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Looking to improve earnings calls?

Start with better information

In the eleventh hour before an earnings call, regardless of the size and complexity of an organization, many C-suite executives can be found combing through metrics, spreadsheet data, and the output from analytical models, searching for insights that could help them better communicate a narrative about performance to investors and analysts.

The significant amount of time and effort public companies put into earnings call preparation is justified. The investor community is demanding more time and information from the C-suite, hoping to better understand the narrative behind traditional earnings guidance and financial statements. Specifically, investors and analysts are looking for comparisons to prior performance, an understanding of why businesses are trending a certain way, how organizations stack up against their peers, and how the financial picture is likely to change in the future.

Addressing such questions can be challenging. As many organizations close their books, the final numbers are often coming together late in the information production process, giving executives a short time frame—sometimes just 24 hours—to cram for earnings calls. By improving information flow on the front end, though, CFOs may have an opportunity to craft a more effective message to the market during earnings calls. And in this issue of *CFO Insights*, we'll examine why streamlining the information production process may provide executives with both insights to manage

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the business more effectively and greater confidence in discussing current and future plans with the investment community.

Walking in their shoes

Generally, organizations prepare for earnings calls in one of two ways. Some wait for internal systems to churn out information that is handed off to senior executives, who then study the output to prepare for questions investors and analysts might pose. Other organizations put themselves in the shoes of investors and analysts, determine what might be important to these stakeholders, and ask internal analytics teams to produce information pertinent to that external view.

The second approach can be more effective because it starts with the end in mind, and is structured to deliver insights around what might surprise or delight investors. Moreover, realigning the preparation to address investor concerns also may help focus the information production process—which often is introspective—and lead to the types of insights that support the messages the C-suite wants to deliver.

Take, for example, data that indicates an increase in capital expenditures. The expectation is that depreciation also will rise. But, if the data shows something different, the anomaly and its cause should be flagged by the analytics team early in the information production process so senior executives know the data point is a potential investor issue. Such early identification can reduce the time executives and investor relations (IR) professionals spend searching for anomalies late in the process.

Focus on what drives the business

How companies convey their financial goals on earnings calls can also be tailored to what may resonate with investors. Using a narrative that builds on the drivers impacting the organization's actions and results is one way to deliver an effective message to investors and other stakeholders. For example, the earnings discussion could start with a focus on the revenue drivers, move to cost drivers, and end with the net income results. In that way, executives are discussing important top-line growth drivers, as well as cost drivers, rather than focusing only on net income.

As a result, the earnings narrative communicates that income is more of a symptom or result of managing the drivers. Similarly, when discussing the effects of external factors, such as a distressed industry, a company may choose to focus on the strength of its balance sheet. The balance sheet takes on a heightened level of importance because solvency is the focus rather than growth.

Another benefit of focusing the narrative on drivers is that it can be based on a feedback loop that operationalizes the organization's strategy. The loop begins by identifying information, metrics, and key performance indicators that help support the business strategy. Then, based on effective synchronization of information, a view of the organization's performance emerges relative to the strategic plan. At that point, management can decide whether it is necessary to correct course and communicate their decision to the market based on insights culled from the data.

When building a communication or narrative focused on business drivers, however, it is likely information will be handed off between departments, highlighting another consideration for organizations: the interdependencies among different data sets. Consider that before an analysis of the sales pipeline can be completed, an analysis of the general ledger might have to be done first. If data flow processes are not synchronized properly, interdependencies can hamper efforts to produce data in a timely fashion, leaving senior executives little time before an earnings call to mine the data for insights.

Streamlining information production

Lining up facts and insights to relay a comprehensive picture to the investor community requires fostering an information production environment that encourages coordination. Often, that means breaking down silos that may exist among systems and functions in order for the analytics team to more easily share and compare financial and business data.

The IR and financial planning and analysis (FP&A) functions may be the natural intermediaries to provide context to analytics teams and keep information flowing at a pace that meets the needs of senior executives (see "Unleashing the potential—and the power—of FP&A," *CFO Insights*, January 2017). But regardless of which function takes the lead to improve the information production process, organizations should consider outlining associated roles and responsibilities. The outline can include a list of sources from which data will be pulled, a logical sequencing of hand-offs among departments, and a schedule for delivery of information to senior executives.

