Q. In Order No. P.U. 13(2013), page 31, lines 13-16, the Board expressed concern on the use of analysts' forecasts of expected growth in the constant growth discounted cash flow model as they produce higher results. Concentric, at pages 21-23 of its report, relies on earnings growth estimates from analysts. What changes, if any, have occurred since 2013 that address the concern that such estimates are overly optimistic and produce unreasonably high results?

A. As discussed on pages 22-23 of Concentric's report, Mr. Coyne believes that financial regulations that were implemented in both Canada and the U.S. in 2001 and 2002 have resulted in fair disclosure and have reduced or eliminated the possibility of analyst bias. As support for this view, Mr. Coyne cites the 2010 article from the Financial Analysts Journal on page 23 of Concentric's report, which found that analyst bias had declined significantly or disappeared entirely in the U.S. since the Global Settlement.

Mr. Coyne notes that the ROE estimates in Figure 16 of Concentric report demonstrate that the Constant Growth DCF results for the U.S. electric proxy group and the North American electric proxy group are generally consistent with the results of other models that he has used to estimate the cost of equity for Newfoundland Power. As discussed on page 23 of Concentric's report, Mr. Coyne has also presented the results of a Multi-Stage DCF model, which tempers the assumption of constant growth in perpetuity with a three-stage approach based on near-term, transitional and long-term growth rates. Mr. Coyne explains on page 19 of Concentric's report that no financial model can exactly pinpoint the correct return on equity, and that quantitative models produce a range of results from which the market required ROE is determined.

Another indicator of analyst objectivity can be found by comparing consensus growth projections with an independent source. Turning to the evidence provided by Mr. Coyne in this proceeding, he considers Exhibit JMC-3 responsive. Examining the North American Electric Proxy Group, the average Value Line EPS growth estimates for the companies in the group is 5.43%, in contrast to 5.28% from Zacks, 5.33% from SNL, and 5.12% from First Call. Due to the close proximity of these growth projections for the sample (the Value Line estimates being the highest) these data would certainly not indicate the presence of analyst bias in relation to the independent Value Line projections.

For reference, the issue of analyst bias has twice been addressed by the BCUC, and the Commission twice rejected any finding of analyst bias. In its 2013 generic proceeding, the BCUC considered the issue:

> *The Panel finds that there is reason to be cautious of potential analyst bias in the utility sector. The expert testimony at this time does <u>not</u>, however, convince the Panel that an adjustment for analyst bias should be made. The Panel expects that*

> *future hearings will be informed of the latest research on bias in the analyst's reports on the utility sector.*[1] *[emphasis added]*

The BCUC also considered this issue in its 2009 Decision for Terasen and found:

> *As for the two most commonly used approaches, the Commission Panel finds that the DCF approach has the more appeal in that it is based on a sound theoretical base, it is forward looking and can be utility specific. The Commission Panel has considered the submission of the JIESC concerning "upward bias" of analysts' estimates and considers that no allegations of upward bias have been leveled against utility analysts and that Value Line estimates will be free from any suggestion of upward bias. Accordingly the <u>Commission Panel will not give any weight to suggestions of analyst bias</u>.*[2] *[emphasis added]*

[1] GCOC Stage 1, Decision dated May 10, 2013, p. 71.
[2] BCUC, Terasen Gas Inc., Return on Equity and Capital Structure, Decision December 16, 2009, p. 45.