Volume 2: Cost of Capital: Expert Opinion of Mr. James Coyne – Return on Equity

Q. Volume 2, Cost of Capital Report, page 43. Mr. Coyne uses a three-year average to calculate the long-term forecast for 10-year government bonds and the risk free rate. In Order No. P.U. 18(2016) the Board accepted a forecast risk free rate based on the two test years.

a) Please explain why Mr. Coyne believes a three year and not a two-year period is appropriate to use.

b) Provide Figures 25 and 26 based on a two-year, not a three-year forecast.

A. a) Concentric typically uses a three-year forecast of interest rates on government bonds in its Canadian cost of capital work because that period generally coincides with the time between rate applications for many utilities, including Newfoundland Power. Under current conditions, there is not a substantial difference between the average two-year forecast and the average three-year forecast. In Mr. Coyne's U.S. testimony, he typically uses a five-year forecast of government bond yields in the CAPM and Risk Premium analyses.

b) Please see the requested data based on a two-year forecast for 2025 and 2026.

Revised Figure 1:
Long-term Forecast for 10-Year Government Bond Yields 2025-2026[1]

	2025	2026	Average
Canada	3.2%	3.2%	**3.20%**
U.S.	3.4%	3.4%	**3.40%**

Revised Figure 2:
Risk Free Rate

30-Year Risk Free Yield	**Canada**	**U.S.**
April 2023 Consensus Forecast Average 2025-2026 Forecasts	3.20%	3.40%
Average Daily Spread between 10-year and 30-year government bonds (2013-2023)	0.38%	0.54%
Sum	**3.58%**	**3.94%**

[1] Consensus Forecasts by Consensus Economics Inc., Survey Date April 11, 2023, at 28 and 3.