



Cost of Capital

By Shannon P. Pratt, Roger J. Grabowski

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In this long-awaited *Third Edition* of *Cost of Capital: Applications and Examples*, renowned valuation experts and authors Shannon Pratt and Roger Grabowski address the most controversial issues and problems in estimating the cost of capital. This authoritative book makes a timely and significant contribution to the business valuation body of knowledge and is an essential part of the expert's library.

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Editorial Review

From the Inside Flap

Cost of Capital

Applications and Examples

Third Edition

Cost of capital estimation has long been recognized as one of the most critical elements in business valuation, capital budgeting, feasibility studies, and corporate finance decisions. It is also the most difficult procedure to perform and assess. In this long-awaited Third Edition of *Cost of Capital: Applications and Examples*, renowned valuation experts and authors Shannon Pratt and Roger Grabowski address the most controversial issues and problems in estimating the cost of capital.

Presenting both the theoretical development of cost of capital estimation and its practical application to valuation, capital budgeting, forecasting of expected investment returns, and rate-setting problems encountered in current practice, *Cost of Capital* is both a learning text and a handy reference for both the practitioner and the reviewer. Pratt and Grabowski deftly review and explore the theory of what drives the cost of capital, the models currently in use to estimate cost of capital, and the data available as inputs to the models to estimate cost of capital.

Now in a thoroughly updated and comprehensive Third Edition, *Cost of Capital* summarizes the results and practical implications of the latest research—much of which is gleaned from never-before-published academic working papers—and includes scores of formulas and elucidating examples throughout to enhance readers' insights. Pratt and Grabowski have updated their text to include a host of new material, including:

- A new chapter covering cost of capital for financial reporting under SFAS 141, 142 and 144
- A new chapter on risk measures and their relationship to cost of capital
- Extensive examples illustrating development of cost of equity by the build-up method and the capital asset pricing model using size premiums from Morningstar and the authoritative Duff & Phelps's Risk Premium Report data; development of company-specific risk premiums using Duff & Phelps's Risk Premium Report risk/return data; and development of capital structure at market value and weighted average cost of capital with constant and varying capital structures
- A new chapter covering cost of capital for companies in developing economies
- A new chapter covering cost of capital for transfer pricing
- An update of "Cost of Capital in the Courts"
- "Handling the Discount for Marketability" chapter is now expanded to include sources of data on minority interest transactions and control transactions
- Specialized chapters by leading experts in real estate, property tax, and family limited partnership valuations

In addition to detailed exposition of the build-up and capital asset pricing models for estimating the cost of capital, Pratt and Grabowski present in-depth analysis of the components, including the equity risk premium, beta and the size effect. The dynamic author team also analyzes criticism of major models for developing estimates of the cost of capital in use today and also present procedures for a number of alternative models. This definitive text is an indispensable reference tool for professional valuation practitioners as well as

attorneys and judges, investment bankers, CFOs, academicians and students, and CPAs.

From the Back Cover

Praise for the Third Edition of Cost of Capital

"Shannon Pratt and Roger Grabowski have not only brought together all of the issues in the cost of capital computation but have done so in a way that melds timely advice for practitioners with serious debate about the best practices in the area; it belongs on the bookshelves of serious valuation practitioners."

—Aswath Damodaran, Professor, New York University, Stern School of Business

"One of the four traits of great executives is their understanding of the fundamental reality of wealth creation—successful organizations invest to earn a rate of return in excess of their cost of capital. Organizations need assistance in better understanding and estimating the cost of capital and in communicating their results. This book can be a valuable tool for executives and their organizations."

—Geoffrey Colvin, Editor at Large, Fortune

"Cost of Capital, authored by two of the leading valuation experts in North America, is a comprehensive resource for financial professionals engaged in business appraisal, fair value measurement for financial reporting, corporate finance, damage quantification, and transfer pricing. This authoritative book makes a timely and significant contribution to the business valuation body of knowledge and is clearly an essential part of the expert's library."

—Richard M. Wise, FASA, MCBA, CVA, FCBV, FCA, Managing Partner, Wise, Blackman LLP

"I do not think you will find, anywhere, as comprehensive a book on cost of capital as this impressive Third Edition. Pratt and Grabowski have presented a great deal of valuable research in a very understandable manner. They also provide information and opinions that challenge some generally accepted data sources and applications, particularly, as it pertains to equity risk premiums. This book is a must-read."

—James R. Hitchner, CPA/ABV, ASA, Managing Director, The Financial Valuation Group, Editor in Chief, Financial Valuation and Litigation Expert journal

"Shannon Pratt and Roger Grabowski have combined painstaking research and writings from other contributors, with thoughtful commentary, views and advice surrounding the topic of the cost of capital, into a single volume. It is written in a style that should appeal to a wide variety of constituents. It advances the state of reference material on this topic for valuation practitioners and will also provide a solid foundation for continued debate and research on the topic for many years to come."

—Anthony V. Aaron, Americas Leader, Quality and Risk Management, Ernst & Young Transaction Advisory Services

About the Author

Shannon P. Pratt, CFA, FASA, MCBA, CM&AA, is the Chairman and CEO of Shannon Pratt Valuations, Inc., and is the founder and Editor Emeritus of Business Valuation Resources, LLC. He is the author or coauthor of several industry standards, including *Valuing a Business: The Analysis and Appraisal of Closely Held Companies*, *Valuing Small Businesses and Professional Practices*, *The Market Approach to Valuing Businesses*, *Standards of Value*, *Business Valuation and Taxes*, *The Lawyer's Business Valuation Handbook*, and *Cost of Capital*.

Roger J. Grabowski is managing director of Duff & Phelps LLC. He has testified in court as an expert

witness, including the Northern Trust case, the first U.S. Tax Court decision that adopted the discounted cash flow method to value the stock of a closely held business with the discount rate based on the capital asset pricing model. Roger coauthors the annual Duff & Phelps's Risk Premium Report. He is also the editor of *Business Valuation Review*.

Users Review

From reader reviews:

Joan McCorkle:

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Kelly Brooks:

Cost of Capital can be one of your beginner books that are good idea. Most of us recommend that straight away because this publication has good vocabulary that could increase your knowledge in terminology, easy to understand, bit entertaining but delivering the information. The writer giving his/her effort that will put every word into pleasure arrangement in writing *Cost of Capital* although doesn't forget the main level, giving the reader the hottest as well as based confirm resource facts that maybe you can be considered one of it. This great information can drawn you into fresh stage of crucial thinking.

Justin Davis:

In this era globalization it is important to someone to obtain information. The information will make professionals understand the condition of the world. The healthiness of the world makes the information simpler to share. You can find a lot of personal references to get information example: internet, newspaper, book, and soon. You can view that now, a lot of publisher this print many kinds of book. The particular book that recommended for your requirements is *Cost of Capital* this e-book consist a lot of the information from the condition of this world now. This kind of book was represented so why is the world has grown up. The dialect styles that writer use to explain it is easy to understand. The particular writer made some study when he makes this book. Honestly, that is why this book suited all of you.

Sandra Easley:

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