

# [Financial management](https://assignbuster.com/financial-management-essay-samples-2/)

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Year 0 Year Year 2 Year 3 Year 4 Year 5 Year 6 Year 7 Year 8 Operating Activities                   Revenue 0 950000 1500000 1500000 1500000 1500000   
1500000   
1500000   
1500000   
Direct Cost   
0   
522500   
825000   
825000   
825000   
825000   
825000   
825000   
825000   
Incremental cost   
0   
80000   
80000   
80000   
80000   
80000   
80000   
80000   
80000   
Depreciation   
0   
200000   
200000   
200000   
200000   
200000   
  
  
  
EBT   
0   
147500   
395000   
395000   
395000   
395000   
595000   
595000   
595000   
Tax (35%)   
0   
51625   
138250   
138250   
138250   
138250   
208250   
208250   
208250   
Net Income   
0   
95875   
256750   
256750   
256750   
256750   
386750   
386750   
386750   
Add: Depreciation   
0   
200000   
200000   
200000   
200000   
200000   
  
  
  
Cash flow from operating activities   
0   
295875   
456750   
456750   
456750   
456750   
386750   
386750   
386750   
Investing activities   
  
  
  
  
  
  
  
  
  
Initial investment   
-1000000   
0   
0   
0   
0   
0   
0   
0   
0   
Additional net investment   
-200000   
0   
0   
0   
0   
0   
0   
0   
200000   
Cash flow from investing activities   
-1200000   
0   
0   
0   
0   
0   
0   
0   
200000   
Cash flow from O and I activities   
-1200000   
295875   
456750   
456750   
456750   
456750   
386750   
386750   
586750   
Note: Because we have no additional info about the WC we assume that it will not change over the projects life. Then Working Capital Change for each year Yi is:   
Change in Working Capital = Previous Year WC - Current WC = 0 (i= 1 to 7) and ChWC0 = -$100, 000 at year 8 and this amount will be recovered during year 8.( (McLaney, 2009)   
NPV:   
The discounted value of all ‘ Cash inflows’ is $2275689. 26.   
NPV= Initial investment – discounted cash inflows which is:   
NPV= (1, 200, 000)+ 2275689. 26   
NPV= $1, 075, 689. 26   
(Shim & Siegel, 2008)   
Payback period:   
At the end of two years the initial investment recovered would be equal to:   
295, 875+ 456, 750= 752625   
Therefore, the payback period is 2 years and   
Payback period: 2 years and 353 days (Warren, Reeve, & Duchac, 2011)   
a)   
The project would be accepted on the basis of NPV and payback period. This project answers to both the queries in positivity. The NPV of this project is $1, 075, 689. 26 which is substantial relative to the project. Moreover, the project would be accepted on the basis of payback method because of its initial investment recovery within 3 years. The company has a policy of not accepting projects with a payback period of over 3 years and this project will recover its initial investment in less than 3 years. (Puxty, Dodds, & Wilson, 1988)   
b)   
Company’s analysis of the project is based on NPV and payback period. Initial investment has large weight age in both of these analyses therefore; our analysis would change if addition investment in land building is required. Our NPV would decline and payback period will increase substantially. If the additional investment is more than $1, 075, 689. 26 then the project would not be accepted on the basis of NPV. Moreover, its payback period would drastically increase leading to refusal of the project’s proposal.   
Works Cited   
McLaney, E. (2009). Business finance: theory and practice. Pearson Education Canada.   
Puxty, A. G., Dodds, J. C., & Wilson, R. M. (1988). Financial management: method and meaning. Taylor & Francis.   
Shim, J. K., & Siegel, J. G. (2008). Financial Management. Barrons Educational Series.   
Warren, C. S., Reeve, J. M., & Duchac, J. (2011). Managerial Accounting. Cengage Learning.