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A General Formula for the Wacc

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Abstract


Recent controversies testify that the tax shield valuation remains a hot topic in the financial literature. Basically, two methods have been proposed to incorporate the tax benefit of debt in the present value computation: The adjusted present value (APV), and the classical weighted average cost of capital (WACC). This note clarifies the relationship between these two apparently different approaches by offering a general formula for the WACC. This formula encompasses earlier results obtained by Modigliani and Miller (1963) and Harris and Pringle (1985).

Keywords: WACC, Adjusted present value, Tax shield, Return on equity

JEL Classification: G30, G32, E22

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