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Survey on Companies' Reporting Behavior in Austria, Germany, and Switzerland

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SURVEY ON COMPANIES' REPORTING BEHAVIOR IN AUSTRIA, GERMANY, AND SWITZERLAND

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Most important Results

- According to company executives *Earnings* is the number one performance measure reported to outsiders. Analysts/Investors indicate to place more importance on the *Free Cash Flow*.
- The most important earnings benchmark is the previous year's annual earnings. (An earnings benchmark is a reference point for the reported annual earnings.)
- As an earnings benchmark, the analysts' consensus forecasts is much less important for the surveyed companies compared to evidence from the US. While 74% of financial executives in the US perceive analyst forecasts as important or very important, only 51% of company representatives in Austria, Germany, and Switzerland do so.
- 45% of company representatives consider it fundamental to report a profit ($EPS > 0$) at the end of the fiscal year, while analysts and investors seem to attach less interest to the company reporting a profit than meeting other benchmarks.
- Meeting or exceeding a specific earnings benchmark is important to build credibility with the capital market.
- Missing an earnings benchmark hurts. Companies in Austria, Germany, and Switzerland express stronger fear of consequences related to missing earnings benchmarks than do US companies.
- Although participants strongly agree on the importance of benchmark beating, companies declare not to undertake any action (expect earnings guidance) in order to actually meet their benchmark at the fiscal year end. Previous evidence shows that US companies in contrast, admit to time discretionary spending and investments in order to meet their benchmark. Analysts and investors perceive some actions related to accounting discretion not as reprehensible as financial executives do.
- More than 50% of firms reviewed assumptions and/or the factual accuracy of analysts draft earnings models for the fiscal year 2004.
- Swiss firms perceive sell side analysts as less important than German and Austrian firms. While 67% of non-Swiss firms consider sell-side analysts as very important, only 44% of Swiss companies do so.
- Companies in Austria, Germany, and Switzerland release bad news in a more timely manner than US firms do.
- While analysts believe that by devising strategic decisions firms pay attention to their opinion, firms strongly disagree on that statement. (The disagreement is especially pronounced among Swiss firms.)

- Analysts and company executives claim that the financial community is increasingly focused on short term earnings. However, while analysts and investors believe that this short term focus discourages companies from long term investing, managers do not concede that investing in long term value is affected.
- Overall, participants agree that analysts' expectations are a good proxy for market expectations. Analysts are perceived to have a profound knowledge of the firms and their industries and to communicate the companies strategy to outsiders. Generally, the acknowledgement of analysts for the firm is significantly lower among Swiss firms compared to German, and Austrian firms.
- Earnings Guidance is considered very important among all, companies, analysts and investors. However, only 38% of the firms provide guidance on EPS, and it is significantly less probable among Swiss firms.
- 40% of firms in Austria and Germany issue management forecasts on EPS, but only 22% of Swiss firms are using this guidance instrument.
- 67% of the firms have either stopped or have never been issuing management forecasts on EPS. Companies that do provide guidance on earnings experience significantly less uncertainty among analysts.

The goal of this survey is to provide an insight into motivations and incentives for companies in Austria, Germany, and Switzerland (three German-origin countries) to provide voluntary disclosure in general and earnings guidance in specific. In order to gain a better understanding of companies' reporting and communication behavior, this survey targeted two groups: Company communication representatives (CFOs or IROs) on the one side, and analysts/investors as the outside-of-the-firm representatives on the other side.

The questions are mostly based on the study by Graham *et al.* (2005), who surveyed 401 financial executives in the US¹. Based on feedback from several CFOs and Investor Relations specialists of Swiss companies, the survey content was modified and supplemented in order to receive additional information on guidance activities in the three countries.

Further, to compare the perceptions of the companies' managements with the demand-side of financial reporting, the questions were slightly modified and sent to representatives of the outside financial community, namely analysts and investors.

By applying part of the questions examined in the US, this survey attempts to compare the perceptions on voluntary disclosure, benchmark beating and earnings guidance not only among management and analysts, but also between the US as a common law system with an equity market focus, and three German-origin countries with their bank-oriented systems². Thus, in a further study, the influence of the institutional setting from the respective legal system on the discussed topics can be examined. In general, the focus on capital markets in Europe has been rising during the 90s, accompanied by an increasing importance of equity capital for listed companies. As a consequence, disclosure and investor relations (IR) activities have become increasingly important. Hence, it is especially interesting to investigate disclosure and earnings guidance within this context.

The questionnaire consisted of 24 (18) questions addressed to CFOs/IROs (Analysts/Investors) divided into the following topics:

I. Performance Measures and Reporting Benchmarks

This section is interested in the following questions: Which is the most important performance measure reported to outsiders? Particularly which benchmarks do managers on the one hand, and the financial community on the other hand consider as important when an earnings number is reported?

II. Meeting or Missing Reporting Benchmarks

This section is motivated by the following questions: What are the consequences of meeting or missing a reporting benchmark, and consequently, what motivations drive management to meet or beat the respective benchmark? Further, it is interested in the actions taken to meet the respective benchmark.

III. Information Intermediaries and Market Expectations

Questions in this section shall identify the most important information intermediaries in general and discover specifically how important financial analysts are for the company with respect to influencing market expectations.

IV. Voluntary Disclosure and Earnings Expectations Guidance

This section aims to provide an insight on how guidance is provided in general and how important guidance on earnings numbers is specifically. It further identifies assets and drawbacks of providing voluntary disclosure, and asks how companies deal with publishing good versus bad news.

Survey Participants

Two different versions of the questionnaire were developed, a written copy sent to all company representatives, and an online-version sent to members of the analyst associations of the respective country³. Firms in the sample were asked to report their company name. The survey was not implemented anonymously mainly for the reason that especially the Swiss and the Austrian markets are very small and respondents would have considered the survey being not anonymously if certain company characteristics would have been asked.

Companies

The written questionnaire was sent to a total of 569 firms (63 in Austria, 306 in Germany, and 200 in Switzerland). Considering the length of this survey, the overall response rate of 15% is satisfying, compared to the response rate of 10.4% reached by Graham *et al.* (2005). The rate results from 18% in Austria, 12% in Germany, and 21% in Switzerland. Table (1) provides mean and median of different firm characteristics.

Analysts and Investors

Financial Analysts were surveyed using the online-version of the questionnaire. The link was sent to all members of the Swiss Financial Analysts Association (SFAA) (www.sfaa.ch), the Society of Investment Professionals in Germany (DVFA) (www.dvfa.ch), and the Österreichische Vereinigung für Finanzanalyse und Asset Management (OVFA) (www.ovfa.at). Overall, 82 complete answers were received, which represents an extremely low answer rate of approximately 4%. Of the participating analysts, 11% are member of the OVFA, 29% of the DVFA, and 60% of the SFAA. 25% work as financial analysts on the buy-side, 18% on the sell-side, 23% as Asset Managers, 12% as Fund Managers, 22% indicated another profession.

<i>Firm characteristic</i>	<i>Mean</i>	<i>Median</i>
Revenue (in million CHF)	10'946	1'220
Market Value (in million CHF)	7'240	961
Debt/Assets	0.6	0.59
Revenue growth	10.44	4.16
ROE	-4.25	8.53
M/B Ratio	2.37	1.71
Intangibles/assets	10%	4%
Operating Profit (in million CHF)	809'733	65'471
Analyst following	9.8	6
Uncertainty	0.73	0.19
Shares held by insiders	33%	32%
Shares held by institutions	20%	18%

Table (1)

Statistical Evaluation

For every question, where participants had to indicate the level of importance or agreement, responses of CFOs/IROS and analysts/investors are provided in one table giving the following information: 1) The percentages of participants that indicated "agree"/"strongly agree" (or "important"/"very important"). 2) The percentages of participants that indicated "disagree"/"strongly disagree" (or "not important"/"not important at all"). 3) The average points for the respective statement calculated by weighting strong agreement with 2, agreement with 1, indifference with 0, disagreement with -1 and strong disagreement with -2. This allows to identify the average agreement level for the answers.

