Case Study 2

2.2.1 Kingspan plc Capital Structure, Value Creation and Dividend Policy Exercise[1]

Unit:	Study Unit 3 – Strategic Treasury Solutions
Case:	Case 2 – Treasury evolution
Date:	1 September 2016
Summary:	Questions looking at gearing and dividend policies and cost of capital issues for Kingspan.
Key words:	capital structure, gearing, shareholder value, dividend policy

Question 1

How optimal has the company's gearing policy been over the past few years and what has been its contribution to shareholder value? Why do you think the company has chosen this level of gearing? What do you propose for the future financial strategy?

Student notes

- You will need to get a feel for market risk premia, risk free rates and borrowing ratios for the exam. For now, use:
  - Irish risk free rate 2.0% (reflecting long run reversion to mean from current 0.90%)
  - Irish market risk premium 5%
  - Maximum debt multiples for a conventionally financed company: Net debt to EV – 25%, Interest cover 5x, Net debt to EBITDA 3x. If maximum debt is taken on, then assume borrowing costs increase by 1.5%.
- Approach this requirement by first commenting on recent historic development of the capital structure, in qualitative terms.
- Then put some numbers around this by calculating Kingspan's current WACC
- You can then examine the effect on the income statement, debt repayment profile and shareholder value of gearing Kingspan up to a sensible maximum. (If this were done, it would be achieved by borrowing € X million and paying a special dividend of € X million, subject to any limitations on distributions.)
- You should then investigate the alternative approach of maintaining overall group gearing as is, and maximising debt overseas to use the tax differential between Ireland and the rest of the world. As a ball park figure, use a generic non-Irish tax rate of 30%.
- When considering net debt, using the 2016 closing balance sheet is a good approximation. There is later data in the 27th April 2017 press release which you can use if you wish.

[1] Post your responses to the various questions and discuss your thoughts and responses in the Case study 2 forum in light of the answers posted by fellow group members and the model answer released by the tutors. You are expected to post during the Case study 2 timeline – see course site U3/Case 2 for dates.

Question 2

Give a critical appraisal of the company's dividend policy, from both company and shareholder perspectives, and its contribution to total shareholder returns.

Student notes

- Look at dividend cover
- Impact on shareholder value
- Is Kingspan a growth stock or income stock? How do you communicate this message to shareholders?
- Who are the shareholders?
- What is likely to happen over 2017 and later, bearing in mind that there was no dividend for 2009, and recent dividend history is as follows:

Year	Dividend
2010	10c
2011	11c
2012	12.25c
2013	14c
2014	16.25c
2015	25c
2016	33.5c

Again, you do not need to make calculations with regard to any acquisitions made but you can comment on the possible approaches that management might take following the acquisitions.