University of OEB **Academic Year: 2024/2025**

Department of Economic Sciences

Third Year Licence Quantitative Economics

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Lecture 02: Economic Evaluation

Economic evaluation is a crucial process used to assess the financial viability of projects, investments, and policies. It helps decision-makers determine whether a particular initiative is worth pursuing by analyzing its potential costs and benefits. This process is widely applied in various sectors, including business, healthcare, infrastructure, and public policy.

At its core, economic evaluation involves comparing the expenses associated with a project to the expected advantages it will bring. These advantages may include financial profits, social benefits, or improvements in overall efficiency. For example, before launching a new business venture, entrepreneurs evaluate whether the projected revenue will exceed the initial and operational costs. Similarly, governments conduct evaluations before investing in large-scale infrastructure projects, such as building highways, railways, or hospitals, to ensure that public funds are used effectively.

One of the main reasons economic evaluation is essential is that resources are limited. Organizations and governments must make informed decisions to allocate budgets efficiently. Without proper evaluation, funds may be spent on projects that do not generate sufficient returns or fail to address pressing economic and social issues. By carefully analyzing costs and expected benefits, decision-makers can prioritize investments that create the greatest value.

Risk assessment also plays a key role in economic evaluation. Financial markets, interest rates, inflation, and unforeseen circumstances can all impact the success of an investment. Therefore, analysts often take these factors into account to estimate potential risks and develop strategies to mitigate them. Investors, for instance, assess the profitability of a project while considering possible market fluctuations that may affect future earnings.

In addition to financial factors, economic evaluation can also consider broader impacts on society and the environment. Some projects may not generate immediate financial profits but can provide long-term benefits, such as improved public health, environmental sustainability, or increased employment opportunities. For example, investing in renewable energy sources may require high initial costs but can lead to long-term economic and environmental advantages.

Overall, economic evaluation is a fundamental tool for making sound financial and policy decisions. It ensures that limited resources are utilized efficiently and that investments generate positive outcomes. By carefully assessing the potential costs, benefits, and risks of a project, businesses, governments, and individuals can make informed choices that contribute to economic growth and stability.

Reading Comprehension Questions

1. What is the main purpose of economic evaluation?
2. Why is economic evaluation important for decision-makers?
3. How does economic evaluation help in resource allocation?
4. Why do governments evaluate infrastructure projects before investing in them?
5. What role does risk assessment play in economic evaluation?
6. How can external factors like inflation and market fluctuations affect investment decisions?
7. Why might some projects be considered valuable even if they do not generate immediate financial profits?
8. How can economic evaluation contribute to environmental sustainability?
9. In what ways does economic evaluation help individuals in their financial decisions?
10. What are some examples of sectors where economic evaluation is applied?

Vocabulary Section

Match the following words with their correct definitions:

Viability, Revenue, Investment, Resources, Risk Assessment, Inflation, Sustainability, Infrastructure, Allocation, Profitability

Definitions:

A. The ability of something to be successful or work effectively.

B. The process of distributing or assigning resources to different projects.

C. The financial income generated from a business activity.

D. The long-term ability to maintain or support economic, social, or environmental systems.

E. The analysis of potential dangers or uncertainties in a financial decision.

F. A rise in the general price level of goods and services over time.

G. The financial gain obtained when revenues exceed expenses.

H. The underlying structures and facilities, such as roads, bridges, and buildings, needed for a society or business to function.

I. Assets, materials, or financial capital that can be used to produce goods and services.

J. Money or capital put into a project with the expectation of gaining financial returns