Chapter Two
Project Identification

2.1. Introduction

Project identification is the first and perhaps, the most crucial stage of project cycles. This chapter discusses phases of project identifications, those who identify project ideas, and how to prioritize, rank and select projects.

2.2. Pre-Identification Activities

"Pre-identification" is an important preface to project identification. This pre-identification stage involves surveying, reviewing, inventorying and analysis of strategies and policies, natural resources data and socio-economic information. It is a very important phase in project planning. Unfortunately, it is an aspect of planning, which is either, almost totally ignored or for which inadequate resources are provided in most developing countries.

There are a number of reasons:

- First, and perhaps most important of all, is *complete ignorance* - an ignorance of need and ignorance of cost- effective ways of carrying the research, surveys, inventorying of resources and integrating and analyzing the information.
- Second, such work tends to be regarded as an expensive overhead cost and therefore, expendable in difficult times of budgetary.
- Third, a lot of the work has tended to be time consuming, people cannot wait for results and do not consider it important to even start it.

Nowadays, modern technology is revolutionizing the survey methods and the means for carrying out synthesis and analysis, speeding up some processes, reducing the costs of others and providing new ways of looking at things.

A good idea being a prerequisite to sound project formulation and the analysis of data identifying gaps and throwing up ideas for possible projects, project identification must be carried out also within a framework of national, regional and sectorial development (including pricing, taxation and subsidy) policies. Otherwise, much time and effort might be wasted in identifying and preparing projects which would be reflected on policy grounds or which

might turn out to be unfeasible because of, for example, a tax and subsidy policy.

Thus, those who are responsible for identifying projects need to be aware of accepted strategies and policies and also be in a position to feedback information to those who are responsible for formulating policies.

2.3. Project Identification

The search for *promising project ideas* is the first step towards establishing a successful venture. The key to success lies in getting into the right business at the right time. The objective is to identify investment opportunities, which are *at first glance* feasible and promising and which merit further examination and appraisal.

Project identification consists in finding projects, which could contribute towards achieving specified development objectives. In principle, project identification should be an integral part of the macro-planning exercise, with sectorial information and strategies as the main source of project ideas.

2.3.1. Phases of project identification

There are four phases of project identification. These are:

1. **Actual project identification**: this involves the generation of project ideas by formal and informal institutions and individuals.
2. **Description of project Idea**-this involves describing, summarizing the idea and putting in writing
3. **Screening**– is an initial review of project ideas and concepts to use if they should be advanced or abandoned at an early stage
4. **Prioritization**- refers to ranking and selection of projects against a set of criteria to identify the best projects to move actively into the design and development stage.

2.3.2. Who Identifies Projects?

Projects can be identified by many different agencies depending on the type of project under consideration. It may be identified by:

- ✓ *Small producers*
- ✓ *Large scale producers*

- ✓ *Product marketing organizations*
- ✓ *State owned enterprises*
- ✓ *Government ministries*
- ✓ *Development banks*
- ✓ *Local governments*
- ✓ *NGOs*

The same project idea may be identified separately in different identification exercises by different agencies and at different stages of development of the idea.

Projects can be identified by institutions from the information they hold and receive. This information can be formal surveys and reviews, or it can be informal, such as local people's views and opinions. The ***main formal information sources*** of a project idea may be:

- ✓ *Policy reviews and development plans made by central government*
- ✓ *Sectorial surveys by technical ministries*
- ✓ *Survey conducted by local government and other organizations*
- ✓ *Formal problem diagnosis and analysis*
- ✓ *Environmental and natural resource survey*
- ✓ *Reviews and evaluations of past projects*
- ✓ *Community meetings and public gatherings*
- ✓ *Private sector, cooperative etc…*
- ✓ Analyze the performance of existing industries;
- ✓ Examine the inputs and outputs of various industries;
- ✓ Review imports and exports;
- ✓ Look at the suggestions of financial institutions and development agencies;
- ✓ Investigate local materials and resources;
- ✓ Analyze Economic and Social Trends; (value of time, leisure and recreational activities)
- ✓ Study new Technological Developments;
- ✓ Draw clues from consumption abroad; (new for the local but well-known abroad)
- ✓ Explore the possibility of reviving sick units of the industry;
- ✓ Attend Trade fairs;