There is extensive empirical evidence on the influence of firm characteristics on disclosure levels. Hence, responses are evaluated conditional on certain firm characteristics. Following Graham *et al.* (2005), firms are categorized into two groups using the median of the firm characteristics (see table (1) for the medians of the characteristics). Subsequently, the agreement levels (as calculated above) are compared. Differences in responses that are statistically significant at the 5% or 1% level are provided in an additional table for every question. The statistical evaluation differs from the one conducted in the US in the firm characteristics used. Since the survey was not implemented anonymously and in order to shorten the questionnaire, the data on firm characteristics were received from databases as Reuters, Datastream, and I/B/E/S. The advantage is, that data are reliable and comparable among all firms. However, since not all variables were available in the databases a direct comparison of this evaluation with the one conducted in the US is only partly possible.

The following firm characteristics are used for building subsamples and conducting conditional analyses:

Firm *SIZE* is proxied by the firms' revenue. Larger firms are generally assumed to be more complex, which suggests the forecasting process to be more difficult. This is expected to result in higher (than mandatory) disclosure levels and increased earnings guidance⁴.

The firms' *leverage ratio* is measured by the debt-to-asset ratio. It proxies the firms' agency costs. Since a company's financial leverage is positively related to its agency costs and hence its monitoring costs, higher leverage is expected to be positively associated with the disclosure level and earnings guidance activity.

The firms' past *growth* rate is measured by the revenue growth over the past 5 years. Firms with high past growth in revenues are expected to be more concerned about negative earnings surprises since investors and analysts tend to interpolate past growth rates into the future⁵. Those firms are therefore expected to provide more guidance on expectations.

Profitability is measured by the return on equity (ROE). Further, companies are grouped into operating profit and operating loss firms. Empirical evidence on the relationship between profitability and disclosure is mixed, but research generally agrees on the existence of an association⁶.

The market-to-book ratio (*M/B-ratio*) proxies for the value of growth opportunities. Firms with high M/B-ratios are considered as growth stocks, which are generally highly priced compared to value stocks (characterized by low M/B-ratios). Since the forecasting process is assumed to be more complex for growth firms, those are expected to provide relatively more earnings guidance.

Also the level of *intangibles* (relative to total assets) are assumed to be positively related to the difficulty of forecasting a firm's future.

Analyst coverage is measured by the number of estimates for the firms annual earnings per share (EPS) in the I/B/E/S database. It can be expected that firms with higher analyst coverage provide more earnings guidance because "if management refuses to provide earnings guidance, analysts may drop coverage rather than damage their accuracy record"⁷.

Uncertainty is proxied by the standard deviation in analyst forecasts on EPS prior to the annual reporting date (available in I/B/E/S). Disclosing more information is expected to reduce uncertainty among analysts.

The firms' ownership structure is considered by the percentage of shares held by *insiders* and the percentage of shares held by *institutions*. The short term focus of institutional investors is likely to increase the probability of earnings guidance and the importance of meeting certain earnings benchmarks.

Conditional analysis is further provided by dividing the sample into 1) firms that indicated in the survey to provide guidance on EPS (*Earnings Guidance provided*) versus firms that do not guide earnings and 2) firms that indicate to issue management forecasts on EPS (*Management forecast issued*) versus those that do not issue management forecasts.

Finally, analysis conditional on the firms' *origin* is provided in order to reveal differences in the firms' disclosure behavior among countries.

Performance Measures and Reporting Benchmarks

2

Earnings versus Free cash flow

The strong emphasis on earnings as the most important financial performance measure reported to outsiders documented by Graham *et al.* (2005) is supported by CFOs/IROs of the German-origin countries underlying this sample. Figure (1) shows that company executives rank earnings as the most important performance measure, followed by revenue, cash flow from operations and free cash flow. Overall, 49% of company representatives of Swiss, Austrian, and German firms ranked earnings on the first position. This is an enormous fraction in comparison to 17% who indicated revenue as the number one performance measure.

Further performance measures specified by the participants in the field "others" were EBIT/EBITDA and ROE. Among analysts/investors, the distribution of the first rank is somewhat more dispersed. 32%

Which are the three most important performance measures reported to outsiders?

	CFOs/IROs	Analyst/Investors
Rank 1	Earnings	Free cash flow
Rank 2	Revenue	Earnings
Rank 3	Cash flow from operations	Cash flow from operations
	Free cash flow	Economic value added
	Economic value added	Revenue
	Pro forma earnings	Pro forma earnings

Figure (1)

mark the free cash flow as most important, while 24% rank earnings and 20% rank the cash flow from operations as the number one performance measure. Thus, on average, analysts/investors put the free cash flow on the first position⁸.

<i>Performance Measure</i>	<i>higher importance, if</i>	
Pro forma earnings	large firm	**
	operating profit	**
Cashflow	low ROE	***
	low analyst coverage	**
	low uncertainty	**
Earnings	low M/B ratio	**
EVA	large firm	**
	high leverage	**
	low revenue growth	**
	high analyst coverage	***
Revenue	small firm	***
	low leverage	**
	high revenue growth	**
	low analyst coverage	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (2)

The analysis conditional on firm characteristics leads to the following results, evident in figure (2): **Pro forma earnings** are relatively more important for large firms and those reporting an operating profit. This is contradicting to the result in the US survey, where unprofitable firms emphasize pro forma earnings. The **Cash flow from operations** is less important for relatively profitable firms (ROE), firms with a high analyst coverage, and firms with high uncertainty among analysts, proxied by the standard deviation in analyst forecasts. **Earnings** are considered more important for firms with low M/B ratios, i.e. the so-called value firms, which are characterized by low growth options and investment opportunities. The **EVA** is a significantly more important performance measure for large firms, highly leveraged firms, firms with low revenue growth, and firms with high analyst coverage. Finally, **Revenue** is less important for large firms, which is in line with the US results. It is also less important for firms with high leverage and firms with higher analyst following. Firms with high revenue growth, on the other side, place higher importance on Revenues, which is again consistent with the US results.

Earnings Benchmarks

Empirical research has provided evidence on discontinuities in distributions of reported earnings relative to different thresholds. For example, Daske *et al.* (2003) document a relatively high frequency of small positive earnings, small positive earnings changes, and zero or small positive forecast errors among 14 EU countries. Further, they find the strongest pronounced avoidance of losses and decreasing earnings in the German-origin countries of their sample, even compared to previous research in the US. Wilde (2004) documents a high frequency of small positive earnings surprises compared to small negative earnings surprises for SMI firms in 1990-2003. These observations suggest that managers try to beat or meet certain performance benchmarks. Thus, the next question intends to discover which earnings benchmarks are considered when reporting or reading annual results.

How important are the following earnings benchmarks when companies report annual results?

CFOs/IROs			
	(very) important	not important (at all)	average points
Last reported audited EPS	74%	10%	1.00 ***
Management forecast of EPS	55%	12%	0.61 ***
Last reported unaudited EPS	51%	27%	0.38 ***
Reporting a profit (EPS>0)	45%	16%	0.38 ***
Analyst consensus forecast	51%	18%	0.32 ***
Lead or most trusted analyst forecast	44%	22%	0.27 ***
Analysts/Investors			
	(very) important	not important (at all)	average points
Management forecast of EPS	76%	9%	1.00 ***
Last reported audited EPS	68%	10%	0.84 ***
Analyst consensus forecast	62%	17%	0.71 ***
Last reported unaudited EPS	61%	18%	0.46 ***
Lead or most trusted analyst forecast	40%	18%	0.29 ***
Reporting a profit (EPS>0)	33%	34%	-0.04

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average point significantly different from zero at the 1%-level

Figure (3)

As evident in figure (3), the average points of the earnings benchmarks in this question indicate that all benchmarks are considered important — they receive an average rating which is positive and statistically significant. With 74% of CFOs/IROs among the three countries, the last reported audited (the annual) EPS receives the highest percentage of agreement as well as the highest average points. However, as expected, firms that report less frequently than quarterly consider the last annual earnings number as significantly more important (average: 1.37) than quarterly reporting firms (average: 0.83).

