Q. NLH-120 CA (Re: Page 29)

Dr. Kalymon adjusts the return of the industrials by 75 basis points for the lower risk of utilities. In the response to NLH – 68 as part of the Newfoundland Hydro 2001 GRA, he noted as the basis for his adjustment, the lower Beta levels of the industrial sample and the significantly higher payout ratio of the utility sample. Please show the calculations using these two factors that produce the 75 basis point result.

A. The Beta values of the industrial sample are on average .21-.25 lower than those of the utility sample. Based on the long run average market risk premium of 4.5%, this suggests an adjustment required in the range of 0.95% to 1.13%. Since the Beta factors are volatile and given the lower apparent current risk premiums in the market, the lower level of 75 basis point adjustment was chosen.