

STUDY GUIDELINE FIN3701 - STUDY UNIT 2

1 GENERAL

This study unit is covered in chapter 9 of the prescribed textbook. The study unit creates problems for students who do not know how to use their calculator. It is important to know how to use your calculator in order to minimize the time you spend on each question in study unit 2 and 3. However, interest factor tables (textbook, pages 758-765) will be provided in the exam.

Please note: Students do not need to know both methods (calculator use and interest factor tables), calculator use is sufficient. This study unit is a continuation of study unit 1. The cash flows discussed and calculated using the different formulae in study unit 1 are used to calculate the Payback period, net present value (NPV) and internal rate of return (IRR).

2 FORMAT OF ASSESSMENT

The content of this study unit will be assessed by means of multiple choice questions. No formulae will be provided in the examination for this study unit.

You will not be required to construct any of the graphs in this study unit.

3 IMPORTANT AREAS IN THE STUDY UNIT

Pay attention to the following:

- The calculation, understanding and interpretation of the payback period.
- The calculation, understanding and interpretation of the NPV.
- The calculation, understanding and interpretation of the IRR.
- The NPV and IRR accept/reject decision criteria.

4 Study Guide Errata

Areas to correct:

Page 14: Project S payback period

$$P_b = 1 + 0.33 = 1.3 \text{ years}$$

Areas to skip:

Page 17-18: Modified IRR (MIRR)

5 Textbook Errata

Areas to correct:

Page 387: Project A and B NPV calculation

NPV_A:

420 000 ± CF_j

140 000 CF_j

5 N

10 I/YR

NPV (DISPLAY: 110 710)

NPV_B:

450 000 ± CF_j

280 000 CF_j

120 000 CF_j

100 000 CF_j

100 000 CF_j

100 000 CF_j

5 N

10 I/YR

NPV (DISPLAY: 109 244)