

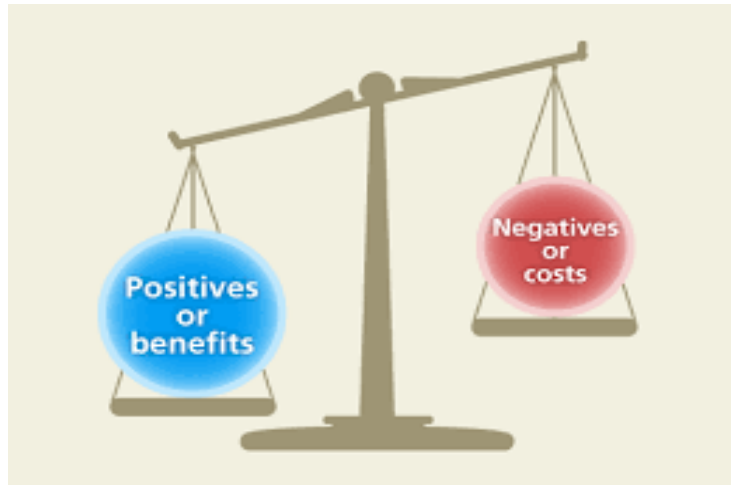
TENTH EXECUTIVE FOREST POLICY COURSE

**REVISITING THE POVERTY REDUCTION AGENDA IN THE CONTEXT OF SDGs:  
OPPORTUNITIES AND CHALLENGES FOR ASIA-PACIFIC FORESTRY**

15-25 MAY 2017  
COLOMBO, SRI LANKA



# TOOLS FOR MAKING THE RIGHT CHOICE: SOCIAL COST BENEFIT ANALYSIS



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# BACKGROUND

- ❑ One way or the other in our daily lives we are all calculating - either explicitly or implicitly - costs and benefits before we take important decisions.
- ❑ Most of the decisions – relating to education, employment, marriage, buying properties, having children, taking vacation, and even for that matter attending a course like this - results in certain costs and benefits.
- ❑ Eventually we are looking for options that will enhance the net benefits: benefits exceeding the costs.



