**Reynolds American Inc. (RAI)**

1. **Examine the capital structure of your firm, Reynolds American Inc. (RAI). Remember that the capital structure refers to outside claimants of the firm and is typically long-term in nature. Capital by definition does not include items like accounts payable, accrued liabilities, deferred compensation, deferred taxes, etc.**
   1. What types of securities are used to finance the company? Provide detail – this may require looking at the long-term debt footnote.
   2. What is the total Market Value of these securities? The fair value of debt can be found in the debt footnote. The market value of equity can be found by multiplying the price per share by the number of shares outstanding. PLEASE NOTE: Watch for different denominations particularly if you are using different sources – do not add debt in millions to market value of equity in thousands!
   3. Using Yahoo Finance to look at a competitor firm’s capital structure and compare to your own firm. **Discuss** differences or similarities.
   4. What conclusions do you draw by looking at your firm’s capital structure? Do you believe this structure is appropriate? Consider the amount of business risk, stability of cash flows, etc. in your answer.
2. **Calculate the firm’s Weighted Average Cost of Capital as we have done in class lectures.** 
   1. For the risk-free rate in the CAPM model, use the 10-year Treasury reported on Yahoo Finance. Assume that the market risk premium (RM – RF) is 8%. To calculate the after-tax cost of debt you can assume a tax rate of 40%.
   2. Demonstrate clearly how you arrived at each component cost and also how you arrived at the appropriate weight (using the firm’s Market Value)to use for each component. Check your answer for appropriateness. Remember that the cost of equity should be higher than the cost of debt since it is riskier!
3. **Examine transactions with the firm’s capital providers over the past three years.**
   1. Has your firm undergone any major restructuring in the past three years such as a stock repurchase, bond refunding, etc? If so, discuss the implications. (You can find this information on the firm’s Cash Flow Statement or Statement of Shareholder Equity)
   2. In terms of rewards to shareholders, how has your firm chosen to distribute benefits?
      1. Does your firm pay regular cash dividends? If so, what is the current dividend yield?
      2. Alternatively, has the firm initiated stock repurchase plans for shareholders?
4. **Examine the valuation of the firm.**
   1. If the firm pays a regular cash dividend use the dividend growth model to estimate a stock price for your firm. Remember to determine the appropriate growth rate for the firm and then use that information to determine the equilibrium stock price.
      1. If your firm does not pay dividends, use free cash flows and the Corporate valuation method. This is similar to the methodology for an acquisition but it is easier since you can assume there is no permanent change being made in the capital structure in the future! Remember that this will yield a value of operations for the firm (not a per share stock price). Make the necessary adjustments to derive market value of equity and divide by shares outstanding.
   2. Find the price-to-earnings (P/E) ratio for a comparable firm from Yahoo Finance. Using your firm’s most recent earnings per share (EPS) calculate a comparable stock price by multiplying your firm’s EPS by the comparable firm’s P/E ratio.
   3. Draw **conclusions** about your firm’s current stock valuation.
5. **Examine your firm’s working capital management**.
   1. Calculate the Inventory conversion period, Receivables collection period, and Payables deferral period.
   2. Calculate the cash conversion cycle.
   3. Calculate Net Operating Working Capital.
   4. Would you describe your firm’s working capital policy as relaxed, moderate or restricted? Comment on any needed areas of improvement in working capital management (or note any specific areas of strength).
   5. What is the firm’s cash balance as a percentage of total assets? **Discuss** the firm’s level of cash.