Suraj Metals are expected to declare a dividend of Rs. 5 per share and the growth rate in dividends is expected to grow @ 10% p.a. The price of one share is currently at Rs. 110 in the market. What is the cost of equity capital to the company?

Solution.

Cost of equity capital is equal to the ratio of current earnings per share to the market price per share.

We have a formula:

$$K_e = \frac{D_1}{P_e} + g,$$

where

D_1 is current dividend per share

P_e is current market price per share

g is expected rate of growth in dividends per share

So

$$K_e = \frac{5}{110} + 0.10 = 0.1454 \ or \ 14.54\%$$

Answer: Cost of equity capital is $14{,}54\%$.