

A STUDY ON CAPITAL BUDGETING

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ABSTRACT

The project entitled “A STUDY ON CAPITAL BUDGETING IN THE INDIA CEMENTS LIMITED AT DALAVOI, ARIYALUR”. The study was set out to determine the capital budgeting techniques used in investment appraisal decisions. Capital budgeting techniques are useful tools to administrators in managing resources. The details regarding the history, finance and inventory policies of the company were collected from records, reports and profile of the company. Data analysis was carried out and findings are listed. Suitable suggestion has been provided.

The tools used in this study where pay-back period, Accounting rate of return, Net present value method, Profitability index, Internal Rate of Return.This study also gives an overall picture of financial position of the firm for five years. From the study, we found that the financial position of the firm is satisfactory.

INTRODUCTION

Capital budgeting involves choosing projects that add value to a company. The capital budgeting process can involve almost anything including acquiring land or purchasing fixed assets like a new truck or machinery. Corporations are typically required, or at least recommended, to undertake those projects which will increase profitability and thus enhance shareholders' wealth. However, what rate of return is deemed acceptable or unacceptable is influenced by other factors that are specific to the company as well as the project. For example, a social or charitable project is often not approved based on the rate of return, but more on the desire of a business to foster goodwill and contribute back to its community. Capital budgeting is concerned with how firms should evaluate projects and make capital investment decisions. Numerous factors enter into the formulation and implementation of corporate investment policy

REVIEW OF LITERATURE

Kengatharan Lingsiya (2016) the main purpose of this research was to delineate unearth lacunae in the extant capital budgeting theory & practice during the last two decades and ipso facto become springboard for future scholarships.

Weerakun Banda YatiwelleKoralalage (2014), the use of capital budgeting techniques in large businesses: Evidence from Sri Lanka, International Journal of Arts & Commerce, 3(9), pp. 77-84, this research article examines the use of capital budgeting techniques & investigates a number of variables & associations relating to capital budgeting practices in large listed companies in Sri Lanka. From the study it was found that Net present value, Accounting rate of return, Payback period, Internal rate of return & Profitability index are used to evaluate investment project.

Ghahremani M. et.al. (2012),Capital budgeting technique selection through four decades: with a great focus on real option, International journal of business and management, 7(17), pp. 98- 117, this paper aims to provide a review and analysis on capital budgeting techniques from 1970- 2012 in developing & developed countries regarding the most effective factors on selecting techniques.

OBJECTIVES OF THE STUDY

- ❖ To determine the types of capital investment undertaken and the methods of appraisal used.
- ❖ To measure the present value of money invested.
- ❖ To study the preferences between Net Present Value(NPV) and Internal Rate of Return (IRR) methods.
- ❖ **To make any suggestions if any for improving the financial position of the company.**

DATA ANALYSIS AND INTERPRETATION

4.1.1 PAY-BACK PERIOD

Pay –back period is the period taken by the firm to get back the investment. The pay-back period shows number of years / month / days required by the firm to get back its investment invested in the project.

Initial investment

Pay-back period = -----

Annual cash inflow

CALCULATION OF ANNUAL CASH INFLOWS:

