March 19, 2025

Kroll Cost of Capital Recommendations and Potential Upcoming Changes – March 2025 Update

Executive Summary

Kroll regularly reviews fluctuations in global economic and financial market conditions that may warrant changes to our equity risk premium (ERP) and accompanying risk-free rate recommendations. The risk-free rate and ERP are key inputs used to calculate the cost of equity capital in the context of the Capital Asset Pricing Model (CAPM) and other models used to develop discount rates. We also update country risk data on a quarterly basis for 175+ countries using various models.

The Kroll Recommended U.S. ERP is being reaffirmed at 5.0% when developing USD-denominated discount rates as of February 28, 2025, but it could be increased in the near future. **The Kroll Recommended Eurozone ERP is being reaffirmed in the range of 5.5% to 6.0%** as of the same date, but we believe that a 5.5% ERP (i.e., towards the lower end of the range) is more appropriate when developing EUR-denominated discount rates as of February 5, 2024, and thereafter, until further guidance is issued.

Notwithstanding the current recommendations, we are monitoring economic and geopolitical events that may change our views and impact our guidance during the first half of 2025. There are three major potential sources of uncertainty.

First, the new U.S. administration threatened to impose tariffs as high as 200% on some U.S. trading partners. Almost daily, new announcements are made of possible new tariffs, followed by a reprieve or delay in effective dates for some of them. The uncertainty created by the scope, magnitude and timing of these tariffs, along with the possible ensuing retaliation by U.S. trading partners may disrupt global trade and potentially lead to higher inflation and/or an economic slowdown in the U.S. and other countries. Businesses are starting to delay M&A and capital expenditure/expansion plans, as they wait for the tariff situation to become less ambiguous. U.S. financial markets are already reeling from this uncertainty, creating significant volatility for bonds and equities.

Second, there is heightened uncertainty about budget policies, potential tax cuts, increased government spending and a related rise in budget deficits, not just in the U.S. but elsewhere (e.g., Germany), which could place upward pressure on long-term interest rates and disrupt global financial markets. The negative impact on markets from higher long-term interest rates could be mitigated if real growth accelerates materially due to the additional fiscal spending measures.

Finally, there are other global geopolitical events warranting close watch including, but not limited to, a reignition of the ongoing conflicts in the Middle East, an unsatisfactory resolution of the Russia-Ukraine war, and a potential withdrawal of the U.S. from NATO.

The combination of these risks has the potential to cause significant upheaval in global financial markets and may lead to a "risk-off" investor sentiment, with a corresponding increase in ERP for certain geographies (i.e., investors may demand a higher premium over the risk-free rate to induce them to invest in those equity markets).

Cost of Capital Recommendations

United States

The **Kroll Recommended U.S. ERP remains at 5.0% as of February 28, 2025**. This is matched with the higher of a U.S. normalized risk-free rate of 3.5% or the spot 20-year U.S. Treasury yield prevailing as of the valuation date. The Kroll U.S. Recommended ERP was last changed on June 5, 2024, when it was lowered from 5.5% to 5.0%.

At this juncture, the U.S. economy continues to be resilient, but there are considerable risks looming in 2025 that warrant close monitoring and may lead to an increase in our U.S. ERP recommendation. The soft-landing scenario (i.e., lower inflation, lower real growth, but no recession) that had been priced in by investors until early 2025 is now being challenged. A scenario of stagflation or even recession has been resurrected by several economists. A deeper economic slowdown and a resurgence in inflation (keeping interest rates higher for longer) could be in the cards for 2025, particularly if the trade war continues to escalate and persists through the rest of the year.

