

CONCEPT: RATIOS – ECONOMIC RETURN FROM INVESTING

- The ***economic return from investing*** is a ratio used by investors to analyze their profits from investments.

- ☐ This ratio doesn't use the financial statements, rather the personal gains of the investor.

- A company can use this ratio to analyze their investments as well.

$$\text{Economic Return from Investing} = \frac{\text{Dividends and Interest Received} + \text{Change in Fair Value}}{\text{Fair Value of Investment at Beginning of Period}}$$

Note: This ratio is generally shown as a _____, make sure to multiply by 100!

Numerator: The numerator shows the _____ from the investment during the period

Denominator: The denominator shows the value of the investment at the beginning of the period.

Analysis: This ratio shows the amount of profit/loss per dollar invested.

- ☐ Economic returns come from two sources:

- Dividends received are known as the ***dividend yield***

- Changes in the fair value of the investment (i.e. stock price) are ***capital gains/losses***

PRACTICE: An investor bought a share of Apple common stock for a cost of \$160. During the year, Apple paid dividends of \$1 per share. At the end of the year, the stock price had increased to \$177. Calculate the economic return from investing.

- a) 10.6%
- b) 11.3%
- c) 0.106%
- d) 0.113%