

10th Assignment

As the amount of debt increases the cost of capital decrease true or false give reason.

False: As the amount of debt increases the cost of capital does not necessarily decrease.

WACC is a calculation used to determine a company's average cost of capital from all sources including debt.

Increased financial distress costs:

Higher debt increases financial distress risk.

Moderate debt level can provide tax benefit increasing EBIT.

Debt can discipline management to optimise operation.

and equity while debt can be cheaper than equity due to tax deductibility of interest. Excessive reliance on debt can increase overall risk and costs.

* As a firm takes on debt more debt it increases its financial leverage. Investors and lenders may require a higher return to compensate for the increased risk leading to an increase in the overall cost of capital.