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A Study on Capital Budgeting in Dodla Dairy Private Limited in Palamaneru

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ABSTRACT

Capital budgeting is a step by step process that business uses to determine the merits of an investment project. The decision of whether to accept or deny an investment project as part of a company's growth initiatives, involves determining the investment rate of return that such a project will generate. This is focuses on payback period of dodla dairy private limited. And also it focuses on calculations on Net present value and internal rate of return value and also profitability index. The result shows that more than one profitability index and positive NPV.

Keywords: Growth, Payback Period, Long-Term Investment, Profitability.

INTRODUCTION

It is a process of investing funds. Current funds which are long term activities with view to earn more profits over a series of years. The investment decision means a decision as to whether (or) not money should be invested in long term projects. Such projects may include:

- Setting up a factory
- Installing a new machinery
- Creating additional capacities
- Make (or) purchases new products

The main characteristics of a capital expenditure are that the expenditure is incurred at one point of time whereas benefits of the expenditure are realized at different points of time in future. Capital budgeting process involves planning, availability and controlling, allocation of long-term investment funds.

CONCEPT OF CAPITAL BUDGETING

Efficient allocation of capital is one of the most important function of the financial management in modern times. This function involves the firm decision to commit its funds in long-term assets and other profitable activities. The decision to invest funds in the long term assets of a firm are quite significant and they will influence the firms wealth, determine the size, get the pace and direction of its growth and also affect the business risk.

In evaluating such investment proposals, it is important carefully consider the expected benefits of investment against the expenses associated with organization are frequently faced with Capital Budgeting decisions. Any decision that require the use of resources is a capital budgeting decisions .Capital budgeting is more or less a continuous process in growing concern

RESEARCH METHODOLOGY

OBJECTIVES OF THE STUDY

The study of the capital budgeting in DODLA DAIRY LIMITED is being attempted with the help of the following objectives.

To achieve and maintain a leading position as supplies of quality equipment.

- To study the capital budgeting process Dodla Dairy Limited
- To analyze and access the financial viability of the investment proposal using the Traditional and modern methods of capital budgeting
- To offer suggestions to the Dodla Dairy Limited., to improve its financial performance.

DATA COLLECTION

The study depends upon secondary data from various sources.

The information is collected directly from the experts, on the basis of which actual position was identified.

SECONDARY DATA

Secondary Data is collected from Annual reports, schedules, budgets, and other statements provided by the finance department Dodla Dairy Limited

SCOPE OF THE STUDY

The scope of the present study includes the flowing

- Understanding the importance of the capital budgeting in Dodla Dairy Limited.,
- Evaluating an investment proposal of setting up facility at Dodla Dairy Limited.,
- Highlighting the necessity of current of assets and current liabilities.

DATA ANALYSIS & INTERPRETATION

Data analysis is process of inspecting, cleansing, transforming and modelling data with the goal of discovering usefull information,information conclusions and supporting decision making.

Table no:1 Calculation of PAY BACK PERIOD

Years	Cash inflows Rs.	Cumulative cash inflows (Rs.)
2016-2017	243761	243761
2017-2018	429661	673422
2018-2019	290561	963983
2019-2020	199561	1163544

INTERPRETATION:From the above table no.1 it is clearly shows that Payback period method is a traditional method of evaluation of capital budgeting decision. The term pays back out payoff refers to the period in which the project will generate the necessary cash and recoup the initial investment or the cash out flows

$$\begin{aligned}
 \text{Payback period} &= \text{current year} + \text{difference in cash flows} / \text{net year cash flows} \\
 &= 3 + 1003500 - 963983 / 199561 \\
 &= 3 + 39517 / 199561 \\
 &= 3 + 0.19 \\
 &= 3.19 \text{ Years}
 \end{aligned}$$

Payback period = 3.19 years

The cumulative cash inflows are Rs. 963983 in 3rd year and Rs. 1163544 in 4th year.

Hence, payback period between 3rd and 4th year

Table no: 2 Calculation of PAY BACK PERIOD

Years	Cash flows Rs.	Cumulative cash flows Rs.
2016-2017	1101737	1101737
2017-2018	1305837	2407574
2018-2019	1135537	3543111
2019-2020	1241487	4784898
2020-2021	1500837	6285435

Payback period = current year + difference in cash flows / net year cash flows

$$\begin{aligned}
 &= 3 + \frac{5921800 - 3543111}{1241487} \\
 &= 3 + \frac{2378689}{1241487} \\
 &= 3 + 1.91 \\
 &= 4.91
 \end{aligned}$$

Payback period = 4.91 years

INTERPRETATION: From the above table no.2 it is clearly shown that Payback period method is a traditional method of evaluation of capital budgeting decision. The term pay back or payoff refers to the period in which the project will generate the necessary cash and recoup the initial investment or the cash out flows.

