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'How To'

How to Appraise a Project

In this how-to supplement, we provide a brief idea about steps before taking up any project appraisal and different appraisal aspects for a development project in brief.

What is a project appraisal?

A typical project cycle comprises of 6 stages as given below.

1. Identification
2. Formulation
3. Appraisal
4. Implementation
5. Monitoring
6. Evaluation

The third phase in the project cycle is appraisal.

Appraisal is a comprehensive and systematic review of all aspects of a project proposal. It involves a careful checking of the basic data, assumptions and methodology used in project preparation, an in-depth review of the work plan, cost estimates and proposed financing, an assessment of the project's organizational and management aspects, and finally the validity of the financial, economic and social benefits expected from the project.

It should highlight the weak areas in the project with the ultimate objective of strengthening them adequately to ensure final success of the project.

If a project is well formulated and thoroughly appraised, a good follow-through on the subsequent stages of the project cycle will see to its goals being achieved.

Points to be kept in view:

Before taking up the project appraisal, it is important to understand the environment in which the project is to be implemented and has to sustain itself.

The appraisal team should have good knowledge and competency in their respective fields – technology, finance, economical and environmental.

Project should be appraised within a time bound program– any undue delay distorts profitability projections and success of the project becomes a difficult proposition.

Steps and methodology for appraisal:

Before taking up for detailed appraisal

Step-1 Verification of Information

Step-2 Inspection

First Step

The first step in detailed appraisal is in regard to the information submitted by the entrepreneur.

The team has to check and verify whether –

Adequate data has been furnished by the entrepreneur

Prime facie, information furnished is correct or not.

During this stage, personal discussions between the financial institutional personnel and the borrowing concerns are necessary and desirable, as this may reduce avoidable correspondence and facilitate expeditious disposal of the application.

After verifying the data, the team can proceed to appraise the project in detail if:

- If it has priority according to government guidelines

- The promoter inspires confidence
- The technology to be adopted is well proven
- The product to be manufactured produced has a market potential
- The price of the product is not unreasonably high
- The promoter's contribution is not unduly low.
- Profitability estimates are conservative and indicate repayment of the loan within reasonable time.

You can reject a project application without detail appraisal if it has some of the below features:

- Banker's report on the applicant/ promoter of the project is not satisfactory
- The applicant reported to have indulged in illegal and anti-social activities
- Cost of the project is unduly high
- Promoter's contribution is unduly low and he is reluctant to increase it.
- Process know-how/ Technology to be adopted has not been proved successful in commercial scale or has been obsolete
- Second hand equipments to be equipped (if any) is too old and will not have trouble free residual life.
- The project is violating any government guidelines
- Product price is unduly high and not in par with the market competitors
- Profitability estimates are unrealistic.

The team can give preference to the project / proposal if it:

- Utilizes any industrial waste or agricultural surplus as raw material
- Is export-oriented or import-substitutes
- Is employment oriented
- Is located in specified backward or less backward areas

Second step—2

Second step is the site inspection by the appraisal team. During inspection, the appraisal team should:

- Give attention regarding suitability of the site, distance from railway station, sources of raw material, national highway, market for end-products, timely availability of utilities.
- Scan the environment protection arrangements
- Ascertain the sources of skilled and unskilled labor
- Availability of social infrastructure
- Collect market report on the financial strength, credibility and capacity of the promoters.

If the team is satisfied with the inspection result, then it can proceed to the third and most important step – Appraisal.

Appraisal of a development project

Appraisal is needed not only for the sake of satisfying the donors but also to ensure that the community selects appropriate projects to fill the gaps it identified as a part of the sub-project cycle. Hence, the process of appraisal should include technical experts as well as the community too.

