The managers of United Medtronic are evaluating the following four projects for the coming budget period. The firm’s corporate cost of capital is 14 percent.

Project Cost IRR

A $15,000 17%

B 15,000 16

C 12,000 15

D 20,000 13

a. What is the firm’s optimal capital budget?

b. Medtronic managers want to consider differential risk in the capital budgeting process. Project A has average risk, B has below-average risk, C has above-average risk, and D has average risk. What is the firm’s optimal capital budget when differential risk is considered? (A Hint: The firm’s managers lower the IRR of high-risk projects by 3 percentage points and raise the IRR of low-risk projects by the same amount.)