Table no: 3 CALCULATION AVERAGE RATE OF RETURN

Years	Cash Flows (Rs.)	Cumulative cash Flows Rs.
2016-2017	1101737	1101737
2017-2018	1305837	2407574
2018-2019	1135537	3543111
2019-2020	1241487	4784898
2020-2021	1500837	6285435

AVERAGE RATE OF RETURN

$$ARR = \frac{\text{AVERAGE PAT}}{\text{AVERAGE INVESTMENT} \times 100}$$

$$ARR = \frac{1138230/5}{1003500/2} \times 100$$

$$ARR = 227646/501750 \times 100$$

$$ARR = 45.37$$

TABLE NO 4: CALCULATIONS OF AVERAGE RATE OF RETURN

Years	Cash flows Rs.	Cumulative cash flows Rs.
2016-2017	1101737	1101737
2017-2018	1305837	2407574
2018-2019	1135537	3543111
2019-2020	1241487	4784898
2020-2021	1500837	6285435

AVERAGE RATE OF RETURN

$$ARR = \frac{\text{AVERAGE PAT}}{\text{AVERAGE INVESTMENT}} \times 100$$

$$ARR = \frac{3620625/5}{5921800/2} \times 100$$

$$ARR = 724125/2960900 \times 100$$

$$ARR = 24.45$$

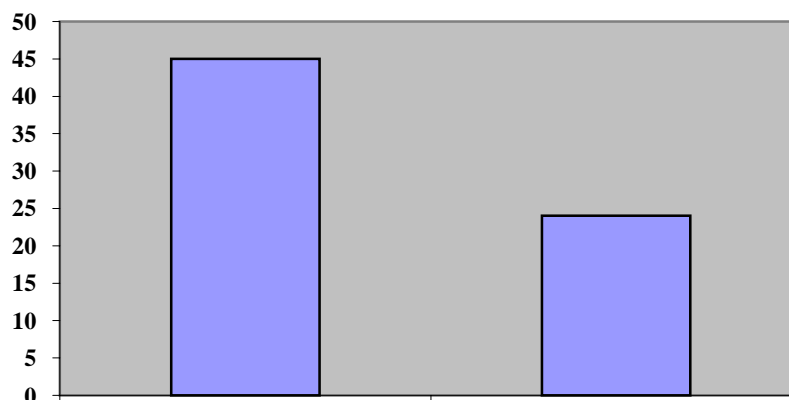
INTERPRETATION:

From the above table no.4, it is clearly shown that Payback period method is a traditional method of evaluation of capital budgeting decision. The term

pays back out or payoff refers to the period in which the project will generate the necessary cash and recoup the initial investment or the cash out flows

TABLE NO 5: CALCULATIONS OF AVERAGE RATE OF RETURN

CASH FLOWS	Values
MILK	45.37
MILK PRODUCT	24.45



INTERPRETATION:

From the above table 5 it is clearly shows that ARR is another traditional method of capital budgeting evaluation. According to this method the capital investment proposals are judged on the basis of their relative profitability. The capital employed and related incomes are determined according to the commonly accepted accounting principles and practices over the certain life of project and the average yield is calculated

TABLE NO 6: CALCULATION OF INTERNAL RATE OF RETURN (IRR) @ 10%

YEARS	CAHS FLOWS	P.V.%10%	P.V.OF NET CAHS FLOWS
2015-2016	1003500	1.00	1003500
2016-2017	243761	0.909	221579
2017-2018	429661	0.826	354900
2018-2019	290561	0.751	218211
2019-2020	199561	0.682	136101
2020-2021	225561	0.620	139848

TOTAL CAHSH FLOWS : 1070639
 LESS: INITIAL INVESTMENT : 1003500
 NPV : 67139

As the NPV is above table is positive, we calculate at a higher rate of discount that is 15% as given

TABLE NO 7: CALCULATION OF IRR @ 15%

YEARS	CAHS FLOWS	P.V.%15%	P.V.OF NET CAHS FLOWS
2015-2016	1003500	1.00	1003500
2016-2017	243761	0.870	212072
2017-2018	429661	0.756	324824
2018-2019	290561	0.658	191189
2019-2020	199561	0.572	114149
2020-2021	225561	0.497	112104

TOTAL CAHS FLOWS : 954338
 LESS: INITIAL INVESTMENT : 1003500
 NPV : -49162

IRR=12.88% As the NPV is 15% is negative, Hence IRR fall in between 10% and 15%. The correct IRR calculated as follows:

IRR = P.V. FACTOR + NPV / TOTAL PV FACTOR * DIFFERENCE IN PV FACTOR

$$IRR = \frac{10\% + 67139}{1070639 - 954338} \times 15\% - 10\%$$

$$IRR = 10\% + 67139 / 116301 \times 5\%$$

$$IRR = 10\% + 0577 \times 5\%$$

$$IRR = 12.88\%$$

YEARS	CAHS FLOWS	P.V.@10%	P.V.OF NET CASH FLWOS
2015-2016	5921800	1.00	5921800
2016-2017	1101737	0.909	1001479
2017-2018	1305837	0.826	1078621
2018-2019	1135537	0.751	852788
2019-2020	1241487	0.682	846694
2020-2021	1500837	0.620	930519

