Quiz: 2/8/12 Name Key

Quiz: Your firm is considering whether or not to build a new factory. Based on the following information, should your firm build the factory if the cost of capital for the factory equals 9% per year?

The factory can be built for a total of $1,200,000. Of this cost, $400,000 would be spent today and $800,000 would be spent six months from today. In addition to the cost to build the factory, the firm spent $125,000 one year ago developing the product that will be manufactured at the new facility. The factory will generate its first monthly cash flow of $60,000 nine months from today. After this initial cash flow, the cash flows will grow by 0.5% each through the closing of the plant five years from today. Net working capital associated with the factory will jump to $300,000 six months from today and will remain at this level until the plant is closed five years from today.

Note: You don't have to solve anything. Just set it up and tell me how you would make a decision (if you had solved it).

−3 if include sunk cost

+5 +2 +3 10

$$r\left(\tfrac{1}{12}\right) = (1.09)^{\wedge\frac{1}{12}} - 1$$

+2 +3 +2 +2 +3 +5 +2 +2 +3 +3 +3 +3 +2 +3

$$NPV = -400{,}000 - \frac{(800{,}000+300{,}000)}{\left(1+r\left(\frac{1}{12}\right)\right)^{6}} + \left(\frac{60{,}000}{r\left(\frac{1}{12}\right)-.005}\right)\left(1-\left(\frac{1.005}{1+r\left(\frac{1}{12}\right)}\right)^{52}\right)\left(\frac{1}{1+r\left(\frac{1}{12}\right)}\right)^{8} + \frac{300{,}000}{(1.09)^{5}}$$

10 12 6 8

WSJ1: A group of top European banks is disclosing that they
a. plan to merge into a European super bank
b. have suspended their operations in Syria
C. didn't borrow money under the European Central Bank's bank-lending program
d. intend to expand their operations in the United States and Canada
e. no longer hold any Greek sovereign debt

WSJ2: The Wall Street Journal reports that key concessions by ____________ over its holdings of Greek government bonds will contribute to a reduction of the country's debt burden and smooth the path toward a new bailout for the country.
a. Credit Suisse
b. the Federal Reserve
c. Goldman Sachs
d. the International Monetary Fund
E. the European Central Bank