Stimulate the flow of information/data

In general, regardless of the approaches/techniques used, it demands stimulating the flow of ideas is valuable because it will give you an opportunity to identify alternative project ideas. This can be achieved by taking the following actions:

i. *SWOT Analysis*:

SWOT is an acronym for ***strengths***, ***weaknesses***, ***opportunities***, and ***threats***. SWOT Analysis represents a conscious, deliberate, and systematic effort by an organization to identify opportunities that can be profitably exploited by it. Periodic SWOT analysis facilitates the generation of project ideas. SWOT analysis involves studying the internal and the external environment as discussed below:

a. *Monitoring the external Environment*

The important aspects studied in monitoring the key sectors of the environment are as follows:

- **Economic Sector**
  - State of the economy
  - Overall rate of growth
  - Cyclical fluctuations
  - Linkage with the world economy
  - Balance of payment situation
- **Governmental sector**
  - Industrial policy
  - Government programs and projects
  - Tax framework
  - Subsidies, incentives
  - Import and export policies
  - Monitory policy
- **Technological Sector**
  - Emergence of new technologies
  - Access to technical know-how, foreign as well as indigenous
  - Receptiveness on the part of industry
- **Socio-demographic sector**
  - Population trends
  - Age shifts in population
  - Income distribution
  - Educational profile
  - Attitudes toward consumption and investment
- **Competition Sector**

- Number of firms in the industry and market share of the dominant firms
- Degree of homogeneity and differentiation among products
- Entry barriers
- Comparison with substitutes in terms of quality, price, functional performance, etc.
- Marketing policies and practices

➢ **Supplier Sector**
- Availability and cost of raw materials and sub-assemblies
- Availability and cost of energy
- Availability and cost of money

b. Corporate Appraisal (internal assessment)

Important aspects to be considered under this are:

➢ **Marketing and distribution**
- Market image
- Product line
- Market share
- Distribution network
- Customer loyalty

➢ **Production and Development**
- Condition and capacity of plant and machinery
- Degree of vertical integration
- Locational advantage
- Cost structure

➢ **Research and development**
- Research capabilities of the firm
- Track record of new product developments
- Laboratories and testing facilities
- Coordination between research and operations

➢ **Corporate resources and personnel**
- Corporate image
- Dynamism of top management
- Competence and commitment of employees
- State of industrial relations

➢ **Finance and Accounting**
- Financial leverage and borrowing capacity
- Cost of capital
- Tax situation
- Accounting and control system
- Cash flows and liquidity

ii. *Clear Expression of Objectives*:

Operational objectives of a firm may be one or more of the following:

- Cost reduction
- Productivity improvement
- Increase in capacity utilization
- Improvement in contribution margin etc.

A clear articulation and prioritization of objectives helps in channeling the efforts of employees and prods them to think more imaginatively.

iii. Fostering a Conducive Climate:

To tap the creativity of people and to harness their entrepreneurial urges, a conducive organizational climate has to be fostered.

2.3.3. Sources of Project Ideas

In practice, however, projects do not always derive from national and sectorial plans. Instead, they may originate from several sources. Irrespective of their origin, project ideas should, in general, are at overcoming constraints on the national development effort, be they material, human or institutional constraints, or at meeting unsatisfied needs, and demand for goods and services.

Constraints, **needs** and **demand** should be interpreted broadly to include, for example foreign exchange constraints that might indicate the need to undertake projects for export promotion or import substitution.

The varieties of projects make it impossible to prepare an exhaustive list of sources from where project ideas emanate; much depend on the experience and imaginative of those entrusted with the task of initiating development project.

