

## CASE STUDY 3:2

### Project Selection at Nova Western, Inc.

Phyllis Henry, vice president of new product development, sat at her desk, trying to make sense of the latest new project proposals she had just received from her staff. Nova Western, Inc., a large developer of business software and application programs, had been experiencing a downturn in operating revenues over the past three quarters. The senior management team was feeling pressure from the board of directors to take steps to correct this downward drift in revenues and profitability. The consensus opinion was that Nova Western needed some new product ideas, and fast.

The report Phyllis was reading contained the results of a project screening conducted by two independent groups within the new product development department. After several weeks of analysis, it appeared that two top contenders had emerged as the optimal new project opportunities. One project, code-named Janus, was championed by the head of software development. The other project idea, Gemini, had the support of the business applications organization. Phyllis's original charge to her staff was to prepare an evaluation of both projects in order to decide which one Nova Western should support. Because of budget restrictions, there was no way that both projects could be funded.

The first evaluation team used a scoring model, based on the key strategic categories at Nova Western, to evaluate the two projects. The categories they employed were: (1) strategic fit, (2) probability of technical success, (3) financial risk, (4) potential profit, and (5) strategic leverage (ability of the project to employ and enhance company resources and technical capabilities). Using these categories, the team evaluated the two projects as shown here. Scores were based on: 1 = low, 2 = medium, and 3 = high.

#### Project Janus

Category	Importance	Score	Weighted Score
1. Strategic fit	3	2	6
2. Probability of technical success	2	2	4
3. Financial risk	2	1	2
4. Potential profit	3	3	9
5. Strategic leverage	1	1	1
			Score = 22

#### Project Gemini

Category	Importance	Score	Weighted Score
1. Strategic fit	3	3	9
2. Probability of technical success	2	2	4
3. Financial risk	2	2	4
4. Potential profit	3	3	9
5. Strategic leverage	1	2	2
			Score = 28

The results obtained by this first team suggested that Project Gemini would be the best choice for the next new project.

The second team of evaluators presented an NPV analysis of the two projects to Phyllis. In that analysis, the evaluators assumed a required rate of return of 15% and an anticipated inflation rate of 3% over the life of the project. The findings of this team were as follows:

#### Project Janus

Initial investment = \$250,000	
Life of the project = 5 years	
Anticipated stream of future cash flows:	
Year 1	= \$ 50,000
Year 2	= 100,000
Year 3	= 100,000
Year 4	= 200,000
Year 5	= 75,000
Calculated NPV = \$ 60,995	

#### Project Gemini

Initial investment = \$400,000	
Life of the project = 3 years	
Anticipated stream of future cash flows:	
Year 1	= \$ 75,000
Year 2	= 250,000
Year 3	= 300,000
Calculated NPV = \$ 25,695	

Thus, according to this analysis, Project Janus would be the project of choice.

The analyses of the two projects by different means yielded different findings. The scoring model indicated that Project Gemini was the best alternative.