Executives value the management forecast as the second most important performance benchmark. The lead analyst's and the analyst consensus forecast are the least important benchmarks. This is somewhat surprising, considering the empirically documented stock market reaction for firms that miss analyst consensus forecasts of earnings. Consistent with this finding financial executives in the US perceive analyst forecasts as much more important. According to Graham *et al.* (2005), this benchmark receives the second highest average points in the US (average agreement in the US: 0.96, compared to 0.32 in this survey). Among other earnings benchmarks indicated by the survey participants were profitability ratios compared to peer companies and three year targets.

Analysts consider the management forecast, the last reported audited EPS, and the analyst consensus forecast as most important. Whereas the least important benchmark is reporting a profit (EPS > 0) with an average agreement not significantly different from zero (indicating neither a positive nor a negative consideration of this benchmark). The difference in the perceptions of "reporting a profit" between executives and analysts/investors is striking.

<i>Performance Benchmark</i>	<i>higher importance, if</i>	
Analyst consensus forecast	low revenue growth	**
	high analyst coverage	***
Management forecast of EPS	management forecast issued	**
	eps guidance provided	***
Last reported unaudited EPS	eps guidance provided	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (4)

The analysis conditional on firm characteristics, summarized in figure (4) leads to the following significant results: The analyst consensus forecast is significantly more important for firms with low growth in revenues and firms with higher analyst coverage. It is worth noting that for firms with high analyst following, the analyst consensus forecast is the second most important performance benchmark after the last reported audited EPS. This suggests that the general results in figure (3) on the relatively unimportance of analyst forecasts compared to other benchmarks is driven by firms with low analyst

following. Interestingly for those firms who provide earnings guidance, the management forecast of EPS and the last reported unaudited (interim) EPS number are more important as an earnings benchmark. However, the order of those benchmarks is not altered within this group. As a matter of fact, the management forecast of EPS is significantly more important for those firms who do issue this forecast. The benchmark order, however, remains unchanged for both, forecast-issuers and non-issuers.

Meeting or Missing Reporting Benchmarks

3

Motivations to meet Earnings Benchmarks

There is plenty of empirical evidence on different reasons for why companies might exercise some discretion in order to meet the earnings benchmarks discovered in the previous section. Graham *et al.* (2005) classify these motivations into the following groups: Stock price driven motivations, Stakeholder motivations, Employee bonuses, Career concerns, and Bond covenants.

The survey participants were asked whether they agree/disagree on the positive influence of meeting earnings benchmarks on different objectives. Overall, the CFO/IRO responses in Germany, Switzerland, and Austria (documented in figure (5)) are very similar to the survey outcome in the US. The strongest and in this survey even stronger represented motivation for meeting an earnings benchmark is to build credibility with the capital market. 95% of the company representatives agree or strongly agree on this motivation (with an average agreement of 1.57 compared to 1.17 in the US). Although somewhat less pronounced, 84% of the analysts agree or disagree on this motivation as well. To company representatives, the second most important motivation is also stock price driven: 83% of the CFOs/IROs (strongly) agree on seeking to maintain or increase the stock price through benchmark meeting/beating. However, analysts and investors believe that the external reputation of the company's management team, i.e. career concerns, is even more relevant. Executives here and in the US significantly disagree on the allegation that the attempt to avoid violating debt-covenants might explain the benchmark beating game.

Meeting an earnings benchmarks helps...

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
... to build credibility with the capital market.	95%	1%	1.57	***
... to maintain/increase stock price.	83%	1%	1.16	***
... to convey growth prospects to investors.	78%	4%	1.05	***
... to increase management's reputation.	77%	3%	1.02	***
... to reduce stock price volatility.	55%	12%	0.61	***
... to assure that business is stable.	49%	22%	0.35	***
... to achieve/preserve credit rating.	45%	26%	0.25	*
... employees to achieve bonuses.	35%	24%	0.11	
... to avoid violating debt-covenants.	27%	45%	-0.30	**

Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
... to build credibility with capital market.	84%	2%	1.32	***
... to increase management's reputation.	79%	6%	0.96	***
... to convey growth prospects to investors.	66%	6%	0.80	***
... to maintain/increase stock price.	63%	4%	0.76	***
... to achieve/preserve credit rating.	57%	11%	0.59	***
... to assure that business is stable.	41%	22%	0.28	***
... to reduce stock price volatility.	44%	26%	0.26	**
... to avoid violating debt-covenants.	26%	28%	-0.09	
... employees to achieve bonuses.	23%	39%	-0.28	**

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average point significantly different from zero at the 1%-level

Figure (5)

According to figure (6) the analysis conditional on firm characteristics leads to the following results: Two stock price driven motivations, that is, **building credibility with the capital market**, and reducing the **stock price volatility**, are significantly more important motivations for benchmark meeting/beating when firms have higher levels of intangible assets. This result is reasonable, since intangible assets increase the complexity of the forecasting process, and the difficulty in valuing the firm. Hence, building credibility and reducing the volatility of the firm's stock price is of higher interest for those firms. **Building credibility with the market** is also of higher interest for firms with higher analyst coverage, which is intuitively reasonable, if one considers: firstly, the increasing importance of the analyst consensus forecast as an earnings benchmark with increasing analyst coverage (as evident from figure (4)), and secondly the perception that analysts' expectations are a good proxy for market expectations (as evident from figure (13)). Thus, firms with high analyst coverage have strong incentives to meet/beat analyst expectations as an earnings benchmark, in order to build credibility with the capital market. Missing those expectations is similar to disappointing the market itself. Achieving or preserving a desired **credit rating** is significantly

<i>Motivation to meet earnings benchmark</i>	<i>stronger, if</i>	
achieve/preserve credit rating	low revenue growth	**
	low ROE	**
	low M/B ratio	***
	no management forecast issued	**
assure that business is stable	low ROE	***
	operating loss	***
	low institutional ownership	***
avoid violating debt-covenants	low ROE	**
	low analyst coverage	**
build credibility with capital market	high intangibles	**
	high analyst coverage	**
	management forecast issued	**
reduce stock price volatility	high intangibles	**
convey growth prospects to investors	non-swiss firm	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (6)

more important for companies with a relatively low growth (or even a decrease) in revenues over the previous five years, firms with low ROE, and firms with low growth opportunities expressed through a low M/B-ratio. For firms with low ROE or an operating loss, it is more important to assure stakeholders that their **business is stable**, an intuition, which is reflected in the conditional results. Moreover, analysis reveals that assuring the steadiness of the business is significantly more important for firms with lower institutional ownership. Firms with low ROE, and low analyst coverage have higher incentives to **avoid violating debt-covenants** through benchmark beating behavior. While the association between profitability and this incentives is reasonable, the relationship between coverage and avoiding to violate debt-covenants through benchmark meeting/beating remains open. Interestingly, the significantly higher importance of **achieving bonuses** for firms with high percentages of insiders found in the US, is not supported. Finally, it is worth noting that **conveying the growth prospects to investors** is a significantly less important motivation for meeting an earnings benchmark among Swiss firms. While it receives the third highest average points among non-Swiss firms, it falls back to rank 4 in Switzerland. Here, the Swiss result is in line with the US survey outcome, where the external reputation of the management team also attracts more attention than conveying the growth prospects to investors.

Consequences of missing Earnings Benchmarks

A motivation to meet an earnings benchmark does not only have to be achieving a certain favorable environment as asked for in the previous question. It can also be provoked by the anticipation of an unfavorable situation resulting from missing the respective earnings benchmark. The survey participants were further asked for certain reasons for why missing an earnings benchmark hurts.

According to figure (7) the most frightening consequences of a failure to meet or beat the earnings benchmark are an increased uncertainty about the company's future prospects, the outsiders' impression of previously unknown problems at the firm, and the increasing time of explaining to outsiders why a certain benchmark could not be reached.

Analysts/investors, however, believe that the increasing time consume is not as important as the increasing scrutiny of all aspects of the company's earnings release.

It is interesting to note, that the disagreement on a higher probability of lawsuits following the failure of beating a certain benchmark is much more pronounced in Europe compared to the US. Although also 38% US CFOs disagree on this, an overwhelming percentage of 68% European CFOs/IROs disagree or strongly disagree. This result is intuitively reasonable if one considers the stronger investor protection and shareholder rights in common-law countries (as the US) compared to German civil-law countries (as Austria, Germany and Switzerland).

