

ENGINEUITY TUTORIAL



Factors Affecting The Share Price



Factors Affecting The Share Price

The company's share price is one of the key performance indicators in measuring the success or failure of the company, with a rising share price signifying increasing industry confidence in the fortunes of the Company.

The share price is influenced by **internal factors**, related to the company's decisions :-

- The level of dividend paid to the shareholders
- Changes in the value of the company
- Changes in the future profitability of the company
- Changes in the debt burden of the Company

and **external factors (world events)**, outside of the company's control.



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Period	Status	Year/qtr	Share price			Equity		Change in share price due to influencing factors				
			Start of the period	% change	End of the period	No. of shares	Equity value	Dividend paid to s/holders	Company value changes	Forward margin changes	Gearing ratio changes	World events
1	History	2024 (Q1)	1.00	-6.80 %	0.93	5,000,000	4,650,000	0.00 %	-6.80 %	0.00 %	0.00 %	0.00 %
2	History	2024 (Q2)	0.93	14.02 %	1.06	5,000,000	5,300,000	0.00 %	-7.98 %	22.00 %	0.00 %	0.00 %
3	History	2024 (Q3)	1.06	-11.07 %	0.94	5,000,000	4,700,000	0.00 %	-6.25 %	-4.82 %	0.00 %	0.00 %
4	History	2024 (Q4)	0.94	15.61 %	1.09	5,000,000	5,450,000	0.00 %	9.83 %	7.28 %	-1.50 %	0.00 %

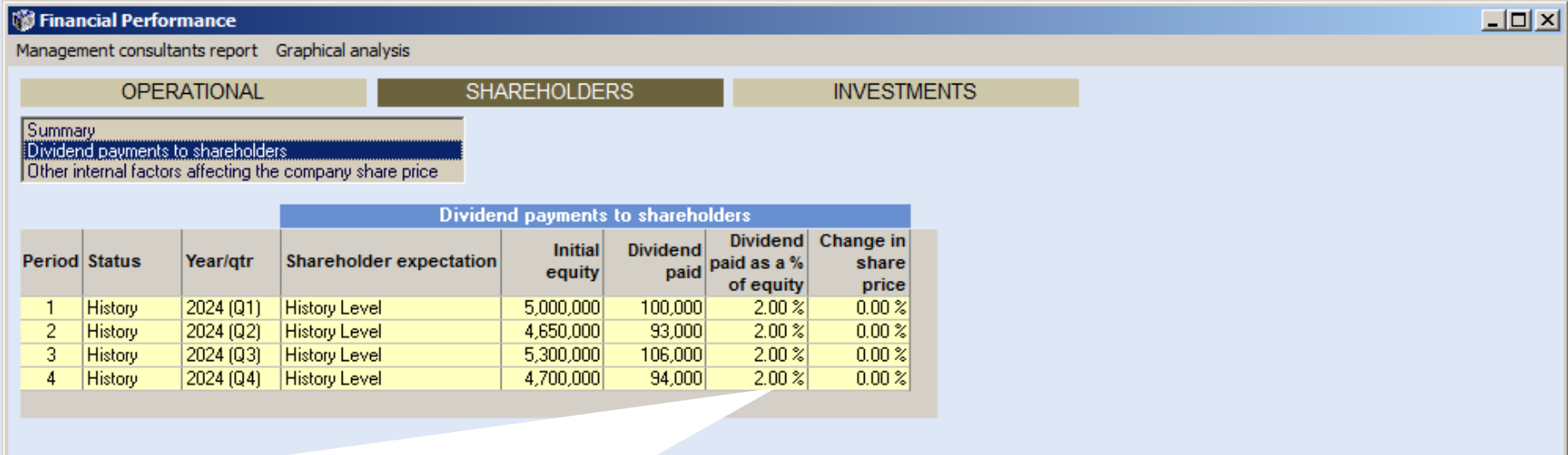
Consider the following example, where a company is in period 5.

Since period 1 the share price has fluctuated, with periods of **improvement (2 and 4)**, and periods of **deterioration (1 and 3)**.