The following six criteria are to be considered during a project appraisal:

1. Feasibility
2. Viability
3. Sustainability
4. Productivity
5. Equity
6. Cost-effectiveness

Feasibility

Feasibility means whether some idea will work or not i.e. whether the proposed project is possible under the given circumstances is to be ascertained:

To check this the team have to ascertain

- Suitability of the proposal to the social and cultural setting.
- Whether and wherefrom the necessary technical know-how to convert the idea into a tangible product may be available? If available, suitability of it to the present condition is to be ascertained.
- What would be the investment requirement and whether can be raised as expected?
- Affect on the economy and ecology is to be verified.

Economy: Whether the investment proposal contributes to the developmental objective of the country and whether this contribution is likely to be large enough to justify the use of scarce resources such as capital, skilled labour, managerial talents etc. that would be needed to implement and operate the project. In economic analysis, input and output prices are adjusted to reflect true social or economic values

Ecology: What is the likely damage caused by the project to the environment?

- What is the cost of restoration measures required to ensure that the damage to the environment is contained within acceptable limits?

Viability:

The team has to ascertain whether the proposed project will yield adequate financial returns or not.

If the person or community decide to keep the money in bank instead of investing it in the proposed activity, he would have received interest on the deposit without facing much risk.

- Will the proposal yield higher returns than the bank rate without unduly increasing the risk?
- Will the persons involved realize higher wage returns for their time?

If the answers to these two questions are yes, the proposal can be considered viable. The assumptions behind the calculations will have to be checked for consistency and feasibility.

The team can use some of the tools to check the financial viability:

- Rate of Return,
- Total Benefits/Total Costs
- Sensitivity analysis

- (Financial tools are explained in detail in the attachment – Appraisal of business/ commercial project)
- Economic viability: Whether the project falls under Banned items – non bio-degradable products, IMFL, tannery, dyeing, activities involving child labour, activities hazardous to health.

Sustainability

The team can consider investing resources in the project only if the proposed benefits of it are going to continue for a extended period of time.

Also check for the sustainability of the benefits economically, environmentally, operationally.

Community understanding and involvement in the project has a great affect on the sustainability of the project.

Productivity

Productivity constitutes positive changes in one or more of the four arrows of livelihoods of the poor. A proposal need not be invested in if it does not contribute positively to any one of the arrows of the poor people.

This means the team has to verify whether it provides enabling environment so as to:

- Increase the productivity – increase in yield, quality, income
- Decrease in expenditure;
- Creating assets; Generation of employment for the poor; Skill building;
- Reduce risks

Equity

The proposal should be such that it does not cause suffering to even a single poor person. This is the negative test for the proposal. The benefit caused to several poor people is not a justification for a poor person to suffer.

For example, for the benefit of several thousands of farmers who gain from irrigation created by a dam, a few hundreds of farmers should not suffer submergence of land. If there is no other way for the dam to be built, the farmers whose lands are submerged should be compensated with a benefit equal to that the farmers downstream would receive from the dam.

Gender Equity- verify whether women are benefited directly, Increased burden/drudgery to any woman, Increased decision-making, New (other than traditional so called 'feminine') Skills acquired by women, New non-traditional jobs to be done, New assets created on/transferred to women's names or joint titles, Resistance from the family or Resistance from the men for women to participate in the process, Curtailed mobility of any woman.

Child Equity – Verify whether Child Labor not increased, Decreased work for children at home, No decrease in attendance at schools, Children's health unaffected, Childcare unaffected

Cost-effectiveness: The appraisal needs to consider whether alternative methods have been examined and whether the proposed method is the least cost method among them all.

- Check whether there is
- Reasonable cost per unit or not
- Availability of other cheaper alternative
- Benefit to beneficiary is more than wage rate

In some cases, the proposal may be passed by the community but may be found not suitable by technical experts. Then a discussion is to be organized between the community and the experts so that the knowledge of the community and that of the technical experts gets integrated and a newer solution or method would emerge in the place of the proposal. This would also build the capacities of the community to appraise the proposals by taking into aspects they had not considered earlier.

Thus the objective of an appraisal is not to disallow a proposal but to make the proposal much stronger.

The appraisers have to consider the proposal and suggest ways to improve the proposal to meet all the criteria for appraisal. ❖