Annual cash inflow =profit after tax +depereciation

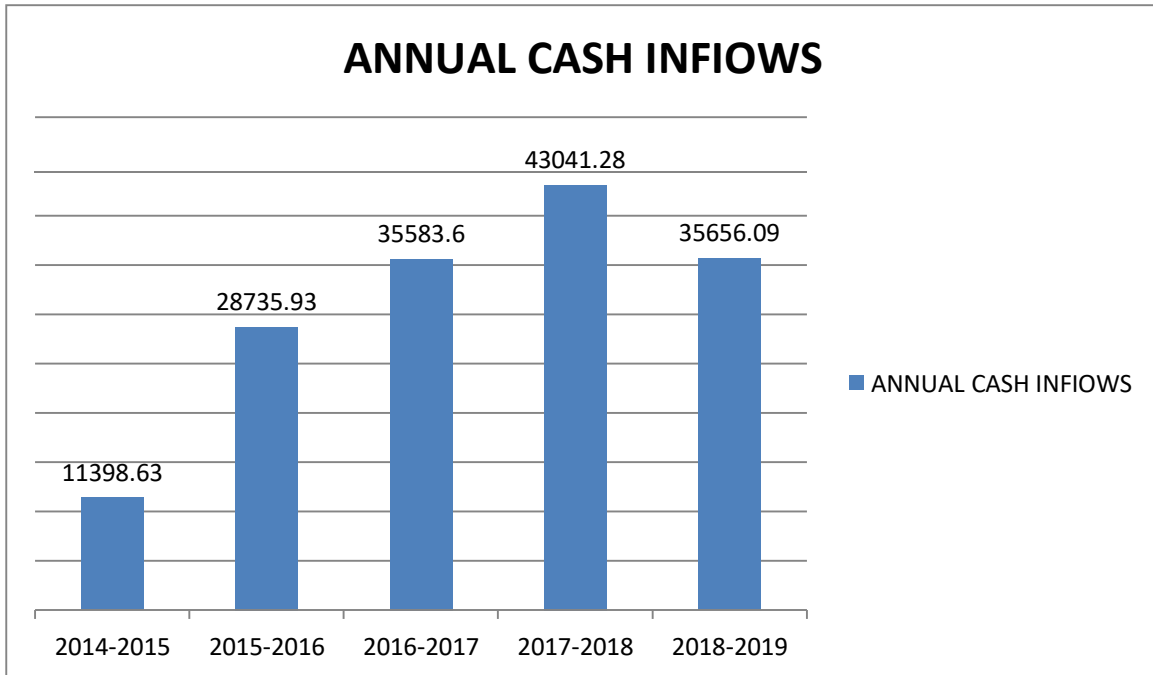
TABLE 1

YEAR	PROFIT AFTER TAX	DEPRECIATION	ANNUAL CASH INFLOWS	CUMULATIVE CASH INFLOWS
2014-2015	-16240.36	27638.99	11398063	11398.63
2015-2016	2944.95	25790.98	28735.93	40134.56
2016-2017	13781.27	21802.33	35583.6	75718.16
2017-2018	17335.02	25706.26	43041.28	118759.44
2018-2019	10061.97	25594.12	35656.09	154415.53

INTERPRETATION

The above table shows the calculation of annual cash inflows. The highest cash inflow was during the period of 2017-2018 is 43041.28 . It also shows the fluctuations in profit after tax and depreciation of past five years .

FIGURE 1



AVERAGE RATE OF RETURN

This method is also known as Total Income method or financial statement method. Here Average investment is being considered for the purpose of calculation, it is called ARR.

$$\text{Average rate of return} = \frac{\text{Average annual earning}}{\text{Average investment}} \times 100$$

