2. Xandu, Inc. has paid very large dividends ever since it started business. Recently, however, Xandu has decided to quit paying dividends and announced that there never will be another dividend payment or any other payments to stockholders during the remaining life of the company. Assuming this information is correct, what should be the value of Xandu’s stock?

a. zero
b. greater than zero
c. less than zero
d. There is not enough information to answer this question.

The value of any asset is determined as follows: 
\[
\text{Value} = \frac{\hat{CF}_1}{(1 + r)^1} + \frac{\hat{CF}_2}{(1 + r)^2} + \ldots + \frac{\hat{CF}_n}{(1 + r)^n}.
\]

If the future expected cash flows equal zero, then \(\hat{CF}_1 = \hat{CF}_2 = \ldots = \hat{CF}_n = 0\), which means the value of the asset equals zero.

RETURN TO THE SAMPLE QUESTIONS