

1 **Q. Evidence of Dr. Vander Weide: US versus Canadian utility risk Pages 30-39: Please**
2 **confirm that Dr. Vander Weide does not believe that Canadian utilities are as risky**
3 **as the Canadian equity market.**
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5 A. Dr. Vander Weide's intuition tells him that the forward-looking risk of investing in
6 Canadian utilities is less than the forward-looking risk of investing in the Canadian equity
7 market as a whole, but greater than the risk implied by the ROE formula, which uses a
8 beta equal to 0.60. However, Dr. Vander Weide's intuition that the forward-looking risk
9 of Canadian utilities is less than the forward-looking risk of the Canadian equity market
10 as a whole is not confirmed by the available historical Canadian market evidence. First,
11 the risk of Canadian utilities is inherently difficult to measure because there are only five
12 large publicly-traded Canadian companies with Canadian utility subsidiaries; and these
13 companies also have unregulated subsidiaries. Second, although the betas for Canadian
14 utilities based on five-years of historical data are less than 1.0, the betas for rolling five-
15 year periods are volatile, and sometimes negative. Thus, calculated historical betas for
16 Canadian utilities simply do not provide much information on forward-looking betas for
17 Canadian utilities. Third, according to the CAPM, the beta for Canadian utilities is equal
18 to the ratio of the risk premium on Canadian utility stocks to the risk premium on the
19 market as a whole. My evidence indicates that the average historical risk premium on
20 Canadian utility stocks is greater than the average historical risk premium on the
21 S&P/TSX Composite, implying that the average historical utility beta should be greater
22 than 1.0. Fourth, the standard deviation of annual returns on the BMO CM Utilities
23 Stock Data Set and the S&P/TSX Utilities Index are approximately equal to the standard
24 deviation of annual returns on the S&P/TSX Composite. Thus, there is considerable
25 historical evidence that contradicts the notion that Canadian utilities are less risky than
26 the Canadian equity market.