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ECONOMIC EXPERTISE OF A BUSINESS PLAN AS AN INSTRUMENT OF CONTROL IN THE FINANCIAL JUSTIFICATION OF AN INVESTMENT PROJECT

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Abstract. The article substantiates the role of economic expertise of a business plan, the integral part of which is the expertise of financial justification of an investment project, for making a final decision on its implementation. Special attention is devoted to the issue of real investment assessment, which remains controversial. The article underlines that in the course of economic expertise of financial justification of an investment project it is important to take into account that application of risk measures, used to evaluate the financial investment, will have a number of disadvantages if applied as a risk measure for real investment: a company's market portfolio cannot consist of business investment; it is inappropriate to single out unsystematic and systematic risks; business investment are not traded assets.

Key words: investment project, investment risk assessment, efficiency of investment projects

INTRODUCTION

Current Ukrainian economy is experiencing a pressing need for the increased investment. One of the conditions for the successful implementation of investment activities is to develop appropriate methods for evaluating the efficiency of investment.

Treating investments as monetary, property or intellectual valuables, which are invested into the businesses for profit and/or social and environmental effect, allows us to formulate a number of theoretical and methodological problems. The

issues of justifying investment decisions in terms of their feasibility, forecasting the results of such decisions and thus providing for the possible risk assessment have gained the leading position among those problems.

The volatility of market conditions and current market environment, as well as the long-term nature of the investment processes result in the necessity to evaluate the interdependence of these factors. The major systemic financial document for an investment project is a business plan. Since the investment management involves the actions that would allow compensating for the deviation of certain factors with some other factors and would provide for achieving the investment objectives, then, while developing a business plan, it is necessary to use the methods of evaluating the impact of possible fluctuations of investment factors with close attention to how those fluctuations might influence the composite efficiency index of investment performance. In each and every case, for each and every project we develop an individual financial model, which allows considering all the aspects of the investment project, provides for a detailed analysis and a favourable presentation of the results.

A business plan includes a comprehensive system of arguments that prove the financial feasibility of a particular type of investment, a detailed description and analysis of the environment in which the investment takes place (or will take place), a profound analysis of the risks associated with the investment activities, specification of prospects in the form of qualitative and quantitative indicators, as well as instantiation of the management system necessary to achieve the desired goals [Perevozova 2011, p. 170]. Expertise of a business plan is necessary for making a final informed decision about an investment project. There are two possible directions for the expertise that determine its cost and timing: evaluation of the methodology selected for developing a business plan and assessment of investment project feasibility as it is submitted, whereas the expertise of its financial justification becomes a component part of such assessment.

Allocation of financial resources for the project is the obvious and fundamental prerequisite for a management decision as such. It is important to note the relevance of economic expertise of the financial justification of investment projects, financed from the budget.

RESEARCH METHODS

Despite a wide range of advisory references available for developing a business plan, its certain parts often turn out to cause considerable difficulties. Practical experience has shown that most problems arise while developing such parts of a business plan as financial plan formation and risk assessment.

The results of conducted market research form the basis for all chapters of a business plan. Therefore, appreciable errors at this stage or failure to conduct appropriate market research will make it impossible to talk about accurate and realistic further calculations.

Assessment of the efficiency of investment projects is complicated enough; therefore this issue has been widely researched by a number of scholars. Research studies include scientific works by A. Amosha, V. Algin, R. Bazzel, G, Birman, I. Blanc, E. Boyko, J. Brigham, A. Vichevich, L. Galenski, M. Danyluk, G. Kleiner, L. Kruszwic, V. Kovalev, I. Kukukina, L. Labsker, E. Lapko, B. Livshits, J. Linter, V. Miklovda, S. Smollyak, E. Chetyrkin, W. Sharpe, S. Schmidt and others.

However, the issue of real investment assessment remains disputable. For example, risk assessment and temporal cashflow ratio are determined on the basis of criteria generated by financial markets, which, in fact, do not adequately reflect the nature of the processes that take place during real investment.

Evaluation methods are not universal in all cases for all investment projects, since they may differ a lot in their cost, project implementation period, as well as in intended results.

The simplest calculation methods are suitable for small investment projects that do not require considerable capital investment or are characterized by a relatively short period of implementation.

At the same time large-scale investment projects (new construction, reconstruction, development of new types of products, etc.), which entail high investment outlay, demand close attention to a number of factors that must be considered and, consequently, require more complex calculations, as well as revised methods for project performance evaluation. The larger the investment project scale is and the more significant changes in the economic results of a business entity it might cause, the more precise calculations of cash flows and methods of evaluating its efficiency it requires.

