

## **Bouygues Telecom's comments on IRG's report on the principles of implementation and best practice for WACC calculation**

This letter sets out Bouygues Telecom's comments on the IRG's report on the principles of implementation and best practice for WACC calculation. It provides general observations on the PIB highlighted in the report and a general comparison with the practice in France. IRG's report highlighted some serious issues on the WACC calculation in Europe which are also characteristic of the French practice.

PIB 4: « IRG observes that there are empirical shortcomings in the CAPM methodology. On the other hand, alternative models also have their own problems such as weak empirical foundations and empirical challenges. Therefore, at the moment CAPM is widely used for the purpose of calculating cost of capital. »

PIB 10: « IRG recognizes that in theory the adoption of a differentiated WACC is reasonable from a regulatory point of view. However, the lack of capital market information at divisional level makes the theoretically correct determination of beta in some cases difficult. »

Bouygues Telecom's main concern is that, in a defined market, the WACC values of mobile operators must reflect the structure of the competition, to remain in accordance with the initial purpose of the CAPM methodology. Indeed, by definition, the cost of capital is a parameter intrinsic to each company which characterizes the competitive, economic and financial specificities of the company. Consequently, in a defined market, WACC values have to be differentiated between mobile operators when the competition is clearly not balanced.

Nevertheless, the practice in Europe is quite different from a regulator to another on this point and, for instance, the difference of practice between the Spanish regulator and the French regulator is significant. On the Spanish market, the national regulator decided to impose different WACC values between mobile operators which reflect the structure of the competition on the market.

However, on the French market - market quite similar from the Spanish market - the recent decision of the national regulator imposed on mobile operators to apply the same WACC value while the structure of the competition justifies the setting of differentiated values.

This result is the consequence of an incorrect implementation of the CAPM methodology. The lack of financial data to evaluate the systematic risk of a company, leads the regulator to use intellectual shortcoming by adopting an alternative methodology based on a general benchmarking which deletes all national specificities.

Indeed, the appreciation of the systematic risk such as is used in the CAPM faced to numerous problems. On the one hand, it appeared that the strong volatility of the stock-exchange and in particular on telecoms' stocks since 2002, made difficult its evaluation. On the other hand, the concerned companies (Orange France, Bouygues Telecom and SFR) are only quoted indirectly on the stock exchange with their group, respectively (France Telecom, Bouygues and Vivendi). So, the "direct" appreciation of the systematic risk turns out complex because no methodologies, unanimously recognized by the world of the finance, allow disaggregating the systematic risk of a group by activity.

So, due to this complexity of the CAPM implementation, the French regulator used an alternative method to evaluate the beta value based of the general observation of the practice in Europe without taking into account the specific structure of the French market.

Unconditionally, this method leads to inconsistent outcomes totally disconnected from the reality of the French market and the initial purpose of CAPM methodology.

Bouygues Telecom is considering that IRG should emphasized, in this report, the principle - accordingly to the purpose of the CAPM - that the WACC values of mobile operators must reflect the structure of the



competition. In other words, in case of dissymmetric competition, the Beta factor, parameter characterizing the systematic risk in the calculation of the cost of capital has to be differentiated between mobile operators.