

Solution 1.47

Last month you lent a work colleague \$5000 to cover some overdue bills. He agreed to pay you in 1 month with interest at 2% for the month, thus owing you \$5100. Today, when the repayment is due, he asked you to extend the loan for another month and he would pay you the \$5100 next month. In the meantime, you have had the offer to invest as much as you wish in an oil-well venture that is expected to pay 25% per year and a hot new IT stock that is estimated to return 30% the first year. If you let your colleague have another month, what is the opportunity cost of your decision? (*Note:* Express your answer in dollar and percentage amounts.)

Solution:

Money: The opportunity cost is the loss of the use of the \$5000 plus the \$100 interest.

Percentage: The 30% estimated return on the IT stock is the opportunity cost in percentage.