Answer on Question #42114, Economics, Finance

Cash flows of \$20 million for 4 years.

Investment = \$48 million.

Tax rate = 40%.

Debt ratio = 45%.

Bonds have 5 years left to maturity, a coupon rate = 7% annually coupons, face value = \$1000, current price = \$960.

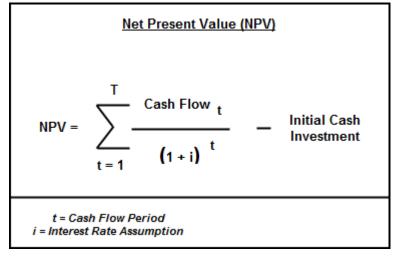
\$6,000,000 in preferred stock (dividend of \$4 with a price of \$42, issue cost = \$2), the rest from retained earnings.

\$2.5 per share next year, retention rate = 40%, return on equity = 25%. Current stock price = \$50.

WACC = E/V * Re + D/V * Rd * (1-Tc)

Re = cost of equity RD = cost of debt E = market value of the firm's equity D = market value of the firm's debt V = E + D E/V = percentage of financing, i.e., equity D/V = percentage of financing, i.e.debt TC = corporate tax rate

WACC = 0.45*0.25 + 0.45*0.4*(1-0.4) = 0.2205



NPV = 20000000/1.2205 + 20000000/1.2205^2 + 20000000/1.2205^3 + 20000000/1.2205^4 - 48000000 = \$1826771,24