

Session 12a: Post Class tests

1. Alfred Inc. is a publicly traded sporting goods company. The company has \$ 250 million in book value of debt, reported interest expenses of \$ 12.5 million in the most recent year and has an average maturity of 5 years for the debt. The pre-tax cost of debt for the firm is currently 4%. What is your best estimate of the market value of debt outstanding at the firm? (You can assume annual interest payments and a marginal tax rate of 40%)
 - a. \$261.12 million
 - b. \$250.00 million
 - c. \$280.29 million
 - d. \$243.01 million
 - e. \$156.68 million
2. Jack's Stores is a retail firm with no conventional debt. It does have operating lease commitments of \$ 12 million each year for the next 8 years. Jack's Stores pre-tax cost of debt is 5%, its cost of capital is 9% and the marginal tax rate is 40%. What is the debt value of operating leases? (The risk free rate is 3%)
 - a. \$96.00 million
 - b. \$84.24 million
 - c. \$77.56 million
 - d. \$66.42 million
 - e. None of the above
3. Faraday Enterprises is a publicly traded company. It currently has 10 million shares trading at \$12/share and \$150 million in book value of equity. The firm also has book value of debt of \$ 75 million and market value of debt of \$ 80 million. The cost of equity for the company is 9%, the pre-tax cost of debt is 4% and the marginal tax rate is 40%. What is the cost of capital?
 - a. 7.4%
 - b. 7.0%
 - c. 7.7%
 - d. 6.36%
 - e. None of the above
4. Lester Inc. has 5 million shares outstanding, trading at \$20/share. The company has one convertible bond, with a face value of \$ 100 million, a ten-year maturity and a coupon rate of 2%; the bond has a market value of \$120 million. If the current cost of equity for the firm is 10% and the pre-tax cost of debt is 5%, what is the cost of capital for the firm? (The marginal tax rate is 40%)
 - a. 5.20%
 - b. 6.18%
 - c. 7.55%
 - d. 8.25%
 - e. None of the above
5. JG Enterprises has 50 million shares, trading at \$4 a share; the cost of equity is 12%. It has debt with a market value of \$ 100 million and a pre-tax cost of debt of 6%. Finally the company has \$100 million in market value of preferred stock; the preferred shares are trading at \$80 a share, with an annual preferred

dividend of \$6/share. If the marginal tax rate is 40%, estimate the cost of capital for the firm.

- a. 8.78%
- b. 8.03%
- c. 9.38%
- d. 9.90%
- e. None of the above