

Question Number	Indicative content	Mark
1	Knowledge 2, Application 2, Analysis 3, Evaluation 3 • All three methods of investment appraisal, payback, average (accounting) rate of return and discounted cash flow use estimated net cash flows and work on the assumption that these cash flows will be received • Vegano operates in a growing market which may attract new entrants. This could impact on future net cash flows which may impact on the accuracy of investment appraisal techniques • Investment appraisal techniques such as payback and ARR don't take into account the time value of money which limits the the value of these methods of investment appraisal • Payback ignores net cash flows after the payback period and therefore does not consider the overall return of the investment • The ARR treats profits arising late in an investment the same way as those which may arise early in the investment • The result obtained from using discounted cash flow depends on the discount rate used and it can be difficult to set an appropriate rate • All investment appraisal methods ignore qualitative factors <i>Potential counter-balance</i> • Investment appraisal techniques may be of value to Vegano as they use quantitative data to help evaluate an investment, in the case, a second café • All three methods use net cash flows which will encourage Vegano to carry out research to ascertain the cash inflows and cash inflows of the second café, as well the cost of the investment. This can help reduce risk and help the owners of Vegano decide whether they should proceed with the investment • Payback focuses on how quickly the initial investment is returned which is a key measure of risk and useful for Vegano who operate in a growing market • The ARR provides a percentage which can be compared to a target return for and/or compared with the banks rate of interest • Discounted cash flow takes into account the time value of money and uses discount factors to bring cash flows back to their present value which can provide a more accurate assessment of whether Vegano should proceed with the investment <i>Possible judgement</i> • Investment appraisal techniques have their limitations as they use forecasted data and caution needs to be exercised when making decisions based purely on quantitative data, especially as Vegano operates in a growing market which could impact on the accuracy of the estimated cash flows • Investment appraisal techniques may be of value as they use quantitative data to aid decision making and allow Vegano to estimate how quickly the investment will be paid back and the overall profitability of the second cafe	(10)