On the other hand, there is still a chance that some of these risks will dissipate during 2025. The decision to reaffirm the U.S. ERP Recommendation at the end of February is based primarily on the following trends in economic and financial market indicators:

- The U.S. economy has proven to be more resilient than anticipated. Despite calls for a recession by most economists due to a surge in interest rates starting in 2022, the U.S. outperformed all other developed economies in both 2023 and 2024. U.S. real GDP grew by 2.8% in 2024, in line with the performance of 2.9% seen in 2023 and better than the 2.5% in 2022. The aggressive rate hiking cycle of the Federal Reserve Bank (Fed) to quell inflation did not slow growth in the U.S. economy, but did help drive inflation down from its multidecade high of 9.1% in June 2022 to 2.9% in December 2024.

- U.S. equity markets had two remarkable consecutive years (2023 and 2024) of stellar performance where all major indices reached new record highs. U.S. markets were lifted by the prospects of productivity gains and earnings growth from generative artificial intelligence (Gen-AI) and, more recently, by the Fed's rate cutting cycle that started with a larger-than-anticipated rate cut of 50 basis points (b.p.) in September 2024. Markets continued their optimism after the election of Donald J. Trump for a second term as the U.S. president in early November 2024. Promises of deregulation and pro-growth policies helped U.S. major indices achieve new record highs, with the S&P 500 index reaching its highest level on February 19, 2025. On February 28, 2025, the S&P 500 closed approximately 3% below its all-time record.

- The VIX index (the volatility index on the S&P 500), also referred to as the "fear index", was lower in 2024 than its long-term-average, with a few exceptional spikes observed during the year. The VIX averaged 15.6, the lowest daily average since 2019, and well below the long-term historical average of approximately 20.[1] The VIX did oscillate considerably during 2024, reaching a low (at close of day) of 11.9 on May 21 (the lowest level since November 27, 2019), and a high of 38.6 at closing on August 5 (the highest level since October 28, 2020, during COVID-19 pandemic), but the latter reading was deemed to be a one-off event.[2] After the S&P 500 index reached its February 2025 record, the VIX index has risen to levels similar to its long-term average, closing at 19.6 on February 28, 2025.

- Until recently, U.S. corporate credit spreads continued a tightening trend that started in mid-2022. For context, the spread between U.S. high-yield and investment-grade corporate bond yields stood at 2.0% as of December 31, 2024, which is lower than when we last changed our U.S. ERP recommendation.[3] This spread is also significantly lower than its long-term average (1996-2024) of 3.7% and a post-global financial crisis (2008-2024) average of 3.6%. The interest rate hiking cycle that the Fed started in 2022 to quell inflationary pressures was intended to tighten financial conditions. Indeed, interest rates rose significantly from their COVID-19 lows, making it harder for households to get new mortgages and placing pressure on riskier businesses to refinance or meet their debt obligations. In general, high yield spreads are seen as a reasonable indicator for the overall health of an economy, since speculative-rated companies tend to be at a higher risk of defaulting in recessionary periods. Despite the higher interest rates observed since 2022, credit spreads have actually narrowed during this period, indicating that investors did not believe the rate hikes were leading to increased system-wide distress risks in financial markets. Part of the explanation for the historically-low-credit spreads through the end of February 2025 appeared to be related to an expectation of forthcoming interest rate cuts and still-strong real economic growth.

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[1] The VIX index averaged 19.9 over the last 30 years (1995–2024; daily basis).

[2] The August 5, 2024 intraday spike was somewhat anomalous – it was one of only two intraday highs during 2024 that were greater than 30. Some analysts explain this spike by an increase in the bid and ask spread of S&P 500 options used in the calculation of the index. See, for example, Todorov, Karamfil, and Grigory Vilkov. *Anatomy of the VIX spike in August 2024*. No. 95. Bank for International Settlements, 2024. A copy of the article can be found here: https://www.bis.org/publ/bisbull95.pdf.

[3] High yield corporate bonds are below-investment grade instruments (i.e., those with a credit rating below BBB-). They are also referred to as speculative-grade or "junk" bonds.

- Implied ERP indications from forward-looking models based on Professor Aswath Damodaran's research and our version of the Default Spread model are at similar levels as when we last changed our U.S. ERP recommendation.

