 750.000 new shares and MV = 7.500.000€
   c. 1.000.000 new shares and MV = 7.500.000€
   d. None of the previous answers is correct

5. Company X has a P/E ratio of 10 and a stock price of $50 per share. Calculate earnings per share of the company.
   a. $6 per share
   b. $10 per share
   c. $0.20 per share
   d. $5 per share

6. The share price of Cookie Factory was $200. To increase the share liquidity, the Company has just announced a 5-for-1 stock split. What was the effect of this measure for a shareholder with 1.000 shares?
   a. After the split the shareholder had 5.000 shares with a value of $1.000.000
   b. After the split the shareholder had 5.000 shares with a value of $200.000
   c. After the split the shareholder had 5.000 shares with a value of $1.000.000
   d. None of the previous answers is correct

7. The valuation of a common stock today primarily depends on
   a. the number of shares outstanding and the number of its shareholders
   b. its expected future dividends and its discount rate
   c. Wall Street analysts
   d. the price to earnings ratio

8. Casino Inc. expects to pay a dividend of $3 per share at the end of year 1 (Div1) and these dividends are expected to grow at a constant rate of 6 percent per year forever. If the required rate of return on the stock is 18 percent, what is the current value of the stock today?
   a. $25
   b. $50
   c. $100
   d. $54

$$\frac{3}{0.18 - 0.06} = 25 \$$$

9. Super Computer Company's stock is selling for $100 per share today. It is expected that, at the end of one year, it will pay a dividend of $6 per share and then be sold for $114 per share. Calculate the expected rate of return for the shareholders.
   a. 20 percent
   b. 15 percent
   c. 10 percent
   d. 25 percent

<u>TOTAL SHAREHOLDER RETURN</u>

10. The dividend yield reported on finance.yahoo.com is calculated as follows:
   a. (dividend/year-high stock price)
   b. (dividend/year-low stock price)
   c. (dividend/closing stock price)
   d. <u>(dividends/earnings)</u> → PAY-OUT RATIO

11. A rights issue is also called a(an)
   a. private placement
   b. shelf registration
   c. initial public offering (IPO)
   d. privileged subscription

12. A Wall Street Journal quotation for a company has the following values: Div: $1.12, P/E: 18.3, Close: $37.22. Calculate the approximate dividend payout ratio for the company.
   a. 18 percent
   b. 35 percent
   c. 45 percent
   d. 55 percent

$$18.3 = \frac{37.22}{EPS} \rightarrow \frac{1.12}{2.0339} = \underline{55\%}$$

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13. Assume General Electric (GE) has about 10.3 billion shares outstanding and the stock price is \$37.10. Also, assume the P/E ratio is about 18.3. Calculate the approximate market capitalization for GE.
    a. \$679 billion
    b. \$188 billion
    c. \$382 billion
    d. \$103 billion

14. One can estimate the expected rate of return or the cost of equity capital as
    a. Dividend yield - expected rate of growth in dividends
    b. Dividend yield + expected rate of growth in dividends
    c. Dividend yield/expected rate of growth in dividends
    d. (dividend yield) × (expected rate of growth in dividends)

15. CK Company stockholders expect to receive a year-end dividend of \$5 per share and then immediately sell their shares for \$115 dollars per share. If the required rate of return for the stock is 20 percent, what is the current value of the stock?
    a. \$132
    b. \$122
    c. \$100
    d. \$110

PROBLEMS:

1. Associated Breweries is planning to market alcohol-free beer. To finance the venture it proposes to make a rights issue at \$20 of one new share for each five shares held (the company currently has outstanding 100.000 shares priced at \$23 a share). Assuming that the new money is invested to earn a fair return, give values for the following:
    a. Number of new shares
    b. Amount of new investment
    c. Total number of shares after the issue
    d. Stock price after the issue
    e. Total value of the company after the issue
    f. The rights issue will give the shareholder the opportunity to buy one new share for less than the market price. What is the value of this opportunity?

2. **Yubalooe Corp. is issuing some new shares.**

You own a 15% of Yubalooe's equity. You are given 1 PSR per share owned and its price is \$0,35.
Data:
Number of outstanding shares = 1.000.000
Market value of an outstanding share = 15,00 \$
Number of shares issued = 200.000
Market value of a new share = 12,00 \$

a. As a current shareholder, are you happy with the PSR price?

b. Which should be the correct PSR price?
c. How many PSR will anyone need to subscribe a new share?
d. How many PSRs should you sell to subscribe some new shares without additional spending ("OPÉRATION BLANCHE")?

PROBLEM SET 2

1

a) $100.000 / 5 = 20.000$ NEW SHARES

b) 20.000 SHARES $\times$ $20\$ = 400.000\$$
MONEY RAISED

c) 120.000 SHARES

d) $$\frac{(100.000 \times 23) + (20.000 \times 20)}{120.000} = 22.5\$$$

e) $2.300.000\$ + 400.000\$ = 2.700.000\$$

f) $23\$ - 22.5\$ = 0.5\$$ → PSR THEORETICAL VALUE

2

a) IF $0.35\$ >$ THEORETICAL VALUE

IF $0.35\$ <$ THEORETICAL VALUE

SINCE THE PSR = $0.5\$$, THE SHAREHOLDER IS UNHAPPY.