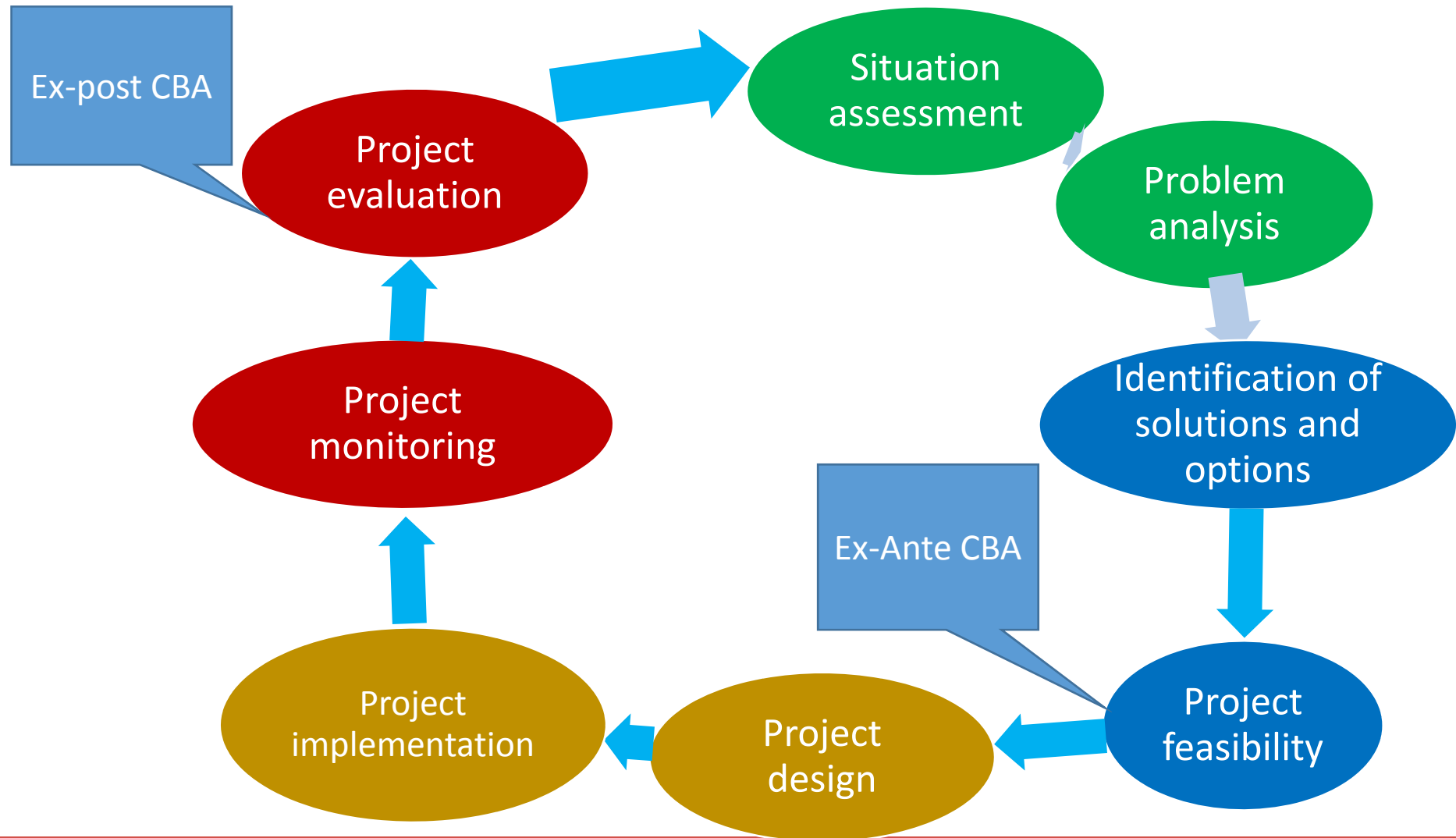
# BACKGROUND

- ❑ **Every public decision, including policies, plans, programmes and projects tend to have economic, social, environmental, cultural and such other impacts.**
- ❑ **Every choice has its associated costs and benefits. It also affects how costs and benefits are distributed between different segments in society as also between generations.**
- ❑ **In the context of poverty reduction, emphasis will be on enhancing the net benefits that accrue to the poor.**

# COST-BENEFIT ANALYSIS

- ❑ **Cost-benefit analysis has become one of the most important tools to assess the impact of public decisions, especially programmes and projects.**
- ❑ **From a simple assessment of net financial benefits, it has been refined to take into account broader economic, social and environmental objectives.**
- ❑ **This session will give you an overview of the how cost-benefit analysis is being used in forestry, especially to address social objectives like poverty reduction.**

# PROJECT CYCLE AND COST-BENEFIT ANALYSIS



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# SCOPE OF COST-BENEFIT ANALYSIS

- Analysis from whose perspectives? – Individual, Organization, Society or specific groups.
- Identification and quantification of costs and benefits.
- Putting a value to costs and benefits and to develop a cash flow table.
- Adjusting the costs and benefits to reflect economic, social and ecological considerations.
- Bringing them to a common time point for comparison using discounting.

