**8th WEEK ASSIGNMENT**

1 Answer true or false to the following statements and state the reason.

a. The return on equity for a project will always be higher than the return on capital on the same project.

b. If the return on capital is less than the cost of equity, the project should be rejected.

c. Projects with high financial leverage will have higher interest expenses and lower net income than projects with low financial leverage and thus end up with a lower return on equity.

d. Increasing the depreciation on an asset will increase the estimated return on capital and equity on the project.

e. The average return on equity on a project over its lifetime will increase if we switch from straight line to double declining balance depreciation.

2 Identify cash flow-based decision rule.

**ACTIVITIES**

1. You have been given the following information on a project:

* It has a 5-year lifetime
* The initial investment in the project will be Rs.25 million, and the investment will be depreciated straight line, down to a salvage value of Rs.10 million at the end of the fifth year.
* The revenues are expected to be Rs.20 million next year and to grow 10% a year after that for the remaining 4 years.
* The cost of goods sold, excluding depreciation, is expected to be 50% of revenues.
* The tax rate is 40%.

a. Estimate the pre-tax return on capital, by year and on average, for the project.

b. Estimate the after-tax return on capital, by year and on average, for the project.

c. If the firm faced a cost of capital of 12%, should it take this project.