



Diamond Chemicals

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RESOLVING THE ISSUES

Issues

- Inflation: Cash flows and discount rate need to be consistent in their assumptions about inflation.
- Sunk cost: Treatment of Engineering costs

Inflation

- The 10% initial discount rate proposed by Greystock is a nominal rate and therefore lacking consideration for inflation. As the inflation rate is 3%, the real rate is 7%. Our suggested solution to this concern is to include a 3% inflation rate adjustment in the cash flow analysis.

Sunk cost

- Preliminary engineering costs of 0.5 mn have been spend on the efficiency and design studies of the renovation and are thus a sunk cost. Hence, these costs should not be included in the analysis.

