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Commentary

Three steps to a more productive earnings call

Traditional earnings calls are painfully unhelpful. Here's how companies and investors alike can get more out of them.

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As every earnings season comes to an end, it is striking how often executives and investors alike complain that earnings calls are a colossal waste of time. It's no wonder. Even a determined listener would be tested by an executive reading highly scripted texts of revenue, margin, and earnings data that would be better presented in tables. And few analysts or investors work up much enthusiasm for earnings-per-share (EPS) data that heed the generally accepted accounting principles (GAAP)—data that say little about value creation. Clearly, the quarterly earnings call needs an overhaul.

Podcast

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Article narration

Short of eliminating them entirely—a step many managers are unwilling to contemplate—what's a CFO to do? There's plenty of room for experimentation with more insightful formats. Beyond the formal and legally required 10-K forms, managers are free to innovate their quarterly (or semiannual) interactions—around both the format and the content of their calls. Most stakeholders would likely be delighted. Three ideas could greatly improve the dialogue.

1. Ditch the prepared text—and allow more time for thinking

Today, very little time passes between a written announcement of earnings and the earnings call. Most companies send around a press release minutes before the call or, at best, the evening before, after the markets close. The call itself often starts with a prerecorded and legalistic review, most often a senior executive reading data from a script, followed by a mundane question-and-answer session in which the company usually selects who asks the questions.

The value of this setup is questionable. Nobody has time to analyze the data before the Q&A session, and the remarks are often a more convoluted way to convey data than simple tables. To improve the dialogue, companies should eliminate the prepared remarks and give investors more time to digest and analyze the data. For example, they could release—a few days in advance of the call—detailed tables and exhibits, as well as a targeted overview in text and perhaps even full quarterly filings.

If investors and analysts have enough time to review the prereleased data prior to the call, companies could likely eliminate the usual prepared remarks and go right to a Q&A session. The advantage of such an approach is obvious—questions are better when the data are clear and understood by the participants. And while executives might worry about volatility in stock price between the release of the data and the earnings call, they should not be. What matters is the longer-term value appreciation, not the day-to-day volatility—and in any case, volatility can be avoided if data are presented clearly in the release and the state of the company is described in a consistent and meaningful way.

2. Be creative in the way the Q&A is structured

Most Q&A discussions are broken. Sell-side analysts often ask questions—"even bad ones," as one analyst told us—just so clients can hear their voice on the call or see their name in the transcript. Managers using sophisticated call-management software often invite questions only from the sell-side analysts they know and like. And buy-side analysts, arguably the most important participants on the call, are reluctant to reveal their thinking, and so are primarily just listening. The result is mediocre at best, routinely requiring numerous follow-up calls, and many questions remain unasked.

We need to start experimenting with systems where more investors can ask more pertinent questions, and perhaps a different way of selecting which ones get answered. New technologies make this fairly easy. If a company sends out data several days in advance of a call, it could, for instance, encourage investors and analysts to submit questions online and then have an online vote on which are the most important. The questions could be posted with the names of the people who sent them in, or perhaps even anonymously, to reduce bias in the vote.

Google, for example, experimented with such an approach in 2009, albeit without sending advanced data. Real-estate company Zillow took another tack to encourage real-time questions during its last earnings call. Anybody could ask a question via Twitter, encouraging analysts and investors in "listen only" mode to speak up. While this doesn't make the poster anonymous, the company "now has less control over who can ask questions and what people can ask, and . . . everyone can see which questions management chose to ignore."

Some companies might even choose to go further. Expeditors International of Washington, a global logistics company, has a long-standing policy not to have earnings calls at all. Instead, managers respond to written questions in writing in a Securities and Exchange Commission filing. A 2000 disclosure form explains, "We do not currently plan to host a conference call . . . . We . . . believe that investors will benefit from real written answers to thoughtful questions. It's a little more work for us, but we feel that the quality of the information disclosed will be better with a more formal process."

3. Stop talking so much about EPS

Given how little investors care about EPS and how far GAAP is away from true operating metrics in many cases, there is still too much emphasis on both in earnings calls, press releases, and announcements, at least with US companies. Managers should leave those numbers to the accountants and lawyers and focus instead on more operating-oriented numbers that make sense for their business. In the simplest form, these would be true pre- or posttax operating-earnings numbers, adjusted for amortization of intangibles, other nonoperating charges like the nonoperating portion of pension costs, and nonrecurring charges. Investors are likely to react positively to such a shift, and some large companies are indeed already reporting a non-GAAP operating margin.

In extreme cases, however, managers should be even more creative, especially those with business models where GAAP rules significantly distort economics. For example, capital expenditures, operating income, and other consolidated GAAP data do not reflect the underlying economics of one large industrial company, which is forced by GAAP to recognize some revenue as product revenue and some—from similar assets and contracts—as lease revenue. Managers and investors would be better off focusing their dialogue on a restated set of numbers that treats all revenue equally. Other examples can be found in businesses that combine manufacturing and large projects, where percentage-of-completion accounting, and in extreme cases even real-estate accounting, can significantly distort aggregated data to the point of irrelevance for a value assessment. Here, managers should clearly separate the data for different businesses and focus on non-GAAP metrics to convey the state of the business.

Finally, managers should eliminate the need for the endless clarifying questions that take up the bulk of most earnings calls by releasing more—and more transparent—data. That means full operating-income statements and key operating-balance-sheet items for business units, ideally by geography, reconciled to the consolidated statements. A number of companies routinely publish full income statements and balance sheets for their financial businesses, either in their regular filings, like GE, or as a separate full report, like Caterpillar Financial Services. Nonfinancial companies that come closest to the ideal, such as Novartis, often offer a full income statement and capital schedule per business unit, in annual statements. These data are typically available internally, and given the size of larger business units, investors deserve a deeper look into the financials than they are getting from the required disclosure.

For competitive reasons, not every company can be equally transparent. However, most are too conservative. A table with historical volume and price movements by region, for instance, would clarify where growth opportunities are. This kind of transparency allows a clearer, more focused discussion without giving away a strategic position that competitors wouldn’t know already. It is hard to imagine why every company can’t disclose data more readily unless they’re deliberately being obscure or simply unable to measure the data internally. Either possibility should make investors more skeptical about underlying performance.

Simple actions can greatly improve investor communication. It’s time for companies to modernize their approach.

About the author
Werner Rehm is a senior expert in McKinsey’s New York office.