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A Study on Capital Budgeting on APSPDCL at Tirupati

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ABSTRACT

'The capital budget is essentially a list of what management believes to be worthwhile projects for the acquisition of new assets together with the estimated cost of each project."

Investment decisions are generally known as capital budgeting or capital expenditure decisions. It is clever decisions to invest current in the long-term assets expecting long-term benefits firm's investment decision would generally include expansion, acquisition, modernization and replacement of long-term assets

DEFINITIONS:

The investment decisions of a firm generallyknown as the capital budgeting or capital expenditure decisions. The capital budgeting decision may be defined as the firm's decisions to invest its current funds most efficiently in the long- term assets in anticipation of an expected flow of benefits over a series of year.

-- I M PANDEY

Capital budgeting is the planning of capital expenditure on long term projects whose returns spread over several years.

--**SC. Siva Rami Reddy**

Capital budgeting is long term planning for making and financing proposed capital outlays.

-- T. Horn green

Capital budgeting is the process of evaluating and selecting long term investment that is consisted with the goal of shareholders (owners) wealth maximization.

-- M Y KHAN / P K JAIN

PROCESS OF CAPITAL BUDGETING:

The process of capital budgeting can be divided into four types. They are

- Project generation
- Project evaluation
- Project selection
- Project execution

PROJECT GENERATION:

Investment proposals originate at different levels like top level, middle level, and lower level. The investment proposals can be formed the following purpose.

- To add new products to the existing products
- Expanding capacity
- To reduce cost of production

NEED FOR THE STUDY

- Investment decisions will play key role in the financial performance of the company. Long-term investment plays major role in the profits of the company. so the study helps to understand the company takes long-term investment decisions
- The project study is under taken to analyse and understand the Capital Budgeting process in Southern Power Distribution Company Limited, which gives main exposure to practical implication of theory knowledge.

SCOPE OF THE STUDY

- The efficient allocation of capital is the most important financial function in the modern times.
- The study covers the calculation of pay-back period, Average rate of returns, net present value, Internal rate of returns etc.
- The study includes the decisions as to be made for investment process. These percentages help in analysing the funds for investment purpose.

OBJECTIVES OF THE STUDY

- To study the practical usage of capital budgeting techniques.
- To find out the technique of capital budgeting for decision-making.
- To study the company is investing in profitable projects or not.

METHODOLOGY OF THE STUDY

Research methodology is a way to systematically solve the research problem. It may be understood as a science of studying now research is done systematically. In thatvarious step, those are generally adopted by a researcher in studying his problem along with the logic behind them.

Data collection is important step in any project and success of any project will be largely depend upon now much accurate you will be able to collect and how much time, money and effort will be required to collect the necessary data, this is also important step. Data collection plays an important role in research work. without proper data available for analysis, you cannot do the research work accurately.

Sources of Data:

Secondary data:

The secondary data collected from published manuals, records, brochures, files of the organization and books, reports etc.;

LIMITATIONS OF THE STUDY

1. The study is conducted in a short period, which was not detailed in all aspects.
2. All the techniques of capital budgeting are not used in company. Therefore, it was possible to explain only few methods of capital budgeting.
3. The information provided in the company balance sheet is only the data source available.
4. non-availability of confidential financial data.

DATA ANALYSIS AND INTERPRETATION

PAY BACK PERIOD (PBP): -

YEAR	INCOME (PAT) (RS)	DEPRECIATION (RS)	CASHIN FLOW (RS)	CUMULATIVE CASH IN FLOWS (RS)
2017-18	23.85	86.36	110.21	110.21
2018-19	47.04	100.95	147.99	147.99
2019-20	94.36	121.73	216.09	474.29
2020-21	80.48	145.77	226.25	700.54
2021-22	167.03	185.38	352.41	1052.95

