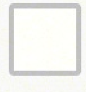
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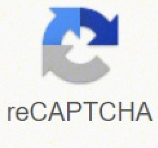
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Payback period example pdf

Formula for Calculating Payback period

1. When Cash inflows are even/equal

When cash inflow of all year is equal, we use the following formula

$$\textbf{Payback period} = \frac{\text{Initial Investment}}{\text{Annual Cah Inflow}}$$

2. When cash inflows are uneven

When cash inflows of each year is different we use the formula below

$$\textbf{Payback Period} = E + \frac{B}{C}$$

Where,

E = Year immediately Preceding to year of recovery

B = Amount left to be recovered

C = Cash inflow during the year of final recovery

Note: Before using these values we must find cumulative cash inflows

Table 1. Payback Period Analysis of Future Cash Flow Payments for Three Capital Projects

	Project A		Project B		Project C	
Year	Cash Flow	Cumulative	Cash Flow	Cumulative	Cash Flow	Cumulative
0	-$1,000			-$1,000	-$1,000	
1	$250	$250	$350	$350	$500	$500
2	$250	$500	$350	$700	$500	*$1,000*
3	$250	$750	$350	*$1,050*	$500	$1,500
4	$250	*$1,000*	$350	$1,400		
5	$250	$1,250	$350	$1,750		
6	$250	$1,500				
7	$250	$1,750				
8	$250	$2,000				
9	$250	$2,250				
10	$250	$2,500				

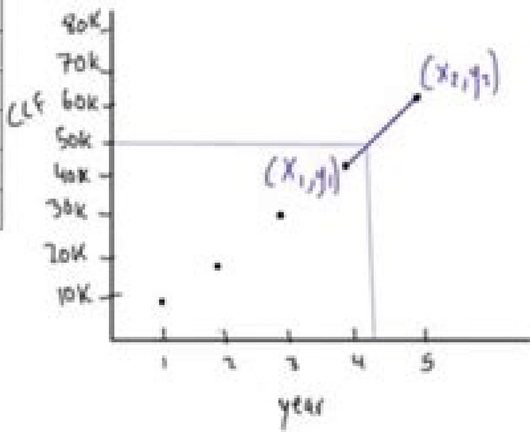
Payback Period Comparison

Project	Payback Period	Cash Return
A	4 yrs.	$2,500
B	3 (2.86) yrs.	$1,750
C	2 yrs.	$1,500

End of Year (Y)	Annual Cash Flows (CF)	Cumulative Cash Flows (CCF)
0	(50,000)	
1	7,000	7,000
2	11,000	18,000
3	12,000	30,000
4	15,000	45,000
5	20,000	65,000