$$\text{Average investment} = \text{original investment} / 2$$

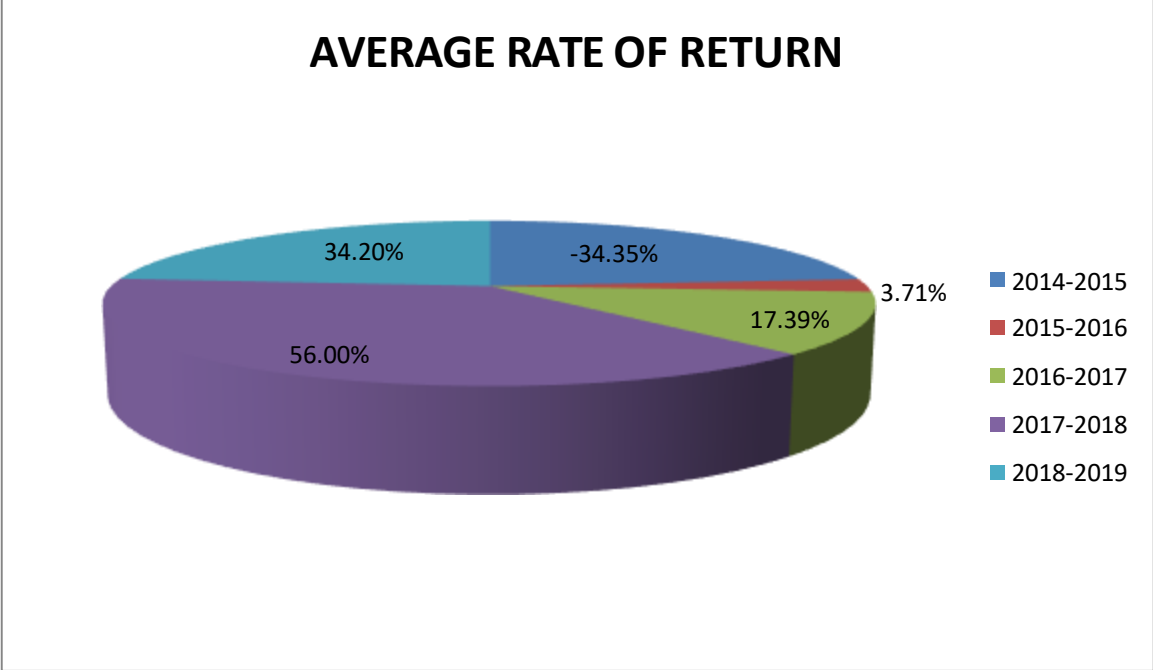
TABLE 2

YEAR	PROFIT AFTER TAX	AVERAGE INVESTMENT	AVERAGE RATE OF RETURN
2014-2015	-16240.36	47276.97	-34.35%
2015-2016	2944.95	72261.12	3.71%
2016-2017	13781.27	79234.67	17.39%
2017-2018	17335.02	30950.38	56.00%
2018-2019	10061.97	29417.00	34.20%

INTERPRETATION

The above table shows the average rate of return during the year 2017-2018 was 56% In the year 2018-2019 the ARR was decreased to 34.2% In the year 2016-2017 the ARR was decreased to 17.39% In the year 2015-2016 and 2014-2015 the payback period was decreased to 3.71% and -34.35%.

FIGURE 2



NET PRESENT VALUE

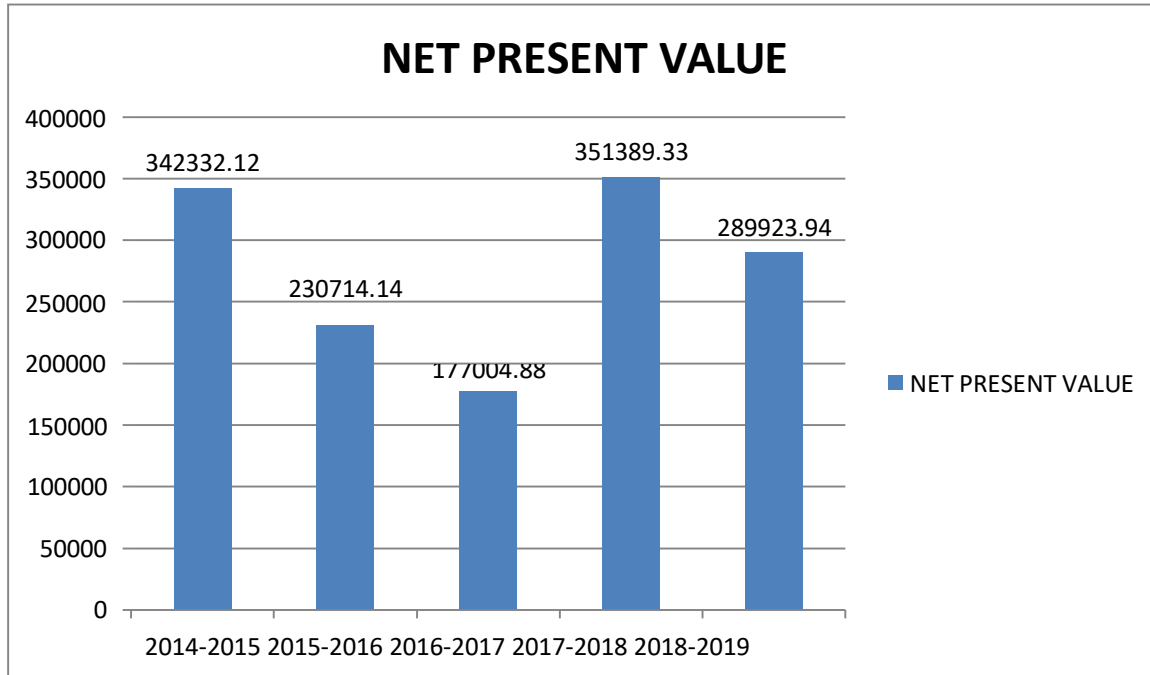
Net present value = Total Present Value of Cash Inflow – Initial Investment
TABLE

