20 True or False

Decide, then check the answer and reason below each statement.

Question 1

NPV stands for Net Present Value.

TRUE

It is the difference between the present value of cash inflows and outflows.

Question 2

A project should be accepted under the NPV rule if its NPV is less than zero.

FALSE

A project is accepted when NPV is greater than zero, since that means it creates value.

Question 3

IRR is the discount rate at which a project's NPV becomes zero.

TRUE

This is the core definition of Internal Rate of Return.

Question 4

A project is accepted under the IRR rule when the IRR is below the cost of capital.

FALSE

The IRR rule accepts a project only when its IRR exceeds the cost of capital.

Question 5

When NPV and IRR conflict on mutually exclusive projects, IRR should be followed instead of NPV.

FALSE

NPV is the correct deciding criterion because it measures absolute value added in rupees.

Question 6

NPV measures value in absolute rupee terms, while IRR measures a percentage rate of return.

TRUE

This difference is why IRR alone can mislead when comparing projects of different scale.

Question 7

IRR can never produce more than one possible answer, regardless of the cash flow pattern.

FALSE

Multiple sign changes in cash flows can produce multiple IRRs, making it unreliable in such cases.

Question 8

NPV assumes reinvestment of project cash flows at the bank's cost of capital.

TRUE

This is considered a more realistic reinvestment assumption than IRR's assumption of reinvestment at the IRR itself.

Question 9

Salvage value should be discounted separately at a different time period from the final year's operating cash flow.

FALSE

Salvage value should be added to the final year's operating cash flow and discounted together.

Question 10

The initial investment outlay at Year 0 is treated as a cash inflow in these problems.

FALSE

The initial investment is a cash outflow, shown as a negative figure at Year 0.

Question 11

Capital budgeting NPV and IRR problems are described as being tested in the CAIIB ABFM paper.

TRUE

ABFM is one of the compulsory CAIIB papers covering advanced financial management topics.

Question 12

If a question gives pre-tax cash flows along with a tax rate, they should be converted to after-tax flows before discounting.

TRUE

Discounting pre-tax flows directly when a tax rate is provided would overstate project value.

Question 13

A bank's cost of capital used in these calculations has no connection to its asset-liability management strategy.

FALSE

The cost of capital depends on the bank's funding mix, which ties directly to its ALM strategy.

Question 14

Riskier projects generally justify a lower discount rate than safer projects.

FALSE

Riskier projects typically justify a higher discount rate to compensate for added risk.

Question 15

Every future cash flow in an NPV problem must be discounted back to Year 0.

TRUE

Ignoring the time value of money and using undiscounted totals is considered a fundamental error.

Question 16

For projects with equal annual cash inflows, IRR can be estimated using an annuity-factor shortcut with interpolation.

TRUE

Dividing the outlay by the annual inflow gives a factor that can be matched against annuity tables.

Question 17

IRR requires no trial-and-error or interpolation for cash flows that are irregular across years.

FALSE

For irregular cash flows, IRR generally needs to be found by trial and error or interpolation, not simple algebra.

Question 18

A smaller project with a high IRR can add fewer total rupees of value than a larger project with a lower IRR.

TRUE

IRR ignores project scale, so a modest IRR on a large project can create more value than a high IRR on a small one.

Question 19

Confusing IRR with the cost of capital is described as a common mistake candidates make.

TRUE

IRR is what a project earns, while the cost of capital is the minimum return a bank requires.

Question 20

NPV and IRR are described as always agreeing on which project to select, with no possible conflict.

FALSE

The two methods frequently conflict on mutually exclusive projects, and NPV is the criterion to follow when they disagree.