

1 **Reference: Volume 3, Cost of Capital Report by James Coyne**
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3 **Q. Volume 3, Cost of Capital Report by James Coyne, page 44. What weight, if any,**
4 **does Mr. Coyne think forecasts of market risk premiums from third parties should**
5 **be given in determining the appropriate market risk premiums? If any should be**
6 **considered, what third party forecasts would be appropriate for the Board to**
7 **consider in Mr. Coyne’s opinion?**
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9 A. Mr. Coyne believes that market data should be used to develop a forward-looking market
10 risk premium. He does not believe it is appropriate to rely on forecasts of the market risk
11 premium from third parties, including investor surveys, or projections from sources such
12 as Duff and Phelps.
13

14 With regard to investor surveys, Finance Professor Aswath Damodaran at the Stern
15 School of Business at New York University, who has published extensively on the
16 question of how to estimate the equity risk premium, wrote in March 2013¹ about his
17 concerns with using investor surveys as follows:
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19 *While survey premiums have become more accessible, very few practitioners*
20 *seem to be inclined to use the numbers from these surveys in computations*
21 *and there are several reasons for this reluctance:*
22

- 23 1. *Survey risk premiums are responsive to recent stock price*
24 *movements, with survey numbers generally increasing after bullish*
25 *periods and decreasing after market decline...;*
- 26 2. *Survey premiums are sensitive not only to whom the question is*
27 *directed at but how the question is asked. For example, asking the*
28 *question, “What do you think stocks will do next year?” generates*
29 *different numbers than asking, “What should the risk premium be for*
30 *investing in stocks?”;*
- 31 3. *In keeping with other surveys that show differences across sub-*
32 *groups, the premium seems to vary depending on who gets*
33 *surveyed...; and*
- 34 4. *Studies that have looked at the efficacy of survey premiums indicate*
35 *that if they have any predictive power, it is in the wrong direction...*
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37 Dr. Damodaran ultimately concludes that “it is also likely that these survey premiums
38 will be more reflective of the recent past than good forecasts of the future.”²

¹ Aswath Damodaran, Equity Risk Premiums (ERP): Determinants, Estimation, and Implications – The 2013 Edition, Updated March 2013, at 19-20.

² Ibid., at 20.

1 Mr. Coyne agrees with these concerns and would therefore not recommend reliance on a
2 survey or third-party forecast as a replacement for available current market data.