Missing an earnings benchmark hurts because...

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
...it creates uncertainty about the future prospects.	87%	2%	1.17	***
...outsiders might think there are previously unknown problems at the firm.	71%	8%	0.83	***
...the firm has to spend a lot of time explaining why it missed.	57%	15%	0.54	***
...it leads to increased scrutiny of all aspects of the earnings releases.	47%	13%	0.34	***
...outsiders might think that the firm lacks the flexibility to meet the benchmark.	29%	38%	-0.15	
...it increases the probability of lawsuits .	2%	68%	-1.01	***
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
...it creates uncertainty about the future prospects.	78%	2%	1.18	***
...it leads to increased scrutiny of all aspects of the earnings releases.	60%	5%	0.71	***
...outsiders might think there are previously unknown problems at the firm.	68%	10%	0.70	***
...the firm has to spend a lot of time explaining why it missed.	48%	26%	0.29	***
...outsiders might think that the firm lacks the flexibility to meet the benchmark.	30%	29%	-0.01	
...it increases the probability of lawsuits .	10%	61%	-0.67	***

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average point significantly different from zero at the 1%-level

Figure (7)

<i>consequence</i>	<i>higher agreement, if</i>	
leads to increased scrutiny of all aspects of the earnings releases	operating loss	**
outsiders might think that the firm lacks the flexibility to meet the benchmark	low ROE	**
	operating loss	**
it increases the probability of lawsuits	austrian firm	***

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (8)

Conditional analyses reveal the following facts, summarized in figure (8): Meeting an earnings benchmark in order to prevent the market from assuming the firm might **lack the flexibility to meet the respective benchmark** is significantly more important for unprofitable firms, such as operating loss and low ROE firms. Firms with an operating loss also stronger agree on the fact that missing an earnings benchmark leads to **increased scrutiny of all aspects of the earnings release**.

Overall, the different perceptions of unprofitable firms compared to profitable firms lead to the conclusion, that reporting a profit itself might be an important benchmark.

Graham *et al.* (2005) found stronger agreement on all consequences among firms that provide earnings guidance on EPS. It is therefore interesting that within the German-origin countries company executives do not assess the drawbacks of missing a benchmark differently depending on whether or not they provide guidance. Rather, there is even a stronger agreement level (expressed in average points) for feared consequences among all firms here compared to the US.

How to meet or beat Earnings Benchmarks

After having investigated the advantages of beating and drawbacks of missing earnings benchmarks, it is still open how companies actively manage to meet or beat their respective benchmark. The survey participants were asked which choices (within what is permitted by accounting rules) a company might realize if it faces the situation of possibly missing its desired earnings target near the end of the financial period. Actions for benchmark beating can be separated into the following groups: Earnings Guidance (also referred to as Expectations Management), and Earnings Management. The latter itself can be subdivided into: Accounting Management and Real Earnings Management⁹.

CFOs/IROs as well as analysts, responded mainly with disagreement (figure (9)), which is somewhat surprising considering the high relevance of benchmark beating documented by previous questions. The only action that receives significant agreement is to guide down market expectation, which shows the importance of earnings expectations as a benchmark, and the management or guidance of expectations by the company. 40% of company representatives (strongly) agree on decreasing discretionary spending, such as R&D expenditures, advertising or maintenance costs. However, since a significant fraction of CFOs/IROs disagree, the average of points on this real economic action is close to zero in contrast to the significantly positive agreement in the US with an average agreement level of 1.

The second of two actions that received a significant positive rating from US executives was the possibility to delay a project even if this delay would be accompanied by a small sacrifice in value. CFOs/IROs in the present survey significantly disagree on this action, while analysts/investors are indifferent, with an average agreement close to zero.

More than half of the company representatives would under no circumstances postpone taking an accounting charge, sell investments or assets (in order to recognize gains this period), alter accounting assumptions (e.g. allowances, pensions, etc.), or repurchase common shares (in order to increase EPS). Analysts/investors, however, only significantly reject the possibilities to alter accounting assumptions or repurchase common shares.

Which of the following choices might the company make, if it looks like the company might miss the desired earnings target?

CFOs/IROs

	(strongly) agree	(strongly) disagree	average points	
Lower market expectations	72%	4%	0.94	***
Decrease discretionary spending	40%	35%	-0.03	
Draw down on reserves	28%	27%	-0.05	
Delay starting a new project	24%	31%	-0.20	**
Provide incentives for customers	23%	39%	-0.34	***
Book revenues now rather than next period	23%	44%	-0.48	***
Postpone accounting charge	2%	57%	-0.75	***
Sell investments/assets to recognize gains	12%	63%	-0.81	***
Alter accounting assumptions	5%	71%	-1.09	***
Repurchase common shares	1%	71%	-1.12	***

Analysts/Investors

	(strongly) agree	(strongly) disagree	average points	
Lower market expectations	74%	12%	1.05	***
Book revenues now rather than next period	49%	34%	0.23	*
Provide incentives for customers	45%	33%	0.16	
Draw down on reserves	40%	34%	0.07	
Decrease discretionary spending	38%	39%	-0.02	
Delay starting a new project	37%	37%	-0.02	
Postpone accounting charge	35%	40%	-0.13	
Sell investments/assets to recognize gains	33%	49%	-0.20	
Alter accounting assumptions	32%	46%	-0.32	**
Repurchase common shares	13%	57%	-0.57	***

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average points significantly different from zero at the 1%-level

Figure (9)

<i>action taken</i>	<i>more probable, if</i>	
Book revenues now	small firm	**
	low leverage	**
	operating loss	***
Provide incentives for customers	operating loss	***
Draw down on reserves	operating loss	**
	low analyst coverage	***
	small firm	***
Sell investments/assets to recognize gains	non-german firm	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (10)

Conditional analyses provide the following insights (figure (10)): Small firms are neutral on **booking revenues now** rather than later, with an agreement level close to zero, compared to -0.58 for large firms. Firms with an operating loss are more tempted to book revenues now, then firms with an operating profit. Further, this action receives significantly stronger disagreement from highly leverage firms. Firms with an operating loss would **provide incentives for customers** in order to meet/beat a benchmark: while 44% of operating loss-firms agree on this possibility with an average rating of 0.33, only 18% of operating profit-firms agree (average disagreement level -0.51). **Drawing down on reserves** is on average accepted among firms with low analyst coverage (average rating: 0.25), firms with an operating loss (average rating: 0.44), and small firms (average rating: 0.38). In contrast highly covered, profitable, and large firms express an average rating of -0.44, -0.19, and -0.36 respectively. German firms indicate stronger disagreement on **selling investment or assets** for meeting the desired earnings target.

Information Intermediaries and Market Expectations

4

In this part of the survey, the influence of information intermediaries on market expectations in general, and the importance of financial analysts for a company in specific are investigated. Firstly, the survey participants were asked which information intermediaries were most important in terms of shaping market expectations about the company and setting its stock price. Based on the average points CFOs/IROs and analysts view analysts (sell-side and buy-side) and institutional investors as the most important groups for the stock price of the firm (figure (11)).

How important are information intermediaries in terms of shaping market expectations about a company?

CFOs/IROs				
	(very) important	not important (at all)	average points	
Sell-side Analysts	88%	3%	1.40	***
Institutional Investors	89%	2%	1.24	***
Buy-side Analysts	80%	4%	1.09	***
Media	60%	9%	0.63	***
Individual Investors	35%	34%	0.00	
Rating Agencies	33%	45%	-0.24	*
Hedge Funds	33%	46%	-0.24	*
Analysts/Investors				
	(very) important	not important (at all)	average points	
Sell-side Analysts	79%	6%	1.15	***
Buy-side Analysts	66%	11%	0.79	***
Institutional Investors	71%	9%	0.76	***
Media	63%	13%	0.65	***
Rating Agencies	57%	13%	0.55	***
Hedge Funds	38%	27%	0.13	
Individual Investors	7%	66%	-0.83	***

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average point significantly different from zero at the 1%-level

Figure (11)

Further, according to company executives rating agencies, hedge funds and individual investors are not important, while analysts view only individual investors as unimportant. It is, however interesting to note the different perception of individual analyst between CFOs/IROs and analysts/investors. While company representatives are indifferent on the influence of individual investors, only 7% of analysts/investors believe that individual investors have an influence at all.

