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Economic Analysis Handbook / 2nd edition

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Defense Economic Analysis Council

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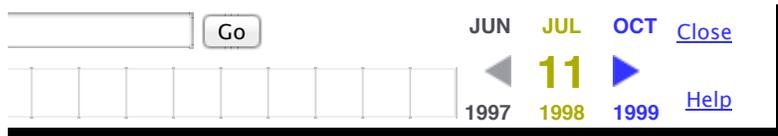
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Economic Analysis Handbook

Introduction

CHAPTER I

A. WHAT THIS BOOK IS ABOUT

Every manager devotes considerable time and effort to planning for the future, and every plan is concerned primarily with allocating scarce resources. This book explains a process which will aid the manager in making resource allocation decisions. This method of approaching a complex problem of choice is called Economic Analysis.

Economic Analysis concerns the basic problem of economic choice (value received for value sacrificed) and as such, has been applied by each of us implicitly and informally whenever we've made a decision in the market place. This handbook formalizes that decision process. However, our objective is not to present a "cookbook" of detailed procedures, nor is it to deal with abstract concepts. Rather, it attempts to promote understanding of economic analysis concepts and methodology so that these techniques may be used as tools for effective decision making at all echelons within the Department of Defense.

The general format for an Economic Analysis involves the determination of the cost and benefit of each future course of action. Through a cost-benefit or cost-effectiveness analysis the decision maker can utilize a set of facts and figures to select a preferred means of achieving certain goals. After specifying the objectives and assumptions, devising appropriate alternative courses of action, costing these alternatives, and determining the benefits or effectiveness of each alternative, a preferred action or investment may be chosen. The criterion used by the decision maker is the maximization of benefit minus cost if the two are commensurable (e.g., both measured in dollars) or, if they are not, the maximization of benefits for a given cost, or the achievement of a given performance objective at a minimum cost.

B. THE AUDIENCE

This book was written in order to establish a procedural routine for personnel who have little or no experience with economic analysis. It will also be of value to those supervisors and functional managers who must initiate or review economic analyses. For those who cannot read this book in its entirety, an adequate knowledge of the methodology of economic analysis can be obtained from Chapter II, "The Process," with special attention to the outline of the method on page Additionally, the supervisor or functional manager should become familiar with the "Guide for Reviewers," Chapter VI.

Lower echelons are encouraged to develop detailed procedures for analysis appropriate to their missions by using the general procedural routine presented in this document.

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