SNS COLLEGE OF ENGINEERING

Kurumbapalayam (Po), Coimbatore – 641 107
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DEPARTMENT OF MANAGEMENT STUDIES

SUBJECT NAME & CODE : 23BAT308 - MERCHANT BANK

YEAR/ SEMESTER : II MBA / III SEMSTER

UNIT 2 : ISSUE MANAGEMENT

Topic : Introduction to Project Appraisal

Project Appraisal

- **Project appraisal** is a crucial process in merchant banking, where financial institutions thoroughly evaluate the **viability and feasibility** of a proposed project before committing to funding or advisory services.
- This evaluation helps determine whether a project is worth pursuing from a technical, financial, economic, and environmental standpoint.
- Merchant banks, as intermediaries between companies and capital markets, play a critical role in ensuring that projects are well-planned, financially sustainable, and have a reasonable risk-reward balance.

Key Concepts in PA

- Technical Feasibility - Evaluates the project's technical capacity to be implemented successfully with available resources.
- Financial Feasibility - Assesses the project's financial soundness, including profitability, costs, and revenue potential through metrics like NPV and IRR.
- Market Feasibility - Analyzes the market demand for the project's product/service and competition in the target market.
- Economic Feasibility - Examines the broader economic impact, including job creation, contribution to GDP, and alignment with government policies.
- Environmental Feasibility - Ensures the project meets environmental regulations and sustainability standards.

Importance of Project Appraisal in Merchant Banking

- Viability and Profitability Project appraisal ensures financial sustainability by analyzing cash flows, NPV, and IRR.
- Risk Management Appraisal helps identify and mitigate risks like operational, financial, and market risks.
- Strategic Alignment Ensures projects align with long-term corporate and investor goals.
- Resource Allocation Guides optimal resource and capital allocation, preventing wasteful investments.
- Stakeholder Confidence Builds trust with investors by providing comprehensive project analysis and clear financial outcomes.

Role of Merchant Banks in Project Appraisal

- Due Diligence
- Financial Structuring
- Advisory Services
- Risk Assessment
- Market Analysis

Net Present Value (NPV)

- NPV is a financial metric that evaluates the profitability of an investment by calculating the difference between the present value of cash inflows and the present value of cash outflows over a specific period.

Formula for NPV:

$$NPV = \sum \left(\frac{C_t}{(1+r)^t} \right) - C_0$$

Where:

- C_t = Cash inflow during the period t
- r = Discount rate (cost of capital)
- t = Time period (years)
- C_0 = Initial investment (cash outflow at time $t = 0$)

Steps to Calculate NPV

- Estimate Cash Flows: Determine the expected cash inflows (revenue from energy sales) and outflows (operating costs, maintenance, etc.) for each year of the project's life.
- Choose a Discount Rate: The discount rate is typically the weighted average cost of capital (WACC) or the required rate of return.
- Calculate Present Value of Cash Flows: Use the NPV formula to calculate the present value of each cash inflow for each year.
- Subtract Initial Investment: Finally, subtract the initial investment from the total present value of cash inflows to get the NPV.

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Internal Rate of Return (IRR)

The IRR represents the annualized effective compounded return rate that can be earned on the invested capital. Essentially, it helps investors understand the profitability of a project and compare it with the required rate of return or cost of capital.

Formula for IRR:

The IRR is found by solving the following equation for r:

$$0 = \sum \left(\frac{C_t}{(1+r)^t} \right) - C_0$$

Where:

- C_t = Cash inflow during the period t
- r = Internal Rate of Return (what we want to find)
- t = Time period (in years)
- C_0 = Initial investment (cash outflow at time $t = 0$)

RECAP

QUESTIONS???

THANK YOU