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A Study on Cost of Capital of Royal Roots Company, Madurai, Tamil Nadu State, India

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Abstract

The cost of capital is important in the financial management of every business. A measure of the cost of capital is required when evaluating various aspects of strategic business plans. The purpose of this research is to study the financial position of Royal Roots Company with respect to its cost of capital. This research includes the analysis of cost of capital of the company and its ability to finance its business. Interview and questionnaire were used for methods of data collection and SPSS analysis was used to analyze the questionnaire. The analysis includes the financial years from 2010 to 2013. The analysis is carried out with the help of ratio analysis, regression analysis and trend analysis. This research also includes projections of weighted average cost of capital for the next 5 financial years. It also includes how the company can increase the profit in the coming years with proper management of capital structure.

Keyword: *Cost of Capital, WACC, Capital Structure.*

INTRODUCTION

Cost of capital is the required return necessary to make a capital budgeting project, such as building a new factory, worthwhile. Cost of capital includes the cost of debt and the cost of equity. A company uses debt, common equity and preferred equity to fund new projects, typically in large sums. In the long run, companies typically adhere to target weights for each of the sources of funding. When a capital budgeting decision is being made, it is important to keep in mind how the capital structure may be affected. Capital structure is a mix of a company's long-term debt, specific short-term debt, common equity and preferred equity. The capital structure represents how a firm finances its overall operations and growth by using different sources of funds. Debt comes in the form of bond issues or long-term notes payable, while equity is classified as common stock, preferred stock or retained earnings. Short-term debt such as working capital requirements is also considered to be part of

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the capital structure. Working capital management is a managerial accounting strategy focusing on maintaining efficient levels of both components of working capital, current assets and current liabilities, in respect to each other. Working capital management ensures a company has sufficient cash flow in order to meet its short-term debt obligations and operating expenses. A company's proportion of short and long-term debt is considered when analyzing capital structure. When people refer to capital structure they are most likely referring to a firm's debt-to-equity ratio, which provides insight into how risky a company is. Usually a company more heavily financed by debt poses greater risk, as this firm is relatively highly levered. Optimal capital structure is the best debt-to-equity ratio for a firm that maximizes its value and minimizes the firm's cost of capital. In theory, debt financing generally offers the lowest cost of capital due to its tax deductibility. However, it is rarely the optimal structure since a company's risk generally increases as debt increases. A healthy proportion of equity capital, as opposed to debt capital, in a company's capital structure is an indication of financial fitness.

For an investment to be worthwhile, the expected return on capital must be greater than the cost of capital. A company's securities typically include both debt and equity, so one must therefore calculate both the cost of debt and the cost of equity to determine a company's cost of capital. The weighted average cost of capital multiplies the cost of each security by the percentage of total capital taken up by the particular security, and then adds up the results from each security involved in the total capital of the company. If there were no tax advantages for issuing debt, and equity could be freely issued, Miller and Modigliani showed that, under certain assumptions, the value of a leveraged firm and the value of an unleveraged firm should be the same. Because of tax advantages on debt issuance, such as the ability to deduct interest payments from taxable income, it will be cheaper to issue debt rather than new equity. At some point, however, the cost of issuing new debt will be greater than the cost of issuing new equity. This is because adding debt increases the default risk and thus the interest rate that the company must pay in order to borrow money. By utilizing too much debt in its capital structure, this increased default risk can also drive up the costs for other sources (such as retained earnings and preferred stock) as well. Management must identify the "optimal mix" of financing–the capital structure where the cost of capital is minimized so that the firm's value can be maximized. The objective of the project hence is to analyze how the company cost of capital and its sources of finances to meet its financial obligations.

RESULTS AND DISCUSSIONS

Analysis and Interpretation of Cost of Capital of Royal Root Company in Madurai, Tamil Nadu State.

Cost of Debt

Debt Issued at par

Kd = (1 – T) R x 100

Table 1: Cost of Debt Issued at Par

Year	1	Tax Rate	Debt Interest Rate	100	Cost of Debt
2010	1	44.07	26.3	100	14.71
2011	1	48.17	29.9	100	15.50
2012	1	50.00	30.7	100	15.35

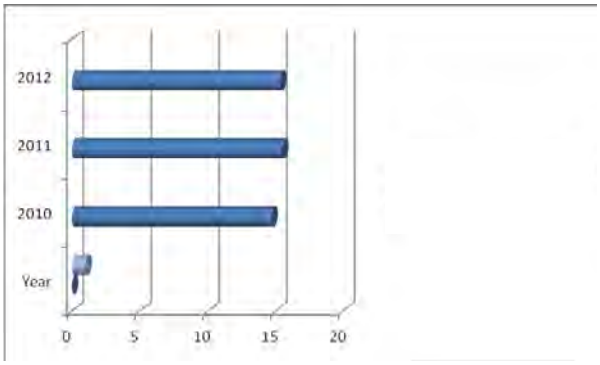

Figure 1: Cost of Debt Issued at Par

With respect to the cost of capital of Royal Roots Company, the cost of debt issued at par, has shown a fluctuation trend over the past 3 years. It has drastically increased in FY 2009-10 due

to increased in tax rate and increased in debt rate during that period. The increased tax rate and debt rate has affected the cost of capital of the company which has also affected the earning per share of the company.