<i>Intermediary</i>	<i>higher importance, if</i>	
Sell-side Analysts	large firm	***
	high ROE	**
	high intangibles	**
	high analyst coverage	***
	high institutional ownership	**
	non-swiss firm	**
	german firm	**
Institutional Investors	non-swiss firm	**
	german firm	**
Rating Agencies	large firm	**
	high leverage	**
	low revenue growth	***
Hedge Funds	large firm	***
	low revenue growth	**
	high intangibles	**
	high analyst coverage	***
	high uncertainty	**
Individual Investors	low analyst coverage	***
	low uncertainty	***
	small firm	**
	high revenue growth	**
Media	low analyst coverage	***
	low ROE	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (12)

21% shares are held by institutions. **Rating Agencies** are rated as significantly unimportant among small firms, firms with high revenue growth and lowly leveraged firms, while the respective counterparts are indifferent on whether Rating Agencies are important or not.

Hedge Funds are not important (at all), when a firm is relatively small, only few analysts follow the firm, and when a firm has been growing relatively quickly over the past five years. Further, Hedge Funds are not important (at all) to firms with relatively few intangibles and less uncertainty among analysts.

Individual Investors are important for small firms and for those firms with a high growth over the past five years, whereas they are not important for large firms or those who grew slowly or experience a decrease in revenues. Further, to firms with low analyst following and low uncertainty among analysts, individual investors are indeed important.

Media are perceived to be more important for firms low analyst following.

The perception of the importance of different groups on the company's stock price strongly varies with firm characteristics. Conditional analyses, summarized in figure (12), highlight the following facts: **Sell-side analysts** are significantly more important for large firms and firms with high analyst coverage. These two characteristics are clearly not independent — large firms have higher analyst following on average. Since it is empirically documented that higher analyst coverage has a positive impact on a firm's market value¹⁰, firms have incentives to increase coverage if possible. Moreover, since large firms can be expected to be more complex, there is a higher demand for analyst reports from the investors' side. This also explains the higher importance of sell-side analysts for firms with high levels of intangibles. It is striking that Swiss firms rate sell-side analysts significantly lower than their peer firms, especially in Germany. While 67% of non-Swiss firms believe that sell-side analysts are *very important*, only 44% of Swiss firms do. Also results in the upcoming sections reveal generally a lower acceptance of sell-side analysts in Switzerland. Surprisingly, the importance of **Institutional Investors** for the stock price does not depend on the degree of institutional ownership. It is, however, less strong for Swiss firms, especially compared to German firms, although German and Swiss sample firms do not have significantly different institutional ownership: Austrian sample firms have an average institutional ownership of 13%, whereas in Switzerland and Germany on average 20% and

The survey participants were further asked to assess the validity of different statements on financial analysts, their profession, and the financial community. According to figure (13), company representa-

Do you agree/disagree with the following statements about analysts and the financial community?

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
Analysts help to communicate the strategy	86%	6%	1.20	***
High coverage has positive impact on share price	75%	6%	1.00	***
Analysts' expectations are a good proxy for market expectations	72%	4%	0.78	***
Analysts have profound knowledge of firm/industry	55%	12%	0.54	***
Financial community has increasing focus on short-term earnings	55%	20%	0.44	***
Short-term earnings focus discourages from investing in long-term value	38%	32%	0.08	
Analysts have less impact on expectations since 2000	31%	37%	-0.02	
It is difficult to communicate complexity of business to analysts	38%	41%	-0.03	
By devising strategic decisions firms pay attention to analysts' opinion	28%	39%	-0.24	**
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
Analysts help to communicate the strategy	79%	9%	0.98	***
Financial community has increasing focus on short-term earnings	72%	18%	0.89	***
Short-term earnings focus discourages from investing in long-term value	66%	17%	0.72	***
Analysts' expectations are a good proxy for market expectations	67%	13%	0.71	***
It is difficult to communicate complexity of business to analysts	55%	16%	0.51	***
High coverage has positive impact on share price	56%	21%	0.49	***
Analysts have profound knowledge of firm/industry	61%	16%	0.48	***
By devising strategic decisions firms pay attention to analysts' opinion	49%	22%	0.29	***
Analysts have less impact on expectations since 2000	39%	38%	-0.01	
* average points significantly different from zero at the 10%-level				
** average points significantly different from zero at the 5%-level				
*** average point significantly different from zero at the 1%-level				

Figure (13)

tives as well as analysts and investors consider that financial analysts have a profound knowledge about the covered firm and its industry, and that they help to communicate the firm's strategy to investors. However, companies indicate that they do not pay attention to analysts' opinion when devising strategic

decisions, although analysts themselves assume that their opinion does influence the managements' decisions. (As will be revealed in the conditional analysis, the companies' opinion here is strongly driven by Swiss companies.) Both participant groups agree on the predications that financial analysts' expectations are a good proxy for market/investors' expectations and that high coverage has a positive impact on a company's share price. While both, company representatives and analysts/investors agree on the financial community's increasing focus on short-term earnings, they differ about this short-term focus discouraging companies from investing in long-term value. Only 38% of CFOs/IROs agree on that statement compared to 66% of analysts/investors. Finally, it is interesting to note that analysts/investors indicate it as difficult for firms to communicate the complexity of their business to financial analysts, whereas companies themselves do not feel a difficulty here¹¹.

<i>Statement</i>	<i>higher agreement, if</i>	
Analysts' expectations are a good proxy for market expectations	high intangibles	***
	non-swiss firm	**
	german firm	**
Analysts have profound knowledge of firm/industry	non-swiss firm	**
	german firm	**
Analysts help to communicate the strategy	non-swiss firm	***
	german firm	***
By devising strategic decisions firms pay attention to analysts' opinion	low leverage	**
	non-swiss firm	**
High coverage has positive impact on share price	high intangibles	***
	non-swiss firm	**
	german firm	***
It is difficult to communicate complexity of business to analysts	high uncertainty	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (14)

Conditional analyses summarized in figure (14) provide the following insights: In general, the perception of analysts knowledge and their use to companies by communicating the strategy to investors is significantly higher for non-Swiss companies: While 76% of Swiss companies agree or strongly agree on this statement, an overwhelming 96% of non-Swiss firms agree or strongly agree. Moreover, while Swiss firms strongly contest the assertion that companies pay attention to analysts' opinion (average points: -0.49), non-Swiss firms are indifferent (average points: 0.00).

The result from the previous section that Swiss firms have a lower perception of analysts is assured further: Not only do non-Swiss firms indicate a stronger agreement on analysts' expectations being a good proxy for market expectations, but also do non-Swiss firms stronger agree on high coverage having a positive impact on a company's share price.

Firms indicating that it is difficult to communicate the complexity of their business to analysts are those firms with high information asymmetry: While firms with low uncertainty among analysts on average disagree (average points: -0.3), companies with high uncertainty agree (average points: 0.28).

Finally, high levels of intangibles let firms agree more on the importance of analyst expectations as a proxy for market expectations and the positive association between analyst following and a firm's stock price.

Voluntary Disclosure and Earnings Expectations Guidance

5

How Guidance is provided

Daske *et al.* (2003) (p. 12) note that evidence on analyst guidance in Europe exists, although "large sample size research on Investor Relations in general and earnings guidance in specific is missing, largely because databases on such activities are virtually non-existent". In order to gain a better understanding on how guidance is provided (received) from firms in Austria, Germany, and Switzerland, CFOs/IROs (analysts/investors) were asked for which measures they provide (are provided with) guidance.

For which measures do companies provide guidance?

