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Mc Don's Corporation- India "CASE STUDY: Application of Capital budgeting techniques on the decision of Mc Drive Thru's V/S Mc Cool Café's. (DCF &Non DCF Techniques)"

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Abstract: With increase in the level of competition and globalization, corporate are required to expand their level of operations which generally results in a decision making situation involving capital expenditure decisions. This in turn involves analyzing and appraising the various investment avenues and proposals involving huge investments. Most firms have numerous investment opportunities before them, some are profitable while others are not. Given the amount of money involved in such decisions, this case study aims to focus on the application of Capital budgeting techniques. It emphasizes understanding the Discounted Cash Flow techniques (DCF) and Non DCF techniques of capital budgeting (Payback period, Discounted Payback, NPV) which are primarily based on the concept of time value of money. It also highlights comparison of different traditional and modern capital budgeting techniques.

INTRODUCTION

McDon's Corporation is the world's largest chain of hamburger fast food restaurants which primarily sells hamburgers, cheeseburgers, chicken products, French fries, breakfast items, soft drinks, shakes, salads, wraps and desserts. As the Head-Delhi/NCR region, Ms Sakshi Tharoor is being asked to identify investment proposals that will help in boosting up the sales in Delhi/NCR and thereafter appraise the available alternatives so as to choose the best option among the available options.

PEDAGOGICAL OBJECTIVES

(1) To understand the Discounted Cash Flow techniques (DCF) and Non DCF techniques of capital budgeting (Payback period, Discounted Payback, NPV).
(2) To understand the concept of time value of money.
(3) To develop an understanding of How to compare different Investment proposals.

Case

Ms Sakshi is working in a team of three members including herself and two more Managers from the Finance Department. After thoroughly understanding and Analyzing the defined market, the team could think on two investment options which are as follows:-

<Option-1> To open up McDrive Thru's:

The first option that the team could identify is to open up Mc Drive Thru's offering full menu to the clients. Drive-thru is a type of service provided by a business that allows customers to purchase products without leaving their cars. This involves opening up three Drive Thru's in each of the four zones of Delhi and 2 in NCR'S. The per annum costs associated with opening up one Mc Drive Thru store is as follows:

Particulars	**Costs for 1 Mc Drive Thru (in Rs Lakhs)**
Initial investments: - Franchisee and Licensing - Construction cost - Machinery and set up costs Total	 30 125 45 200
Staff salary (@1.8 lac for 5 persons)	9
Raw material cost	50
MCD tax cost	6

An estimation on the basis of the take away's from Mc Don's restaurants says that each Mc Drive Thru will be able to generate a revenue of Rs. 97,50,000 per annum.

s<Option-2> To open up Mc Cool Cafe's:

The second option that the team could identify is to open up Parasite stores in 50 major malls in Delhi& NCR region in the name of McCool Cafe. McCoolCafe will offer ice creams, shakes and Desserts to the clients. The per annum costs associated with one McCoolCafe are as follows:

Particulars	Costs for 1 McCoolCafe (Rs in Lakhs)
Initial Investment: - Franchising and licensing fees - Store set up costs - Purchase of Machinery Total	 30 6 20 56
Store rent (i.e. mall rent for parasite store@ Rs50 k per month)	6
Staff salary (@1.8 Lakhs for 3 persons)	5.4
Raw material costs	16.6

On the basis of the estimation, the team could make out that one Mc Cool Cafe will be able to generate revenue of Rs 42 Lakhs per annum.

REQUIRED:

Considering yourself as one of the managers working in the team you are suppose to :

- Find out the number of years in which the initial investment will be recovered in case of both the options.
- Evaluate the two options on the basis of the NPV of the options taking into account the inflows and Outflows associated with them.
- Considering the above calculations, which investment alternative should Ms Sakshi Tharoor go for and why?
- Draw a contrast between the DCF and Non DCF techniques of Capital budgeting.

Note: The tax rate applicable to the company is 35% and the overall COC of the company is 10%.Consider a time frame of 8 years.

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