Also important to the financial communication process is recognizing that organizations run their businesses on multiple systems that don't always reconcile. Consider that the financial reporting system likely provides a view of the numbers that is different than the view presented by systems used to run the business, such as sales pipeline data, vendor management systems, and commodity price cycle information. Those disparate views can lead senior management to question the integrity of the numbers late in the information production process, forcing them to reconcile numbers when instead they should be using that time to absorb information and uncover insights.

In the same way breaking down silos between data gathering teams may help provide context, it can be an effective tactic for addressing reconciliation issues. More coordination among departments allows unreconciled views to be flagged earlier in the process and eventually synthesized into usable insights.

Another effective tactic to help improve information production is to resist overloading executives with data that doesn't support investors' interests.

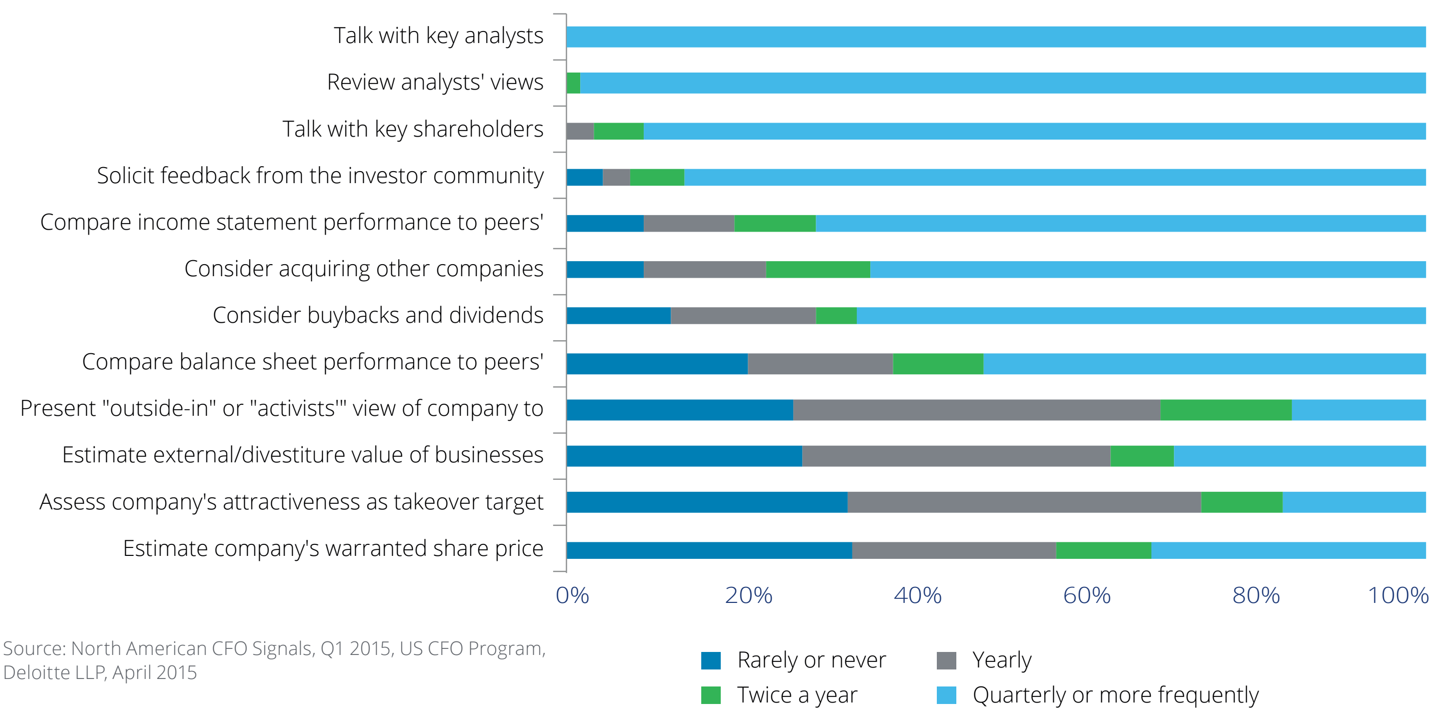
Distilling data into relevant information often begins with training in-house analysts—who often are excellent at producing large quantities of data—to search for variances and succinctly explain them. Storyboarding may help sharpen these skills.

A storyboarding exercise often starts with the ending and works through the narrative's highlights to support the conclusion with data. The end result should be a presentation that stays on message and frames the discussion in a way that highlights the organization's performance and vision of the future. Importantly, storyboarding helps shift the thinking of in-house analysts from data production to anticipating questions that might concern the C-suite and investors and analysts.