% CFOs/IROs that provide guidance on respective measure		% of Analysts/Investors that receive guidance on respective measure	
Sales/Revenues	81%	Sales/Revenues	79%
EBIT	65%	EBIT	74%
Net Income	48%	EPS	62%
EPS	38%	Net Income	54%
Cash flow	19%	ROE	39%
FCF	19%	FCF	35%
ROE	17%	Cash flow	27%

Figure (15)

More than 50% of the sample firms provide guidance on Sales/Revenues and EBIT, while more than 50% of the analysts/investors indicate to receive guidance on Sales/Revenues, EBIT, EPS, and net income. Guided measures specified by CFOs/IROs in "others" were EBITDA, EBITA, EBT, Capital Expenditures (CAPEX), Gross Margin, Order in take, and Return on Capital Employed (ROCE). One participant noted that "we give out consensus numbers, but no guidance in numbers, only general guidance on market conditions [...]. [G]uidance [is] only given in case of restated results". Another IRO stated that "[w]e give out consensus numbers but no quantitative guidance, only qualitative".

<i>Measure</i>	<i>Guidance more probable, if</i>	
ROE	operating profit	***
	high leverage	**
	low intangibles	***
	non-german	**
Cash flow	high insider ownership	**
FCF	small firm	**
	low leverage	**
	low analyst coverage	***
	swiss firm	**
	non-austrian firm	**
EPS	low uncertainty	**
	low institutional ownership	***
	non-swiss firm	***
	german firm	**
Net Income	low analyst coverage	***
	low institutional ownership	***
	eps guidance provided	**
	non-german firm	**
EBIT	low leverage	***
	low uncertainty	***
	eps guidance provided	***
Sales/Revenues	small firm	**
	low ROE	**
	low leverage	**
	german firm	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (16)

Overall, the average number of guided measures is 3.3. Conditional analyses reveal significant differences in the number of guided measures. Higher guidance activity is associated with smaller firm size, lower analyst coverage, lower leverage, and lower institutional ownership. Moreover (as documented in figure (16)), it is interesting to note, that firms with higher analyst following provide significantly less guidance on **FCF** and **net income**. Lower information asymmetry (that is, lower uncertainty among analysts) is predominant in firms that provide guidance on **EBIT** and **EPS**, which is intuitively reasonable. Guidance on **EPS** is significantly more observable in non-Swiss firms. While 52% of Austrian and German firms guide EPS numbers, only 22% of Swiss firms do so. With 29%, however, Swiss firms provide significantly more guidance on the **FCF**, compared to 10% of the non-Swiss firms. Guidance on **Sales** is significantly more likely in small firms, lowly leveraged firms and low ROE-firms. With 92% of the German firms providing guidance on **Sales**, this is significantly more common in Germany than in Austria and Switzerland, where 73% of the firms guide sales numbers. Instead, German firms provide significantly less guidance on **ROE** and **Net Income**. **FCF** guidance is less likely in large firms, highly leveraged firms, and firms with high analyst following. Finally, highly leveraged firms, profitable firms, and intangible intensive firms provide more guidance on **ROE**.

How do you issue management forecasts on EPS? (Companies' view only)

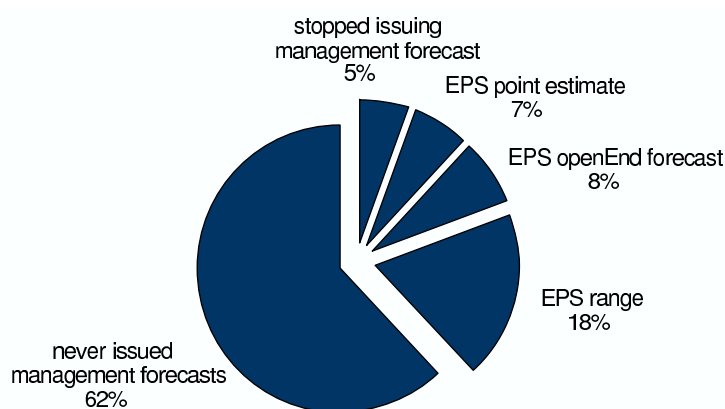


Figure (17)

Survey participants were further asked, in which way companies issue management forecasts on EPS. As evident from figure (17), 62% of the companies indicate that they have never issued those forecasts. This is the same amount of companies that indicated not to provide guidance on EPS. However, there are 29% companies, which provide EPS guidance without issuing management forecasts, 12% companies, which indicated not to guide EPS number, but issue management forecasts on EPS, and 7% companies, who do not provide guidance on EPS and recently stopped issuing management fore-

casts.

Overall, 23% of the companies issue management forecasts on EPS, whereby most of the firm provide an EPS range. Analysts support the result of the issuance of EPS ranges as the most frequent way to provide management forecasts (figure (18)). They indicate that about 45% of the firms they follow have never issued management forecasts on EPS, while about 21% of the firms recently stopped. Analysis conditional on the firms' origin (summarized in figure (19)) reveals that in Austria 45% of the firms issue management forecasts by providing an EPS range, and 55% of the firms have never issued management forecasts at all. In Switzerland, 71% of the firms indicate that they have never issued management forecasts, 2% have recently stopped issuing them, while among the rest of the firms all ways of issuing management forecasts are represented with almost the same frequency. In Germany, 50% of all firms have never issued management forecasts on EPS, 11% have recently stopped, and among the rest of the companies, the most frequent method is issuing an EPS range. Conditional analysis further indicates that overall, issuing EPS point estimates is less likely in Austria, whereas in Switzerland providing EPS ranges is less frequent.

How do companies issue management forecasts on EPS? (Analysts' view only)

% of Analysts/Investors that observe the respective way of management forecast issuance	
stopped issuing management forecast	21%
EPS point estimate	16%
EPS openEnd forecast	35%
EPS range	74%
never issued management forecasts	45%

Figure (18)

management forecast issued as	more probable, if	
EPS point estimate	non-austrian firm	**
EPS range	non-swiss firm	***

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (19)

Subsequent to the questions on measures for which guidance is provided and on the ways of issuing management forecasts, the survey participants were asked which specific actions companies accomplished for the fiscal year 2004 in order to provide earnings guidance.

How important are the following actions to the company in order to provide earnings guidance for the current year?

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
Review assumptions of analysts' draft earnings models	55%	20%	0.34	***
Review factual accuracy of analysts' draft earnings models	51%	27%	0.27	**
Only long-term guidance provided	35%	31%	0.02	
Issue management forecasts on EPS	23%	48%	-0.45	***
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
Issue management forecasts on EPS	50%	5%	0.61	***
Review assumptions of analysts' draft earnings models	52%	9%	0.52	***
Review factual accuracy of analysts' draft earnings models	45%	21%	0.23	**
Only long-term guidance provided	33%	16%	0.21	**
<i>Companies do not provide guidance at all</i>	12%	33%	-0.37	***

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average points significantly different from zero at the 1%-level

Figure (20)

As evident from figure (20), more than 50% of the firms agree or strongly agree on reviewing assumptions and the factual accuracy of analysts' draft earnings models¹². CFOs/IROs significantly disagree on the issuance of management forecasts as an instrument for guidance in 2004, although analysts view this as the mostly used instrument at all. 35% of the companies indicate to only provide long-term guidance, which corresponds to the response from analysts, who indicate that 33% of the firms covered only provide long-term guidance.

Additionally, analysts were asked whether firms they follow do not provide any earnings guidance at all. On average, analysts significantly disagree on this statement.

Conditional analyses, summarized in figure (21) reveal the following facts: Earnings guidance through the issuance of management forecasts is significantly more probable if firms have high growth opportunities (proxied by the M/B ratio). Those firms are less likely to provide only long term guidance. Also to firms with higher levels of intangibles issuing management forecasts is more important. However, al-

<i>actions taken</i>	<i>more probable, if</i>	
Review assumptions	austrian firm	**
Issue management forecasts	high ROE	**
	high M/B ratio	**
	high intangibles	**
	management forecast issued	***
	eps guidance provided	***
	non-swiss firm	**
	austrian firm	**
Only long-term guidance provided	low M/B ratio	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (21)

though those two characteristics related to the difficulty of the forecasting process let firms tend to value the issuance of management forecasts a bit more important, the average points are still negative. As expected, firms who indicated to provide guidance on EPS and to issue management forecasts in the two previous questions, believe that this is a very important instrument (average points significantly positive). The already documented aversion of Swiss firms to issue management forecasts is confirmed: Swiss firms have a significant higher objection against issuing management forecasts in this question. Austrian firms on the other hand value the issuance of management forecasts with positive average points and are more probable to *review assumptions* of analysts' draft earnings models.