Debt Issued at Premium or Discount When the Debt in Perpetual

$$Kd = \frac{I}{NP} (1 - T) \times 100$$

Table 2: Debt Issued at Premium or Discount when the Debt in Perpetual

Year	Annual Interest Payment	Net Proceeds of Debt	1	Tax Rate	100	Cost of Debt
2010	100	2880	1	44.07	100	1.942
2011	100	2880	1	48.17	100	1.799
2012	100	2880	1	50.00	100	1.740

4% floatation cost of 3000 debt is 120 and NP = 3000-120 = 2880

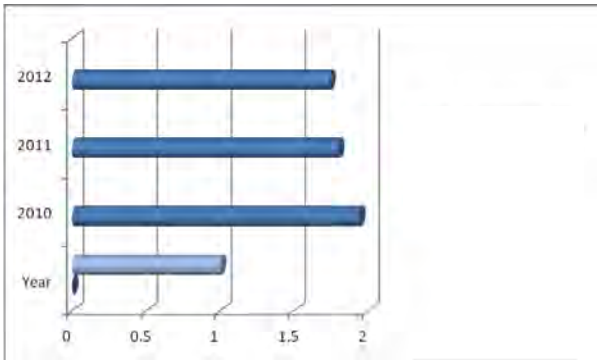

Figure 2: Cost of Perpetual Debt Issued at Discount or Premium

With respect to the cost of capital of Royal Roots Company, the cost of perpetual debt issued at discount or premium has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to increase in tax rate of the company as a result of macroeconomic factors and has maximized the wealth of shareholders in the company.

Table 3: Cost of 10 Years Redeemable Debt at Par

Year	I	1	Tax Rate	$\left(\frac{P - NP}{N}\right)$	$\left(\frac{P + NP}{2}\right)$	100	Cost of debt (Kd)
2010	100	1	44.07	12	2940	100	2.131
2011	100	1	48.17	12	2940	100	1.975
2012	100	1	50.00	12	2940	100	1.905

Cost of 10 Years Redeemable Debt at Par

$$Kd = \frac{I(1 - T) + \left(\frac{P - NP}{N}\right)(1 - T)}{\left(\frac{P + NP}{2}\right)} \times 100$$

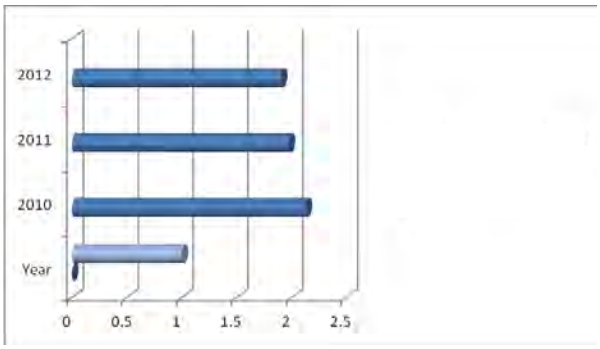

Figure 3: Cost of Redeemable Debt at Par

With respect to the cost of capital of Royal Roots Company, the cost of redeemable debt issued at par has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to an increase in tax rate of the company as a result of macroeconomic factors and has maximized the wealth of shareholders in the company. However, the net proceedings remain the same throughout the 3 years.

Table 4: When Debentures are Issued at 10% Discount

Year	I	1	Tax Rate	$\left(\frac{P - NP}{N}\right)$	$\left(\frac{P + NP}{2}\right)$	100	Kd
2010	100	1	44.07	42	2790	100	2.847
2011	100	1	48.17	42	2790	100	2.638
2012	100	1	50.00	42	2790	100	2.545