- Contrary to the expectations of many economists, the steep increase in interest rates during 2022 and 2023 did not result in a significant increase in the unemployment rate. Furthermore, the unemployment rate has been low and stable since we last changed our recommended U.S. ERP in June 2024. Through January 2025 the unemployment rate in the U.S. has varied within a tight range of 4.0% and 4.2%.[4] For perspective, these levels are lower than the unemployment rate observed during past expansion periods. Since 1990, the average unemployment rate during U.S. economic expansions was 5.7%.[5] In addition, according to data published by the non-partisan Congressional Budget Office (CBO), the natural rate of unemployment is currently around 4.3%.[6] This suggests that the U.S. economy is still slightly expansionary and that the unemployment rate is near its long-term stable level. Recent data releases show that the U.S. is still seeing relatively strong job creation, although there are various signs of a cooling market.

All economic and financial market indicators that we review on a regular basis show that conditions have either improved or remained at similar levels since the Kroll Recommended U.S. ERP was lowered from 5.5% to 5.0% in June 2024.

Recently, however, uncertainty has risen materially, which is leading market participants to rethink their expectations for the remainder of 2025. We believe that there are major sources of downside risks and uncertainty that may lead us to increase our U.S. ERP recommendation in the near future.

- First, President Donald Trump has threatened to impose tariffs as high as 200% on U.S. trading partners. The uncertainty created by tariffs could lead to potential disruptions in supply chain management and invite retaliation from trade partners, which could lower GDP growth and increase price levels, at least temporarily. Inflationary pressures would make the Fed's task of deciding on the path of interest rates even more difficult. Headline inflation, as measured by the Consumer Price Index (CPI), began a rapid descent since its multidecade high of 9.1% in June 2022. As the Fed embarked on its rate hiking cycle, inflation decelerated significantly through mid-2024 and at a faster pace than many anticipated. However, the process of disinflation has been a bumpy one, and inflation has yet to reach the Fed's 2.0% target. Recent readings have shown an uptick in headline inflation, a trend that began in October 2024 and continued through January

[4] The U.S. unemployment rate was 4.1% in December 2024, 4.0% in January 2025, and 4.1% in February 2025.

[5] Expansion periods defined by the National Bureau of Economic Analysis (NBER).

[6] The natural rate of is the hypothetical unemployment rate that is consistent with stable inflation and aggregate production being at its long-run level. In other words, it is the lowest unemployment rate that can be sustained without causing wages growth and inflation to rise. The more technical term (in economics) for this concept is Non-Accelerating Inflation Rate of Unemployment (NAIRU). The NAIRU cannot be directly observed and needs to be estimated. There are various models that economists use to estimate the NAIRU, and definitions may vary among them. Since July 2021, the CBO renamed its NAIRU estimate series from "Natural Rate of Unemployment (Long-Term)" to "Noncyclical Rate of Unemployment". For the latest CBO estimates visit: https://fred.stlouisfed.org/series/NROU.

2025.[7] Services prices have been particularly sticky and continue to be a driver of inflation. A resurgence in inflation due to tariffs may compel the Fed to keep short-term interest rates higher for the remainder of 2025, which can add further pressure to the U.S consumer's waning spending power and slow economic activity further. In March 2025, consumer confidence, as measured by the University of Michigan's survey of consumers, dropped to its lowest level since November 2023.[8] Some economists are now predicting the U.S. economy will tip into recession as a result of the uncertainty created by trade policy uncertainty. Actions undertaken by the new Department of Government Efficiency (DOGE), including massive layoffs of U.S. federal employees, is also contributing to the heightening uncertainty.

