Lessons 25 & 26: Evaluating Business Investments and Capital Budgeting

Part A: Payback Period

A machine costs $120,000. Annual cash inflows: Year 1 $40,000 | Year 2 $45,000 | Year 3 $35,000 | Year 4 $30,000

Year	Cash Inflow	Cumulative Cash Inflow	Recovered?
1	$40,000		
2	$45,000		
3	$35,000		
4	$30,000		

Payback Period = _____ years

Part B: NPV Analysis

Discount rate = 10%. PV factors: Year 1 = 0.909, Year 2 = 0.826, Year 3 = 0.751, Year 4 = 0.683

Year	Cash Flow	PV Factor	Present Value ($)
1	$40,000	0.909	
2	$45,000	0.826	
3	$35,000	0.751	
4	$30,000	0.683	
Total PV of Inflows			
Less: Initial Investment	($120,000)		
NPV			

Decision: Should the company invest? Why?

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