

## SUMMARY

# Guidelines for the Economic Analysis of Projects



Economic viability depends on the sustainability of project effects over the project's life. Photo credit: ADB.

*The Asian Development Bank has revised its guidelines for project economic analysis, which help ensure investment decisions are based on economic and efficiency considerations.*

## Overview

The economic analysis of development projects helps to ensure that scarce resources are allocated efficiently, and investment brings benefits to a country and raises the welfare of its citizens. It is a tool used by the Asian Development Bank (ADB) to ensure that its operations comply with the ADB Charter and contribute to the broad objectives of poverty reduction, inclusive economic growth, environmental sustainability, and regional integration.

The guidelines in this publication are a revised version of the 1997 edition. The revision responds to the changing development context and ADB operational priorities, and aims to address the recommendations of the ADB Quality-at-Entry Assessments for more methodological work on project economic analysis.

The revised guidelines provide general principles for the conduct of project economic analysis. The appendices provide illustrations of their application.

Changes in the guidelines from the 1997 edition include

- revised minimum required economic internal rate of return for investment decisions;
- several issues that have emerged or become more important since the adoption of the 1997 edition, including economic analysis under various financing modalities, the treatment of the social cost of carbon, and economic analysis of regional economic cooperation projects; and
- a new chapter on benefit valuation by sector, which details the method for valuing project, benefits in major sectors of ADB operations.

These guidelines should be read together with handbooks, technical reports, and other reference materials published by ADB, which discuss sector-specific project economic analysis in detail.



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## I. Introduction

The Agreement Establishing the Asian Development Bank (ADB Charter) requires staff to “take the necessary measures to ensure that the proceeds of any loan made, guaranteed or participated in by the Bank are used only for the purposes for which the loan was granted and with due attention to considerations of economy and efficiency” (Article 14.11). It also states that “only economic considerations shall be relevant to their decisions” (Article 36.2).<sup>1</sup> Project economic analysis is a key tool to ensure that ADB operations comply with the mandate of the ADB Charter and contribute to the broad objectives of poverty reduction, inclusive economic growth, environmental sustainability, and regional integration. [Read more.](#)

## II. Scope of Project Economic Analysis

A well-conducted economic analysis should show that

- i. a project is in line with the development context of a borrowing country and ADB’s country partnership strategy;
- ii. there is strong rationale for the public sector and ADB to finance the project; and
- iii. the selected project represents the most efficient or least-cost option among all the feasible alternatives for achieving the intended project benefits and, when benefit can be valued, it will generate a positive economic net present value (ENPV) using the minimum required economic internal rate of return (EIRR) as the discount rate, i.e., the project has an EIRR higher than the discount rate.

[Read more.](#)

## III. Identification of Project Benefits and Costs

### **With and Without Project Scenarios, Constant Prices, and Project Life**

There are four broad steps in project economic analysis:

- i. Identify gross project benefits and costs;
- ii. Quantify and value the benefits and costs, initially in market or financial prices;
- iii. Adjust the costs and benefits to reflect their economic values; and
- iv. Compare gross economic benefits with economic costs..

[Read more.](#)

## IV. Economic Valuation of Benefits and Costs

Economic valuation of project benefits and costs involves converting their financial values into economic values, also known as “shadow pricing.” This conversion requires economic prices of project outputs and inputs to be estimated. Economic prices reflect values of goods, services, and other project effects on the national economy. The basis for estimating economic prices differs between internationally traded