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## ***Advances in Project Management Series<sup>1</sup>***

# **Project economics: Wishful thinking, conspiracy of optimism or a self-fulfilling prophecy?**

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### ***Introduction to the December 2013 Advances in PM Series Article***

Financial management is crucial to the successful delivery of projects, especially when success, as so often is the case, is primarily measured in monetary terms. The Sixth Edition of the Association for Project Management's Body of Knowledge, published in 2012, defines financial management as "the process of estimating and justifying costs in order to secure funds, controlling expenditure and evaluating the outcomes." (p. 162)

In essence, financial management relies on estimating the cost of the work and quantifying the value of potential benefits likely to be derived from the expected outcomes. The feasibility study, options appraisal and development of a business case typically provide the initial justification for undertaking the work through the evaluation of costs, benefits and risks of alternative options. This underpins the rationale for commissioning the work and may also be utilised in selecting between competing solutions, projects or programmes.

Indeed, securing funds is a growing challenge, especially in times of financial austerity, limited resources, greater public scrutiny and an overarching need to achieve more with less. The constant stream of public projects failing to meet their budgetary baselines provides a continuous reminder of the need to get a better grip on the financial aspect of project work.

### **Enter Economics**

Economics endeavours to discuss how a society, or a connected group, can balance ever expanding human wants with the increasingly scarce resources at their disposal. It is particularly pertinent as it increasingly emphasises human wishes, behaviours and interactions as the basic elements of microeconomics, alongside capability, resources and targets. It can be particularly useful in determining if investment decisions are sound and sensible, and provide a basis for comparing and devaluing alternative options, solutions and projects in terms of utility, impacts or effectiveness.

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<sup>1</sup>The *Advances in Project Management* series includes articles by authors of program and project management books published by Gower in the UK. Each month an introduction to the currently monthly article is provided by series editor **Prof Darren Dalcher**, who is also the editor of the *Gower Advances in Project Management* series of books on new and emerging concepts in PM. For more on Gower project management, visit <http://www.gowerpublishing.com/default.aspx?page=2063>.

If we accept the view advocated in the front pages of the popular press, and some of our own surveys that the majority of important projects experience significant cost overruns, we are obliged to consider the circumstances that build up towards such 'failures'. It is also incumbent upon us to interrogate the dynamics leading to these outcomes.

### **The question**

Assuming that the majority of projects considerably exceed their baseline estimates, we can develop three potential lines of interpretation:

- EITHER we are singularly inept and incompetent in estimating costs,
- OR there are systematic errors that creep into our calculations and models,
- OR we have a case of wilful manipulation, political games or consensual and mutually agreed strategic misinterpretation, a kind of an agreed conspiracy.

The first option is reasonably straight forward, but it might be useful to expand on the two remaining alternatives.

Researchers often refer to optimism bias, where participants, decision makers and planners underestimate the complexity and risks in a situation, or overestimate the potential benefits. In other words, through certain biases participants 'convince' themselves of the plausibility, magnitude and likelihood of a good, or best outcome.

Recently, the phrase 'conspiracy of optimism' has begun to appear in public audit bodies reporting on major projects. The phrase implies an implicit agreement exercised during the project bidding and procurement processes, whereby potential contractors place extremely low tenders, or bids, to facilitate an initial approval. Project sponsors subsequently accept the unrealistically low tenders in the understanding that costs will escalate as the scope of the projects is adjusted to accommodate inevitable changes and improvements. The politics of approval, and the need for savings can thus account for the initial acceptance of unrealistic bids in the understanding that the costs will be allowed to escalate to a more realistic level reflecting the realities of the project.

The obvious question is 'which of the above interpretations provides the most plausible explanation for the apparent inability to estimate and manage costs?'

For the answer we turn to our guest author: This month's column features Derek Salkeld, an experienced risk analysts and manager. Derek's book *Project Risk Analysis: techniques for forecasting funding requirements, costs and timescales*, published by Gower makes the case for improving the initial estimates of projects using more accurate assessments of risk and opportunity. Investment in methodologies and processes often ignores the importance of the initial assessment of cost required to deliver the proposed vision.

