

## Calculation of Weighted Average Cost of Capital

### KOSTT Changes in Assumptions

Component		ERO Assumptions		rd @ 9% and 9.5%		g @ 35%		Combined Scenario	
		Min	Max	Min	Max	Min	Max	Min	
Real risk-free return	<i>rf</i>	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	
Debt risk premium	<i>pd</i>	2.0%	2.5%	2.0%	2.5%	2.0%	2.5%	2.0%	
Small company debt premium	<i>sd</i>	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	
<b>Cost of Debt</b>	$rd = rf + pd + sd$	7.9%	8.4%	9.0%	9.5%	7.9%	8.4%	9.0%	
Gearing	<i>g</i>	60.0%	60.0%	60.0%	60.0%	35.0%	35.0%	35.0%	
Equity risk premium	$rm - rf$	5.0%	6.0%	5.0%	6.0%	5.0%	6.0%	5.0%	
Equity beta	$\beta$	0.8	1.0	0.8	1.0	0.8	1.0	0.8	
Small company equity premium	<i>se</i>	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	
<b>Cost of equity</b>	$re = rf + \beta * (rm - rf) + se$	10.8%	12.8%	10.8%	12.8%	10.8%	12.8%	10.8%	
<b>Real WACC</b>	$g * rd + (1 - g) * re$	9.06%	10.16%	9.72%	10.82%	9.79%	11.26%	10.17%	1
<b>Tax rate</b>	<i>tc</i>	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	
<b>Tax wedge</b>	$1 / (1 - tc)$	1.25	1.25	1.25	1.25	1.25	1.25	1.25	
Pre-tax cost of equity	$1 / (1 - tc) * re$	13.5%	16.0%	13.5%	16.0%	13.5%	16.0%	13.5%	
<b>Pre-tax real WACC</b>	$g * rd + (1 - g) * 1 / (1 - tc) * re$	10.14%	11.44%	10.80%	12.10%	11.54%	13.34%	11.93%	1
<b>Average</b>		10.79%		11.45%		12.44%		12.83%	

Notes: Variable input data identified in blue text.

ERO calculates the WACC on the basis of standard corporate finance theory. The relevant formula elements are identified above.

The ERO calculation of the real cost of debt is based on applying the theoretical criteria. To incorporate the present view of 12% nominal borrowing rates in Kosovo, the formula is over-written with the value of 9% and 9.5% (subject to inflation; 12% - 2.5% or 3% inflation).

The alternative Gearing assumption is based on the Business Plan projections. Reducing the Gearing ratio will increase the proportion of the Cost of Equity in the WACC calculation: since the Cost of Equity is higher than the Cost of Debt the value of the weighted average will increase.