

Project management argumentative essay examples

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Te Au Rangahau (The Maori Business Research Centre at Massey University) Project

- Payback Period

Project A's payback period falls in the seventh year while project B's payback period falls in the sixth year. Project B would, therefore, be a better option using the payback period method. Note that for project A, the total payback is 20000 only, while for project B, the total payback is 22000.

The payback period decision method has the following assumptions, advantages and disadvantages. Ignores the time value of money. No discounting takes place. It also makes the assumption that inflows accrue evenly throughout the year. This could be contrary to the unfolding as inflows may fluctuate. Its advantages include the fact that it is simple and easy to use and apply. The method employs the concept of time it would take to recoup the initial outflow. This way, the investor is able to know how much in terms of time he would invest in the investment. In addition, payback could be equated to the breakeven concept. It indicates the point at which the project breaks even. Anything over and above the payback period is considered profits.

The payback method comes with disadvantages. First, the fact that it does not take into account the time value of money makes it unhelpful. Time value of money has the effect of varying the value of money depending on the year of reception. Assuming mere periods without taking into account the time value of money is flawed. In addition, the payback period only considers the payback time. To that extent, it fails to capture the entire cash-flows. This method could influence decision making against a project

with more cash-flows but longer periods for a shorter period project but with lesser cash-flows. It, therefore, does not necessarily lead to the realisation of the shareholder's objective of profit maximisation.

- Net Present Value

The Net Present Value of project B = total inflows - total outflows

= 19846.5 - 22000

= \$ (2153.5)

Represents a net loss of \$ 2153.5

The net present value has a number of assumptions. First, it works on the premise that the discounting rate would be constant throughout the years. This way the time value of money is computed through discounting. In addition, net present value assumes that it is possible to predict the total inflows that would accrue throughout the life of the project and any outflows that would possibly be incurred throughout the life of the project. The method has the advantage of being inclusive. It takes into consideration the total cash inflows throughout the life of the project. This way, it does not exclude any cash-flows and would be essential in making the most informed decision. The fact that it takes the time value of money makes the method more informed to apply because of factoring the real value of money rather than just the face value. The net present values has its disadvantages. For instance, it has limitations as to application. It can only be applied for mutually exclusive projects. It also fails to take into account non-monetary benefits that cannot be quantifiable.

The two methods discussed above are financial measures of project

evaluation. They employ the use of financial indicators to inform the decision making in project evaluation. Through these methods, forecasters can tell what business to settle for and why based on the monetary gains. The use of discounting factors increases the accuracy of financial evaluations as it gives the real values and financial returns likely to be received. In addition to the payback period and the net present values, other financial project evaluation methods include the internal rate of return and the probability index. The internal rate of return entails the calculation of a return on the investment which must be at a rate more than the rate of return in the market. The internal rate of return is premised on the assumption that the required rate of return is known and constant. Its advantage lies in the fact that it incorporates the time value of money while the disadvantage is that the required rate of return is not usually practically constant. The probability index is obtained by dividing the net inflows by the net outflow. The ratio should be more than 1.00 so as to be acceptable. The probability index merely employs the discounted inflows and outflows. In other words, it is a simple expansion of the net present value. It, therefore, carries with it the advantages and disadvantages characteristic of the net present values. On the other hand, projects could be evaluated using non-financial indicators. In the earlier methods, the main indicator is the financial gain. The project is evaluated for acceptance based on the financial components, that is, inflows and outflows. However, one can also employ the use of non-financial measures. Non-financial measures consider other factors consequent to making a decision as to what project to implement. This section would dwell in a number of non-financial methods of project

evaluation and outline the key considerations, bringing out the advantages and disadvantages.

One common method is that of benchmarking. In benchmarking certain arbitrary aspects are considered. The projects to be evaluated are considered in terms of whether they meet the aspects as set by the arbitrary standards. This method enables the decision maker to settle for the project that best addresses mundane characteristics at the heart of the business rather than concentrate merely on the financial returns. This approach comes with two main advantages. One, it leads to pursuit of quality projects rather than financial outputs. It also enables the decision maker to consider other essential factors such as the need to make strategic decisions for the long term benefit of the company rather than pursuit of short term benefits. However, benchmarking comes with the disadvantage that it fails to tackle the key issues of finance. The most essential decision making element in business is the finances in terms of inflows and outflows. Benchmarking may lead the decision maker to drop a highly finance earning project for a loss making project which has the attributes of the arbitrary setting.

Another critical non- financial evaluation technique is the customer satisfaction method. This method considers whether the customer's needs are met in full. It looks into whether the project contains the customer requirements. This method is in line with the philosophy that the customer is the king. In that vein, for success it is essential to impress on the king. The project application, therefore, concentrates on exciting the customer rather than making financial gains. Such a technique has the advantage of winning over the loyalty of the customer. It could also lead to the building of the

brand image of the company. After that, the company may reap in the long run from a loyal client base. The disadvantage of the application of this technique is twofold. First, it could fail to gain the loyalty of the customer. The customer may be influenced in his decision making by factors such as cost. In that event, no amount of design and product specialisation would lure him or his loyalty. Secondly, the method fails to consider the financial repercussions of a project. Financial outcomes remain an essential element in business success.

Finally, another non-financial method that could be employed is the balanced score card technique. In this method, the project is considered through several aspects. One looks at the internal and external perspectives. In the internal perspective, one looks at the business objectives, values and virtues and relates the same to the project. If pursuit of the project would be in consonance with the objectives, then it would be essential to select it. However, if the project does not satisfy the business objectives, it would be important to reject the project. This method comes with the advantage of making the best decision that addresses the objectives, values and virtues of the businesses. It, therefore, develops in the business a long term element that would enable it be competitive. The disadvantage of such a technique again lies in its silence on financial gains. The fact that other rewarding projects may be dropped in favour of one with less financial rewards but relevant to the objectives of the business could be disadvantages to the business. On the other hand, one could also consider an external perspective and consider the customer perspective. In this strain, one would want to settle on a project that resonates well with the customers at that prevailing

time. The advantage derived from such a technique is the positive customer reception that comes with the approach. However, it could impede the unit from settling on a different but more fulfilling project.

Works Cited

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Dlabay, Les R and James L Burrow. Business Finance. New York: Cengage Learning, 2007.