In the article Derek makes a strong case for getting a better handle on the expected costs of infrastructure projects. In order to achieve his vision he calls for new processes to be applied during the initiation phase of projects. He also suggests that a new

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profession may emerge from the proposed changes and agitates for a revolution in how project costs are shared.

## **Moving forward**

To determine which interpretation is correct, we require detailed information about initial project estimates. However that information is almost impossible to find. The answer will depend on what we find, but first we may need to disclose and share that data. An open approach may facilitate the development of more responsible and accountable profession and result in new methods and perspectives required to deliver projects successfully.

Given the importance of initial estimates in defining the context for projects, it is essential that we develop mechanisms for scrutinising and questioning baseline assumptions and assessments. For at the moment it is the initial mistakes, wishful thinking or conspiracy that may be playing a part in defining the success of projects. We make the case for a shift from management to leadership and from making to shaping, but the limits of our projects are shaped not by vision and potential, but by accidental resource limitations that grow to constrain our ambition. When leaders are not allowed to define reality, but are instead tasked with conforming to compromises, they are relegated to working around artificial constraints and limitations.

Bjorn Lomborg noted that wishful thinking is not sound public policy. Our experiences in projects confirm that nor is it a sound estimating approach or a workable management style. Until we learn to utilise projects for growth and develop the economics for objectively balancing human wants with scarce resources we may be condemned to repeat the same mistakes expecting different results.

*“The optimist proclaims that we live in the best of all possible worlds; and the pessimist fears this is true.”*

- James Branch Cabell

To form an informed opinion about where we stand, we will require visibility and access to the data, which continues to shape projects, thereby impacting our ability to deliver them successfully.

Howard Zinn observed that *“pessimism becomes a self-fulfilling prophecy; it reproduces itself by crippling our willingness to act.”* Wishful thinking, optimism bias, conspiracies or optimism, or simple errors and incompetence, whichever is the real cause, seem to be equally capable of locking us into a constrained context and limiting what can be achieved and how it can be managed.

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*Editor's note: Darren Dalcher is the editor of the series of books on Advances in Project Management published by Gower in the UK. Information about the Gower series can be found at <http://www.gowerpublishing.com/advancesinprojectmanagement>. The above article is an introduction to the invited paper this month by another Gower author. You can find previously published articles by Prof Dalcher and Gower authors at [www.peworldlibrary.net](http://www.peworldlibrary.net).*

## About the Author



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**Darren Dalcher**, Ph.D. HonFAPM, FRSA, FBCS, CITP, FCMI is Professor of Project Management at the University of Hertfordshire, and founder and Director of the National Centre for Project Management (NCPM) in the UK. He has been named by the Association for Project Management (APM) as one of the top 10 “movers and shapers” in project management in 2008 and was voted Project Magazine’s “Academic of the Year” for his contribution in “integrating and weaving academic work with practice”. Following industrial and consultancy experience in managing IT projects, Professor Dalcher gained his PhD in Software Engineering from King's College, University of London. Professor Dalcher has written over 150 papers and book chapters on project management and software engineering. He is Editor-in-Chief of *Software Process Improvement and Practice*, an international journal focusing on capability, maturity, growth and improvement. He is the editor of the book series, *Advances in Project Management*, published by Gower Publishing of a new companion series *Fundamentals of Project Management*. Heavily involved in a variety of research projects and subjects, Professor Dalcher has built a reputation as leader and innovator in the areas of practice-based education and reflection in project management. He works with many major industrial and commercial organisations and government bodies in the UK and beyond. He is an Honorary Fellow of the APM, a Chartered Fellow of the British Computer Society, a Fellow of the Chartered Management Institute, and the Royal Society of Arts, and a Member of the Project Management Institute (PMI), the Academy of Management, the Institute for Electrical and Electronics Engineers, and the Association for Computing Machinery. He is a Chartered IT Practitioner. He is a Member of the PMI Advisory Board responsible for the prestigious David I. Cleland project management award and of the APM Professional Development Board. Prof Dalcher is an editorial advisor for the *PM World Journal*. He can be contacted at [d.dalcher2@herts.ac.uk](mailto:d.dalcher2@herts.ac.uk).