The Importance of Earnings Guidance

This section examines the importance of earnings guidance under specific circumstances. As documented in figure (22), more than 50% of CFOs/IROs and analysts/investors (strongly) agree on the importance of earnings guidance in general, when the market misestimates the prospects of the firm and prior to an equity issuance.

How important is earnings guidance to companies?

CFOs/IROs				
	(very) important	not important (at all)	average points	
In general	77%	9%	0.87	***
If market overestimates prospects	61%	6%	0.71	***
If market underestimates prospects	62%	10%	0.66	***
Before equity issuance	54%	16%	0.46	***
Before earnings release	43%	18%	0.29	***
Before bond issuance	40%	19%	0.19	*
Before major strategic decision	29%	25%	0.03	

Analysts/Investors				
	(very) important	not important (at all)	average points	
In general	80%	4%	1.05	***
If market overestimates prospects	74%	4%	1.04	***
If market underestimates prospects	72%	5%	0.96	***
Before equity issuance	60%	11%	0.66	***
Before major strategic decision	59%	13%	0.66	***
Before earnings release	48%	16%	0.39	***
before bond issuance	39%	38%	0.10	

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average points significantly different from zero at the 1%-level

Figure (22)

While analysts/investors consider guidance prior to major strategic decisions significantly important, CFOs/IROs are neutral (neither agreement nor disagreement).

Both sides agree on earnings guidance not being important prior to the issuance of bonds.

Analysis conditional on firm characteristics summarized in figure (23) again confirms that Swiss firms view earnings guidance significantly less valuable and important than firms in Germany and Austria. Average points for the importance of guidance *in general*, or when the market *misestimates the firm's prospects* are double as high in Austria and Germany, compared to Switzerland. *Prior to an earnings release*, non-Swiss firms regard guidance as important (average points 0.6), while Swiss firms are undecided (average points 0).

<i>importance of earnings guidance</i>	<i>higher, if</i>	
In general	high M/B ratio	**
	high intangibles	***
	management forecast issued	**
	eps guidance provided	***
	non-swiss firm	***
	german firm	**
If market overestimates prospects	high ROE	**
	high intangibles	**
	high analyst coverage	**
	management forecast issued	**
	non-swiss firm	**
	german firm	**
If market underestimates prospects	non-swiss firm	***
	german firm	**
Before equity issuance	low revenue growth	**
Before earnings release	non-swiss firm	***
	german firm	**
Before bond issuance	low M/B ratio	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Moreover, conditional analysis indicates that *in general*, earnings guidance is more important if firms have high investment opportunities (high M/B-ratios), and high levels of intangibles. Thus, the more difficult the forecasting process, or the higher the information asymmetry, the more important earnings guidance.

Needless to say, firms that provide EPS guidance or issue management forecasts, place more importance on earnings guidance *in general* than other firms. If the *market overestimates prospects*, firms are more likely to provide guidance if they have a relatively high ROE, and if guidance is easier, i.e. if they are followed by many analysts. Before the *issuance of new equity*, guidance is especially provided when firms have relatively low, or even negative revenue growth over the past five years.

Figure (23)

Voluntary Disclosure - For Better or for Worse

Benefits - Voluntarily communicating financial information...

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
...promotes a reputation for transparent/accurate reporting	92%	2%	1.35	***
... reduces information risk that investors assign to the stock	82%	3%	1.02	***
...provides important information not included in mandatory reports	63%	11%	0.72	***
... attracts more analysts	61%	11%	0.56	***
... reduces risk of not being compliant with ad-hoc-publicity rules	57%	14%	0.53	***
... corrects undervalued stock price	57%	8%	0.52	***
...increases stock liquidity	54%	14%	0.41	***
...reduces cost of capital	42%	19%	0.26	**
...increases P/E ratio	32%	15%	0.17	**
... reveals skill level of managers	31%	26%	0.01	
... reduces risk premium employees demand for holding stock granted as compensation	13%	44%	-0.49	***
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
...promotes a reputation for transparent/accurate reporting	77%	4%	1.00	***
... reduces information risk that investors assign to the stock	72%	6%	0.80	***
... attracts more analysts	62%	12%	0.56	***
... reduces risk of not being compliant with ad-hoc-publicity rules	46%	13%	0.41	***
...provides important information not included in mandatory reports	43%	12%	0.41	***
... corrects undervalued stock price	41%	21%	0.23	**
... reveals skill level of managers	34%	32%	-0.04	
...reduces cost of capital	28%	38%	-0.15	
...increases stock liquidity	26%	33%	-0.15	
...increases P/E ratio	23%	34%	-0.18	*
... reduces risk premium employees demand for holding stock granted as compensation	13%	43%	-0.35	***
* average points significantly different from zero at the 10%-level				
** average points significantly different from zero at the 5%-level				
*** average point significantly different from zero at the 1%-level				

Figure (24)

A comprehensive review of disclosure literature is given by Healy & Palepu (2001), who divide corporate disclosure into disclosure through regulated financial reports, firms' voluntary disclosure, and disclosure about the firm through information intermediaries. Voluntary disclosure by issuing management forecasts, arranging conference calls or providing interim reports when not mandatory is an instrument to guide the market with respect to upcoming earnings numbers. It is beyond that certainly motivated by other benefits associated to voluntarily providing information to the market. Following Graham *et al.* (2005), the participants were therefore asked for the benefits associated with voluntarily communicating financial information to the market (figure (24)).

92% of the companies presume that providing voluntary disclosure promotes a reputation for transparent/accurate reporting. This is together with the reduction of information risk (82%), the provision of important information not included in mandatory disclosure (63%), the reduction of not being compliant with ad-hoc-publicity rules (57%) and the correction of an undervalued stock price (57%) the most important motivations to provide disclosure voluntarily.

Both, CFOs, and analysts agree on the fact that providing voluntary disclosure is not motivated by a subsequent reduction of the risk premium employees demand for holding stock granted as compensation. The results are in line with the US survey outcome.

<i>statement</i>	<i>more agreement, if</i>	
reduces cost of capital	large firm	***
	austrian firm	**
increases P/E ratio	large firm	***
	low uncertainty	**
	non-swiss firm	**
	austrian firm	**
reduces risk of not being compliant with ad-hoc-publicity rules	low leverage	**
increases stock liquidity	low uncertainty	**
reveals skill level of managers	high insider ownership	**
	low institutional ownership	**
provides important information not included in mandatory reports	high analyst coverage	**
corrects undervalued stock price	non-swiss firm	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Conditional analyses (see figure (25)) reveal that **reducing the cost of capital** and **increasing the P/E ratio** is a significantly more important factor driving the decision to voluntarily disclose information for large firms. Against one's expectations, for firms with a lower percentage of institutional owners and more insiders, it is important to **reveal the skill level** of the companies' management to outsiders, whereas this is relatively unimportant to firms with low insider ownership and high institutional ownership. Firms with low uncertainty among analysts stronger believe that they increase their **P/E ratio** and the **stock liquidity** by voluntarily communicating with the market. Firms with high analyst coverage have a relatively higher intention to **provide important information** to investors that is not included in mandatory reports. In Switzerland, firms view an **increasing P/E ratio** and the **correction of an undervalued stock price** as relatively less motivating to provide voluntary disclosure.

Figure (25)

tary disclosure.

Certainly, providing information voluntarily is not only associated with benefits. Opponents even argue that those do not outweigh the subsequent costs. Thus, participants were asked why companies should limit voluntary disclosure.

Limiting voluntary communication of financial information helps avoid...