- Second, the U.S. administration indicated its plan to extend the Tax Cut and Job Act of 2017 (TCJA) that was signed into law during President Trump's first term. Making the TCJA permanent would increase the U.S. budget deficit significantly. According to the Penn Wharton Budget Model, from the University of Pennsylvania, the permanent extension of the TJCA with all its provisions would increase the U.S. budget deficit by around $4 trillion over the next 10 years.[9] More recently, the Penn Wharton Budget Model prepared various scenarios based on the budget reconciliation proposal for fiscal year 2025 released by the House of Representatives in February. Under the House's proposed reconciliation legislation, $4.5 trillion in net tax cuts over the next decade are allowed, provided the U.S. Congress achieves a goal of $2 trillion in spending cuts. The Penn Wharton Budget Model estimated that the combined spending and tax proposals proposed by the Trump administration would increase 10-year primary deficits by $5.1 trillion before accounting for economic growth effects, and assuming that many of the provisions would expire after calendar year 2033. Taking into consideration positive growth effects, they estimated the deficit would increase by $4.9 trillion.[10]

  According to the U.S. Government Accountability Office (GAO), the federal government is on an unsustainable fiscal path.[11] As of December 31, 2024, the GAO estimated that under the current revenue and spending policies, (i.e., before President Trump's policies were enacted) the debt held by the public would reach a historical high of 106% of nominal GDP in 2027, growing to 200% of GDP by 2047. During 2024, spending on debt servicing (i.e., paying the interest on the debt) exceeded spending on Medicare and national defense.

[7] CPI inflation (before seasonal adjustments) was 2.4% for the 12-month period ending in September 2024, the lowest level since February 2021, but rose progressively to reach 3.0% in January 2025, declining to 2.8% in February. The Personal Consumption Expenditures (PCE) price index, the Fed's preferred measure of inflation rose from 2.1% in September 2024 to 2.5% in January 2025.

[8] Based on preliminary survey results for March 2025 for Index of Consumer Sentiment. Source: Survey of Consumers – University of Michigan. For the latest survey results, visit: http://www.sca.isr.umich.edu/.

[9] "The 2024 Trump Campaign Policy Proposals: Budgetary, Economic and Distributional Effects", August 26, 2024. Available here: https://budgetmodel.wharton.upenn.edu/issues/2024/8/26/trump-campaign-policy-proposals-2024.

[10] "The FY2025 House Budget reconciliation and Trump Administration Tax Proposals: Budgetary, Economic, and Distributional Effects", February 27, 2025, updated on March 3, 2025. Available here: https://budgetmodel.wharton.upenn.edu/issues/2025/2/27/fy2025-house-budget-reconciliation-and-trump-tax-proposals-effects.

[11] "The Nation's Fiscal Health: Strategy Needed as Debt Levels Accelerate", February 5, 2025. Report available here: https://www.gao.gov/products/gao-25-107714#:~:text=Despite%20strong%20economic%20growth%2C%20the,billion%20in%20fiscal%20year%202024.

The new U.S. administration promised savings in the federal government budget by trimming some programs, eliminating waste, and cutting down on the spending agenda initiated by the previous administration. Plans to implement pro-growth policies, including deregulation, lowering corporate taxes, and increasing domestic energy production could spur economic growth and mitigate some of the issues related to national debt. On the other hand, the new U.S. administration is planning to implement restrictive immigration policies that would affect labor force growth. The Trump administration outlined its immigration policy to include two major components: restricting immigration and deporting undocumented people already living in the U.S. These policies could be disruptive for industries that rely on this labor force and create uncertainty in some sectors and add to inflationary pressures.

- Third, the new U.S. administration has announced several policy changes in international relations that are leading to an increase in geopolitical risks. In general, these shifts reflect a general trend towards nationalism and de-globalization observed in the election results of many other countries in 2024 and earlier. President Trump is seeking to recalibrate and/or withdraw U.S. support for various multi-lateral agreements (e.g., OECD global minimum tax) and international organizations. Of particular concern is the possibility of U.S. removing support for the North Atlantic Treaty Organization (NATO). These discussions have caused an uproar in Europe and are leading European governments to recognize the need to rearm and increase defense spending. This is particularly pressing, given the new U.S. administration's display of closer ties to Russia when negotiating an end to the Russia-Ukraine war. Conflicts in the Middle East, including the Israel-Hamas, may also escalate. President's Trump rhetoric on annexing Greenland or in making Canada a 51st state are examples of how volatile the U.S. foreign policy is becoming.

