

MASSACHUSETTS INSTITUTE OF TECHNOLOGY

PROJECT EVALUATION (1.011)

Spring 2011

Instructors: Professor Joseph Sussman (JS)  
Carl Martland (CDM)

Teaching Assistants:  
Nihit Jain (NJ)  
Edna Edzell (EE)

---

**Assignment 3.2 – Advanced Concepts 2**

*Distributed:* Lecture 19

*Due:* Lecture 22

*This is an individual assignment. Estimated time to complete including reading the teaching note is about 2 hours.*

This question is based on the Real Options teaching note discussed in class during Lecture 12. For this entire question, consider only the “partial” solution, where we consider **only** case A and C. That is, we don’t have the choice of building 2 decks in 2010.

- a) In algebraic terms, for what value of  $p$  are we indifferent between strategy A and C.
- b) Assume  $r=0.05$ ,  $CA=100$ ,  $CC=105$ ,  $CAA=50$ . Sketch the relationship between  $p$  and CCC such that we are indifferent between A and C ( $p$  on the x-axis and CCC on the y-axis). Please interpret the result.
- c) We have assumed away some real world complexities in this teaching note. Please identify some of these. Four (4) reasonable ones will get you full credit. Some are actually mentioned in the teaching note and it’s fair to use them!

MIT OpenCourseWare  
<http://ocw.mit.edu>

1.011 Project Evaluation  
Spring 2011

For information about citing these materials or our Terms of Use, visit: <http://ocw.mit.edu/terms>.