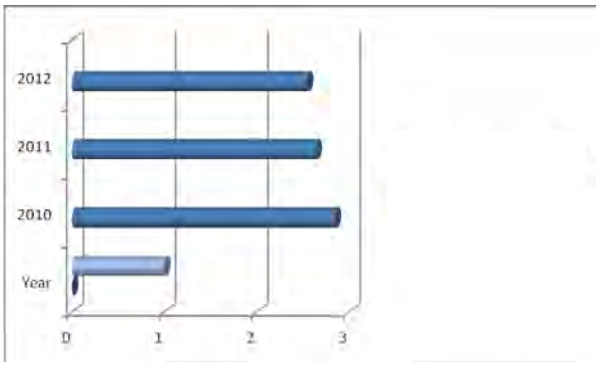

Figure 4: Cost of Redeemable Debt Issued at 10% Discount

With respect to the cost of capital of Royal Roots Company, the cost of redeemable debt issued at discount has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to an increase in tax rate of the company as a result of macroeconomic factors such as inflation, interest rate, exchange rate, etc and has maximized the wealth of shareholders in the company. This has helped to create the value of shareholders since the cost of debt keep on decreasing from year to year and profit of the company also keep on increasing.

Table 5: When Debenture is Issued at 10% Premium

Year	I	1	Tax Rate	$\left(\frac{P - NP}{N}\right)$	$\left(\frac{P + NP}{2}\right)$	100	Kd
2010	100	1	44.07	-18	3090	100	1.484
2011	100	1	48.17	-18	3090	100	1.375
2012	100	1	50.00	-18	3090	100	1.327

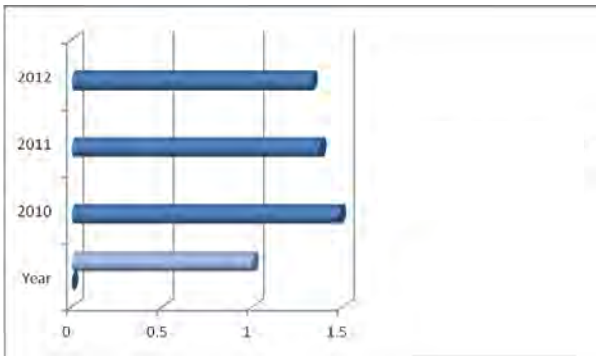

Figure 5: Cost of Redeemable Debt Issued at 10% Premium

With respect to the cost of capital of Royal Roots Company, the cost of redeemable debt issued at premium has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to increase in tax rate of the company as a result of macroeconomic factors such as inflation, interest rate, exchange rate, etc and has maximized the wealth of shareholders in the company. This has helped to create the value of shareholders wealth since the cost of debt keep on decreasing from year to year and profit of the company also keep on increasing

Cost of Redeemable Preference Shares

$$Kp = \frac{D + \frac{F}{N}(1 - T) + \frac{RP}{N}}{\frac{P + NP}{2}} \times 100$$

Royal Roots Marketing Private Ltd issues 48, 10% preference shares of Rs.225 each, redeemable at par after 10 years and assuring

5% floatation costs on face value of shares. The company issues 48 coupons to the public for 48 months and a person has to pay Rs.6000 to the company before you become independent Business Co-ordinator member.

Table 6: Cost of Preference Shares Issued at Par

Year	D	$\frac{F}{N}$	1-T	$\frac{RP}{N}$	$\frac{P + NP}{2}$	100	K_p
2010	10	0.5000	0.5593	0.0000	219.3750	100	4.686
2011	10	0.5000	0.5183	0.0000	219.3750	100	4.677
2012	10	0.5000	0.5000	0.0000	219.3750	100	4.672

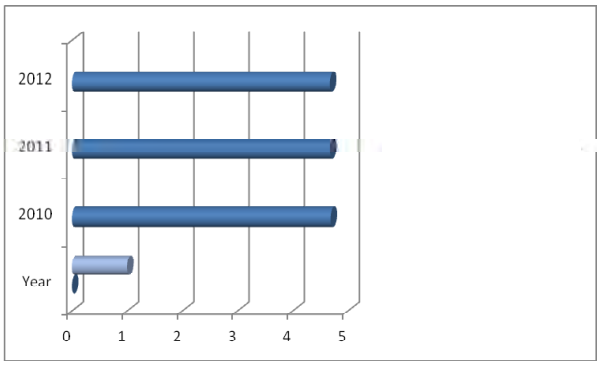

Figure 6: Cost of Preference Shares at Par

With respect to the cost of capital of Royal Roots Company, the cost of preference shares issued at par has shown slightly decreasing trend over the past 3 years. It has slightly decreased from FY 2009-10 to FY 2011-12 due to slightly increase in tax rate (from year to year) of the company as a result of macroeconomic factors such as inflation, interest rate, exchange rate, etc and has maximized the wealth of shareholders in the company. This has helped to create the value of shareholders wealth since the cost of debt keep on decreasing from year to year and profit of the company also keep on increasing.