The pressure on management to perform has never been higher, and developing a message that resonates with the market can be challenging. Streamlining the information production process—with the goal of obtaining relevant insights from the data—can help organizations deliver an effective message within that narrow timeframe between when the books close and the earnings call begins.

Figure 1. Frequency of corporate IR activities

Public company CFOs' selections based choices as noted (n=61-66)



Source: North American CFO Signals, Q1 2015, US CFO Program, Deloitte LLP, April 2015

Beyond earnings calls: Gauging the effectiveness of IR

Editor's note: Charles Holley, retired CFO of Walmart, is currently the CFO-in-residence for the US CFO Program, Deloitte LLP. In this essay, he shares his views on what makes a strong investor relations (IR) function.

Effective IR depends in part on having a strong IR team, which is why I stayed very close to IR when I became CFO. It was important to me that IR have the communications, relationship-building, and analytical capabilities to first make sure that the company story was clear, consistent, and accurate, and second, to help the CEO and CFO effectively communicate the story to investors and analysts.

To do that well, I believe the head of IR should have open access to the CFO and CEO. It also means the IR team should be right there with them in meetings with investors and analysts. That gives them the chance to pick up on things that management may not see or hear. Equally important to me was IR's understanding of the business. I wanted my heads of IR deeply networked and connected inside the company, so they understood what was going on across the organization. Having a deep understanding of the business enables IR to talk substantively about the company, which gives them credibility when speaking with analysts and portfolio managers. And when the stock takes an unexpected turn, the IR team should be able to pick up the phone and talk to the specialist on the trading floor to find out what's going on.

So, as a CFO, how can you assess whether your IR team is effective? For me, it goes back to making sure that IR paints a clear picture of the company and the current results for Wall Street and to make sure that story connects back to the strategy, always reminding people of the long-term goals and what the company has done to achieve those. And if results aren't meeting expectations, IR has to be adept at explaining why and what is being done about it. Coming in at quarter-end with a different story or flexing the strategy according to short-term results generally loses the investor community's trust.

I also assessed my IR team's effectiveness by its ability to establish a two-way dialogue with the investor community based on trust and on their listening and information-gathering skills. How well the IR team connected with public relations (PR) was another point of evaluation. PR sometimes doesn't understand financial compliance issues and other reporting matters, so IR should ensure it's aligned with PR not only on the messaging, but on the cadence of it.

One criteria I *did not* use to evaluate IR was the stock price. I've seen some IR professionals think it's their job is to get the stock price up, but to me, that's not IR's job. I believe that the job of IR is to get the company story out clearly and accurately, and then let Wall Street and the market take it from there. It's also IR's job to establish the kind of relationships and engagement to enable them to ask why an investor is selling or why an analyst has a "hold" on the stock. Asking those questions produces important information and creates more opportunities to explain what the company is doing.

Finally, although it's important that CFOs be engaged in IR, it's also critical they strike a balance between doing what's important to get the message out and build relationships with the investor community against leaving time to run the business. You can do that by laying out the IR program a year ahead, figuring out which conferences and events are important, and deciding who's doing what, so you don't overburden the people who have to execute the strategy. After all, executing the strategy well is what builds shareholder value.

For the full essay, see "For Effective IR: Ask, Listen, Learn: Charles Holley, CFO-in-Residence," Deloitte Module, *CFO Journal*, October 18, 2016.

Deloitte CFO Insights are developed with the guidance of Dr. Ajit Kambil, Global Research Director, CFO Program, Deloitte LLP; and Lori Calabro, Senior Manager, CFO Education & Events, Deloitte LLP. Special thanks to Marie Leone, Senior Manager, US CFO Program, Deloitte LLP, and Andrew Marks, Senior Manager, US CFO Program, Deloitte LLP, for their contributions to this edition.

Contacts

Rolf Epstein
Partner | Head of CFO Program & Finance Consulting
Deloitte Germany
repstein@deloitte.de

Chris Ruggeri
Advisory Principal
Deloitte Transactions and Business Analytics LLP
cruggeri@deloitte.com

Charles Holley
Independent Senior Advisor
CFO-in-residence, US CFO Program
Deloitte LLP

Jonathan Schuldenfrei
Advisory Senior Manager
Deloitte Transactions and Business Analytics LLP
jschuldenfrei@deloitte.com