FIN 220 Major 2 solutions

20 Pharmacy made two announcements concerning their common stock today. First, the company announced the next annual dividend will be $1.48 a share. Secondly, all dividends after that will increase by 2.5 percent annually. What is the maximum amount you should pay to purchase a share of this stock if your goal is to earn a 12 percent rate of return?   


21.How much are you willing to pay for one share of Delphia stock if the company just paid a $1.34 annual dividend, the dividends increase by 2.8 percent annually, and you require a 14 percent rate of return?



22.The Good Life offers a common stock that pays an annual dividend of $2 a share. The company has promised to maintain a constant dividend. How much are you willing to pay for one share of this stock if you want to earn a 9 percent return on your equity investments?   


23.The common stock of BJ's Auto Clinic sells for $38.25 a share. The stock is expected to pay $1.90 per share next month when the annual dividend is distributed. BJ's has established a pattern of increasing their dividends by 2.5 percent annually and expects to continue doing so. What is the market rate of return on this stock?   


24.Home Interiors has net income of $248,000. The firm has decided to pay $160,000 of that income out to the shareholders. What is the firm's retention ratio?   
  **Retention ratio = ($248,000 - $160,000)/$248,000 = .355**

25.KB Adventures will pay an annual dividend of $3.15 a share on their common stock next week. Last year, the company paid a dividend of $3.00 a share. The company adheres to a constant rate of growth dividend policy. What will one share of this common stock be worth ten years from now if the applicable discount rate is 12.5 percent?   
  


26.Super Sounds is expecting a period of intense growth and has decided to retain more of their earnings to help finance that growth. As a result, they are going to reduce the annual dividend by 20 percent a year for the next three years. After that they will maintain a constant dividend of $1 a share. Last year, the company paid $2.25 as the annual dividend per share. What is the market value of this stock if the required rate of return is 16 percent? 



27.Lantern Corporation reported net income of $55 million for last year. Depreciation expense totaled $20 million and capital expenditures came to $5 million. Free cash flow is expected to grow at a rate of 4.5% for the foreseeable future. Lantern faces a 40% tax rate and has a 0.45 debt to equity ratio with $185 million (market value) in debt outstanding. Lantern's equity beta is 1.3, the risk-free rate is currently 5% and the market risk premium is estimated to be 6.5%. What is the current total value of Lantern's equity (in millions)? 



28.The Grand Isle has 12,000 shares of stock outstanding at a market price of $31.60 per share. The book value per share is $12.08. The firm has earnings per share of $1.86 and a dividend payout ratio of .40. What is the firm's sustainable rate of growth?   
 **Sustainable growth rate = ($1.86/$12.08) × (1 - .40) = 9.24 percent**