Table 7: Cost of Preference Shares Issued at 10% Discount

Year	D	$\frac{F}{N}$	1-T	$\frac{RP}{N}$	$\frac{P + NP}{2}$	100	K_p
2010	10	0.5000	0.5593	0.0000	208.1250	100	4.939
2011	10	0.5000	0.5183	0.0000	208.1250	100	4.929
2012	10	0.5000	0.5000	0.0000	208.1250	100	4.925

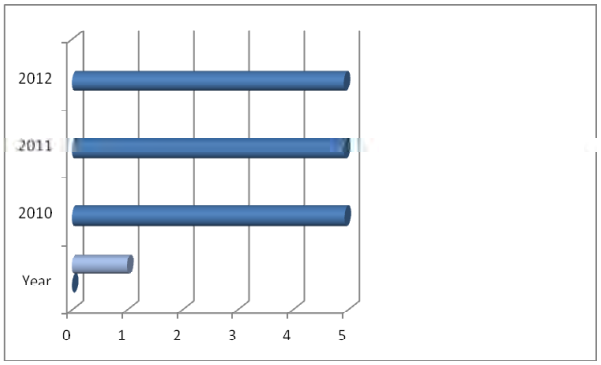

Figure 7: Cost of Preference Shares Issued at 10% Discount

With respect to the cost of capital of Royal Roots Company, the cost of preference shares issued at 10% discount has shown unchanging trend over the past 3 years. The cost of preference shares has remain the same throughout FY 2009-10 to FY 2011-12 even though the tax rate keep on increasing from year to year. This is because the preference shareholders receive a fixed rate of dividend.

Table 8: Cost of Preference Shares Issued at 10% Premium

Year	D	$\frac{F}{N}$	1-T	$\frac{RP}{N}$	$\frac{P + NP}{2}$	100	Kp
2010	10	0.5000	0.5593	0.0000	236.25	100	4.351
2011	10	0.5000	0.5183	0.0000	236.25	100	4.448
2012	10	0.5000	0.5000	0.0000	236.25	100	4.444

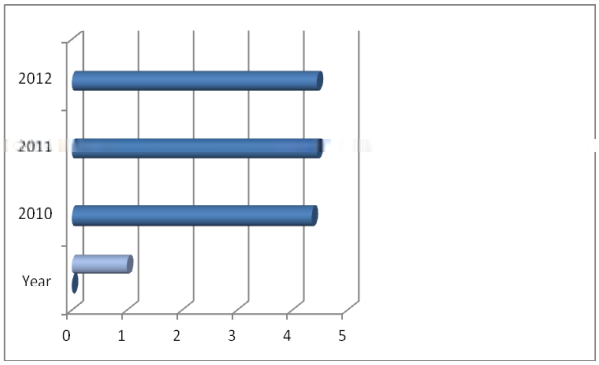

Figure 8: Cost of Preference Shares Issued at 10% Premium

With respect to the cost of capital of Royal Roots Company, the cost of preference shares issued at 10% premium has shown unchanging trend over the past 3 years. The cost of preference shares has remained the same throughout FY 2009-10 to FY 2011-12 even though the tax rate keeps on increasing from year to year. This is because the preference shareholders receive a fixed rate of dividend.

Cost of Equity

The cost of equity shares basically depends upon the expectation of the equity shareholders. The market value of the shares depends on the dividend paid and the rate of dividend depends on the degree of financial and business risk. Royal Roots issues 10,00,000 equity shares.

Dividend Price Approach

Cost of equity share, $K_E = \frac{\text{Dividend for share}}{\text{Market Price per share}} \times 100$

Table 9: Cost of Equity Using Dividend Price Approach

Year	Dividend	Dividend per share	Market price	Market price per share	K_E
2010	20,25,000	2.025	130,00,000	13	15.577
2011	20,25,000	2.025	150,00,000	15	13.500
2012	20,25,000	2.025	200,00,000	20	10.125

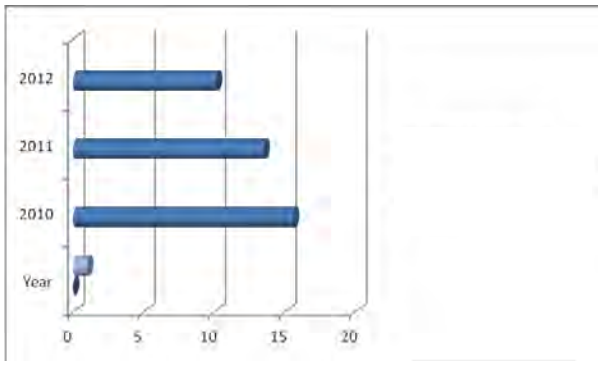

Figure 9: Cost of Equity Using Dividend Price Approach

With respect to the cost of capital of Royal Roots Company, the cost of Equity using dividend price approach has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to an increase in the book value (increased market price per share) of the company as a result of favorable macroeconomic factors such as inflation, interest rate, exchange rate, etc and has maximized the wealth of shareholders in the company. This has helped to create the value of shareholders

since the cost of Equity keep on decreasing from year to year and profit of the company also keep on increasing.

