5. EQUITIES: ANALYSIS AND VALUATION

1. (a) A firm has just paid (the moment before valuation) a dividend of 55 cents and is expected to exhibit a growth rate of 10% into the indefinite future. If the appropriate discount rate is 14%, what is the value of the stock?

   (b) The analyst who supplied you with the information in (a) has just revised her forecast. She now realises that the growth rate of 10% can continue for only five years, after which the company will have a long-term growth rate of 6%. Furthermore at the end of five years she expects the company's payout rate to increase from its current 30% to 50%. What value would you now apply to the company?

   (c) Assume that the forecast for the company in (b) was such that at the end of the fifth year it's growth was to decline linearly for four years to reach the steady state 6% growth rate. Assume the payout ratio was constant at 30% until it is changed to 50% at the end of the ninth year. What is the value of the company?

2. Blue Boxes plc has just announced a rights issue of 2m. new shares. The pre-announcement share price was 145p and the rights issue involves the issue of one new share (for every existing three shares held) at a price of 115p.

   (a) What will be the theoretical ex rights price and the value of the 'rights'?
   (b) How much new money will be raised (before transaction costs)?
   (c) Mr Blair already holds 3,000 shares. Outline the main alternatives available to him. Can Mr Blair simply do nothing without financial loss?

3. Discuss the impact of a company issuing new shares and using the proceeds to repay a floating rate note issue on.

   (a) the market-related risk of the stock
   (b) the company's cost of capital
   (c) the dividend policy of the company