**Solution:**

(1)

To calculate the present value of lease, we add the present value of all the leases as follows:

Thus, the present value of all the operating lease comes out to be **$10,165.50 million**.

(2)

If we were to capitalize the operating leases, we need to create a liability for the same.

(a)

|  |  |  |  |
| --- | --- | --- | --- |
| JOURNAL ENTRY FOR LEASE CAPITALIZATION  (Amounts in millions of $) | | | |
| Date | Particulars | Debit | Credit |
| June 1, 2011 | Leased Assets  To Lease Obligations  (Being creation of a capital lease for the operational leases.) | 10,165.50 | 10,165.50 |

(b)

For the first year, the interest expense on the capitalized costs will be $10,165.50 x 0.1 = $1,016.55. The payment for the lease will be $1,794 million. Thus, the lease obligations will reduce by $1,794 - $1,016.55 = $777.45.

|  |  |  |  |
| --- | --- | --- | --- |
| JOURNAL ENTRY FOR LEASE CAPITALIZATION  (Amounts in millions of $) | | | |
| Date | Particulars | Debit | Credit |
| June 1, 2012 | Interest Expense  Lease Obligations  To Cash  (Being first payment.) | 1,016.55  777.45 | 1,794.00 |

(3)

The debt-to-equity ratio is given by:

If they capitalized all their operational leases, then the new value of the debt-to-equity ratio will become:

There is a very huge jump in the D/E ratio when the operational leases are capitalized, which indicates that FedEx might be making its leases operational to keep the D/E ratio in control as well.

A D/E ratio > 1 is always presumed to be an unstable company, which indicates that FedEx needed to keep their operational leases mainly.