Corporate Finance, Module 24: “Financial Analysis and Planning”

Corporate finance module 24: Homework Assignment

(The attached PDF file has better formatting.)

Economic value added

ABC Insurance Company is financed by $500 million of equity and $500 million of debt. (The debt is through a holding company; this makes no difference for the financial analysis.)

The yield to maturity on ABC’s debt equals its coupon rate of 8% per annum. The risk-free rate is 5% per annum, the market risk premium is 7%, and ABC has a CAPM beta of 1.000. The corporate tax rate is 35%.

In 20X1, ABC paid $40 million in interest and earned $75 million in accounting income.

A. What is ABC’s after-tax debt payment?
B. What is ABC’s after-tax debt plus net income?
C. What is ABC’s weighted average cost of capital?
D. What is ABC’s economic value added (EVA)?