

Syllabus reference

Determine the financial consequences of dealing with medium-term projects, in particular the importance of accounting for time value of money

Question 1

Company T has decided to undertake a project, which will last four years and have a residual value of £0.

The initial cost and revenues are as follows:

| | Year 0 £'000 | Year 1 £'000 | Year 2 £'000 | Year 3 £'000 | Year 4 £'000 |
|---------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Capital expenditure | (200) | | | | |
| Revenue | | 50 | 150 | 100 | 100 |

The cost of capital is 12%. Assuming that the forecasts provided are correct, which of the following statements most accurately describes the consequences of undertaking the project?

- A. Company T will increase its value by £200,000
- B. Company T will increase its value by £99,000
- C. Company T will increase its value by £400,000
- D. Company T will increase its value by £78,000