Example 1

Ruhi ltd is having equity share capital of Rs 1 Crore (10 Rs per share). For the purpose of expansion, they are planning to raise additional funds of 10 lakh using equity issue of 10 Rs. Per share and 5 lakh using debt at 7%. Calculate EPS considering tax rate of 40% if there earnings before interest and tax is 1 crore.

Example 2

Capital structure of Munjal ltd. consists of 3.5 lakh equity shares of 10 rs each. The company wants to raise additional capital of Rs. 35 lakh for buying a new factory. For expansion they have two alternative plans

a) Issue of share capital of 3.5 lakh shares (10 Rs. Each)
b) Issue of debentures of 35 lakh carrying 12% interest.

Calculate EPS for both of the above plans for two levels of PBIT, 14 lakh and 7 lakh. Determine the break-even PBIT for both alternative plans of financing. Tax rate 50%.

Example 3 Badshah Brothers are manufacturer of disposable pens. They manufacture and sales are 700 pens a year. The pens are sold at 10 Rs per unit having 4 Rs as variable cost, 2 Rs other selling and distribution cost and 1000 being fixed cost. Sales of company is expected to reach to 1100 in coming year. From above information calculate operating leverage.

Example 4

Capital structure of Zenga Ltd consists of 3 Crore equity shares. The company wants to raise additional fund of ₹ 15 crore using external financing considering three alternatives.

A) 0.5Issue 75,00,000 equity shares of ₹ 10 par at ₹ 20 each
B) Issue 45,00,000 equity shares of ₹ 10 par at ₹ 20 each and 60,00,000 preference shares of ₹ 10 par carrying 11 percent dividend.
C) Issue 15,00,000 equity shares of ₹ 10 par at ₹ 20 each and ₹12 crore of debentures carrying 14 percent interest rate.

The company's tax rate is 50 percent. What is the EPS – PBIT equation for these three alternatives?

What is the EPS – PBIT indifference point for alternatives A & B?

Example 5

A Ltd. Has a share capital of Rs. 1,00,000 divided into share of Rs. 10 each. It has a major expansion program requiring an investment of another Rs. 50,000. The Management is considering the following alternatives for raising this amount:

Issue of 5,000 equity shares of Rs. 10 each

Issue of 5000 12% preference shares of Rs. 10 each

Issue of 10% debentures of Rs. 50,000

The company's present Earning Before Interest and Tax (EBIT) are Rs. 40,000 per annum subject to tax @ 50%. You are required to calculate the effect of the above financial plan on the earnings per share presuming: (a) EBIT continues to be the same even after expansion (b) EBIT increases by Rs. 10,000

Example 6

The Rainbow Ltd. requires ₹ 10,00,000 for expansion of current product line. The fund can be raised using below three plans.

a) Issue of 1,00,000 equity shares at ₹ 10 per share.
b) Issue 50,000 equity shares at ₹ 10 per share and 5,000 debentures of ₹ 100 denomination bearing an 8% rate of interest.
c) Issue 50,000 equity shares at ₹ 10 per share and 5,000 preference shares at ₹ 100 per share bearing 8% rate of interest.

If the company's EBIT is ₹ 20,000, ₹ 40,000, ₹ 80,000, ₹ 1,20,000 and ₹ 2,00,000 for five years, calculate EPS under each of the three financial plans. Which alternative plan will you recommend? Justify your answer. Assume corporate tax rate to be 50%.

Example 7

PBIT of Company alexander is 1,00,000$ which is expected to increase to 1,20,000$. Being interest on debentures fixed at 60,000$ and tax rate of 50%, calculate company's financial leverage if their share capital consists of 20,000 equity shares.

Example 8

Consider example 3. If interest on debentures in the same example is 700 Rs and tax rate is 50% then calculate combined leverage if company holds 200 equity shares in the capital structure.