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#### The Engineering Economist >

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**Original Articles** 

# Average Internal Rate of Return and Investment Decisions: A New Perspective

#### Carlo Alberto Magni

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project's profitability and correctly ranks competing projects. With such a measure, which we call average internal rate of return, complex-valued numbers disappear and all the above-mentioned problems are wiped out. The economic meaning is compelling: it is the project return rate implicitly determined by the market. The traditional IRR notion may be found as a particular case.

## Notes

For example, the cash flow stream (-4,12,-9) has a unique IRR equal to 50%. According to the IRR criterion, the project must be accepted if the market rate is smaller than 50%, but the NPV is negative for any rate different from 50%, so the project is not worth undertaking. (Note that this example implicitly introduces a further class of problems: if a project is not unambiguously individuated as either an investment or a borrowing, the IRR profitability rule is ambiguous.)

The approach is compatible with a bounded-rationality perspective: in this case r is a subjective threshold (<u>Magni, 2009b</u>).

| The IRR rule is semantically not satisfactory because it is | not associated with a univocal |
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