We will now look in more detail at why this has been the case.



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DIVIDEND PAYMENTS

Dividends are taxable payments declared by a company's board of directors and given to its shareholders, normally quarterly. They provide an incentive to own stock in stable companies even if they are not experiencing much growth.

The affect on share price is determined by the **% of the company's equity** that is paid as a dividend.

The **equity** of the company at any time is the overall share value.

$$\text{EQUITY} = \text{NUMBER OF SHARES} \times \text{CURRENT SHARE PRICE}$$

There is a level of dividend, measured as a % of the equity, at which the share price **does not change**. Paying more than the 'equilibrium' level will cause the share price to rise, but paying less will be not be well received by the shareholders, and the price will fall.

Since period 1 the company has paid a dividend of 2% of equity every period (8% per annum), and this has been **sufficient to keep the shareholders content** because there has been no change in the share price.

If dividend has had little affect on the share price, what about other factors ?



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1	History	2024 (Q1)	5,000,000	-3.08 %	4,845,920	-6.80 %	0	0.00 %	0	0.00 %	0.000	0.000	0.000	0.00 %
2	History	2024 (Q2)	4,845,920	-3.79 %	4,662,431	-7.98 %	0	100.00 %	826,173	22.00 %	0.000	0.000	0.000	0.00 %
3	History	2024 (Q3)	4,662,431	-2.75 %	4,534,196	-6.25 %	826,173	-24.08 %	627,212	-4.82 %	0.000	0.000	0.000	0.00 %
4	History	2024 (Q4)	4,534,196	5.46 %	4,781,791	9.83 %	627,212	41.41 %	886,934	7.28 %	0.000	0.015	0.015	-1.50 %

COMPANY VALUE

Changes in the value of the company from period to period also affect the share price.

If the company value falls in a period, it will have a **depressing effect on share price** as shareholder and industry confidence falls. Conversely, if the value increases then confidence will improve, and the **share price will increase**.

As can be seen the during periods 1,2 and 3 the value of the company fell, with adverse affects on share price, but in period 4 the value increased with a positive affect on the share price.

Overall there was a clear **negative affect** on the share price.



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FUTURE PROFITABILITY

Another factor that affects the share price is the **changes in the future profitability** (forward margin) of the company, which is based upon the company's work in progress.

At the end of period 1, whilst the company was being established, there were no ongoing jobs, and hence no forward margin. However, during period 2, when some new work was secured, forward margin increased dramatically, falling back slightly in period 3, and increasing again in period 4.

Overall there was a clear **very positive affect** on the share price.



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GEARING RATIO

The final internal factor that affects the share price is **changes in the gearing ratio**.

The gearing ratio is the ratio of the company's liabilities (cash account overdraft) to its assets (capital base and investments, and indicates the **debt burden** of the company. If there are no liabilities, the gearing ratio is 0.

If the gearing ratio increases the company will be viewed as being vulnerable to both interest rate rises, and its ability to service its debts from its future profit flows. Consequently, this will have a **depressing effect on share price**. Conversely, if the gearing ratio decreases then the company will be viewed as being more financially sound, and the **share price will increase**.

As can be seen, the cash account was overdrawn in period 4, when the increasing gearing ratio had a **negative affect** on the share price, albeit a slight one.



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EXTERNAL FACTORS

External factors that affect the company's share price are **caused by world events** outside the control of the company's management team.

During periods 1 to 4 no external factors affected the company share price, but this could change in the future.



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IN SUMMARY

Both internal and external factors have different levels of impact upon the company share price. It may be that the share price rises even though most of the factors have negative affects, but the positive affect of one factor has the greatest impact.

Careful examination is needed of the company data to determine which factors have had which affects, and to what level :-

- During period 1 the **share price fell** because of the falling company value
- Even though company value fell further during period 2, this was more than offset by a rapidly improving forward profitability, and the **share price rose** considerably.
- During period 3 the **share price fell** due to falls in the company value and forward profitability
- During period 4 the **share price rose** due to increases in the company value and forward profitability, only offset slightly by a rise in gearing