

The Coloplast experiment

The development of PricewaterhouseCoopers Corporate Reporting Framework included the assertion that companies reporting the types of information that investors are seeking will be rewarded. The results of our geographic and industry specific research confirms that there are indeed perceived rewards.

To test the hypothesis that a company could reap rewards from more expansive, context-rich reporting, the PricewaterhouseCoopers network sought the participation of Coloplast, a Danish company that has won awards for the quality of its presentation of corporate performance. Where most companies supplement financial reports with a simple statement of strategic intent backed by a few well-chosen metrics to illustrate performance, Coloplast goes further by identifying, and where possible, quantifying, the key activities critical to its strategy, then linking these activities to expected operating and financial outcomes. The information presented by Coloplast is impressive, far exceeding regulatory reporting requirements.

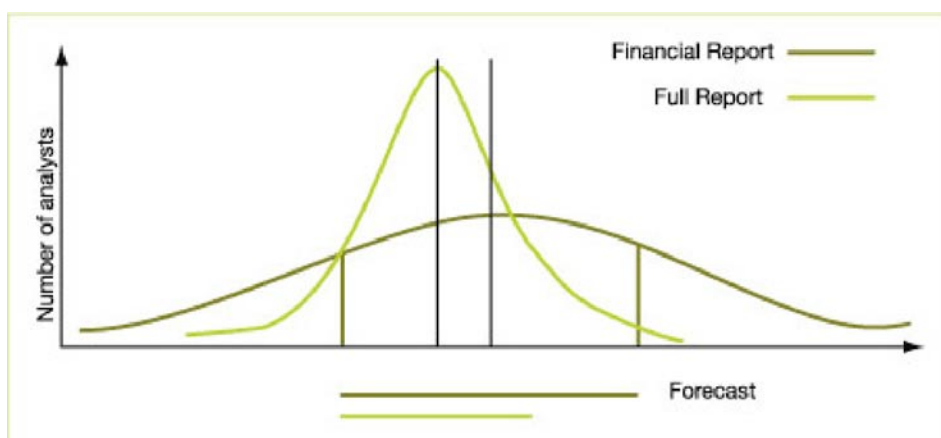
For the experiment, we created an edited version of Coloplast's 2002 annual report that omitted all of the contextual information and non-financial data. This modified, pared-down version of the report complied with accounting standards and included the sort of narrative that companies typically provide in annual reports, but nothing more. Different teams of analysts were then given either the original or the edited version of the report, but not both, and asked to:

- Develop a forecast of revenue and earnings
- Provide a "buy" or "sell" recommendation for the stock
- Provide an assessment of the relative riskiness of the company
- Provide a supporting rationale for their recommendations

The teams had two hours to complete their task - without consulting others or referencing external information sources. The outcomes of the teams' efforts proved quite interesting.

The analysts given the original, information-rich report actually forecast lower revenue and earnings than did the analysts who used the financially-based, regulatory-compliant version. Hypothesis disproved? Not really. Despite the lower forecasts, 60 % of the analysts with more complete information recommended buying the stock. By contrast, nearly 80 % of the analysts with less complete information recommended selling the stock.

With more contextual information to support the financial data, the analysts had more confidence in their forecasts and were much more likely to issue a "buy" recommendation (see the graph below.). Conversely, the analysts who used financial information alone showed less certainty in their economic projections, questioned the value of the company, and came up with an overwhelming "sell" recommendation.



The message to companies that fail to communicate contextual and non-financial information in a credible and well-structured fashion is that although analytical investment models may be financially driven, confidence in their use increases when there is greater access to more contextual and non-financial information.