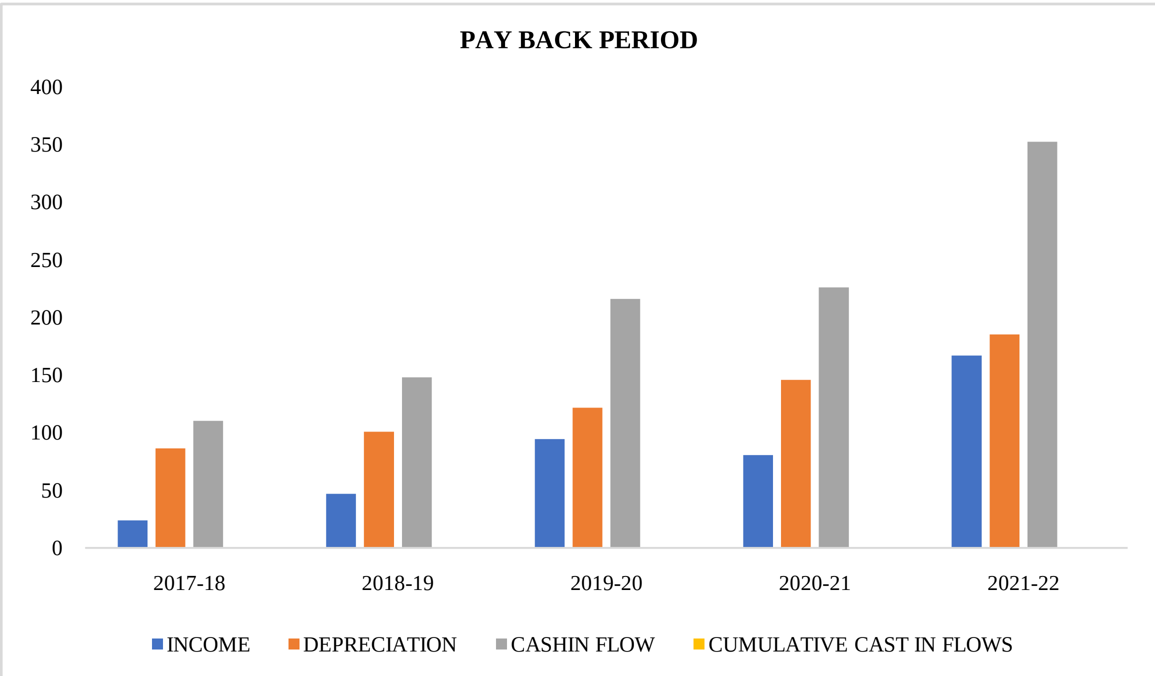
Initial outlay = 491.11

Pay back period = $3+\dfrac{16.82}{226.25}$

= 3+0.074

= 3.074 Months

GRAPH: 3.2



INTERPRETATION:

From the above table and graph 3.2 In the year 2017-18 total cash flow 110.21 depreciation 86.36 income 23.85 and 2018-19 cash flow 147.99depreciation 100.95 income 47.04 and 2019-20 cash flow 216.09 depreciation 121.73 income 94.36and 2020-21 cash flow226.25Depreciation145.77in come 80.84and 2021-22 cash flow 352.41 Depreciation185.38 income 167.03

Criteria for evaluation:

The paybackperiod computed for a project is less than the payback period set by management of the company, it would be accepted. A project actual payback period is more than the determined period by the management, it will be rejected.

Decision:-

The standard payback period is set by APSPDC LTD for considering the expansion project is five years whereas actual payback period is 3.074 months. Hence we accept the project.

AVERAGE RATE OF RETURN (ARR): -

YEAR	INCOME	DEPRECIATION	CASH IN FLOWS
2017-18	23.85	86.36	110.21
2018-19	47.04	100.95	147.99
2019-20	94.36	121.73	216.09
2020-21	80.48	145.77	226.25
2021-22	167.03	185.38	352.41

$$\text{ARR} = \frac{\text{Average profit}}{\text{Average Investment}} \times 100$$

