

Topic: WACC (Weighted Average Cost of Capital)

- the expected rate of return on a portfolio of all the securities of the firm
- the discount rate for the NPV evaluation of new projects of similar risk
- the minimal acceptable rate of return on firm's portfolio
- the rate of return expected to earn on firm's average-risk investments
- the discount rate only for a project with similar risk as that on firm's existing business
- weighted average of $[r_D(1-T_c)]$ and $[r_E]$
- lower cost of debt because interest payments are tax deductible
- If the expected IRR of project $>$ WACC, then the project will have positive NPV.
- If there are no corporate taxes, changing capital structure does not affect the WACC (as well as β_A and r_A). [since changing capital structure does not affect the risk of future CFs.]