Q. Vander Weide Evidence - Comparable utilities, pages 14-25

a. Please indicate where in Dr. Vander Weide's testimony he has compared capital market conditions in the US versus Canada?
b. Please explain what Dr. Vander Weide understands by the term structure of interest rates or yield curves?
c. Does Dr. Vander Weide believe that the yield curves in the US and Canada are identical at the current point in time? If so please report the following interest rates for both the US and Canada: 3 month T. bills, 1 year treasury notes, 5 year treasury notes, over ten year bonds and 30 year bonds.
d. Please provide the annual deficits of the Federal Governments of both the US and Canada as a proportion of GDP since the introduction of the ROE formula in 1994 and comment on whether the trajectories are the same.
e. Please provide the annual average foreign exchange rate of US dollars per Canadian since 1994 and would Dr. Vander Weide agree that the Canadian $ has appreciated in value since the early 2000's?
f. Would Dr. Vander Weide agree that investors take currency appreciation and depreciation into account when make foreign investment decisions?
g. Please explain what the concept of interest rate parity means and whether this affects the ability to compare US with Canadian interest rates.

A. a. Dr. Vander Weide does not compare capital market conditions in his direct written evidence because capital market conditions are reflected in the economic data he uses to estimate the cost of equity. In addition, Dr. Vander Weide is aware that capital market conditions in Canada and the U.S. are generally similar. Specifically, Dr. Vander Weide recognizes that interest rates in the two countries are generally similar, inflation expectations are similar, and equity investors in both countries are concerned with stock market volatility, volatility in commodity prices including oil and gas, and economic events that affect both Canada and the U.S., including the Euro debt crisis, and growing weakness in the Chinese, European, and other world economies. Dr. Vander Weide is also aware that the Canadian and U.S. economies are interdependent in the sense that Canada receives approximately fifty percent of its imports from the United States, and approximately seventy-five percent of Canadian exports are sold to the United States. Thus, many macroeconomic factors that affect the U.S. economy also affect the Canadian economy.

b. The term structure of interest rates or yield curve reflects the relationship between interest rates on securities with different maturities

c. Dr. Vander Weide believes that the U.S. and Canadian yield curves are generally similar, but not identical. In August 2012, the average yields on 3-month Treasury bills, 1-year Treasury notes, 5-year Treasury notes, 10-year Treasury bonds, and 30-year Treasury bonds for the United States and Canada are shown in the table below. These data indicate that interest rates on Canadian securities are higher than interest rates on U.S. securities for maturities ranging from 3-months to ten years, and the interest rate on 30-year government securities is slightly higher for U.S. securities than for Canadian securities. (Data are from the U.S. Federal Reserve and the Bank of Canada.)

TABLE 1
COMPARISON OF YIELDS ON CANADIAN AND U.S. TREASURY SECURITIES
AUGUST 2012 AVERAGES

	3-month Treasury Bills	1-year Treasury Note	5-year Treasury Note	10-year Bonds	30-year Bonds
United States	0.10%	0.18%	0.71%	1.68%	2.77%
Canada	1.00%	1.12%	1.40%	1.83%	2.38%

d. Dr. Vander Weide agrees that the annual deficit of the U.S. Government as a proportion of GDP has been increasing and that the annual deficit for the Canadian Government has been decreasing. However, he did not gather or use the information requested in this interrogatory in preparing his written evidence in this proceeding because he believes such information is irrelevant to his conclusion that U.S. and Canadian utilities have similar risks, and, hence, similar costs of equity. Dr. Vander Weide believes that such information is irrelevant because there is no evidence that investors consider U.S. Government debt to be significantly more risky than Canadian Government debt. Foreign investors consider the United States to be a "safe haven," and large amounts of foreign capital have been flowing into U.S. Government securities in response to economic difficulties in other parts of the world. Dr. Vander Weide also notes that changes in U.S. economic activity have a considerable effect on Canadian economic activity because approximately fifty percent of Canadian imports come from the United States, and approximately seventy-five percent of Canadian exports are sold to the United States. Thus, economic events that affect the risk of investing in U.S. securities also affect the risk of investing in Canadian securities.

e. Dr. Vander Weide agrees that the Canadian dollar has appreciated in value relative to the U.S. dollar since the early 2000s. Dr. Vander Weide did not gather data on average foreign exchange rates since 1994 in the preparation of his written evidence in this proceeding because he believes that such information has no bearing on his conclusion that information on the cost of capital for U.S. utilities is useful for evaluating the cost of capital for Canadian utilities. In this regard, Dr. Vander Weide notes that The Economist Intelligence Unit forecasts that the Canadian exchange rate will remain relatively constant through 2016. These data indicate that the Canadian dollar was/is valued at 1.02 U.S. dollars in 2011 and 2012, and that the Canadian dollar is expected to depreciate slightly to 0.97 U.S. dollars in 2015 and 2016.

TABLE 2
FORECASTED EXCHANGE RATE
CANADIAN $ TO U.S.$
ECONOMIST INTELLIGENCE UNIT, AUGUST 2012

	2011	**2012**	**2013**	**2014**	**2015**	**2016**
Exchange rate C$ to US$	1.02	1.02	0.99	0.98	0.97	0.97

f. Dr. Vander Weide agrees that investors generally take expected currency appreciation and depreciation into account when making foreign investment decisions. Because the exchange rate of Canadian dollars to U.S. dollars is expected to be relatively constant over the next several years, Dr. Vander Weide does not agree that expected currency appreciation and/or depreciation affects the results of his written evidence in this proceeding.

g. Interest rate parity means that interest rates in two countries adjust to reflect expected appreciation or depreciation in the relative values of the countries' currencies. Dr. Vander Weide does not believe that the concept of interest rate parity currently affects one's ability to compare Canadian and U.S. interest rates and costs of equity because the value of the Canadian dollar is not expected to materially appreciate or depreciate relative to the value of the U.S. dollar over the next several years.