In general, these policies introduce a considerable amount of downside risk to the current outlook and are already creating increased volatility in both U.S. equity and bond markets. Major U.S. stock market indices have erased all their 2025 gains and are nearing a correction.[12]

Long-term interest rates would likely move up if the net effect of the new administration's policies lead to higher budget deficits that could result in a further downgrade of the U.S. fiscal position and its credit rating. Similarly, trade wars and restrictive immigration policies could create inflationary pressures, raise yields at the long end of the curve, and push the Fed back to raising rates at the short end of the curve to bring inflation back to target.

Importantly, the net effect of these policies could be to slow economic activity and hinder earnings growth. The longer this environment of heightened uncertainty persists, the more likely it is to lead to a retrenchment in consumer spending, as well as a delay or cancellation of capital spending plans and M&A activity by businesses.

[12] A stock market index correction is generally defined as a decline by more than 10% (but less than 20%) from a recent record high.

Eurozone (From a German Investor Perspective)

The **Kroll Recommended Eurozone ERP remains in the range of 5.5% to 6.0%**, to be used in conjunction with the higher of a German normalized risk-free rate of 2.5% or the spot 15-year German government bond yield as of the valuation date. We continue to believe that a **5.5% ERP (i.e., towards the lower end of the range) is more appropriate** when developing EUR-denominated discount rates as of February 5, 2024, and thereafter, until further guidance is issued.

Incremental country risk adjustments for other Eurozone countries with a sovereign debt rating below AAA may be appropriate. Please note that this information does not supersede Germany's IDW (Institut der Wirtschaftsprüfer) guidance for projects that will be reviewed by German auditors or regulators.

After two consecutive years of strong (above-potential) growth, the Eurozone saw its economy nearly stagnate in 2023 (0.4% in real terms), due in good part to the aftereffects of the Russia-Ukraine war. The recovery in 2024 was shallow for the region (0.9% real GDP growth), with Germany (traditionally seen as the growth engine of the Eurozone) contracting in both 2023 and 2024.[13,] Rising populism has been a common denominator in elections across the Eurozone, making economic policies more difficult to implement. For example, parliamentary elections in France in mid-2024 left President Emmanuel Macron's ability to govern in a precarious situation.

The Eurozone outlook for 2025 has become more uncertain by the changing policies by the new U.S. administration. First, President Trump announced tariffs on EU steel and aluminum products. The European Commission responded with countermeasures and its own set of tariffs on U.S. exports.[14] President Trump threatened to levy tariffs on further EU products should the EU pursue its own set of tariffs. If tariffs are implemented and escalation continues, we would likely see a negative impact on real GDP growth for the Eurozone.

Second, the U.S. administration's possible withdrawal from NATO and indications of diminishing support for Ukraine's position in its fight against Russia is leading to a major shift in strategic direction for the EU. European countries have realized the need to boost security independence and invest in the region's defense. As a result, the EU launched its "ReArm Europe" plan, with the aim of unleashing the use of public funding in defense. Among other measures, the plan proposed relaxing budget deficit rules to allow governments to increase borrowing to fund defense spending.[15] Increased defense spending could help offset some of the potential negative effect from tariffs on real economic growth.

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[13] "Preliminary Flash Estimate for the Fourth Quarter of 2024 – GDP stable in the euro area and up by 0.1% in the EU", Eurostat, January 30, 2025. Available here: https://ec.europa.eu/eurostat/web/products-euro-indicators/w/2-30012025-ap#fragment-15944082-grio-inline-nav-2.