YEAR	CASH INFLOW	P.V.FACTOR @ 10%	P.V. FACTOR OF CASH INFLOW	CASH OUTFLOW	NET PRESENT VALUE
2014-2015	480622.75	0.909	436886.07	94553.95	342332.12
2015-2016	471230.5	0.826	389236.39	158522.25	230714.14
2016-2017	446703.37	0.751	335474.23	158469.35	177004.88
2017-2018	605109.97	0.683	413290.10	61900.77	351389.33
2018-2019	561607.01	0.621	348757.95	58834.01	289923.94

INTERPRETATION

The above table shows the net present value during the year 2017-2018 was 351389.33 . In the year 2014-2015 the net present value is decreased to 342332.12 in the year 2018-2019 the net present value decreased to 289923.94 in the year 2015-2016 and 2016-2017 in the net present value decreased to 230714.14 and 177004.88.

FIGURE 4.1.6



FINDINGS

- ❖ Pay-back period indicates that the time taken to recover the initial investments of project is always less than one year and it shows that the period 2017-2018 is having the faster rate in getting back the investment amount.
- ❖ Return on investment during the year 2017-2018 is 28%. It shows the year 2017-2018 is having the highest rate of return and it increases the company's earning capacity.
- ❖ Net Present Value During the year 2017-2018 IS 351389.33; It shows the income over the entire life time of the project.

SUGGESTION

- ❖ It has been suggested to the India Cements Limited, to select the projects which all are having lesser pay-back period like the investment made in past twoyears.
- ❖ The company is suggested to avoid the projects which all are having higher pay back period like the financial year 2014-2015 because it does not bears any profit to the company.
- ❖ The company is advised to concentrate in return on investment. It increases the earning capacity of the project.
- ❖ It is suggested that the company wants to reduce their borrowings for increasing their profit.
- ❖ It is suggested that the company can improve their efficiency through technology upgradation.
- ❖ It is suggested to the India Cement limited, to issue debentures because it will increase the profit of the company than shares.

CONCLUSION

Capital budgeting is an analysis of long term investment, which mainly focuses upon acquisition and improvement on fixed assets it is a part of the long-term decision taken by the top management and involves large expenditure. The capital budgeting is very important to firms future capital budgeting. It is long term planning for making and financing major long term projects. Each of the capital budgeting techniques outlined has advantage and disadvantages. The

traditional method is simple but it does not consider the time value of money. Discounted cash methods consider the time value of money.

Through this study the overall financial performance has been analyzed, if the company focus on capital budgeting, surely the company can run with desirable profit for longer extend because capital budgeting helps to select the right investment proposals in the light of earning capacity. the gives several steps to overcome from the stated problems in the company.

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