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Earning Per Share

Basic EPS

- It is the most commonly used corporate profitabiliy performance measures for publicly-traded firms.

Basic EPS = \( \frac{\text{Net Income} - \text{Preferred Dividends}}{\text{Weighted Average Number of Shares Outstanding}} \)

Diluted EPS

- It measures the quality of a company's earning per share (EPS) if all dilutive convertible securities were exercised.

\[
\text{Diluted EPS} = \left( \frac{\text{net income} - \text{preferred dividends}}{\text{weighted average shares}} \right) + \frac{\text{convertible preferred dividends}}{\text{conversion of conv. pfd.shares}} + \frac{\text{convertible debt interest}}{\text{conversion of conv. debt}} + \frac{\text{issuable from stock options}}{(1 - \text{tax})}
\]

Calculated through Treasury Stock Method (TSM)
TSM Operation

Option Exercised → Shares Created → Fund Received → Used to Purchase Co's share @ Avg. Market Price

Net Increase in Outstanding shares

Net Issuance = Shares Created - Share purchased
Concept Checker

Suppose R&M has 100,000 stock options outstanding at the end of the year, convertible into 100 normal equity shares per option at the strike price of $25. If average market price of the stock for the entire year 2009 was $50, the basic & diluted EPS for 2009 is

A. $1.41 & $1.33
B. $1.35 & $1.44
C. $1.41 & $1.30
**Answer**

- **Preferred Dividend** = $10,000 \times 1000 \times 8\% = $0.8mn

- **Basic EPS** = \((120.5 - 0.8)mn/85mn = $1.41\)

<table>
<thead>
<tr>
<th>Diluted EPS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>New equity shares created</td>
<td>100000*100</td>
</tr>
<tr>
<td>Fund Received</td>
<td>10mn * $25</td>
</tr>
<tr>
<td>Repurchase of shares</td>
<td>$250mn/$50mn</td>
</tr>
<tr>
<td>Net shares Issued</td>
<td>10mn – 5mn</td>
</tr>
<tr>
<td>Total Outstanding shares after dilution</td>
<td>85mn+5mn</td>
</tr>
<tr>
<td><strong>Diluted EPS</strong></td>
<td>($120.5 –$0.8)mn/90mn</td>
</tr>
</tbody>
</table>