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This month's focus: **New Horizons in Cost of Capital Studies**

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The fundamental condition of value creation is that return on invested capital is higher than the cost of capital (the expected return of investors). A large firm, which has several divisions with different market risk, has to apply different cost of capital measures depending on each division's risk in order to avoid over-or under-investment. The global company can avoid agrowth investment with negative NPV by using the correct cost of capital that reflects local business risk.

Estimating implied cost of equity capital using the simultaneous back calculation method and application to empirical research	<i>Yuki Ota</i>	19
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This paper introduces a typical method for simultaneously estimating the implied cost of equity capital and implied expected growth rate. In addition, an empirical analysis is conducted using the implied cost of equity capital estimated by this method. As a result of analysis, it became clear that the amount of capital investment and cost of equity capital had a negative relationship only when the simultaneous back calculation method was used to estimate the cost of equity capital. This is evidence in support of Abel and Blanchard [1986]'s theoretical predictions.

Accounting Fundamentals and Cost of Equity Capital	<i>Yusuke Takasu</i>	29
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The purpose of this research is to analyze relations between accounting fundamentals based on financial statements and the cost of equity capital. It was found that accounting fundamentals have an explanatory power regarding the cost of equity capital. Exploiting this result, it was also found that there is a positive correlation between the cost of equity capital predicted from accounting fundamentals and future stock returns. These results suggest financial statement analysis has implications about not only future cash flow but also risk.

Estimating Cost of Capital for Operations: A Log-linear Present-value Approach	<i>Shin-ichiro Ono / Katsuhiko Muramiya</i>	39
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The purpose of this study is to provide an alternative technique for estimating cost of capital for operations. Specifically, we derive a log-linear present-value (LPV) identity at the enterprise level to generate the model-implied expected return (i.e., cost

of capital for operations). We find that the LPV-based cost of capital for operations retains significant predictive power for future asset returns up to three years ahead and is positively associated with future operating risk, as predicted by theory. In contrast, the estimated cost of capital based on standard factor models fails to exhibit systematic predictive power/reflect operating risk. Thus, we conclude that the LPV approach produces a reliable estimation of the cost of capital for operations in the Japanese setting.

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ESG Disclosure Score and Investment Performance	<i>Tomonori Yuyama, CMA / Yoko Shirasu / Soichiro Moridaira</i>	72
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For investors with fiduciary duty, when making ESG investments, their investment performance is important. This paper considers investment in companies that are proactive in disclosing ESG information, and examines stock returns using factor models, propensity score matching, and other methods. The results were not necessarily positive, nor were they negative. However, in 2017, it was suggested that they might be positive.

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