

1 **Q. Written Evidence of James H. Vander Weide – Volume 3**

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3 **Pg. 30, A83 - Given the difficulty of using Canadian utilities due to the lack of**
4 **analysts' forecasts and relatively small number of companies, is the DCF**
5 **methodology less relevant in estimating the required return on equity for**
6 **Newfoundland Power? Do these factors reduce its applicability to Canadian utilities**
7 **in general?**
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9 A. No. The DCF model is highly relevant in estimating the required return on equity for
10 Newfoundland Power because the DCF can be applied to a large group of U.S. utilities
11 that are comparable in risk to Newfoundland Power. Furthermore, the lack of available
12 data for Canadian utilities also applies to other cost of equity methods such as the CAPM.
13 For example, traditional beta estimates for Canadian utilities based on weekly or monthly
14 data are generally unstable, and, as Dr. Vander Weide demonstrates in his written
15 evidence, the CAPM does not explain or predict the historical returns on Canadian utility
16 stocks. With regard to this second point, the CAPM predicts that the average historical
17 risk premium on Canadian utility stocks should be approximately fifty to sixty percent of
18 the historical risk premium on the S&P/TSX Composite, whereas, the actual average
19 historical risk premium on Canadian utility stocks, based on either the BMO CM data or
20 the S&P/TSX Utility data, exceed the average historical risk premium on the S&P/TSX
21 Composite.