Earning Price Ratio or Earning Yield Approach

According to this approach, the cost of shares is based upon the stream of unchanged earnings earned by a company. This approach holds that each investor expect a certain amount of earnings whether distributed by way of dividend or not from the company in whose shares he invests. This approach assumes that, the invested capital in a business firm is equal to the market price of shares. Royal Roots invested capital of Rs.30,00,000 for the business.

$$K_E = \frac{\text{Dividend for share}}{\text{Market Price per share}} \times 100$$

Table 10: Earning Price Ratio OR Earning Yield Approach

Year	Earnings	Earning per share	Market price	Market price per share	K_E
2010	1,45,000	0.145	30,00,000	3	4.833
2011	3,40,000	0.34	30,00,000	3	11.333
2012	4,40,000	0.44	30,00,000	3	14.667

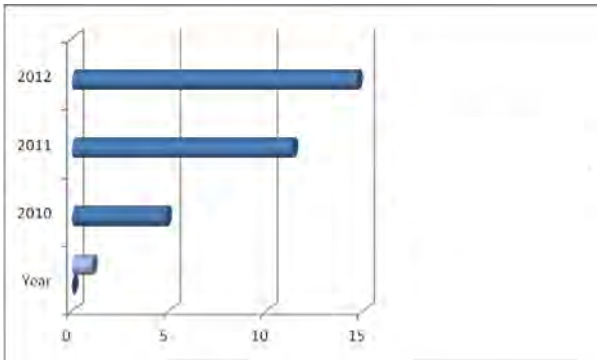

Figure 10: Earning Price Ratio OR Earning Yield Approach

With respect to the cost of capital of Royal Roots Company, the cost of Equity using Earning yield approach has shown an increasing trend over the past 3 years. Even though the market price per share remains the same, the cost of Equity has drastically increased from FY 2009-10 to FY 2011-12 due to increasing Retained Earnings per share of the company as a result of favorable macroeconomic factors such as inflation, interest rate, exchange rate, etc. This affects the profit of the company negatively which also has negative impact on shareholders wealth. This approach is not good for cost of Equity of a firm. This approach can be objected on the following grounds. Firstly, it wrongly assumes that the earning per share will remain constant in the future which is not true. Secondly, the market prices of the shares will not remain constant, as the shareholders will expect capital gains as a result of reinvestment of retained earnings. Thirdly, all the earnings may not be distributed among the shareholders by way of dividend.

Table 11: Dividend Price Plus Growth Approach

Year	Dividend	Dividend Per Share	Market Price	Market Price Per Share	Growth Rate	K_E
2010	20,25,000	2.025	130,00,000	13	4	19.577
2011	20,25,000	2.025	150,00,000	15	4	17.500
2012	20,25,000	2.025	200,00,000	20	4	14.125

Dividend Price Plus Growth Approach

According to this approach, the investor is prepared to pay the market price of the share as he expects not only the payment of the dividend but also a growth in the dividend rate at a uniform rate perpetually. Royal Roots Company expects 4% growth rate in the dividend at perpetual uniform rate.

$$\text{Cost of equity, } K_E = \left(\frac{D}{P} + G\right) \times 100$$

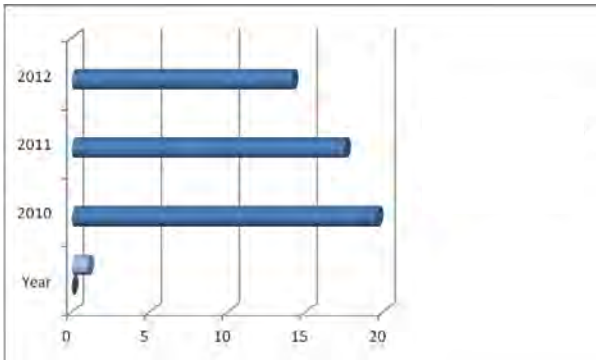

Figure 11: Dividend Price Plus Growth Approach

With respect to the cost of capital of Royal Roots Company, the cost of Equity using dividend price plus growth approach has shown decreasing trend over the past 3 years. Even though the dividend per share remains the same, the cost of Equity has drastically decreased from FY 2009-10 to FY 2011-12 due to increasing market price per share of the company as a result of favorable macroeconomic factors such as inflation, interest rate, exchange rate, etc. This affects the profit of the company positively which also has positive impact on shareholders wealth. This has helped to create the value of shareholders since the cost of Equity keep on decreasing from year to year and profit of the company also keep on increasing.

