

# Chapter 19

## EARNINGS PER SHARE (IAS 33)

### 1. Basic Earnings per Share

$$\text{Basic EPS} = \frac{\text{Profit attributable to ordinary shareholders of the parent}}{\text{Weighted average number of shares}}$$

If the number of shares has changed during the period the following assumptions are made regarding the weighted average number of shares:

|                         |                                                                                                                                                                               |
|-------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Full price issue</b> | Normal weighted average calculation                                                                                                                                           |
| <b>Bonus issues</b>     | Assume that the bonus shares have always been in issue (and therefore alter the comparative EPS amount)                                                                       |
| <b>Rights issue</b>     | Assume that the shares issued are a mix of bonus and full price shares. For the bonus element assume that they have always been in issue and therefore adjust the comparative |

If bonus issues or rights issues occur after the reporting date, but before the date of approval of the accounts the EPS should be calculated based on the number of shares following the issue.

#### Example 1 – Basic EPS

Ruth makes up its accounts to 30 June each year. On 1 July 20X5 Ruth has 500 million ordinary shares in issue.

Profits for the year to 30 June 20X6 were \$250m. There were no preference shares in issue.

**Calculate the basic earnings per share assuming:**

- Share capital has not changed during the year**
- An issue of 50 million new shares at full market price on 1 August 20X5.**
- A 1 for 4 bonus issue occurring on 1 November 20X5.**
- A 1 for 5 rights issue on 1 February 20X6 held at \$1.25. The price of a share immediately before the rights issue was \$1.40.**

#### Example 2 – Multiple share issues and prior year comparatives

Ernie had earnings of \$750,000 for the year-ended 31 March 2019. There were 2,000,000 \$1 equity shares in issue on 1 April 2018, and a new issue of 3,000,000 shares at full market price was carried out on 30 September 2018. A bonus issue of one new share for every two shares held was issued on 1 December 2018.

The EPS figure reported for the year-ended 31 March 2018 was 15.5c.

**Calculate the basic EPS for Ernie for the year-ended 31 March 2019, and restate the comparative figure for 31 March 2018.**



## 2. Diluted earnings per share

This is calculated where potential ordinary shares have been outstanding during the period which would cause EPS to fall if exercised (dilutive instruments).

The earnings should be adjusted by adding back any costs that will not be incurred once the dilutive instruments have been exercised. This will include for post-tax interest saved on convertible debt.

The number of shares will be adjusted to take account of the exercise of the dilutive instrument. This means that adjustment is made:

**For convertible instruments** By adding the maximum number of shares to be issued in the future

**For options** By adding the number of effectively "free" shares to be issued when the options are exercised

### Example 3 – Diluted EPS

Flanagan makes up his accounts to 31 December each year and has calculated the basic EPS based on actual shares of 1,000 million and earnings of \$500m, for the year ended 31 Dec 20X5.

Convertible debentures

On 31 December 20X6 Flanagan had in issue of \$10m of 5% convertible loan stock.

The loan stock is convertible at the following dates with the following terms:

31 Dec 20X6 125 shares for every \$100 of loan stock

31 Dec 20X7 120 shares for every \$100 of loan stock

The tax rate is 20%

Share options

Flanagan also granted 100m options at the same date. The option price is \$2.50 but the average fair value of a share is \$4.00.

**Calculate the fully diluted EPS for the year to 31 December 20X5.**