TOTAL CASH FLOWS : 4710101

LESS: INITIAL INVESTMENT : 5921800

NPV : -1211699

IRR = P.V. FACTOR + NPV / TOTAL PV FACTOR * DIFFERENCE IN NPV FACTRO

$$IRR = 6\% + \frac{-664369 \times 10\% - 6\%}{5257431 - 4710101}$$

$$IRR = 6\% + (-1.21) \times 4$$

$$IRR = 6 - 4.85$$

$$IRR = 1.14$$

TABLE NO:7CALCULATIONS OF PROFITABLEINDEX (PI)

YEARS	CAHS FLOWS	P.V.%10%	P.V.OF NET CAHS FLOWS
2015-2016	1003500	1.00	1003500
2016-2017	243761	0.909	221579
2017-2018	429661	0.826	354900
2018-2019	290561	0.751	218211
2019-2020	199561	0.682	136101
2020-2021	225561	0.620	139848

TOTAL CAHS FLOWS : 1070639

LESS: INITIAL INVESTMENT : 1003500

NPV : 67139

Decision making: NPV is positive; hence the project can be accepted.

PROFITABILITY INDEX

PROFITABLE INDEX (PI)

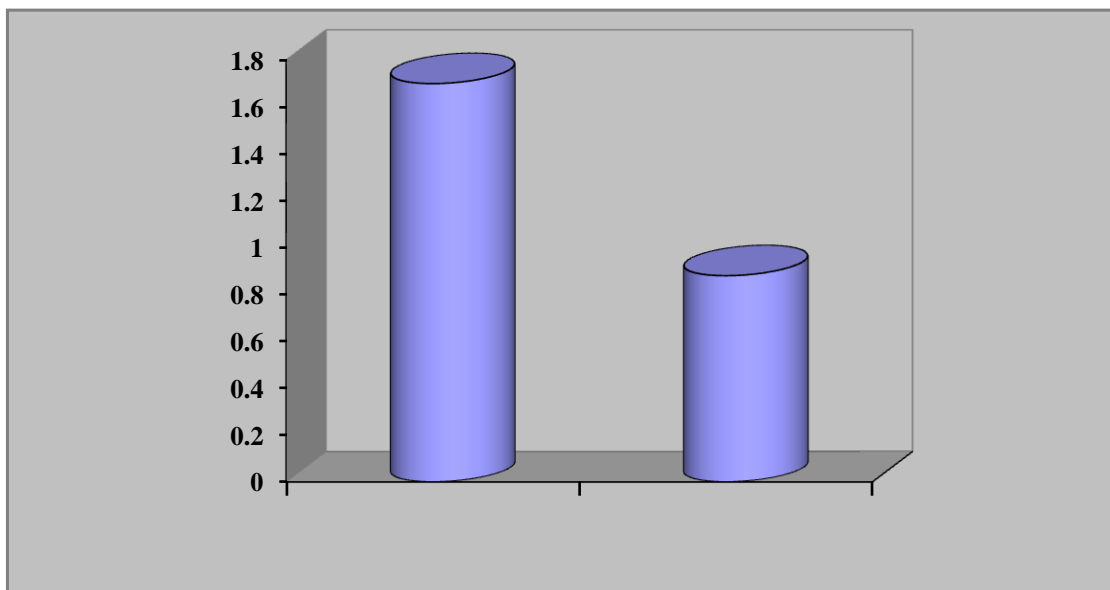
$$PI = \frac{\text{TOTAL PRESENT VALUE OF CASH FLOWS}}{\text{TOTAL INVESTMENT}}$$

$$PI = 1070639 / 1003500$$

$$PI = 1.07 \text{ times}$$

Decision making: The profitability index is greater than 1, so the project is accepted.

Cash flows	Values
Milk	1.07
Milk product	0.88

**INTERPRETATION:**

From the above table it is clearly shows Profitability index method is also known as time adjusted method of evaluating the investment proposals. Profitability also called as benefit cost ratio in relationship between present value of cash inflows and the present value of cash out flows.

FINDINGS

- The following are the findings during the study of the project.
- As per the management the minimum rate of return expected is 10%. The project ARR greater than 40% greater than 40% is accepted.
- The net income of the project is discounted at the minimum required rate return which is grater then – 8% and NPV is positive so the project is accepted.
- The capital invested is getting more return which is greater than 10%
- The project showing Profitability Index is more than one. So the project is accepted.

SUGGESTIONS

- ❖ The pay back indicates that the investment is fully recovered in short period.
- ❖ NPV of the project is considered as better because of its higher net present value.
- ❖ The profitability index is more than the giving value and where projects show NPV as positive.
- ❖ To offer suggestions to the Dodla Dairy Limited., to improve its financial performance

CONCLUSION

The capital budgeting process generally helps the company in taking two types of decisions: Investment decisions and financing decisions.

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