$$\text{Average profit} = \frac{412.6}{5} = 82.552$$

$$\text{Average investment} = \frac{491.11}{2} = 245.55$$

ARR =.82.552÷245.55×100

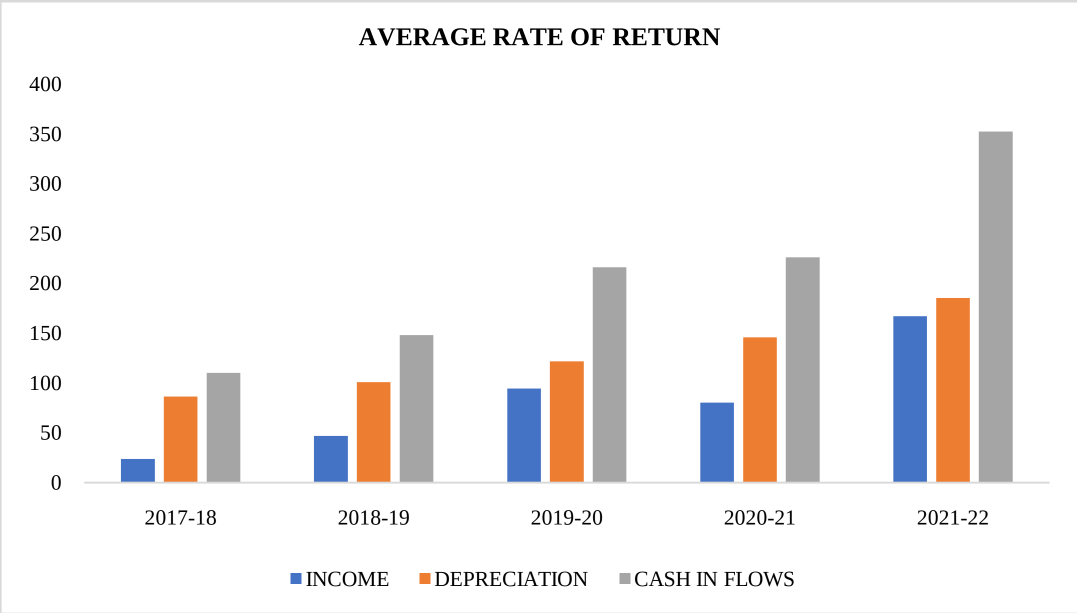
= 0.3362 × 100

= 33.62

$$\text{ROI} = \frac{\text{Average profit}}{\text{Initial investment}} \times 100$$

$$= \frac{82.552}{491.11} \times 100 = 0.1680\times 100 = 16.80$$

Graph



Criteria for evaluation:-

According to this method ARR is higher than minimum rate of return established by the management are accepted. It rejects the project have less ARR than the minimum rate set by the management.

Decision:-

The standard ARR set by APSPDC LTD management is 21%. The actual ARR is 16.80% is higher than the standard ARR set by the management, hence we accept the project.

INTERPRETATION:

From the above table and graph 3.3In the year 2017-18 cash flow 110.21Depreciation 86.36 income 23.85 and 2018-19 cash flow 147.99 Depreciation 100.95 in come 47.04 and 2019-20 cash flow 216.09Depreciation 121.73 in come 94.36and 2020 -21 cash flow 226.25Depreciation 145.77 in come 80.84and 2021-22 cash flow 352.41 depreciation 185.38 in come 167.03