In general, one can distinguish two levels where project ideas are born: *the **macro**-level & the **micro**-level.*

a) Macro-Level project Ideas

At the macro-level, project ideas emerge from:

1. National policies, strategies & priorities as may be enunciated by government from time to time;
2. National, sectorial, sub-sectorial or regional plans and strategies supplemented by special studies, sometimes called *opportunity studies,* conducted with the explicit aim of translation of national and sectorial, sub-sectorial and regional programs into specific projects;
3. General surveys, resource potential surveys, regional studies, master plan and statistical publications, which indicate directly or indirectly investment opportunities.
4. Constraints on the development process due to shortage of essential infrastructure facilities, problems in the balances of payments, etc.
5. Government decision to correct social and regional inequalities or to satisfy basic needs of the people through development projects.
6. A possible external threat that necessitates projects aiming at achieving, for example, self-sufficiency in basic materials, energy, transportation, etc.
7. Unusual events such as droughts, floods, earthquakes, hostilities, etc.
8. Government decisions to create project-implementing capacity in such area as construction etc.
9. At the macro-level, project ideas can also originate from multilateral or bilateral development agencies & as a result of regional and international agreements in which the country participate.
10. In addition, individual inspiration, institutions, workshops, and development experiences of other countries may point to some interesting project ideas.

b) Micro-Level project Ideas

At the micro-level, the variety of sources is equally broad. Project ideas emanate from:

1. The identification of unsatisfied demand or needs.
2. The existence of unused or underutilized natural or human resources and the perception of opportunities for their efficient use.
3. The need to remove shortages in essential materials, services or facilities that constrain development efforts;
4. The initiative of private or public enterprises in response to incentives provided by the government
5. The necessity to complement or expand investments previously undertaken;

6. The desire of local groups/organizations to enhance their economic status & improve their welfare;
7. Project Proposals could also originate from foreign firms either in response to government investment incentives or because they consider production within the country a better way to secure a substantial share of the domestic market for their products.

Project ideas are identified where there is a demand for the output of the project and where it is thought that the resources can be made available to satisfy the demand. In other words:

- ✓ Demand
- ✓ Need, and
- ✓ Resource are the base for project identification

2.3.4. Project concepts and profiles

Once a project idea has been conceived, the next stage is to describe the idea so that it can be prioritized and move on to the next stage in the process. This may involve the preparation of a project identification ***report*** or ***project concept*** or ***profile***. It might be part of a more general sectorial or regional planning exercise or the result of a participatory approach at the village level by a district officer. Whenever, or how, it is developed it is essential to have a clear idea of what the proposed project is supposed to be and what it hopes to achieve. A project concept or profile should be short but should include answers to the following questions:

1. <u>Justification and purpose</u>

- ✓ *What goal is the project contributing to?*
- ✓ *What is the purpose of the project, what does it intend to achieve?*
- ✓ *What problem is the project addressing?*
- ✓ *What is the justification of the project?*
- ✓ *What demands, needs or opportunities is the project addressing?*
- ✓ *What are the main alternative ways for meeting the project's objectives?*
- ✓ *What existing information sources were, or can be used, in identifying and developing the project?*

2. <u>Beneficiaries and stakeholders</u>

- ✓ *Who will benefit from the project?*
- ✓ *Who identified the project?*
- ✓ *Who has a shared or stake in the project?*
- ✓ *Who will be positively, and negatively, affected by the project?*
- ✓ *Which institutions are targets of the project?*

3. **Resources and institutions**
   - ✓ *What potential resources may be available for implementing the project?*
   - ✓ *Which organizations are to be involved in project planning and implementation?*
4. **Policies and plans**
   - ✓ *How does the project proposal fit into sectorial or regional plans?*
   - ✓ *Does the project fit in to current policies of the government?*
5. **Impacts**
   - ✓ *What are the likely the major positive and negative impacts of the project?*
   - ✓ *What are the likely the major positive and negative environmental impacts of the project?*
6. **Support**
   - ✓ *What is the level of the government's support?*
   - ✓ *Does the project have the support of the beneficiaries or local community?*
7. **Risks**
   - ✓ *What are the chances of the project achieving its objectives?*
   - ✓ *What are the main risks associated with the project?*

2.3.5. Prioritization, Ranking and Selecting Potentially promising ideas

Once a list of project ideas has been put forward, the first step is to select one or more of them as potentially promising. This calls for a quick preliminary screening by experienced professionals who could also modify some of the proposals. At this stage, the screening criteria are vague and rough, that becomes specific and refined as project planning advances.

