BUST 211: SPECIAL CAT

1. The following are the projected incremental earnings before interest, depreciation and tax (EBDIT) for a firm that is contemplating a factory automation project. The project is expected to cost Ksh. 10 million, and this cost is to be written off over a period of 5 years.

|  |  |
| --- | --- |
| YEAR | EBDIT (CASH INFLOW/ OUTFLOW (Ksh. Millions)) |
| 0 | -10 |
| 1 | 3 |
| 2 | 4 |
| 3 | 7 |
| 4 | 3 |
| 5 | 4 |

The cost of capital for the firm is 12%, and the tax rate is 30%.

REQUIRED

1. The cash flows for the company for each of the years 1- 5 (5 mks)
2. An evaluation of whether the project is viable using the NPV method of evaluating investments (13 mks).
3. Discuss the limitations of the capital asset pricing model (12 mks)