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
...setting a disclosure precedent	43%	20%	0.28	***
...giving away " company secrets "	45%	27%	0.19	*
...potential follow-up questions	28%	34%	-0.11	
...attracting unwanted scrutiny by stock-/bondholders	14%	46%	-0.43	***
...possible lawsuits	12%	49%	-0.47	***
...attracting unwanted scrutiny by regulators	13%	49%	-0.52	***
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
...setting a disclosure precedent	35%	22%	0.20	*
...possible lawsuits	29%	32%	-0.07	
...potential follow-up questions	28%	35%	-0.10	
...attracting unwanted scrutiny by stock-/bondholders	21%	39%	-0.22	**
...attracting unwanted scrutiny by regulators	17%	48%	-0.38	***
...giving away " company secrets "	20%	55%	-0.48	***

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average point significantly different from zero at the 1%-level

Figure (26)

According to both, companies and analysts/investors, setting a disclosure precedent that may be difficult to continue in the future is most important reason for why companies should limit voluntary disclosure (see figure (26)). Evident from the average points, CFOs/IROs also intent to avoid giving away "company secrets" or otherwise harming their competitive position. This was also the second strongest motive to US companies for limiting disclosure. 55% Analysts/investors, in contrast, significantly disagree on this motive. On the other hand, analysts are indifferent on the argument that avoiding possible lawsuits if future results don't match forward looking disclosures might be a reason for limiting disclosure. Nearly 50% of the companies disagree on this motive. In the US, however, this motive receive the third highest (significantly positive) agreement level. Avoiding unwanted scrutiny by either stock-/bondholders or regulators is not an important incentive for limiting voluntary disclosure here as well as in the US. Finally, one company representative stated that, "if you follow legal disclosure rules, you cover [...] all investors/analysts need[s] [...] Info outside the classic pattern causes more concern than trust. Ad-hoc publicity regulations have very clear rules for this and [...] take care of all "out of the rule" events".

<i>statement</i>	<i>more agreement, if</i>	
setting a disclosure precedent	low leverage	**
giving away "company secrets"	low leverage	**
attracting unwanted scrutiny by regulators	low leverage	***
attracting unwanted scrutiny by stock-/bondholders	low leverage	**
	high insider ownership	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
*** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (27)

Conditional analyses are summarized in figure (27).

Overall, lowly leveraged firms are significantly more prbable to limit voluntary disclosure in order to avoid setting a disclosure precedent, giving away company secrets, and attracting unwanted scrutiny either by stock-/bondholders or by regulators.

Firms with a high fraction of insider ownership have a lower disagreement level on avoiding attracting unwanted scrutiny by stock-/bondholders. It is, however, still negative.

Academic literature discusses two potential sources of costs associated with large negative earnings surprises: The risk of lawsuits, and the loss of reputation (Skinner (1994)). Moreover, Skinner (1994) provides evidence for an asymmetric stock price response to bad news versus earnings news releases. These costs motivate managers to disclose bad news faster in order to prevent large negative earnings surprises. Bagnoli *et al.* (2005) examine the strategic timing of earnings news during the week and provide evidence for the attempt to delay bad news until the end of the week (Fridays). With respect to the timing of voluntary disclosure, participants were finally asked for the motives related to disclosing bad or good news faster.

Do the following statements describe a company's motives related to the timing of voluntary disclosure?

CFOs/IROs				
	(strongly) agree	(strongly) disagree	average points	
Disclosing bad news faster enhances the companies' reputation for transparent and accurate reporting	82%	3%	0.98	***
Disclosing bad news faster reduces risk of potential lawsuits	43%	25%	0.24	**
Good news is released faster than bad news because bad news takes longer to analyze/interpret	16%	48%	-0.51	***
Good news is released faster because companies try to package bad news with other disclosures	6%	68%	-0.89	***
Companies tend to delay positive news in order to offset bad news	4%	75%	-1.03	***
Analysts/Investors				
	(strongly) agree	(strongly) disagree	average points	
Disclosing bad news faster enhances the companies' reputation for transparent and accurate reporting	74%	17%	0.71	***
Good news is released faster because companies try to package bad news with other disclosures	51%	18%	0.51	***
Disclosing bad news faster reduces risk of potential lawsuits	46%	26%	0.24	**
Companies tend to delay positive news in order to offset bad news	29%	22%	0.11	
Good news is released faster than bad news because bad news takes longer to analyze/interpret	28%	44%	-0.30	**

* average points significantly different from zero at the 10%-level
 ** average points significantly different from zero at the 5%-level
 *** average points significantly different from zero at the 1%-level

Figure (28)

82% of the surveyed companies (strongly) agree that disclosing bad news faster enhances their reputation for transparent and accurate reporting. Although less significant, 43% (strongly) agree that it reduces the risk of potential lawsuits. This is a relatively lower level of agreement compared to surveyed firms in the US, where 77% endorsed this statement. This result is in line with research on differences between civil-law and common-law countries. For example, Ball *et al.* (2000) and Bushman & Piotroski (2005) document that bad news disclosure is more timely in common-law countries, which might be caused by the fact that German civil-law countries have weaker legal shareholder rights than common-law countries, as documented by La Porta *et al.* (1998). Companies listed in the US face a greater risk of lawsuits and are therefore expected to disclose bad news more timely.

When asked whether bad news take longer to be analyzed and interpreted and are therefore slower released than good news, company representatives as well as analysts/investors strongly disagree, which contrasts the responses in the US remarkably, where 67% of CFOs (strongly) agree on this statement.

Also the statement on the strategy of packing bad news with other disclosure causing those bad news being released slower than good news is strongly rejected by company representatives in this survey. Analysts/investors, however, indicate to observe this behavior by companies. US executives neither accepted nor rejected this behavior.

To summarize the findings: Graham *et al.* (2005) conclude that some companies in the US might delay bad news despite arising risks of a damaged reputation or lawsuits. Evidence in the surveyed German origin countries strongly contradicts to this behavior, suggesting that those firms report news (both bad and good news) more timely than US firms.

<i>statement</i>	<i>more agreement, if</i>	
bad news faster reduces risk of lawsuits	low leverage	**
	operating loss	**
delay positive news in order to offset bad news	low institutional ownership	**
	management forecast issued	**
	guidance on eps provided	**
good news faster because bad news takes longer to analyze/interpret	austrian firm	**

** different perception between the respective low- and high-group is statistically significant at the 5%-level
 *** different perception between the respective low- and high-group is statistically significant at the 1%-level

Figure (29)

suggests a more conservative disclosure in the German-origin countries. Firms seem to be more cautious and issue news as soon as they occur.

Conditional analyses summarized in figure (29) reveal the following facts: Lowly leverage firms and firms with an operating loss stronger agree on the fact that disclosing bad news faster reduces the risk of potential lawsuits. Firms with lower institutional ownership, and those that issued management forecasts on EPS or generally provide guidance on EPS are more probable to delay positive news for which ad-hoc-publicity rules are not applicable in order to offset bad news. However, the average agreement level remains negative.

Overall, the outcome of this question

Notes

1. The questionnaire of Graham *et al.* (2005) is available at <http://faculty.fuqua.duke.edu/~jgraham/finrep/survey.htm>.
2. Commercial Law is distinguished in English-origin common law, and Roman origin civil law. The latter is further divided into French origin, German origin, and Scandinavian origin civil law. Austria, Germany and Switzerland belong to German civil law countries. (See La Porta *et al.* (1998)).
3. A copy of the two versions may be requested via Email (wilde@isb.unizh.ch).
4. Another reason for a positive relationship between firm size and disclosure level are decreasing disclosure costs with increasing firm size. See Lang/Lundholm1993 for a discussion on the relation between firm size and disclosure.
5. See Skinner & Sloan (2002), p. 290.
6. See Lang & Lundholm (1993) for a discussion on the association between performance and disclosure level.
7. See Hutton (2005).
8. This result, however, is driven by Swiss analysts; in accordance to company executives, analysts in Austria and Germany agree on earnings as the number one reporting measure for company performance.
9. Real Earnings Management is "accomplished by timing investment or financing decision to alter reported earnings or some subset of it" (see Schipper (1989)).
10. See for example Chung & Jo (1996).
11. Since Graham *et al.* (2005) did not ask this question in their survey a comparison is not possible at this point.
12. The "Corporate Disclosure Practices Survey 2001" in the US, implemented by the National Investors Relations Institute (NIRI) and cited in Hutton (2005) documented that in 2001, 40% (22%) of the companies reviewed factual accuracy (assumptions) of analysts' draft earnings models.

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