Is free cash better than dividend per share (dps)

Technology, Information Technology

Is Free Cash Better Than Dividend per Share (DPS) Introduction A company may decide to reinvest some or all of its profits or distribute it to the shareholders. Investors are interested in businesses that have potential to generate revenue and give an assurance of growth of share value (Brigham & Daves, 2012, p. 64). Depending on how the company decides to spend it income it can attract more investors by expanding its operations or may seem unattractive to the investors if they cannot generate adequate revenue. The company may distribute profit to the shareholders either in the form of cash or dividend (Ehrhardt & Brigham, 2010). This study examines between Earnings per Share and Free Cash to determine the best investment option.

Earnings per Share

Dividend is a payment made by public corporations to the shareholders from the profits. Dividend per Share (DPS) refers to the sum or dividends of declared dividends for every ordinary share issued (Brigham & Daves, 2012). Dividends are a proportion of company's profits reported by the business to the shareholders since shareholders are owners of the company and deserve a share of company's profit. When a corporation decides to issue a dividend to the shareholders they allocate a fixed amount per share with shareholders getting a fraction of dividend proportionate to the shares, they hold (Brigham & Daves, 2012). Some corporations issue fixed sum of dividends to the shareholders and transfer the other undistributed profit amount is maintained as retained earnings. Investing in companies that issue shareholders with dividend gives the investors an opportunity to generate a steady return through income from the stock purchases (Ehrhardt &

Brigham, 2010). However, the company should examine the pay-out ratio to ensure the earnings of the company are capable of supporting the current dividend payment amount. Investing in a corporation with the dividend per share implies the shareholders have the higher chance of increasing income, but the company has a problem with managing its operations due to inadequacy of cash (Ehrhardt & Brigham, 2010)

Free Cash

Free cash flow refer to pay a firm has generated for its shareholders after deducting expenses investing in its growth. It measures the amount of cash per share a company makes after accounting for capital costs such as buildings and equipment (Westbrook, 2014, p. 111). It is equivalent to total cash flow less capital spending. It is essential in a corporation because it plans the financial health of the company and gets rid of all accounting suppositions built into earnings. It is a measure of the company's spending and is used to compare long-term spending with long-term assets. It is a way of estimating the company's spending (Westbrook, 2014, p. 111). Free Cash is available for use for various purposes such as expanding the business, paying debts, issuing dividends, etc.

Free Cash is better than earnings per share because it can make an immediate decision on how to spend the available money (Westbrook, 2014, p. 113). For example, they can use the cash to expand business operations, can use it to repurchase the stock, can invest the money in developing new products pay dividend or even repay the loan. Investors are interested in company's having better performance thus free cash is the best determinant of how company generates revenue and how it spends its income

(Westbrook, 2014, p. 112). It helps in attracting investors to the firm because they are optimistic that a corporation with good performance has the higher chance of increasing share price. On the other hand, Earnings per Share reduce the company's revenue and reduce the cash available for improving business performance (Ehrhardt & Brigham, 2010).

Bibliography

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