[14] The European Commission is the executive body of the European Union (EU). The Eurozone is a subset of EU member states that have adopted the euro as their currency.

[15] "Press statement by President von der Leyen on the defence package", European Commission, March 3, 2025. Available here: https://ec.europa.eu/commission/presscorner/detail/sv/statement_25_673.

Similarly, German parliamentary elections in early 2025 are paving the way to increased government spending fueled by additional borrowing. In March, German lawmakers passed a historic package of constitutional reforms to allow the federal government to increase borrowing levels. The loosening of budget deficit rules is expected to unleash government spending in Germany's aging infrastructure and in defense, which could boost economic growth – at least temporarily. On the other hand, long-term German government bond yields have been rising steadily, under the prospects of a higher debt burden.

Eurozone inflation has decelerated significantly since it last peaked at 10.6% in October 2022. In September 2024, the annual change in the Harmonized Index of Consumer Prices (HICP), dipped to 1.7%, below the European Central Bank (ECB) target rate of 2.0%, although it has re-accelerated since then. The ECB rate cutting cycle started in June 2024 and continued at a steady pace of 25 b.p. cuts through all its remaining meetings in 2024, with the deposit facility rate reaching 3.0% at the end of December 2024. Despite inflation ticking back up to 2.4% in December 2024, the ECB lowered its policy rates further at its January 2025 meeting, indicating that monetary policy remained restrictive. Inflation increased further to 2.5% in January, but came down to 2.3% in February, supporting the ECB's decision to lower rates by another 25 b.p. in both its February and March meetings. The ECB is expected to continue its rate-cutting cycle in 2025, which may help with economic recovery in the Eurozone.

European equity markets trailed the U.S. in 2024. However, the pan-European STOXX Europe 600 index began 2025 on a much stronger note. In early March, it reached new record highs, which was also true for Germany's DAX index. Defense stocks have performed particularly well. Equity volatility in Europe has been relatively low as measured by the VSTOXX index. In early March 2025, the VSTOXX has risen somewhat, approaching its historical average of around 23. Nonetheless, should the uncertainty around trade wars and geopolitical risks persist, we could see spikes in volatility in the remainder of 2025.

United Kingdom

The Kroll Cost of Capital Navigator contains historical ERP data compared to long-term government bonds for various countries, including the U.K. Historical ERP data for the U.K. begins in 1900 and is available for every year until the present.[16] However, Kroll does not currently publish an official ERP recommendation for the U.K. which takes into consideration both historical and forward-looking indications.

In general, the country's high exposure to Europe, especially since the onset of the Russia-Ukraine war, indicates that U.K. equity market risks are more aligned with Europe than they are with the U.S. Nonetheless, there are certain risks unique to the U.K. that should be monitored in 2025.

The U.K. economy saw a significant negative impact from the Russia-Ukraine war, particularly due to rising energy prices and supply chain disruptions. To fight the surging inflation, the Bank of England raised its policy interest rate at a rapid pace in 2022 and 2023, bringing it to the highest level since 2008. As a result, the U.K. economy almost came to a halt in 2023, experiencing a technical recession in the second half of

[16] For additional details on the data sets included in the International Cost of Capital module within the Kroll Cost of Capital Navigator, visit: https://www.kroll.com/en/cost-of-capital/international-cost-of-capital

the year. Real GDP grew at 0.4% in 2023, recovering to a still moderate level of 0.9% in 2024.[17] The U.K. has lagged behind all other G7 countries in the aftermath of the Russia-Ukraine conflict, with the exception of Germany. The U.K. has also continued to struggle domestically with transition issues following Brexit.[18] The country has seen political turmoil since the Brexit vote, including various changes in prime ministers. Furthermore, the fallout from the U.S. administration trade tariffs is also making the outlook for the U.K. economy more uncertain.

