Dockets UE-121697, UG-121705, UE-130137, UG-130138

Exhibit No. (SGH-7)

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**PUGET SOUND ENERGY**

PROOF

If market price exceeds book value,

the market-to-book ratio is greater than 1.0,

and the earnings-price ratio understates the cost of capital.

MP = market price

BV = book value

i = cost of equity capital

r = earned return

E = earnings

1. At MP = BV, i = r = .

2. E = rBV.

3. Then, = .

4. When BV < MP, *i*.e., <1, then,

a. < r, since = < r, because < 1;

b. i < r, since at = 1, i = = , but if < 1, then i < r; and

c. < i, since at = 1, i = = , but if < 1, then < i, because,

1) < 1, through MP increasing, and, if so, decreases, therefore, < i, or

2) < 1, through BV decreasing, and, if so, given E = rBV, decreases, therefore, < i.

5. Ergo, < i < r, the earnings-price ratio is lower than the cost of capital, which is lower than the earned return.