More than that, it is important to underline that there is a lack of practical recommendations, developed by our native scholars, on economic expertise methodology for real investment assessment. Best practices on the issue hardly cover 1–2 pages of a coursebook, determining the necessity of business plan expertise and listing the subject of such expertise and its disadvantages.

Methodological and procedural issues of economic expertise of a business plan remain an open question, and so does a unified approach to expert review. It would be perfect if person(s), responsible for economic expertise of a business plan, was/were not directly related to the investment project, but competent and honest enough to formulate a professional opinion on all the essential aspects, that would be critical for the success of the project. If we take into account the low cost of these services in Ukraine, it will become evident that this additional

step might be an exceptionally profitable deal that could significantly influence the result.

Systematic and logical approaches to the analysis of economic expertise of a business plan constitute the methodological basis of the current article. General scientific methods were used in the study to justify the expediency of business--plan expertise: dialectical method, abstraction, deduction and induction, analysis and synthesis.

The subject of the research is the process of economic expertise of a business-plan, the object are real investment evaluation methods that are useful for financial explanation of investment.

The objective of the article is to establish the method of evaluating the efficiency of real investment projects, carried out by an enterprise, in the process of business plan expertise.

RESULTS

Expertise of a business plan, as a certain direction of human activities, produces information (product of labor), has its production technology, conditioned by labor object, its purpose and objectives. With this in mind, we can define the subject of labor in the process of a business plan expertise: the objects specified in the requirements of a customer. Within the frame of the article, the object of economic expertise is financial justification for a particular investment project.

Basic evaluation criteria for a subject of expertise should include: clarity, completeness, reliability and quality of generated information. Apart from these, measurability, comparability and consistency are also considered while assessing investment project efficiency.

An important peculiarity of organizing the expertise process for a business plan is that the phases of research and practical procedures of financial explanation of investment are clearly associated with a specific task set by a customer of such expertise. Therefore, the main objective of investment projects (consequently, of a business plan) is to satisfy the needs of a customer in best possible way. At the same time, economic expertise can be used as an independent form of control of financial justification of an investment project.

Economic expertise of a business plan can be examined in two aspects: organizational-technological and methodical. Consequently, the consistency characteristics of the study should be based on such imperatives:

- connectivity (including reverse);
- division into parts;
- structural evaluation (presence of structured elements);
- purposefulness;

- the ability to maintain a certain stability within the prescribed limits under the influence of external factors;
- multidimensionality.

Current article focuses on the analysis of certain fragments regarding economic expertise of investment project feasibility. Only certain individual fragments are under study since a qualified expert will easily determine whether a project can be implemented at all, in other words, is there a technical and economic potential for successful implementation of a project. If there is, then it is possible to determine the efficiency of a project. Thus, the bulk of methods, applied to evaluate the efficiency of investment projects, are based on comparing its profitability to some required (recommended) value. Financial rate of return is determined on the basis of alternative profitability principle: investment project return rate should not be poorer than financial return rate for the best alternative investment directions at equal risk level, while in most cases different financial assets are understood as alternative investment directions. The basic concept, applied to evaluate the yield of financial assets, is the risk-free rate of return.

Risk-free assets are the ones with clearly defined associated expected return, that is, the actual return is always equal to the expected return [Damodaran 2004, p. 202]. Current economic conditions in Ukraine have turned risk-free assets into fiction: its stock market has a very short history of operations, inflation is extremely unpredictable. Nominal interest rate on securities varies significantly from one period to another. As a consequence, using its current value for long--term calculations may lead to significant errors. While evaluating real investment efficiency, a risk-free return rate is not considered even in theory.

Risk is a measure of uncertainty in further results of ongoing operations, but it is possible to determine the probability of potential events and the scope of their consequences. Risk can be understood in two ways:

- as the loss (pure risk);
- as a deviation from the expected result – the direction of deviations does not matter: positive or negative (speculative risk).

The following values are used as a measure of risk: dispersion, standard deviation, variation.

The variety of risk types has made it possible to group them in accordance with certain features [Orlova 2003, pp. 64–65]:

- by investment application object: financial investment risk, real investment risk;
- by type of ownership: State investment risk, private investment risk;
- by the nature of investment participation: direct investment risks, indirect investment risks;
- by organizational forms: risks of investment programs and projects, investment portfolio risks;

- by investment period: short-term investment risks, long-term investment risks;
- by regional characteristic: domestic investment risks, international investment risks;
- by the scale of risk: general economic, industrial, enterprise, individual;
- by the types of losses: profits risks, downside risk, risk of direct losses;
- by the degree of risk predictability: predictable risk, unpredictable risk;
- by the sources of occurrence: systematic (external) market risk, unsystematic (internal) risk.