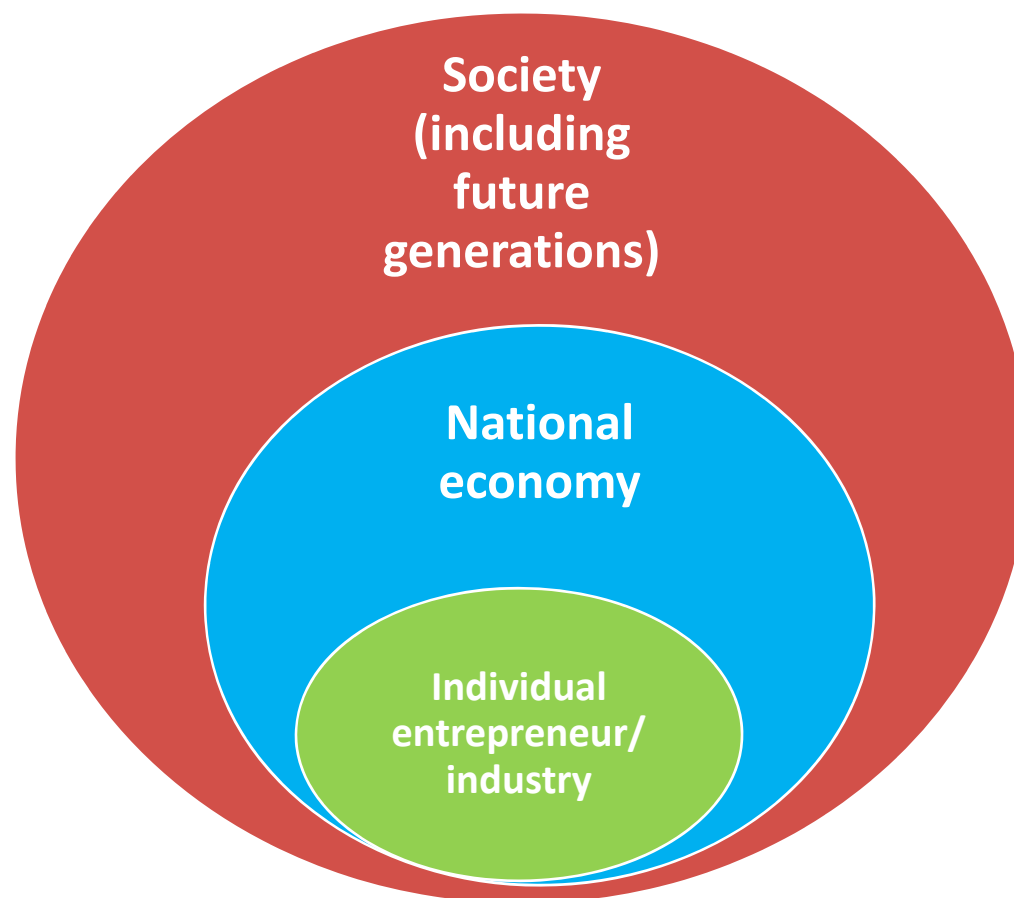
# SCOPE OF COST-BENEFIT ANALYSIS

- **Expressing the net effect of the project in terms of:**
  - ❖ **Net present value - NPV (Discounted Benefits minus Discounted Costs)**
  - ❖ **Benefit – Cost Ratio: ( if it exceeds 1, the investment is considered as viable)**
  - ❖ **Internal Rate of Return (IRR): If the IRR exceeds the prevailing rate of interest the project is considered viable.**

# SCOPE OF COST-BENEFIT ANALYSIS

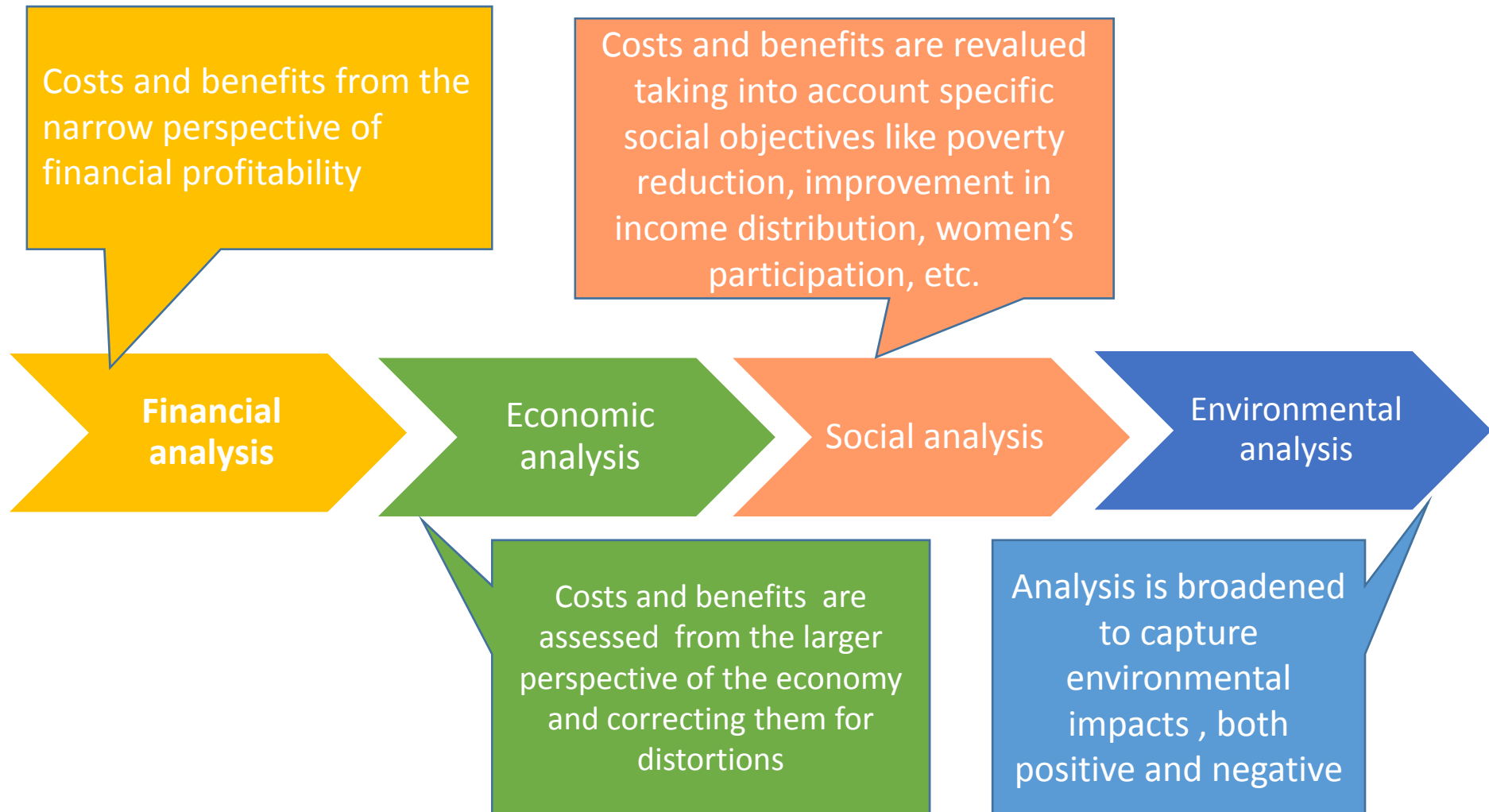
**Cost benefit analysis has evolved over time to address a range of issues from the varying perspectives of those undertaking it.**

