# Best practices in estimating the cost of capital assignment

Business

Firms were chosen or excellence in strategic financial risk management, tax and accounting, performance evaluation and other areas of financial management The companies included were those that were mentioned the greatest number of times by their peers. ” eliminated 18 headquartered outside North America. ‘ Of those remaining, five declined to be interviewed, leaving a sample of 27 firms. The companies included in the sample are contained in Exhibit 1, We approached the most senior financial officer first with a letter explaining our research, and then with a telephone call.

Our request was to interview the individual in charge f estimating the firm’s WAC, We promised our interviewees that, in preparing a report on our findings, we would not identify the practices of any particular company by nameвЂ?? we have respected this promise in our presentation. In the interest of assessing the practices of the broader community of finance practitioners, we surveyed two other samples: 15 active’ advisers. We applied approximately’ the same set of questions to representatives of these firms’ mergers and acquisitions departments.

We wondered whether the financial advisers’ interest in promoting deals might lead them to lower WAC estimates than those estimated by operating companies. This proved not to be the case. If anything, the estimating techniques most often used by financial advisers yield higher, not lower, capital cost estimates, вЂў Textbooks and Deadbolts. From a leading textbook publisher, we obtained a list of the graduate-level textbooks in corporate finance having the greatest unit sales in 1994, From these, we selected the top four. In addition, we drew on three trademarks that discuss the estimation of WAC detail.

Names of advisers and books included in these two samples are shown in Exhibit 1, Ill. Survey Findings The detailed survey results appear in Exhibit 2. The estimation approaches are broadly similar across the three samples in several dimensions, ; Discounted Cash Flow (DOC) is the dominant investment-evaluation technique, analyses, вЂў Weights are based on market not book value mixes of debt and equity,* Financial Advisers.

Using a “ league table” of merger and acquisition advisers presented in Institutional Investor is&aes of Papal 1995, 1994, and 1993, we drew a sample of 10 of the most Ђў The CAMP is the dominant model for estimating the cost of equity. Some firms mentioned other multi-factor asset-pricing models (e. G,. Arbitrage Pricing Theory) but these were in the small minority, ‘ For instance, Institutional Investor and Rooney publish lists of firms with the best Scoffs or with special competencies in certain areas.