32 Lecture - MGT201

Important Subjective

1. **What is financial leverage and how does it impact a company's return on equity (ROE)?**
   Answer: Financial leverage refers to the use of debt financing to fund a company's operations. When a company uses debt, it can amplify its returns on equity, but it also increases the risk of losses. The impact of financial leverage on ROE depends on the company's ability to generate returns that exceed the cost of debt.

2. **How does a company's capital structure impact its cost of capital?**
   Answer: A company's capital structure, or the mix of debt and equity financing it uses, can impact its cost of capital. Generally, using more debt financing can lower a company's cost of capital, but also increase its risk. Using more equity financing can increase a company's cost of capital, but also decrease its risk.

3. **What is the break-even point and how does it relate to a company's capital structure?**
   Answer: The break-even point is the point at which a company generates enough revenue to cover its fixed and variable costs. A company's capital structure can impact its break-even point by affecting the amount of fixed costs it has. Using more debt financing can increase a company's fixed costs, while using more equity financing can decrease them.

4. **What are the benefits of using debt financing?**
   Answer: Some benefits of using debt financing include lower cost of capital, tax advantages, and the ability to leverage returns on equity.

5. **What are the risks of using debt financing?**
   Answer: Some risks of using debt financing include the potential for bankruptcy, the need to make interest payments, and the risk of default if the company is unable to make payments.

6. **How does a company's financial leverage impact its risk profile?**
   Answer: Financial leverage can increase a company's risk profile by increasing the risk of bankruptcy or default. However, it can also increase the potential for returns on equity.

7. **How can a company determine its optimal capital structure?**
   Answer: A company can determine its optimal capital structure by balancing the benefits and risks of debt and equity financing. This may involve considering factors such as its cost of capital, risk profile, and ability to make interest payments.

8. **How does a company's capital structure impact its ability to raise funds?**
   Answer: A company's capital structure can impact its ability to raise funds by affecting its perceived riskiness to lenders and investors. Generally, a company with more debt financing may be seen as riskier and may have a harder time raising funds than a company with more equity financing.

9. **How can a company adjust its capital structure over time?**
   Answer: A company can adjust its capital structure over time by raising or lowering the amount of debt or equity financing it uses. This may involve refinancing debt, issuing new equity, or repurchasing existing equity.

10. **How does a company's cost of debt and cost of equity financing impact its overall cost of capital?**
Answer: A company's cost of debt and cost of equity financing are both components of its overall cost of capital. The relative weight of each component in the company's capital structure can impact its overall cost of capital. Generally, the higher the proportion of debt financing, the lower the overall cost of capital, but also the higher the risk.