Q. Vander Weide Evidence (page 39) – For Dr. Vander Weide's CAPM estimate, Dr. Vander Weide states that he uses the average value line beta of .73 "for his larger proxy utility group." When arriving at an average beta, why did Dr. Vander Weide select his larger group and not his smaller group of electric and natural gas utilities (described at p. 20) which included only utilities that have at least 80% of total assets devoted to regulated utility operations and S&P band ratings equal to or greater than BBB?

A. Dr. Vander Weide used the average Value Line beta for his larger proxy group because he believes the cost of equity estimate from a larger proxy group of comparable risk companies is generally more reliable than the cost of equity estimate from a smaller proxy group of comparable risk companies. Dr. Vander Weide notes that the average beta for his larger proxy group, 0.73, is statistically indistinguishable from the average 0.71 beta for the smaller proxy group. Furthermore, both beta values are very much less than the ratio of the average long-run risk premium for utility stocks to the average long-run risk premium for the S&P 500.