Risk factors for real investment are as follows [Halikov 2003, p. 173]:

- production technology: traditional, modernized, new;
- resources: availability in free market, monopolization of resources;
- shifts in demand and prices for the products;
- the need for research and development.

Risk evaluation methods can be divided into four groups:

- sensitivity analysis;
- scenario analyses;
- market investment valuation (Capital Asset Pricing Model, options valuation);
- risk-free equivalent.

The methods of sensitivity analysis and scenario analysis usually cause no methodological difficulties.

The method of risk-free equivalent lies in minus adjustment of the expected cash flows in accordance with the expected value of risk for the project. The greater the risk, the larger the subtractive correction. Due to this method, it is easy to differentiate the risks by the year or by the risk type. Each type of risk has its time profile, their total amount being business's gross exposure at each moment. This method also helps to consider all the risks introduced by each new development project undertaken by a company. It should be noted that in case of real investment an investor is less exposed to inflation risk than in case of financial investment. An error in predicting inflation peril will not play a significant role for real investment, because if a company can boast a steady market position, it can raise its selling prices in accordance with the inflation rate, which means that its effective yield rate will remain unchanged. Consequently, the risk of shifts in real return rates as a result of inflation does not exist.

More than that, in most cases, it is impossible to widely diversify the risks of an enterprise: it makes no sense to single out unsystematic and systematic risks. Usually risks vary significantly over time.

Therefore, application of such valuation models as Capital Asset Pricing Model, Arbitration Pricing Model is unfeasible for the financial evaluation of a real

investment project. Risk taking by increasing the discount rate is also methodologically unsound.

It follows, that risk assessment by minus adjustment of the expected cash inflows, which means the use of risk-free equivalent method, is the best methodologically sound option. Such procedure of risk assessment may be organized through the scenario analyses. However, these analyses will not allow for risk assessment procedure. The choice of variables for this or that scenario is entirely subjective judgment of an expert, not limited by formal procedures. As a result, the range of opinions on probability of each scenario and its consequences can be wide enough, which will involve a question in difficulty.

We come to the conclusion that in most cases, to evaluate the efficiency of real investment projects, implemented by an enterprise, it is reasonable to use capital-growth model, which differs from the compound interest model.

CONCLUSIONS

A business plan is a comprehensive system of proofs of financial feasibility of a specific type of investment. To make a final informed decision about the investment project, it is appropriate to conduct economic expertise of a business plan, an integral part of which is the expertise of financial explanation of an investment project.

Allocation of financial resources for an investment project is an obvious and a fundamental prerequisite for a management decision. However, the issue of real investment assessment remains disputable.

In the course of economic expertise of financial justification of an investment project it is important to take account of the fact that application of risk measures, used to evaluate the financial investment will have the following disadvantages if applied as a risk measure for real investment:

- a company's market portfolio cannot consist of business investment, since the diversification opportunities for business investment are limited (in comparison with financial investment);
- it is inappropriate to single out unsystematic and systematic risks;
- business investment are not traded assets (even when they are, a range of customers is extremely narrow); therefore there is no reward for a higher level of risk.

Thus, in the process of economic expertise of financial justification of an investment project, a capital-growth model is suitable to evaluate the efficiency of real investment projects.

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EKSPERTYZA EKONOMICZNA BIZNES PLANU JAKO INSTRUMENTU KONTROLI W RAMACH UZASADNIENIA REALIZACJI PROJEKTU INWESTYCYJNEGO

Abstrakt. W niniejszym artykule uzasadniono celowość przeprowadzenia ekspertyzy planu biznesowego, której składnikiem jest ekspertyza projektu inwestycyjnego w celu podjęcia ostatecznej decyzji o jego realizacji. Skupiono uwagę na kwestii oceny realnych inwestycji. Ustalono, że w trakcie przeprowadzenia ekspertyzy ekonomicznej projektu inwestycyjnego należy uwzględnić, że wykorzystanie miary ryzyka stosowanej do oceny inwestycji finansowych ma wiele wad: brak możliwości tworzenia przez przedsiębiorstwo rynkowego portfela inwestycji produkcyjnych; brak możliwości wyróżnienia ryzyka niesystemowego i systemowego; inwestycje produkcyjne nie są aktywami do sprzedaży.

Słowa kluczowe: projekt inwestycyjny, ocena ryzyka inwestycyjnego, efektywność projektów inwestycyjnych