

Ans-2 Under capitalization means the

Under capitalization may be preferred in those cases where there is genuine rise in earning, better financial planning and efficient management.

The rate of dividend will be very high and the market price of the shares will also be very high. But this situation also leads to certain evil consequences.

Remedies of Under capitalization

① splitting up of shares :- The

director should split up the share in order to decrease the rate of earning per share. It does not affect the total capitalisation because only the par value of the stock is reduced.

② INCREASE PAR VALUE OF SHARES

Under capitalisation may be remedied by increasing the par value of equity shares by revising upwards the value of asset. This will decrease in the rate of earning per share. The company may offer shareholders a share split-up and an increase in par value.

③ ISSUE OF BONUS SHARES

The most widely used and effective remedy for under capitalisation is the conversion of reserves into shares. This will reduce both dividend per share and the overall rate of earnings.

④ ISSUE OF SHARES AND DEBENTURES

Where under-capitalisation is due to inadequate capital more share and debentures are issued to the public.