While U.K. inflation has come down significantly from its cycle peak, inflationary pressures remain. For instance, 12-month headline inflation in the U.K. accelerated to 3.0% in January 2025 from 2.5% in December 2024, after having reached a cycle low of 1.7% in September.[19] Economic growth has been subdued at the beginning of 2025 and a rise in inflationary pressures would make the task more difficult for the U.K.'s central bank. The Bank of England was one of the last major central banks to start its rate cutting cycle in August 2024, by lowering its policy rate from 5.25% to 5.0%. Since then, the Bank of England cut its policy rate twice, down to 4.5% in February 2025. From the beginning of the current rate cut cycle, the Bank of England lowered its bank rate by a cumulative 75 b.p. In contrast, the ECB has cut its deposit facility rate by a cumulative 150 b.p. from June 2024 through March 2025. While markets expect the Bank of England to continue to lower its policy rate in 2025, they also anticipate that the bank will be holding rates steady for a while longer.

The Labour Party won U.K. parliamentary elections in July 2024, the first time it was able to form a government since 2010. When Labour came to power, it announced to have found a "fiscal black hole" of £20 billion left by the previous government. Upon releasing its first budget in October 2024, the Labour government proceeded to rewrite government borrowing rules to allow for higher spending and taxation. The new budget, while intended to increase productivity by investing in technology, energy transition and infrastructure, also called for increased borrowing. Long-term government bond yields rose in response.

Chancellor Rachel Reeves has been trying to convince markets that this government's plans are not a repeat of those of the ill-fated government of former Prime Minister Liz Truss. The turbulence created by Prime Minister Liz Truss' short-lived "mini budget" in 2022 led to market panic in the U.K. gilt market and to her becoming the shortest-serving prime minister in U.K. history. At the time, the Bank of England was forced to intervene to calm markets over concerns regarding pension fund liabilities. While currently we do not appear to be experiencing a similar situation, close monitoring is warranted.

U.K. long term government yields have been rising since the start of 2024, with 20-year yields experiencing significant volatility. At the end of 2023, the 20-year yield stood at 3.9%, but as the year progressed, yields oscillated substantially and ended the year at 4.9%.[20] In mid-January 2025, U.K. 20-year government bond yields climbed to 5.2% and have settled at around 5.0% in mid-March.

[17] Source: "GDP first quarterly estimate, UK: October to December 2024", Office for National Statistics, February 13, 2025.
[18] The U.K. officially left the EU on January 31, 2020.
[19] Source: "Consumer price inflation, UK: January 2025", Office for National Statistics, February 19, 2025.
[20] Based on the nominal par yield on 20-year British Government Securities. Source: Bank of England.

The FTSE-100, the U.K. stock market benchmark index, increased by 5.7% in 2024 (in price terms), following a 3.8% increase in 2023, a disappointing performance compared to most other major equity markets. Nevertheless, since the beginning of 2025, the FTSE-100 has reached new record highs, buoyed by strong corporate earnings (supported by a weak pound, as many of the index companies earn a significant amount of their revenues and profits abroad), and expectations for further rate cuts. In contrast, the more domestically focused FTSE-250 index has been struggling and exhibiting negative performance since the beginning of 2025.

Valuation professionals should consider these the risks of diversion between different European economies when selecting a U.K. ERP.

Volatility of Current Spot Yields on Government Bonds

As investors attempt to predict the pace and magnitude of future rate cuts by major central banks, we continue to observe high levels of volatility in the spot yields of government bonds of major economies. The uncertainty created by policies from the new U.S. administration could add further volatility to bond markets in 2025. Long-term bonds yields may continue to fluctuate considerably in the near future, before stabilizing. During these periods, valuation professionals may need to consider using a moving average of spot yields to mitigate the impact of this volatility on their valuation analyses (e.g., weekly or monthly averages).

We will continue to closely monitor the situation and publish new guidance when appropriate.

Please contact our support team with any questions: costofcapital.support@kroll.com.