- ❑ From the perspective of an individual or private enterprise focusing on financial viability, costs and benefits are considered from a narrow perspective.
- ❑ As we broaden the framework what may be considered as costs and benefits will change.





# EVOLUTION OF COST-BENEFIT ANALYSIS



# EVOLUTION OF COST-BENEFIT ANALYSIS

**Cost-benefit analysis has evolved over time largely based on the changes in the concept of socio-economic development.**

<b>Concept of development</b>	<b>Cost-benefit analysis</b>
<b>1. Emphasis on private profit generation</b>	<b>Financial cost-benefit analysis</b>
<b>2. Enhancing efficiency and viability from the larger perspective of the economy.</b>	<b>Economic analysis</b>
<b>3. Fulfilment of social objectives</b>	<b>Social cost-benefit analysis</b>
<b>4. Accomplishing environmental objectives</b>	<b>Environmental analysis</b>

# KEY STEPS IN COST-BENEFIT ANALYSIS



# AGGREGATION OF COSTS AND BENEFITS OVER TIME

- ❑ Costs and benefits flow from different programmes and projects at differing time periods. For example logging natural forests generates income immediately. On the other hand investments in long rotation plantations generate income after many decades.
- ❑ Making comparison between different projects will require bringing all costs and benefits to a common time-point.
- ❑ This is done through discounting the entire stream of costs and benefits and deriving their present values.
- ❑ The rationale of discounting and the rate to be used for discounting is one of the most debated issue in cost-benefit analysis.

# COST-BENEFIT ANALYSIS AND SOCIAL OBJECTIVES

With social objectives becoming an important concern, there have been efforts to modify cost-benefit analysis to assess their social impacts, in particular:

- Impact on regions that are considered as backward.
- Livelihood of specified groups, especially poor and impact on the provision of basic needs.
- Income distribution.
- Gender aspects – in particular betterment of the condition of women in terms of their economic and social well-being.

# COST-BENEFIT ANALYSIS AND SOCIAL OBJECTIVES

- ❑ Once the social objective is specified, costs and benefits are considered from the perspective of the specific objectives.
- ❑ For example if poverty reduction becomes the key objective, then the entire focus is on the costs and benefits that the target group confronts.
- ❑ Benefits accruing to the poor are given a higher weightage in comparison with what accrues to the non-poor
- ❑ If basic needs fulfilment becomes a development objective, then every programme and project is assessed on the basis of their impact on (a) producing basic needs goods and (b) enhancing income that enables the fulfilment of basic needs.

## Right to Basic Needs:

- ❑ The basic needs mean those goods and services which are necessary for a dignified living of people.



# CHALLENGES IN THE USE OF COST-BENEFIT ANALYSIS

- Although one of the most useful tool, CBA is also one of the most mis-used tools.
- Unless there is transparency, it is convenient to manipulate CBA to justify any decision. In fact there are several instances where favourable decisions are engineered through manipulation of cost-benefit analysis.
- Correctly identifying the entire cost and benefit stream is the greatest challenge.
- Many of the project proponents have a strong tendency to exaggerate the benefits and underestimate the costs.
- Finding the right price that reflects the true value/ cost to society remains challenging.
- Choosing the discount rate is another contentious issue.

# CHALLENGES IN THE USE OF COST-BENEFIT ANALYSIS

- ❑ There is a strong tendency to come up with one aggregated number that purportedly capture all dimensions.
- ❑ Aggregation of different numbers representing different objectives is extremely challenging and provides enormous scope for manipulation.
- ❑ Probably a “dash-board” approach that gives different indicators will be a better approach.





# SUMMING UP

- Social cost benefit analysis is a very useful tool for decision making and to make sure that pro-poor programmes and projects are given priority.**
- Meaningful SCBA however requires reliable information and this is often challenging in many situations.**
- In the absence of transparency subjectivity could creep in at various stages – key variables can be “adjusted” - defeating the very purpose of cost-benefit analysis.**
- Consequently misuse of SCBA by decision makers is quite widespread.**

**Thank you**



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