



SNS College of Technology

Coimbatore - 35



23BAT611 – Financial Management

Unit - III

COST OF CAPITAL & CAPITAL STRUCTURE



Presented by

Ms.S.Swarnam
Design Thinker

1st Indian Institution to Implement Design Thinking Curriculum
Redesigning Common Mind and Business Towards Excellence



Recall



Discussed Problem related to Equity Share capital



Topic



Equity Share
Capital



Preference Share
Capital



Debts



Retained
Earnings



Cost of Capital





Cost of Equity Share



Problem : 10

A company cost of equity capital (k_e) is 15%. The average tax rate of shareholders is 40% and the brokerage cost for purchase of securities is 2%.

Calculate the cost of retained earnings.



Cost of Equity Share



Solution

Particulars		%
Cost of equity capital	=	15.00
Less: Tax at 40% on 15	=	6.00
	=	9.00
Less: Brokerage at 2% on 9	=	0.18
	=	8.82 %



Cost of Equity Share

Problem : 11 The following particulars relate to Prakash Ltd.

Equity share capital 1,00,000 share of Rs. 10	10,00,000
Profit after tax	9,00,000
Current market price of equity share	75

- Calculate the cost of equity.
- What is the cost of retained earning if the average personal tax rate of shareholders is 30% and the brokerage cost for making new investment is 2%.



Cost of Equity Share



Solution

Cost of equity capital $k_e = \text{EPS} / \text{MP}$

$\text{EPS} = \text{profit after tax} / \text{No.of equity shares} = 9,00,000 / 1,00,000 = \text{Rs. } 9$

$\text{MP} = \text{Market Price} = \text{Rs. } 75$

Cost of Equity Capital $k_e = 9/75 = 12\%$



Cost of Equity Share



Solution

Particulars		%
Cost of equity capital	=	12.00
Less: Tax at 30% on 12	=	3.60
	=	8.40
Less: Brokerage at 2% on 8.40	=	0.17
	=	8.23 %



Summarize

Cost of Retained earnings





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