

Analyzing project feasibility

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Analyzing project feasibility Introduction Capital budgeting decisions are commonly made by firms in response to the investment practices or opportunities that most firms engage in with the aim of profitability. The resolution to capitalize in a certain project is dependent on the criteria that a firm selects to be applied in the evaluation of the project. There are numerous motives why a company may select on a particular criterion, one being the need to ensure a balanced maximization of wealth, being that it is the main objective for the firm's involvement in capital budgeting (Dayananda, 2002). The firm may want to maintain the independence of its business when making such investment decisions. Consequently, the choice of the criterion may be based on the availability of personnel resources, time and expertise required to analyze the project as well as the capital constraints that make the liquidity of a project a principal issue (Joos & Zhdanov, 2008).

Discounted cash flow analysis

Dell Corporation is a large firm that has its operations based on the manufacture of electronic items; particularly computers (desktops and laptops). In the determination of the feasibility of its projects, Dell Corporation estimates the cash flows and net present value as + \$10. The recognition or dismissal of the venture is dependent on the type of analysis that the corporation adopts (Danielson & Scott, 2006). The best type of analysis that can be used to regulate the practicability of the project is the discounted cash flow analysis method.

The discounted cash flow analysis method is a project valuation method that applies the time value of money concept, particularly in relation to the estimation of the investment opportunity. This method is essential in the <https://assignbuster.com/analyzing-project-feasibility/>

case of Dell Corporation given that it will use the future cash flow projections to attain the present value by discounting by discounting the values, mostly by the weighted average cost of capital (WACC) (Danielson & Scott, 2006). This method works in the manner that if the project's value is higher than the current investment cost, the project may be a good one for Dell Corporation to invest.

Subsequently, the method conveys certain essential economic information about the firm under certain circumstances such as when faced by the issue of capital constraints. Besides, the corporation's use of the method will be justified by the fact that the firm has always been changing its product lines. The discounted cash flow analysis is quite useful in the assessment or evaluation of the project given that, in this case, it would be quite easy to obtain estimates of cash flow that are reliable (Peterson & Fabozzi, 2002).

Real options valuation model

Dell Corporation after having engaged the discounted cash flow technique can then determine the relation of its earnings to the price of its stock. This is best achieved through the construction of an appraisal model founded on the real options investment approach. The firm has an NPV of +\$10 hence, initiating the project at the inception point would entail that the corporation invests in its R & D so as to evaluate its economic justifiability. Subsequently, this model enables the firm to determine the likely market successes considering the differentiation of the quality of the products (Baker & English, 2011).

Conclusion

The main concept for the study in this situation has been the determination of the best feasible project evaluation technique that can be adopted by Dell
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Corporation taking into consideration the outlined factor of an NPV of +\$10. The analysis of the same reveals that mainly the discounted cash flow technique would be best placed as a technique to evaluate the intended project and associated returns. Various companies have in their evaluations used this criterion owing to its ability to convey the economic situation of a company under capital constraints (Danielson & Scott, 2006). However, as has been noted above, Dell Corporation could integrate this technique with a real options model for capital valuation in order to obtain sufficient results.

References

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