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The Importance of Investment Decisions in Project Management

The financing decision alongside with investment decision represents the core of financial management. The paper presents the main steps in realizing investment projects, the option criteria used in pre-investment analysis, the techniques of financing the investments project, but also the methods of evaluation applied in selecting the most suitable project, accordingly with company's developlment strategy and policy.

Keywords: *investment projects, financial decision, project evaluation, economcal and financial analysis*

1. Introduction

Through the investments projects the investors pursue the fulfillment of the targets defined in the development strategies and policies of every company, satisfying this way the interest of all types of investors – shareholders, creditors, managers, employees.

The investments' issue is an up-to-date one, because as Alvin Toffler emphasize "the anonymous decision groups that operate the investments' lever represent the elites in all industrial societies"(Toffler, 1980:267).

The investments should be tightly approach with the process of development and the economical increase. The economical development depends on the management's ability to (Zaiţ, 1987: 2):

a) find the investment alternatives accordingly to the defined targets and objectives;

b) improve the development strategies and policies in order to increase the investments' effects;

c) select the investment projects that allows the reasonable use of all material, financial and labor resources in order to achieve the targets.

All these conditions have to insure the efficiency of investment projects, making the investment decision extremly important for the financial management.

2. Option criteria in investments decisions

In order to coordinate the companies' investment process is necessary to ground a coherent financial strategy, because all the other company's activities are conditioned by this.

The investment strategy set the companies' main objectives in investment field, the actions that should develop, the methods of accomplish the targets, the financial resources and the ways this resources will be distributed. This strategy is bound up with the other strategies of the company – market, technical or labour strategy.

The investment decision require the elaboration of the budget, that is not just an investments list, it should include analyse and the hierarchy of different investments projects. In order to realize the budget it is necessary to follow up next steps:

1. the collection of necessary data in order to establish the costs of the investments project and the choice of the suitable project, according to company's defined strategy, from technical view;
2. the verification of the concordance between project's output and the legal settlements (e.g. environmental requirements) and acquiring the necessary licenses;
3. the analyse of the opportunity of the project referring to the profitability, effectiveness, generated cash-flows and it's accordance with the investment strategy;
4. the elaboration of the budget of the project, the prediction of the cash-flows within the entire period of the project – pre-investment, investment and exploiting stage, and the comparison with it's costs.

Finally, these analysis lead to one of the following investments decisions: the acceptance, the rejection of a project and choosing of one ore more projects from all the alternatives. In order to choose an investment project, there are three option criteria that should be considered:

a) The simply option criteria – are easy to be applied, being common used; such criteria are: the cost criteria, the recover period criteria and profitability criteria. These criteria do not take into account the risks and the time influence on investment cash-flows.

b) The option criteria based on actualization – time influence is decisively upon investment projects because time strongly affects the future cash-flows through the inflation and other factors.

c) The option criteria in uncertainty conditions. The uncertainty is specific to the investments projects because it affects all the cash-flows elements: the expected values of economical and financial results – profit, net value, revenues, expenses – all these being influenced by the costs, selling prices, sales. Some of the most important data used in project evaluation can not be accurately foreseen: the output, the selling prices, the costs, the consumptions or the evolution of the markets. During the exploiting process can appear difficulties in assuring the human, material, energetic or financial resources or modifications of loans' interest rate or inflation rate.

These are the reasons why the investment projects should be preceded by analytical analyses of the associated risks. Choosing the optimal project should take into consideration the profitability, the economical and financial effectiveness, liquidity or solvency requirements, but also the specific risks.

3. The mechanisms of financing the investments projects

The financing decision alongside with investment decision represents the core of financial management. The financial management has to find not only enough financial resources to achieve the objectives, but also at a low cost.

Long, medium or short term financing can be provided from own or borrowed capital. Finding the optimum combination between own and external funds represents the essence of financing decision and a challenge for any financial manager (Giurgiu, Duma, 2005: 64).

A. Private equity capital represents the funds obtained as increase of capital from shareholders. For blue chips companies is easy to attract funds when new shares are offered; but more difficult is for the new companies. The most used types to increase the own capital is considered:

A.1. Venture capital represents a form of private equity capital provided to immature, high potential companies in the interest of generating a return through an eventual realization event. Venture capital investments are generally made as cash in exchange for shares in the invested company. Venture capital generally comes from institutional investors and high net worth individuals, being pooled together by dedicated investments companies.

A.2. Business Angels are affluent individuals that provide capital for start-up businesses in exchange for ownership equity or convertible debt.

A3. Growth of own capital - issuing new shares or incorporation of own funds in capital.

B. Borrowed capital represents external funds obtained in order to finance the projects, the most used forms are:

B.1. Bank loans are well known and the most used external financing form. In order to get a credit, the companies have to present an application with a detailed presentation of the company, of the investment project that would be financed, the efforts' and effects' foresight, the financials of the company, the business plan and the available guarantees.

B.2. Bonds issuance – create the possibility to the issuer to borrow funds for a defined period of time at a fixed interest rate. There is a variety of types of bonds because of the adjustment process to the issuers' needs and investors' requirements.

B.3. Leasing is a financing form that may provide more flexibility to a business.

B.4. Other forms like amortization, net profit, reserves, funds obtained from assets liquidations, etc.

There are six elements considered relevant for the financing decisions known as FRICTO Analysis – acronim for the following parameters: Flexibility, Risk, Income, Control, Timing and Others.

4. Evaluation methods for investment projects

The evalution of the investment projects is one of the key components in the analysis of economic development strategies. The economical and financial assessments of investment projects within the financial institutions realized in developed countries is based on the combination of traditional and modern methods, characterized through scientific fundament, tested and validated by years of practice.

Within the last decades extensive studies and researches were realized in order to set principles and improve the methods and techniques used in the economical and financial analysis of the projects in pre-investment phase.

For the traditional methods used to asses the economical and financial effectiveness is specific:

- the static approach of the processes and phenomena;

- the simplification of the real economical situations during the realized products' cycle, working with constant numbers and average values of the predicted economical effects and costs;

- the ignorance of the variability of the expenses, revenues and profits within the project period;

- the uncertainty and the economical risk are not strongly approach, but in concordance with recovery period.

For the modern, rational methods used in the assesment process of the projects, the main characteristics can be considered:

- the dynamic approach in analysis of the investment projects,

- the consideration of the time as an important factor in order to generate the actual value of costs, revenues or expenses within he entire period (investment and utilization)

- the uncertainty and the economical risk are strongly approach within the analysed period, through the sensitivity analysis or probabilistic evaluation of indicators.

The combination of traditional and rational methods is used for small and medium investment projects, but for far-reaching projects the dynamic analyse based on modern methods is preferred.

The evaluation of the investments projects is realized by a system of indicators, no matter the method used. The system includes specific indicators adapted to the technical and economical industry of the project, with high significance for the project's performances and investors' interests. Generally, a system of indicators includes among five and nine technical and economical indicators.

Therefore is important that the methods used to assure a pertinent, realistic analysis of the investments projects from economical effectiveness and to suit the investors' objectives.

5. Conclusion

The great variety of risks that threat the effectiveness of investment projects makes necessary to realize a proper analyse. The association of traditional and modern methods, the variable number of technical and economical indicators has to ensure an accurate, pertinent and realistic analysis in order to lead the manager to the right decision which projects to be financed.

Finding the financial resources for the investments projects in the optimum combination related to term, risks and costs represents the greatest challenge for a financial manager. This way the financial manager can assure the projects' performance, but also the increase of the company's value and investors' interest.

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