$$PBP = X_1 + \left(\frac{cost - y_1}{y_2 - y_1}\right)(x_2 - x_1)$$

$$= 4 + \left(\frac{50,000 - 45,000}{65,000 - 45000}\right)$$



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Âtivitidder al erarusim rep elitu odotem nu ¨Ã non otnematromma id odoirep li ,otnatreP .enoizaredisnoc ni oserp eresse non the investment involves business decisions long-term, investment decisions in the business in the long term become even more important.¹ important. The great quantity which is the business the entity's long-term company. Capital balance sheet techniques are used to help the management assess various investment projects. This is the basic principle behind the repayment period. However, such an investment carried out over a period of ten years may not hold the same value.Clearly, the proposals considered above may generate higher funding inflows during the subsequent years of the investment project which is ignored if the repayment period method is used to evaluate investment proposals. If one has a longer repayment term¹ than the other, it may not be the best option. Analytics Repayment Term Forecast The other hand, the reseller's calculations can be so fast and easy to be completely simplistic. One of the drawbacks of this type of analysis Ã¨ which, although it shows the time needed for a return on investment, does not show the profitability specific. Helps an entity business to decide on the desirability of of an investment proposal based on the useful life and expected returns of a project. This method does not take into account the value of money time that Ã¨ is an important factor in determining the desirability of an investment project Used in other capital budgeting methods. The payback period is one of the oldest and easiest methods to evaluate investment proposals and Ã¨ is widely used in the small business. The payback period¨ calculated on the basis of information available from the books of accounts of an entity company. Under the above-mentioned repayment term formulae, the repayment term is nothing more than the number of years required to recover the initial cash recovery investment in a particular project. ala ala OLLOF led otuia'l noc enoizacilppa aus al e osrobmir id odoirep led alumrof al erednerpmoC oipmesE orepucer id odoireP)osrocs onna'l etnarud assac id ossulF / osrocs onna'lled oizini'lla otartsiger non otsoc(+ orepucer la onif atelpmoc inna = orepucer id odoirep Kapoor Kapoor Enterprises is considering investments A and B each requiring an investment of Rs 20 Lakhs today and cash flows at the end of each of the following 5 years. However, the business entity should not take investment decisions simply on the basis of the Payback Period of the investment proposals given the inherent drawbacks of the Payback Period Method.Demerits of Payback Period MethodAs mentioned above, Payback Period Method neither takes time value of money nor cash flows beyond the payback period into consideration. This can be a problem for investors choosing between two projects on the basis of the payback period alone. Let¢ÂÂs evaluate how much time does it take to get this initial investment of Rs 20 Lakhs back in each of the projects.The following table shows the expected cash flows from investment proposals A and B.Proposal AYear EndExpected Cash InflowsCumulated Cash Inflows0(20,00,000)(20,00,000)12,00,000(18,00,000)22,00,000(16,00,000)32,00,000(14,00,000)42,00,000(12,00,000)52,00,000(10,00,000)62,00,000(8,00,000)72,00,000(6,00,000)82,00,000(4,00,000)92,00,000(2,00,000)102,00,0000112,00,0002,00,000Thus for Proposal A,Payback Period = Full Years Until Recovery + (Unrecovered Cost at the beginning of the Last Year/Cash Flow During the Last Year)= 9 + (2,00,000/2,00,000)= 9 + 1= 10 YearsProposal BYear-EndExpected Cash InflowsCumulated Cash Inflows0(20,00,000)(20,00,000)12,00,000(18,00,000)23,00,000(15,00,000)34,00,000(11,00,000)42,00,000(9,00,000)54,00,000(5,00,000)65,00,000074,00,0004,00,000Thus for Proposal B,Payback Period = Full Years Until Recovery + (Unrecovered Cost at the Beginning of the Last Year/Cash Flow During the Last Year)= 5 + (5,00,000/5,00,000)= 5 + 1= 6 YearsSince Project B has a shorter Payback Period as compared to Project A, Project B would be better. reward, investors should combine a variety of these models.We can helpGoCardless helps you automate payment collection, cutting down on quantity Administrators that the team should handle when chasing invoices. Learn more¹ about how you can improve payment processing in your business today.To get startedLearn more¹ Learn how GoCardless can² help you with ad hoc payments or recurring payments.Over 70,000 companies use GoCardless to be paid on time. It is based on the incremental cash flows resulting from a particular investment project. Therefore, various investment proposals are assessed according to the number of years needed for © unâÂ the initial cost of the investment proposal. Ã closely related to the break-even point of an investment.The recovery period Ã¨ a quick and easy way to assess opportunities investment and risk, but instead of a break-even analysisÂunitÂ Â, the recovery period Ã¨ in years. In a hurry? Go to the recovery period formula.Before making any investment decision, ÂÂ it is useful to think about how long it will take to recover the initial cost. Another option Ã¨ is to use the discounted recovery period formula instead, which adds the value of the money time in the equation.For the moreÂ¹ complete, balanced look in a project riskÂÂ against a project could be repaid moreÂ¹ quickly, but Ã ④ ÂÂ in the long term ÃÂÂÂ Â ÂÂ The shorter the recovery period, the more attractive the The recovery period is used not only in the financial sectors, but also by companies to calculate the rate of return on any new asset or technology update. Provides a quick overview of speed with which the initial investment can be recovered. The resulting number¨ in years or fractions of Payback periodWritten as a formula, the calculation of the payback period could also be similar to this:Payback period = Initial investment / Annual repaymentFor example, imagine a company invests £200,000 in new production .4 .4 af 000.05 rep osivid 0000,002 ©Âhcrep inna 4 id ebbares osrobmir id odoirep li ,osac otseuq nI000.05£ÂÂ / 000.002£ÂÂ = osrobmir id odoireP.onnaâlla 000.05£ÂÂ id ovitisop assac id ossulf nu ni ecudart is ehc

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