Acme Corporation consists of 250 grocery stores throughout the Midwest. At the beginning of 2010, its statement of net worth showed the following information: Common stock ($2 par) $800,000; capital paid in excess of par $1,400,000; and retained earnings $500,000. During the year, net income equaled $160,000. Management was undecided on what to do with the income. Acme paid an annual dividend of $.25 per share last year and the stock price is currently $14.50. Acme has a 6% growth rate in earnings and dividends, and is in the 40% tax bracket.

a) What return on investment would Acme have to earn in order to justify retaining 2010's earnings? Use the formula from Chapter 10:

$$K_e = \frac{D_1}{P_0} + g$$

b) What changes would occur in stockholder's equity if a $.15 cash dividend was paid? What if a 5% stock dividend was given and no cash dividend was paid?

c) What would EPS be before and after the stock dividend?