UNIT – 1

Generation and Screening of a project idea

Generation and Screening of a project idea begins when someone with specialized knowledge or expertise or some other competence feels that he can offer a product or service

♦ Which can cater to a presently unmet need and demand

♦ To serve a market where demand exceeds supply

♦ Which can effectively compete with similar products or services due to its better quality/price etc.

An organization has to identify investment opportunities which are feasible and promising before taking a full fledged project analysis to know which projects merit further examination and appraisal.

Generation and Screening of a project idea involves the following tasks :-

(1) *Generation of ideas –*

A panel is formed for the purpose of identifying investment opportunities. It involves the following tasks which must be carried out in order to come up with a creative idea –

(a) SWOT analysis – Identifying opportunities that can be profitably exploited

(b) Determination of objectives – Setting up operational objectives like cost reduction, productivity improvement, increase in capacity utilization, improvement in contribution margin

(c) Creating Good environment – A good organizational atmosphere motivates employees to be more creative and encourages techniques like brainstorming, group discussion etc. which results in development of creative and innovative ideas.

(2) Monitoring the Environment –

An Organization should systematically monitor the environment and assess its competitive abilities in order to profitably exploit opportunities present in the environment. The key sectors of the environment that are to be studied are :-

(a) Economic Sector –

It includes, State of economy, Overall rate of Growth, Growth of primary, secondary and tertiary sectors, Inflation rate, Linkage with world economy, BOP situation, Trade Surplus/Deficit.

(b) Government Sector –

It includes, Industrial policy, Government programmes and projects, Tax framework, Subsidies, incentives, concessions, Import and export policies, Financing norms.

(c) Technological Sector –

It includes, State of technology, Emergence of new technology, Receptiveness of the industry, Access to technical know how.

(d) Socio-demographic sector –

It Includes, Population trends, Income distribution, Educational profile, Employment of women, Attitude towards consumption and investment.

(e) Competition Sector –

It includes, No. of firms and their market share, Degree of homogeneity and production differentiation, Entry barriers, Marketing policies and prices, Comparison with substitutes in terms of quality/price/appeal etc.

(f) Supplier Sector – Availability and cost of raw material, energy and money

(3) Corporate Appraisal –

It involves identification of corporate strengths and weaknesses. The important aspects that are to be considered are:-

(a) Market and Distribution –

i. Market Image
ii. Market share
iii. Marketing and Distribution cost
iv. Product line
v. Distribution Network
vi. Customer loyalty

(b) Production and Operations –

i. Condition and capacity of plant and machinery
ii. Availability of raw materials and power
iii. Degree of vertical integration
iv. Location advantage
v. Cost structure – Fixed and Variable costs

(c) Research and Development –

i. Research capabilities of a firm

ii. Track record of new product developments
iii. Laboratories and testing facilities
iv. Coordination between research and other departments of the organization

(d) Corporate Resources and Personnel –

i. Corporate Image
ii. Clout with government and regulatory agencies
iii. Dynamism of top management
iv. Competence and commitment of employees
v. State of industrial relations

(e) Finance and Accounting –

i. Financial leverage and borrowing capacity
ii. Cost of capital
iii. Tax situation
iv. Relations with shareholders and creditors
v. Accounting and control system
vi. Cash flows and liquidity

Tools for identifying investment opportunities →

(a) Porter 5 forces Model → It helps in analyzing profit potential of an industry depending upon strength of –

i. Threat of new entrants
ii. Rivalry amongst existing companies
iii. Pressure from substitute products
iv. Bargaining power of buyer
v. Bargaining power of seller

(b) Life cycle Approach → There are four stages a product goes through during his life cycle each stage represents different investment and net profit value →

(a) Pioneering Stage – In this stage the technology and product is new, there is high competition and very few entrants survive this stage.
(b) Rapid Growth Stage – This stage witnesses a significant expansion in sales and profit.
(c) Maturity Stage – It marks developed industries with mature product and steady growth rate.
(d) Decline Stage – Due to introduction of new products and changes in customer preference the industry incurs a decline in market share and profits.
(c) Experience Curve → Experience curve analyzes how cost per unit changes with respect to accumulated volume of production. Investment must be such that reduces costs.

(4) Looking for Project Ideas –

Various sources to look for good project ideas include:-

i. Trade fairs and exhibitions
ii. Studying Government plans and guidelines
iii. Suggestion of financial institutions and development agencies
iv. Investigating local materials and resources
v. Analyzing performance of existing industries
vi. Analyzing social and economic trends
vii. Analyzing new technological developments
viii. Studying the consumption pattern of people abroad

ix. Stimulating creativity to produce new ideas

x. Reducing exports and imports

(5) Preliminary Screening –

It refers to elimination of project ideas which are not promising. The factors to be considered while screening for ideas are:-

♦ Compatibility with the promoter – The idea must be consistent with the interest, personality and resources of entrepreneur.

♦ Consistency with Government priorities – The idea must be feasible with national goals and government regulations.

♦ Availability of inputs – Availability of power, raw material, capital requirements, technology.

♦ Adequacy of Market – Growth in market, prospect of adequate sale, reasonable Return on Investment.

♦ Reasonableness of cost – The project must be able to make reasonable profits with respect to the costs involved.

♦ Acceptability of risk level – The desirability of the project also depends upon risks involved in executing it. In order to access risk the following factors must be considered:-

-Project`s vulnerability to business cycles

-Change technology

-Competition from substitutes

-Government`s control over price and distribution

-Competition from imports

(6) Project Rating Index →

It is a tool used for evaluating large number of project ideas. It helps in streamlining the process of preliminary screening. Hence a preliminary evaluation may be converted in project rating index.

Steps to calculate project rating index→

I. Identifying the factors relevant for project rating

II. Assigning weights to these factors according to their relative importance(FW)

III. Rate the project proposal on various factors using suitable rating scale (FR) (5 point scale or 7 point scale)

IV. For each factor multiply the factor rating with factor weight to get factor scores (FR X FW = FS)

V. All the factor scores are added to get the overall project rating index.

Organization determines a cut off value and the project below this cut off value are rejected.

(7) Sources of the Net Present Value

In order to select a profitable and feasible project, a project manager must carry out a fundamental analysis of the product and factor market to know about entry barriers which lead to positive net present value. There are six entry barriers which result in a positive NPV project. They are –

i. Economies of scale
ii. Product differentiation

iii. Cost advantage
iv. Marketing reach
v. Technological edge
vi. Government policy

(8)Entrepreneurial skills →

An individual must possess the following traits and qualities in order to be a successful entrepreneur –

i. He must be Willing to make sacrifices
ii. He must be a good Leader
iii. He must be able to make quick and rational decisions
iv. He must have confidence in the project
v. He must able to exploit market opportunities
vi. He must have strong ego in order to survive ups and downs of a business