B2. (Dividend policy) A firm has 20 million common shares outstanding. It currently pays out $1.50 per share per year in cash dividends on its common stock. Historically, its payout ratio has ranged from 30% to 35%. Over the next five years it expects the earnings and discretionary cash flow shown below in millions.

a. Over the five-year period, what is the maximum overall payout ratio the firm could achieve without triggering a securities issue?

b. Recommend a reasonable dividend policy for paying out discretionary cash flow in years 1 through 5.

**1 2 3 4 5 THEREAFTER**

Earnings 100 125 150 120 140 150+ per year

Discretionary

cash flow 50 70 60 20 15 50+ per year