Using Gordon Model for Estimating Cost of Equity

This model is used to calculate cost of equity by using the dividend capitalization approach. He made the following assumptions:

Retained earnings represent the only source of financing for firm.

The rate of return on the firm's investment is constant.

The growth rate of the firm is the product of retention ratio and its rate of return.

The firm has perpetual life.

No taxes are in existence.

$$K = \frac{E\ (1-b)+b(r)(Po)}{Po} \times 100$$

Table 12: Using Gorden Model for 2010

Growth Royal Roots (r > *k*)	Normal Royal Roots (r = k)	Decline Royal Roots (*r* < *k*)
r =17%	r =17%	r =17%
E= Rs.4	E= Rs.4	E= Rs.4
b = 0.25	b = 0.25	b = 0.25
Po =30	Po =23	Po =8

Table 13: Using Gorden Model for 2011

Growth Royal Roots (r > *k*)	Normal Royal Roots (r = k)	Decline Royal Roots (*r* < *k*)
r =17%	r =17%	r =17%
E= Rs.4	E= Rs.4	E= Rs.4
b = 0.25	b = 0.25	b = 0.25
Po =40	Po =23	Po =10

Table 14: Using Gorden Model for 2012

Growth Royal Roots (r > *k*)	Normal Royal Roots (r = k)	Decline Royal Roots (*r* < *k*)
r =17%	r =17%	r =17%
E= Rs.4	E= Rs.4	E= Rs.4
b = 0.25	b = 0.25	b = 0.25
Po =50	Po =23	Po =15

Table 15: Using Gordon Model for Estimating Cost of Equity

Year	Growth Royal Roots (r > *k*)	Normal Royal Roots (r = k)	Decline Royal Roots (*r* < *k*)
2010	14.25	17.29	41.75
2011	11.75	17.29	34.25
2012	10.25	17.29	24.25

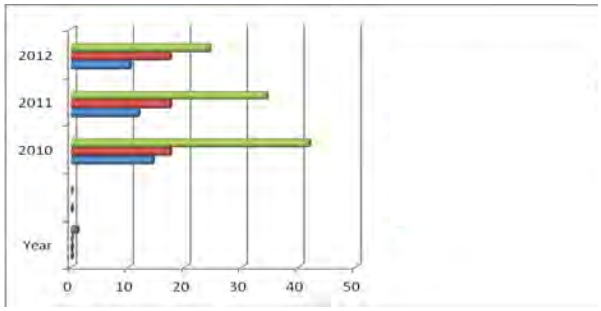

Figure 12: Estimating Cost of Equity using Gorden Model

With respect to estimating of capital of Royal Roots Company, the estimated cost of Equity using Gordon Model has shown decreasing trend over the past 3 years for growth, normal and decline of the company. In this model, the retained earnings of Royal Roots Company represent the only source of financing the business and the rate of return on the firm's investment is constant. However, the growth rate of the firm is the product of retention ratio and its rate of return. The firm has perpetual life and we assume no taxes are in existence. Therefore, for growth, the rate of return is greater than the cost of equity and for normal, the rate of return is equal to cost of equity but for decline, the rate of return is less than the cost of equity.

Composite Cost of Capital or Overall Cost of Capital or Weighted Average Cost of Capital

Table 16: Funds for 2010

Sources of funds	Book Value (Weights Rs.)	Specific Cost	Weighted Cost (Rs.)
Debenture	30,00,000	2%	60,000
Preference Shares	180,00,000	6%	10,80,000
Equity Shares	135,00,000	15%	20,25,000
Retained Earnings	1,45,000	5%	7,250
Total	346,45,000		31,72,250

Table 17: Funds for 2011

Sources of funds	Book Value (Weights Rs.)	Specific Cost	Weighted Cost (Rs.)
Debenture	30,00,000	2%	60,000
Preference Shares	240,00,000	6%	14,40,000
Equity Shares	135,00,000	15%	20,25,000
Retained Earnings	3,40,000	5%	17,000
Total	408,40,000		35,42,000

Table 18: Funds for 2012

Sources of funds	Book Value (Weights Rs.)	Specific Cost	Weighted Cost(Rs.)
Debenture	30,00,000	2%	60,000
Preference Shares	300,00,000	6%	18,00,000
Equity Shares	135,00,000	15%	20,25,000
Retained Earnings	4,40,000	5%	22,000
Total	469,40,000		39,07,000

$$\text{Composite Cost of Capital} = \frac{\text{Total Weighted Cost}}{\text{Total Weights}} \times \frac{100}{1}$$