During the preliminary screening/selection to eliminate ideas, which prima facie are not promising, it is required to look into aspects such as:

- ❖ ***Compatibility with the promoter*** (interest, personality and resources of entrepreneur)

- ***Consistency with government priorities*** (license, national goals & priorities, environmental effects contrary to government rules, etc.)
- ***Availability of inputs*** (capital requirements, technical know-how, raw materials, power supply...)
- ***Adequacy of market*** (current domestic market, competitors & their market shares, export markets, quality-price profile of the product Vs competitive products, sales and distribution system, projected increase in consumption, barriers to the entry of new units, socio-economic and demographic trends favorable to increased consumption, patent protection etc.)
- ***Reasonableness of costs*** (costs of material inputs, labor costs, factory overheads, general & admin expenses, selling and distribution costs, service costs, economies of scale etc.)
- ***Acceptability of risk level*** (vulnerability to business cycles, technological changes, competition from substitutes, competition from imports, governmental control over prices & distribution etc.)

During preliminary selection, the analyst should eliminate project proposals that:

- Are technically unsound and risky;
- Have no market for the output;
- Have inadequate supply of inputs;
- Are very costly in relation to benefits;
- Assume over-ambitious sales and profitability.

Obviously, since the criteria tend to be somewhat unclear, much depends on the *experience* and *sense of objectivity* of the professionals applying them. It is, therefore, necessary to conduct this screening, even with distinct criteria, in order to reduce to a manageable number of project alternatives to which more work and time will be devoted. Indeed, project planning can be viewed as a process of elimination, i.e., elimination of interior alternatives.

As a result of the preliminary screening exercises, a project profile, an opportunity study report, or an identification study report, as appropriate, is prepared showing which project alternatives should be rejected and which ones may be advanced to the next stage. One way of preliminary selection is rating.

Project Rating Index

When a firm evaluates a large number of project ideas regularly, it may be helpful to streamline the process of preliminary screening. For this purpose, a preliminary evaluation may be translated into a project-rating index.

The steps involved in determining the project-rating index are as follows:

1. Identify factors relevant for project rating.
2. Assign weights to these factors (the weights are supposed to reflect their relative importance).
3. Rate the project proposal on various factors, using a suitable rating scale. (Typically a 5-point scale of a 7-point scale is used for this purpose).
4. For each factor multiply the factor rating with the factor weight to get the factor score.
5. Add all the factor scores to get the overall project-planning index.

The following table illustrates the determination of the project-rating index. Once the project rating index is determined, it is compared with a pre-determined hurdle value to judge whether the project is *prima facie worthwhile or not.*

Rating Index:

Factors	***Factor Weight***	***Rating***					***Factor Score***
		VG *5*	*G* *4*	*A* *3*	*P* *2*	*VP* *1*	
Input availability	*0.25*			✓			*0.75*
Technical know-how	*0.10*		✓				*0.40*
Reasonableness of cost	*0.05*		✓				*0.20*
Adequacy of market	*0.15*	✓					*0.75*
Complementary relationship with other products	*0.05*		✓				*0.20*
Stability	*0.10*		✓				*0.40*
Dependence on firm's strength	*0.20*	✓					*1.00*
Consistency with governmental priorities	*0.10*			✓			*0.30*

Rating Index	*4.00*

During the selection process, each project can be assessed against each of the criteria to give a rating. At this stage of the project cycle this is more likely to be qualitative than quantitative. Certain criteria can be given greater weighting to reflect the importance of the criteria in determining the overall rank of the project as shown in the above example.