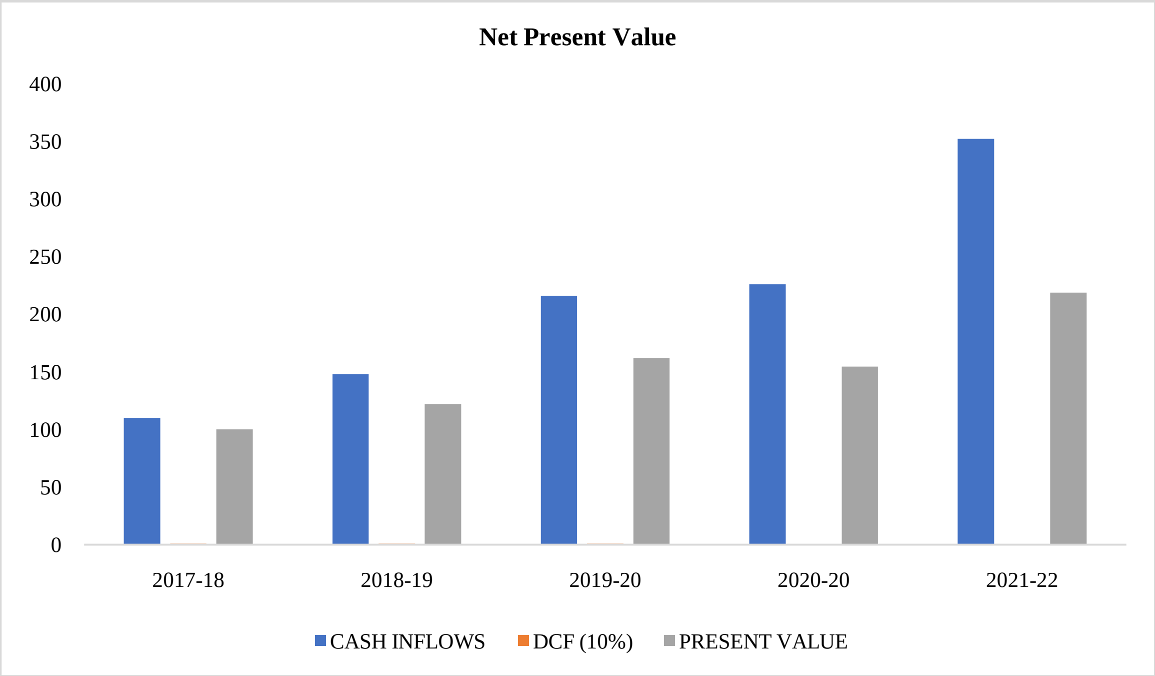
Net Present Value: -

YEAR	CASH INFLOWS	DCF (10%)	PRESENT VALUE
2017-18	110.21	0.909	100.180
2018-19	147.99	0.826	122.239
2019-20	216.09	0.751	162.283
2020-20	226.25	0.683	154.528
2021-22	352.41	0.621	218.85
		TOTAL	758.079

NPV = 758.079– 491.11

= 266.96

Graph: 3.4



Criteria for evaluation: -

In case of calculated NPV is positive or zero, the project should be accepted. If the calculated NPV is negative, the project is rejected.

Decision: -

The project is accepted due to calculate NPV is positive.

INTERPRETATION:

From the above table and graph 3.4 In the year 2016-17 cash inflows 110.21 DCF (10%) 0.909 presentvalue 100.180and 2017-18 cash inflows 147.99Dcf(10%)0.826 present value 122.239 and 2018-19 cash inflow216.09 DCF(10%)0.751 present value 162.283 and 2019 -20 cash inflows 226.25 DCF(10%)0.683 present value154.528 and 2020-21 cash inflows 352.41 DCF(10%)0.621 present value 218.85

FINDINGS

Based on the objectives framed, findings are briefly summarized as follows.

- The standard payback period is set by APSPDC LTD for considering the expansion project is five years, whereas actual payback period is 3.074 months.hence, we accept the project.
- The standard ARR set by APSPDC LTD management is 21%. The actual ARR is 16.80% is higher than the standard ARR set by the management, hence we accept the project.
- The net present value of the project at 10% discount rate factor is positive 50.51

SUGGESTIONS:

- To improve net profit, the company should have a strict control over administrative expenses and management expenses.
- The management has to take necessary steps to handle the funds that are entrusted with them effectively, in order to have a higher return on equity.
- The concern is required to develop an effective capital structure system.
- The systematic program for efficient operation of the plant should be involved.

CONCLUSION:

From the analysis, it was observed that we are getting back our investment within the expected period and the NPV, IRR. also, positive and profitability index is greater than one. So, we can accept the project. so, the investors invest their amount in this project, based on these we can know the financial position of the firm. And also, we allocate the funds based on the requirement it gives the information to planning commission for allocating the funds.

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