

# Investments critical thinkings examples

[Finance](#), [Investment](#)



**Solution**

- Give a general comparison/breakdown of the two opportunities (separately); for example what are the risks and benefits associated with each?

**Investing in the means of production (innovation) or, for example, bank deposit, carries certain risks.**

In a market economy, innovation is an effective means of competition , as the lead to the creation of new needs , to reduce production costs, to encourage investment , to enhance the ranking producer of new products, to discover and reach new markets, including foreign ones.

**In the investment and financial management at risk realize the degree of uncertainty :**

- in the system reaches the intended target at a chosen method of achieving this goal ;

**System falls within the field of risk factors in the presence of three conditions:**

- the system tends towards a certain goal ;
- selection is carried out under conditions of uncertainty ;
- system has a range of ways to achieve it .

For low-risk instruments are giving conditionally guaranteed income .

Percentage yield of this group is comparable to the yield of the most reliable banks deposits , and its value is an average of 5 to 7 % per annum. Yield listed instruments is practically guaranteed , and the invested capital will be returned to the investor , at least in the amount of absolute value. The only

risk here may be a failure of the state to fulfill its obligations . However, if we talk about savings programs , some insurance companies take the guarantee payments even in this case , because they themselves are reinsured with the most reliable foreign insurers.

- What is the NPV of the purposed project?

### **Computing NPV (Using Excel):**

$$NPV = \sum_{i=0}^n \frac{C_i}{(1+r)^i} = \$4,214.08$$

- What is the IRR of the purposed project?

### **Computing IRR (Using Excel):**

$$\sum_{i=0}^n \frac{C_i}{(1+IRR)^i} = 0 \Rightarrow IRR = 0.07298 = 7.298\%$$

- What is the pay back period on the purposed project?

Payback period is a period of time necessary to revenues generated by investments , covered the cost of investment . For example, if the project requires an investment of (outgoing cash flow) in \$2000, and this investment will return to \$1000 per year , we can say that the payback period is two years. At the same time value of money is not considered. This figure determines the sequence of calculation of net income (Present Value) for each period of the project. The point at which the net income will take a positive value will be the point of return.

### **Look at the outflow:**

We can see that on 8th year, the outflow becomes positive. Hence, the payback period is 8 years.

- Which option, investment or new product line would you recommend and why?

We have to compare two options. First option is to invest \$250, 000 with the rate of return of 7% - it + \$17, 500. The second option is to invest in new production line – then we will get +\$4, 214. 08 plus the present value of salvation:

$$300001 + 0, 0710 = \$15, 250. 48$$

$$15, 250. 48 + 4, 214. 08 = \$19, 464. 56$$

As \$19, 464. 56 is higher than \$17, 500, it is preferred to invest in new production line.

- What if the salvage value was only worth \$20, 000, would your decision change and why? Provide supporting details to justify.

**We have to compare the net present values once again. The present value of salvation this time will be:**

$$200001 + 0, 0710 = \$14, 381. 06$$

$$\$14, 381. 06 + 4, 214. 08 = \$18, 595. 14$$

Since \$18, 595. 14 still higher than \$17, 500, our decision will not be changed.

- Do some research on your own and suggest what type of investment (real world) would achieve a 7% return today-justify your response to be included at the end of the paper separate paragraph.

In my opinion, the real world example of such investment can be an investment in mixed type bond with the return payment in the start of the accounting period.

## Sources

Baker, Samuel L. (2000). " Perils of the Internal Rate of Return". Retrieved January 12, 2007.

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