8 Lecture - MGT201

Important Subjective

1. **What is capital budgeting?**
   Answer: Capital budgeting is the process of evaluating and selecting long-term investment projects that will generate the highest returns for a business.

2. **What is the difference between capital budgeting and operational budgeting?**
   Answer: Capital budgeting focuses on long-term investment decisions while operational budgeting focuses on short-term decisions related to day-to-day operations.

3. **What is the payback period method and what are its limitations?**
   Answer: The payback period method is a capital budgeting technique that calculates the length of time it takes to recover the initial investment. Its limitations include ignoring cash flows beyond the payback period and not considering the time value of money.

4. **What is the net present value (NPV) method and how is it calculated?**
   Answer: The NPV method is a capital budgeting technique that calculates the present value of expected cash inflows minus the present value of expected cash outflows. It considers the time value of money and helps determine the profitability of a project.

5. **What is the internal rate of return (IRR) method and how is it calculated?**
   Answer: The IRR method is a capital budgeting technique that calculates the discount rate at which the present value of expected cash inflows equals the present value of expected cash outflows. It considers the time value of money and helps determine the rate of return of a project.

6. **What is the profitability index (PI) method and how is it calculated?**
   Answer: The PI method is a capital budgeting technique that calculates the ratio of the present value of expected cash inflows to the initial investment. It helps determine the profitability of a project relative to its cost.

7. **What is the cost of capital and how is it determined?**
   Answer: The cost of capital is the rate of return required by investors to invest in a project. It is determined by calculating the weighted average of the cost of debt and the cost of equity.

8. **How can risk be incorporated into capital budgeting decisions?**
   Answer: Risk can be incorporated by adjusting the discount rate used in capital budgeting techniques to reflect the riskiness of the project. A higher discount rate is used for riskier projects.

9. **What is the difference between the net present value (NPV) and internal rate of return (IRR) methods?**
   Answer: The NPV method calculates the present value of expected cash inflows minus the present value of expected cash outflows while the IRR method calculates the discount rate at which the present value of expected cash inflows equals the present value of expected cash outflows.

10. **What are the advantages and disadvantages of the payback period method?**
Answer: The advantages of the payback period method include its simplicity and ease of use. The disadvantages include ignoring cash flows beyond the payback period and not considering the time value of money.