

For we were saved in this hope, but hope that  
is seen is not hope; for why does one still  
hope for what he sees? But if we were hope  
for what we do not see, we eagerly wait for  
it with perseverance. (Romans 8:24-25)

## CONTENTS

Approval of Thesis	ii
Wise Words	iii
Contents	iv
Acknowledgments	vi
Abstract	vii
Chapter I INTRODUCTION	1
I.1. Significance of the Study	1
I.2. Company's Problem	1
I.2. Purposes	2
I.3. Method of Research and Data Collection	2
I.4. Method of Analysis	2
I.5. Scope and Organization of the Study	3
Chapter II THE THEORETICAL FRAMEWORK OF CAPITAL STRUCTURE AND COST OF CAPITAL	5
II.1. Definition and Characteristic of Capital	5
II.2. The Capital Tradeoffs	5
II.2.1. Advantages of Borrowing	7
II.2.2. Disadvantages of Borrowing	8
II.3. The Cost of Capital Approach	10
II.3.1. Definition and Calculation the Cost of Capital	10
II.3.2. The Role of Cost of Capital in Optimal Capital Structure	12
II.3.3. Assumptions in Cost of Capital Approach	13
II.3.4. Practical Framework for Analyzing Capital Structure	14
II.3.5. Betas from Cross-Sectional Regressions	18
II.4. Framework for Capital Structure Changes	18
II.4.1. Factors to be Considered in Quick or Gradual Change	19
II.4.2. The Process of Capital Structure Change	20
II.4.3. Summarized Framework for Analyzing Optimal Capital Structure	21
Chapter III OBSERVATION AT THE COMPANY'S CAPITAL STRUCTURE AND COST OF CAPITAL	23
III.1. Company's Short Background	23
III.1.1. General	23
III.1.2. Organization and Management	24
III.2. Company's Capital Structure	24
III.2.1. Debt Capital	24

	III.2.2. Equity Capital	30
	III.3. Company's Cost of Capital	32
	III.3.1. Calculating Cost of Debt	32
	III.3.2. Calculating Cost of Equity	33
	III.3.3. Calculating Weighted Average Cost of Capital	35
Chapter IV	ANALYSIS AND EVALUATION	36
	IV.1. Cost of Debt	36
	IV.2. Cost of Equity	37
	IV.3. Cost of Capital	39
	IV.4. Evaluation	39
Chapter V	SUMMARY	45
	V.1. Conclusion	45
	V.2. Recommendation	46
Bibliography		
Appendix : Consolidated Financial Statements of PT Riau Andalan Pulp & Paper and subsidiary for the year ended 31 December 1997 and 1996 with Independent Auditors' Report Thereon		