Return on Stockholders' Equity

(assuming no preferred stock)

Return on stockholders' equity = Net income (after taxes) for the year divided by the **average stockholders' equity during the year**

The amounts used on this form are hypothetical amounts.

Calculation of the **return on stockholders' equity** includes:

Net income from the income statement for the year ended *December 31, 2022* .

Average stockholders' equity computed from balance sheets during the year.

Earnings (net income after taxes)	*$ 21,000*	**E**	
divided by average stockholders' equity	*$ 200,000*	**ASE**	
= Return on stockholders' equity	***10.5%***	**RSE**	(E / ASE)

Notes:

The return on stockholders' equity is also known as *return on equity*, and *return on common stockholders' equity.*

E Earnings or net income after taxes appears at or near the bottom of a corporation's income statement. For this example, we will assume that the corporation's after-tax earnings were $21,000 for the calendar year 2022.

ASE Average stockholders' equity is the average amount appearing on the balance sheets throughout the year of the income statement. Since we are assuming there is no preferred stock outstanding, the total amount of stockholders' equity is used to compute the average stockholders' equity. If the changes in the total stockholders' equity are reasonably consistent throughout the year, a simple average of the amounts at the beginning and end of the year may be used. However, if the changes in the total amount of stockholders' equity do vary significantly from month month to month, it is better to use a 13-month average. **Form G3** can assist in the calculation.

In this example, we will assume that there is no preferred stock and that the average amount of stockholders' equity for the year 2022 was $200,000.

RSE The return on stockholders' equity is the return on the book value of the corporation's common stock. The book value of the common stock is likely to be significantly different from the market value of the common stock.

For a blank form see **Form R20**.

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