

2) Rate of Return on Assets = (Net Income + Interest Expense) ÷ Average Total Assets

Shows how profitably a company has used its assets.

Example: Net Income for the year is \$111,300, Interest Expense is \$19,500, Total Assets on December 31, 1999 was \$675,000, and Total Assets on December 31, 2000 was \$750,000.

$$\begin{aligned}\text{Rate of Return on Assets} &= (\$111,300 + 19,500) / [(675,000 + 750,000) / 2] \\ &= 130,800 / [1,425,000 / 2] \\ &= 130,800 / 712,500 \\ &= 0.1836 \\ &= 18.36\%\end{aligned}$$

3) Rate of Return on Common Stockholders Equity = (Net Income - Preferred Dividends) ÷ (Average Common Stockholders Equity)

Shows how much income was earned with the common stockholder's investment.

Example: Net Income for the year is \$111,300, there are 25,000 shares of 5% Preferred Stock (par value \$10) outstanding, Common Stockholder's Equity on December 31, 1999 is \$514,000, and Common Stockholder's Equity on December 31, 2000 is \$530,000.

First the Preferred Dividends must be calculated:

$$25,000 \text{ shares} * \$10 \text{ par value} * 5\% = \$12,500$$

Now the Rate of Return can be calculated:

$$\begin{aligned}\text{Rate of Return on CS Equity} &= (\$111,300 - 12,500) / [(514,000 + 530,000) / 2] \\ &= 98,800 / (1,044,000 / 2) \\ &= 98,800 / 522,000 \\ &= 0.1893 \\ &= 18.93\%\end{aligned}$$

4) Earnings per Share of Common Stock = (Net Income - Preferred Dividends) ÷ number of shares of common stock outstanding

The net income per one share of common stock.

Example: Using the same information as in the previous example and the fact that there are 265,000 shares of common stock outstanding.

$$\begin{aligned}\text{Earnings per Share of Common Stock} &= (\$111,300 - 12,500) / 265,000 \\ &= 98,800 / 265,000 \\ &= \$0.37\end{aligned}$$