Cost of Capital in the Current Environment

June 2023 Update

Although at a slower pace, major central banks are continuing to hike interest rates to tame high inflation. Headline inflation appears to have peaked, but core inflation (i.e., excluding the volatile energy and food prices) continues to be stubbornly high. Economists have upgraded real growth expectations for 2023 relative to the beginning of the year, partly due to China’s reopening (after ending its zero-COVID policy) and warmer weather that helped lower energy prices. Nevertheless, several countries are still expected to fall into recession in 2023 or in early 2024. In fact, Germany and the Eurozone are already in technical recession (i.e., two consecutive quarters of contraction). However, global financial markets are generally pricing a soft landing rather than a deep and prolonged recessionary period. Amidst this uncertain environment, cost of capital estimates are more similar to levels observed around the Global Financial Crisis of 2008-2009.

Carla S. Navas, CFA – Managing Director, Kroll