



Industry Risk Premium

- **Cannot blindly apply the industry risk premium as published in Morningstar's SBBI Valuation Edition Yearbook.**



DO WE KNOW WHAT IS IN THE MORNINGSTAR INDUSTRY PREMIUM DATABASE?

- 1. A company must have at least 36 months of data**
- 2. Sales > \$1 million in the most recent year**
- 3. Market Capitalization of at least \$10,000 in the most recent month**
- 4. Must have at least 5 companies in the industry**

DOES IT MAKE SENSE?



Questions that Need to Be Asked Before Using:

- *How many observations are there?*
- *What's the validity of the SIC code?*
- *Does it make sense?*
- *Is it CAPM in a Build-Up wrapper?" [1]*
-

[1] "Cost of Capital Controversies: It's Time to Look Behind the Curtain" (Part 1 of 3), James Hitchner, pg. 6



Questions that Need to Be Asked Before Using:

- How has the industry reacted to similar general economic conditions in the past?
- What are the industry forecasts and how do they relate to this Company?
- What is its position in the industry?



Questions that Need to Be Asked Before Using:

- What is the comparison of the financial analysis of the Company to the Industry financial analysis?