**Making Investment Decisions A2 Business Studies Unit 3**

***Scenario****: You are part of Walkers (the crisp company)’s management team. You are about to embark on an* ***investment strategy*** *which will have the objective of making the companies production techniques more efficient by buying new machinery. You are however unsure of the merits of buying different machinery. Therefore you must use* ***Investment Appraisal Techniques*** *to assess which option is the best for Walkers. You have been provided with the following* ***cash inflow and cash outflow*** *figures for the two options.*

|  |  |  |
| --- | --- | --- |
|  | **Machine A** | **Machine B** |
| Initial Cost | £750,000 | £310,000 |
| ***Inflows:*** |  |  |
| Year 1 | £150,000 | £125,000 |
| Year 2 | £200,000 | £127,000 |
| Year 3 | £260,000 | £140,000 |
| Year 4 | £260,000 | £140,000 |
| Year 5 | £300,000 | £130,000 |
| ***Outflows:*** |  |  |
| Maintenance Costs | £7,500 per year | £15,000 per year |

To conduct the three methods of investment appraisal, a table must be drawn up for both options to judge which is the best. This table must show:

* Year
* Cash Out
* Cash In
* Net Cash Flow (Cash in – Cash out)

The table for Machine A has been drawn up on the other side of this sheet…..

**Net Cash Flow for Machine A**

|  |  |  |  |
| --- | --- | --- | --- |
| **Year** | **Cash Out** | **Cash In** | **Net Cash Flow** |
| **0** | £750,000 | 0 | (£750,000) |
| **1** | £7,500 | £150,000 | £142,500 |
| **2** | £7,500 | £200,000 | £192,500 |
| **3** | £7,500 | £260,000 | £252,500 |
| **4** | £7,500 | £260,000 | £252,500 |
| **5** | £7,500 | £300,000 | £292,500 |

*You are now to calculate the Net Cash Flow for Machine B*

**Net Cash Flow for Machine B**

|  |  |  |  |
| --- | --- | --- | --- |
| **Year** | **Cash Out** | **Cash In** | **Net Cash Flow** |
| **0** |  |  |  |
| **1** |  |  |  |
| **2** |  |  |  |
| **3** |  |  |  |
| **4** |  |  |  |
| **5** |  |  |  |

***Now use the steps in your notes to calculate:***

* Payback
* Average Rate of Return
* Net Present Value