Capital budgeting - capital investment appraisal

Capital Investment Appraisal a) Machine A Present Value Purchase Price (1570000) Working Capital (47000) Running cost

(151671)

Overhaul Cost

(73494)

Disposal Cost

(51072)

Labor Cost Saved

2823414

WC Released

21432

Net Present Value

£ 951609

b) Report to the Managing Director:-

After carefully combining all the information provided by salesmen and management accountant, I have performed an NPV analysis of the both proposed project's cash flows. Results have shown that NPV of Machine B is 80% greater than NPV of machine A. So, Temple Ltd. should install Machine B for more effective automation process and to reduce its production costs and operate much more cheaply.

But still there are some factors that make us reluctant in taking this decision, as there is no information available about the production capacities of both machines so we can not say accurately that which machine is more beneficial, as production capacity and quality of Machine A may be many times higher than B and it may generate more cash inflows in six years than what Machine B may generate in eight years. So, we can not make any exactly educated decision until we have information, at least about both machine’s production capacities.