Relevant Capital Budgeting Cash Flows are *Future, Operating, Incremental, Aftertax, Cash Flows*

Initial (Year 0) Cash Flows:
1. Cost of new equipment including shipping and installation (this is the number that will be depreciated (depreciable basis)), always a cash outflow (-).
2. Change in working capital (increases in assets are a use (-) of cash, increases in liabilities are a source (+) of cash).
3. Tax impact of new equipment (usually not tested).

Operating Cash Flows (Years 1 until the End), a modified income statement for each year of the Project
Change in
+ Sales
- Variable Operating Expenses
- Fixed Operating Expenses
- Depreciation (depreciable basis * depreciation percentage) = EBIT
- Taxes = NOPAT
+ Depreciation = Operating Cash Flows

Terminal (End/Last Year) Cash Flows
1. Salvage Value of the now old New Equipment, always a cash inflow.
2. Tax impact of Old Equipment = ((Book Value – Salvage Value) * tax rate). Note, book value = purchase price – accumulated depreciation. If you sell machine for more than book value, this is a profit that creates a tax liability or a cash outflow (-). If you sell the machine for less than book value, this is a loss/reduction in profits that creates a tax credit or a cash inflow (+).
3. Recovery of Working Capital (the exact same number as line 2 in Initial Cash Flows with the opposite sign).