Nike Inc. Cost Of Capital

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**Executive Summary**

The report focuses on Nikes Inc.'s cost of capital and its financial importance for the firm and its future investors. Nike Inc. has not increased its revenue following the cost of capital evaluation. Since 1997, the company has progressed with a revenue of $9 million. Also, most of their recent net income fell from $800 million to $580 million, as seen in exhibit 1, and their shares in footwear also dropped from 48% to 42% in 2000. Additionally, its recent supply chain issues and adverse effects of a strong dollar have negatively affected its recurrent growth in revenue. The following vital steps are opted for to boost revenue through growth at the top line level and its operating performance. The Nike Company is mandated to develop more of their athletic footwear in a stipulated area they have stayed from, which changes the price segment. A higher focus is placed on increasing sales in the apparel line. However, changes in its capital level raise the target goal of having long-term revenue growth of 10% as opposed to the previous 8%, and an increase in earnings growth surpasses 15%.

With the current inflation in the economy, Kimi Ford is about to enter a board meeting and evaluate the WACC, which will help present a better judgment call on the company's financial strategy. Ford has created a discounted cash flow in which she obtained a 12% discount rate, overvaluing Nike's $42.09 shares and also sensitive analysis in which Nike has undervalued at an 11.17% discount rate. The major purpose of calculating the WACC is to analyze Nike's Cost of capital, which includes common and preferred stocks as well as short and long-term debt that the investors have chosen to invest in. The cost of capital represents the firm's financing cost and the minimum rate of return that the project must earn to increase the firm's value. This is done to get a clearer cost of capital for the firm inputs. However, the report also evaluates how a single cost was chosen due to the same level of risk through having a separate business segment. The analysis shows that Nike Inc.'s common stock is undervalued, in contrast to Kimi Ford's assumption of 7% WACC, obtained from the calculated WACC.

**Calculations**



The weights of the equity and debts are calculated using the market value of equity, which is analyzed as follows;

The market value of equity =

Due to a lack of vital information on the market value of debt, we prefer to use the book value for the calculation given in Excel. Market value debt = Therefore, from computation, the weight of equity gives us 10.19%. Next is the Mve, the stock price in the Yahoo Finance Times. The outstanding shares have a value of $11427.435. For the cost of debt, we calculate the current yield to maturity of the company bond to represent Nike's current cost of debt, and using a financial calculator and semiannual view, the value becomes 3.58%, So Rd is 7.16% since the value initially was calculated semi-annually. The cost of equity is analyzed using the 20-year T-bond rate to represent a risk-free rate, as the rate of return of a T-bond with 20 years of maturity is the longest available rate. So Rf = 5.74%, and the geometric mean of market risk premium is 5.9%. The most recent beta is valued at B =0.69, which gives the Re a value of 9.81%. The overall average WACC for both becomes 7.87%.

**Sources of Data**

All of the information given is vital for calculating the WACC for Nike Inc. as it can be derived from financial statements found in Yahoo Finance. The components necessary for calculating the weights are found in the balance sheet, such as the current portion of LTD, notes payable, and outstanding shares. One can locate the variable in the income statement for the cost of debt and tax rate. Regarding issues associated with the cost of equity, the source for the Rf is the US treasury yield curve rates. Therefore, for Kimi Ford to make a valid decision regarding investment in Nike Company, she must accurately compare the calculated WACC to the sensitivity of equity value and discount rate, as shown in Exhibit 2.

It is valid that the sensitivity chart in Exhibit 2 is stated at a discount rate of 11.17%. However, Nike's current share price is fairly valued at $42.09. Therefore, if a discount rate is to be calculated below 11.17%, then the company would be undervalued in the current market, but if the discount rate is higher than 11.17%, then Nike's share price would be considered overvalued as in contrast with the current share price. Lastly, the value outcome of WACC is estimated at 7.87%, which is below the estimated value, and thus, we believe that Nike shares are currently undervalued in the market. Outcome belief speculates that Nike's company, based on a WACC of 7.87%, should fall somewhere between $55.68 and $61.25, and thus, Kimi Ford should recommend adding Nike shares to the Nike stock fund as based on its analysis.

**Effects of change on WACC**

If the company is underestimated, then the Nike firm tends to be in a safer environment than an overestimated value, where the company tends to be a riskier investment. In Nike's firm case, their stock is undervalued, suggesting that there is a larger room for growth and great room for seeking an initial plan to expand the appeal and midpoint of the price for the footwear. The outcome suggestion on this matter shows that having a long-term investment is considered riskier and safe for the investment.