Appendix 2: Answer

(a) Proposed move to the town centre

| | **Time** | | | | | |
| | **0** | **1** | **2** | **3** | **4** | **5** |
	$	**$**	**$**	**$**	**$**	**$**
Lease	(3,500)	(3,500)	(3,500)	(3,500)	(3,500)	
Hairdresser		(6,000)	(6,000)	(6,000)	(6,000)	(6,000)
Local papers	(2,000)					
Local radio	(5,000)					
Revenue increase		18,000	18,000	18,000	18,000	18,000
Overheads		(2,500)	(2,500)	(2,500)	(2,500)	(2,500)
Direct costs		(900)	(900)	(900)	(900)	(900)
Net cash flows	(10,500)	5,100	5,100	5,100	5,100	8,600
Discount factors	1.000	0.909	0.826	0.751	0.683	0.621
	(10,500)	4,636	4,213	3,830	3,483	5,341

The net present value is $11,003, therefore Mrs Clip should move her business to the town centre.

Workings:
Revenue increase: 0.45 x $40,000
Overheads: $4000 – $1,500
Direct costs: 0.05 x $18,000

(b) Advertising the move to the town centre on local radio

Time	Description	Cash flow	Discount factor	Present value $
0	Advertising	(5,000)	1	(5,000)
1–5	Extra revenue (0.05 x $40,000)	2,000	3.791	7,582
1–5	Extra direct costs (0.05 x $2,000)	(100)	3.791	(379)
				2,203

The net present value is positive, and Mrs Clip should advertise the move to the town centre on local radio.