Table 19: Weighted Average Cost of Capital

Year	Book Value (Weights Rs.)	Weighted Cost (Rs.)	Weighted Average Cost of Capital
2010	346,45,000	31,72,250	9.156
2011	408,40,000	35,42,000	8.673
2012	469,40,000	39,07,000	8.323

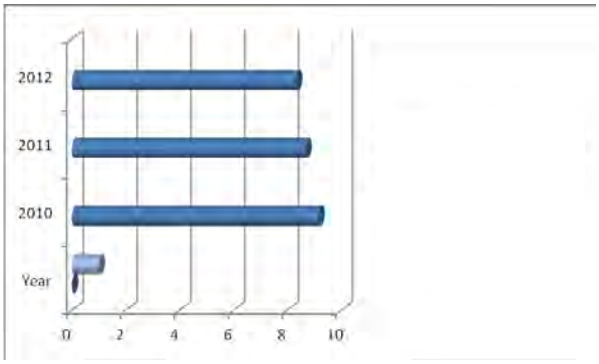

Figure 13: Weighted Average Cost of Capital

With respect to the composite cost of capital of Royal Roots Company, the weighted average cost of capital has shown decreasing trend over the past 3 years. It has drastically decreased from FY 2009-10 to FY 2011-12 due to increase in the book value (increased market price per share) of the company as a result of favorable macroeconomic factors such as inflation, interest rate, exchange rate, etc and very small increased in weighted cost. Thus maximizing the wealth of shareholders in the company. This has helped to create the value of shareholders since the weighted average cost of capital keep on decreasing from year to year and profit of the company also keep on increasing.

REGRESSION ANALYSIS

Let us consider the regression equation,

$Y = a + bx$

$\Sigma y = Na + b\Sigma x$

$\Sigma xy = b\Sigma x2 + N\Sigma x$

Table 20: Regression Analysis

Year	Weighted Average Cost of Capital (y)	X	x2	xy
2009-2010	9.156	-1	1	-9.156
2010-2011	8.673	0	0	0
2011-2012	8.323	1	1	8.323
N=3	37.423	0	2	-0.833

$Y = a + bx$

$\Sigma y = Na + b\Sigma x$

Since $\Sigma x=0$,

$a = \Sigma y/N = 37.423/3=12.474$

$\Sigma xy = b\Sigma x2 + N\Sigma x$

Since $\Sigma x=0$,

$b = \Sigma xy/\Sigma x2 = -0.833/2=-0.4165$

Substituting values,

$y = 12.474 - 0.4165x$

Table 21: Weighted Average Cost of Capital Projections

Year	X	WACC
2012-13	2.00	11.641
2013-14	3.00	11.2245
2014-15	4.00	10.808
2015-16	5.00	10.3915
2016-17	6.00	9.975

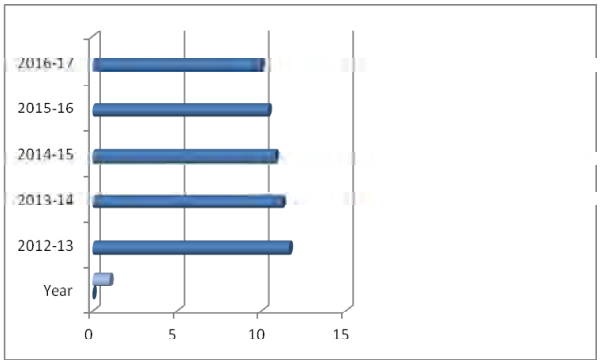

Figure 14: Weighted Average Cost of Capital Projection for Five (5) years

With respect to the 5 years projection of composite cost of capital of Royal Roots Company, the weighted average cost of capital has shown decreasing trend for the next 5 years. It has drastically decreased from FY 2012-13 to FY 2016-17 due to increase in the book value (increased market price per share) of the company as a result of favorable macroeconomic factors such as inflation, interest rate, exchange rate, etc and very small increased in weighted cost. Thus maximizing the wealth of shareholders in the company. This is has helped to create the value of shareholders since the weighted average cost of capital keep on decreasing from year to year and profit of the company also keep on increasing.

FINDINGS

After the research, it was found that, the capital structure of Royal Roots Company are debt, equity and preference shares. Moreover, other sources of funds into the company are investment and loans from financial institution. Therefore, the main source of funds available to the company to meet both short term and long term financial requirement is sales. The company is able to make sales of not less than 20 lakh every month and out of this 20 lakh, 2% of the total sales for the month will be given to the franchise as salary. Furthermore, the company has four (4) different departmental stores in different location in Chennai, India. The first one is in Coimbatore which is owned directly by the owners of Royal Roots Company. The second (2) is in Madurai, the third (3) is in Tirupur and the last is in Trichy, all being managed by franchising.

However, the franchisee deposits 30 lakh to the company and the franchisor provide a store, well and full stocked with workers and hand it over to the franchisee to run and manage the company. After my research, it was found that, the cost of capital keep on decreasing from year to year due to the fact that tax rate also keep on increasing from year to year. The company also obtain funds from the public by issuing shares (coupon) to the public. A person has to pay Rs.6000 to the company before you become Independent Business Co-ordinator of Royal Roots Company and forty-eight (48) coupon is issued for 48 months, each worth Rs.225. The Independent Business Co-ordinator can redeem each coupon per month by purchasing products in the store and credit is giving to the person up to Rs.1600. Presently, the company has over five thousand (5000) Independent Co-ordinators. One of the marketing strategies is that, If a new member is introduced by an old member of the company and any time the new member buy from a product the company, the old member's account will be credited 4%. The cost of capital is affected by level of tax, book value, weighted cost, interest rate and other macro-economic factors.

RECOMMENDATIONS

The company may focus more towards the Research and Development activities that will help in finding further sophisticated and low cost techniques of doing business. The company can enter into other forms of expansion by mergers, acquisition, diversification, etc. Therefore, we recommend that the company retain more earnings for reinvestment in order to maximize profit of the company. Moreover, we recommend that debt capital should dominate the capital structure since the cost of debt is less than other cost of capital. We also recommend that the book value of the company should be increased so that shareholders value creation will be high.

CONCLUSION

From the findings, it could be seen clearly that, the main sources of funds available to Royal Roots Company to meet both short-term and long term financial requirement are sales, shares and debentures. It is also concluded that other sources of funds available to the company are investment and loans from financial institutions. The weighted average cost of capital (WACC) reflects the overall costs of combined debt and equity capital used to finance business operations or acquisition. It is the basis of determining the discount rate for the Discounted Cash Flow business valuation method. The cost of capital of the company is low which shows a good sign of financial position. Thus, cost is less and profit is high. The cost of capital is inversely proportional to tax rate of the company. From the findings, it could be seen clearly that, the WACC is directly proportional to cost of equity. Thus, an increase of WACC also increases cost of equity and a decrease of WACC also decreases cost equity. Therefore, a change of cost of equity affects the overall cost of capital of the company. The weighted average cost of capital is also directly proportional to the weighted cost. The higher the weighted cost, the higher the weighted average cost of capital. Moreover, the cost of capital is also affected by the book value of the company. Finally, market influence is directly proportional to cost of capital.

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Financial Statements (2010-2013)

Particulars/Year	2010-2011 (Rs.)	2011-2012 (RS.)	2012-2013 (Rs.)
Current Assets			
Cash and Bank balances	43,00,000	46,55,000	48,50,000
Debtors	27,90,000	29,80,000	32,72,000
Loans and advances	16,89,000	18,90,000	20,00,000
Stocks and stores	39,86,000	43,20,000	45,20,000
Total Current Assets	127,65,000	138,45,000	146,42,000

Fixed Assets			
Prepaid expenses	7,25,000	8,85,000	9,85,000
Investment	18,90,000	19,80,000	19,80,000
Total Assets	153,80,000	167,10,000	176,07,000
Liabilities			
Secured Loans	3,90,000	7,90,000	8,80,00
Sundry Creditors	1,65,000	4,20,000	5,30,000
Other Current Liabilities	1,80,000	2,30,000	3,20,000
Total Current Liabilities	7,35,000	14,40,000	17,30,000
Long-term Loans	5,25,000	7,30,000	9,89,000
2% Debentures	3,75,000	4,80,000	6,88,000
Total Liabilities	16,35,000	26,50,000	34,07,000
Share Capital	135,00,000	135,00,000	135,00,000
Retained Earnings	1,45,000	3,40,000	4,40,000
Capital Surplus	1,00,000	2,20,000	2,60,000
Total	153,80,000	167,10,000	176,07,000
Income Statement for the year			
Gross Income	187,26,000	192,95,000	198,99,000
Less:			
Operating expenses including administration	11,79,000	12,22,800	12,99,900
Depreciation	9,90,000	10,95,000	10,95,000
Interest on term loans	7,40,000	6,76,000	6,98,000
Interest on debentures	7,90,000	8,98,000	9,20,000
Provision for bad debts	9,20,000	9,94,000	9,94,000
Net Profit before tax	141,06,000	144,09,200	148,92,100
Provision for tax	13,22,000	14,45,000	15,00,000
Net Profit after tax	127,84,000	129,64,200	133,92,100
Less: Dividend	20,25,000	20,25,000	20,25,000
Net Profit after dividend	107,59,000	109,39,200	113,67,100