

Finance case study: Cash flow and NPV

Assume that you will start your personal retail fashion store business. You selected good location in Al Rashed mall in Khobar and your are expected the following variables based on your expertise:

1. Store rent in annual basis of 200,000 SR which have to paid immediately and then every year.
2. Decorations and location setup will cost you 300,000 SR which will be paid immediately.
3. You need to hire 4 employees and each is getting total package at the end of each month 4,000 SR. They will start working in first day of store operation. You need also to pay the recruiting agency sum of 15,000 SR at the time of employee arrival (assume it's the first day of store operation).
4. The store is planned to operate for 3 years and then is expected to be sold by 1,600,000 SR and payment will be received instantly. This value does not include the value of goods.
5. Employees benefits at the end of 3 years is estimated to be 200,000 SR which have to be paid immediately after selling the business.
6. Assume that suppliers are paid immediately after sales made for their products at the end of each month. However, you need to deposit total of 200,000 SR at their first delivery which is planned to arrive one month before store operation. This value will be returned back after selling the business and the new buyer will deal with his own suppliers. The suppliers will take back all of their goods after selling the business with no extra cost.
7. Assume that the gross profit for all merchandize is 20%.
8. Assume that the store will operate 4 months after taking the location due to preparation and setup required.
9. Assume no tax is applied to your business.
10. The electricity is paid at the end of each month and it's estimated to be 10,000 SR.
11. Your required rate of return for this business is 11%.
12. The sales is expected to be 100,000 SR (10,000 BD) in 1st month and the sales will grow in monthly basis by 30% for 3 months, then 20% for 6 months, then 15% for 4 months, then 10% for the rest of months.
13. The business is planned specified marketing budget which includes 100,000 SR at 1st day of operation. 50,000 SR after 6 months of operation and 100,000 SR after 1 year of operation.
14. Decoration will be renewed after 2 years of starting the operation and it's estimated to be 300,000 SR.

You are required to:

1. Put all cash flow in excel sheet.

2. Calculate the minimum cash required to be available with you when you will start this business. Use word document and justify your steps.
3. Calculate payback period, discounted payback period, NPV, and IRR. Use word document and justify your steps.
4. The assumptions made in this case done for case study purpose; however, practically, many other issues need to be included or modified. Please discuss this statement highlighting issues in the case that will differ in practice and the effect of these differences in cash flow calculation and capital appraisal.
5. Assumes that the previous figures are actual figures, and then you implemented a system of incentive which states that any sales achieved higher than the recorded values earlier, the sales team will receive each 4% from total value of sales increment (the difference between the sales achieved and previous records). Then assumes only in last year of operation, you got 20% increase in sales. Evaluate the new incentive system and their effect in different financial figures then discuss the advantage and disadvantages of such incentive system.

Answer: