Week 4 Discussion Problem: WACC

Let's try calculating the weighted average cost of capital (WACC). Calculate the WACC given the following assumptions:

1. Company tax rate is 40 percent.
2. Company has an outstanding bond issue with a 7-7/8 coupon, market price of 103-5/8 (percent of 100% par, in 32nds.), semiannual coupon payments, and 12 years to maturity.
3. Company has an outstanding preferred stock issue paying an 8 percent dividend, $100 par, and a market price of $98.35. Flotation (issuance) costs on a new issue are 8 percent.

1. Common equity financing is through retained earnings. The Company has a beta of 1.22. The market risk premium is 6 percent and the risk-free rate is 4 percent. The company's capital structure is 40 percent debt, 10 percent preferred, and 50 percent common equity.