

Pigs-R-Us Example 7 (Uncertainty)



Pigs-R-Us is trying to decide whether or not to automate their meat packing process. The machine costs \$200,000, has a useful life of 10 years and a salvage value of \$10,000. At some point, the machine will need a \$60,000 overhaul. There is a 50% chance that will occur in Year 5, a 30% chance that it will occur in Year 6, and a 20% chance that the equipment will make it to Year 7. The machine costs \$9000 per year to operate and maintain but will save the company \$50,000 per year in labor costs. Pigs-R-Us has asked you to evaluate the economics of this purchase. Assume their MARR is 14% per year.