Question 5 **45**

Dividend Yield	$\frac{\text{DPS x 100}}{\text{Market Price}}$ =	$\frac{6.25c \times 100}{130c}$	=	**4.81%**	[10]
Opening stock	$\frac{\text{Cost of sales}}{\text{Average stock}}$ = 10	= $\frac{630{,}000}{10 \times \text{average stock}}$			
Average stock		= 63,000			
Opening stock		= (63,000 x 2) less 64,000	=	**€62,000**	[9]
Earnings per share	$\frac{\text{Net profit after Pref Div}}{\text{Number of ordinary shares}}$	$\frac{84{,}000 - 20{,}000}{400{,}000}$	=	**16c**	[9]
Period to recoup price	$\frac{\text{Market price}}{\text{Dividend per share}}$	= $\frac{130}{6.25c}$	=	**20.8 years**	[9]
Price/earnings ratio	$\frac{\text{Market price}}{\text{EPS}}$	= $\frac{130}{16c}$	=	**8.125 times** **8.125 years**	[8]

(b) **40**

Profitability **[8]**

Whelan Ltd is a profitable business. The return on capital employed was 10.94% in 2007 and 9% in 2006. This indicates that the firm is earning over twice the return available from risk free investments of about 5%. The profitability has improved by 1.94%.

Dividend policy **[7]**

The Dividend Per Share in 2007 is 6.25c and was 5c in 2006. This has improved by 1.25c since 2006.
The company's dividend cover in 2007 is 2.56 times but was 3 times in 2006.
A smaller percentage of the profits is retained in 2007 than in 2006.
The company is re investing ample profits for expansion purposes
The dividend yield is 4.81% in 2007 and 6% in 2006.
This yield has declined since last year but is still above the return from risk free investments of about 5%.
The real return to ordinary shareholders would be 12.30% based on available profits.
The shareholders would prefer a high dividend yield.

Liquidity [7]

The company has a liquidity problem. The quick ratio in 2006 was 1.1 to 1 but this deteriorated to 0 .7 to 1 in 2007. The company has only 70c available to pay every €1 owed in the short term.
The deterioration of the ratio indicates a difficulty in paying debts and possible future interest.
If this trend continues, ability to pay interest would come under pressure and funds would not be available for the purpose of repaying the loan.

Gearing [8]

The gearing of the company is 44.86%. [81.34%]. This is a lowly geared company and this means that the company is not dependant on outside borrowing
This would please the shareholders as it increases their chance of getting a dividend and there is little risk from outside investors.
However, the gearing has slipped from 40% of total capital in 2006.
Interest cover was 8 times but it is now down to 6.25 times. If this trend continues it could jeopardise interest payment.

Market value of shares [5]

The market value of the share in 2006 was €1.35 while in 2007 it has dropped to €1.30.
The EPS has dropped from 18c to 16c.
The share may be overpriced as it takes 8.125 years to recover its market price.
This would indicate a lack of public confidence in the company.
Shareholders would be unhappy.

Sector [5]

The long term prospects in the building materials industry are not encouraging
There has been a slow down in the construction industry which has led to unemployment and lower profits in the sector. Forecasts for the future indicate a slowing down in the sector.

Investment Policy

The investments made by the company cost €170,000.
These investments now have a market value of €160,000 - a drop in value of 5.88%.or €10,000
This indicates poor management of resources and would not please the shareholders.

(c) **15**

A rising liquidity ratio is not **always** a sign of prudent management.

A rising liquidity ratio could be a sign of prudent management because it indicates that it is easier for the firm to pay it's short term debts on time and thus avoid paying interest or enables it to avail of cash discounts.

However, if the liquidity ratio rises significantly above 1:1, it could mean that too much of the company's resources are tied up in liquid assets when they could be used to earn more profits. Management may be leaving cash resources idle.