

## NEERAJ BHATT'S VIEWS ON MANAGING INVESTOR SENTIMENT

To enable practitioners to provide appropriate information to both the financial media and analyst, let me explain three things. First, how financial analysis is done, second what additional information do analysts require and what the media and the analysts expect out of companies.

*...understand what an analyst looks at...*

Analysts or investors get their basic information from these four sources:

- annual report and the quarterly statements
- news and magazines reports
- company advertisements, which are quite informative
- stock exchanges, SEBI, RBI filings

*...annual reports are a good starting point...*

In the annual reports the analyst examines the equity data - in terms of the bonus, the rights, dilution or the extent of dilution that has happened in the past. They will also consider the growth rates in sales, operating profits, net profits, as well as look at profitability ratios, operating profit margins and net profits margins. The return on capital employed and return on equity would also be important because it tells the investor how much he is earning on the money invested.

*...parallel growth in earnings per share and price earnings implies stock price hikes...*

Market capitalisation is a very important figure these days and we saw HLL recently cross the Rs. 50,000 crore mark. Debt is another important issue, and how leveraged the company is, what are its costs and profitability. The next would be cash-flow and book value. Cash-flow statements have become mandatory since 1998 and the book-value also gives an indication, especially in light of the relevance of M&As. Working capital of a company and how a company manages its working capital, inventories and receivables, is another important issue. As well as the great obsession of monitoring earnings per share and the price earnings ratio. If the earnings per share shows a growth and price earnings also shows a growth after that, then the stock price goes up substantially more than it would without a price-earnings revaluation.

News reports also play a very important role - the past news reports would provide a historical perspective in the sense on what the company has been doing, important decisions taken in the past, its diversification plans and its core business strengths. That gives a lot of information to the analyst.

The company track record of honouring its commitments is another important issue. Companies have a habit of

promising various things at various stages. They may say something a year back, but whether they deliver it is a very important aspect.

*...keep the lines of communication open...*

Meeting the media and the analyst community is again an important issue. There are lots of companies even now who do not meet media or the analyst community at all. Current news reports are where PR practitioners can definitely help in changing sentiment at least. What analysts seek in the news reports is whether the development is important, whether it will change anything at all in the company, demanding a review of current opinions on the company.

Company advertisements, new products, new developments, orders, contracts, are very important for analysts. The Chairman's speech has again become a very important piece of advertisement, but it is more of a PR exercise. The chairman's speech should relate what is happening to the industry and the specific company in the current year and not the chairman's view on the economy. Recruitment advertisements tell us what the company is doing, where the growth is going to come from, what other businesses it is entering. For example, Himachal Futuristic entering software.

Stock exchange filings are another important source of information. A fire at your plant is reported at the stock exchange first, and then becomes known in the media. If the company is small and the media does not find it very important to report the incident, the daily bulletin and weekly bulletins of the stock exchanges prove useful. SEBI and RBI will give information on FI holdings, which again is relevant information today.

Apart from all this information, what else does an analyst look for – growth trends, whether they are positive for the company and will these change how the company performs next year. This is the **growth approach**. Analysts also consider the **value approach**, whether the stock is under-priced in the first place, and if it is under-priced verify whether all the conditions are fair. If the company is expected to show growth in the future as far as its sales and earnings go and the stock price reflects that growth, then it gets recommended for an investment.

*...with accurate & timely reports...*

An analyst expects accuracy and timeliness in reporting and disclosures of various figures. They expect transparency from companies and also expect the company to share data and information, especially the non-quantitative type. We have seen a sea change in annual reports in the last two years - cash flows have

come in and moreover, companies have found it important to talk to investors through the annual report. This obviously has to be the best method as it is the only opportunity when the chairman gets to write a letter to the vast pool of investors these days.

*...product /brand information is of interest..*

Normally there would two categories in the extreme ends. One end would be, an annual report made for the financial accountants, which would include copious data but not give any information. On the other extreme end is the coffee table annual report, which include glossy pictures but very little information on the company. So there is room for improvement in annual reports. What analysts would like to see in the annual reports next year would be management discussions of financial conditions and business operations of the company. They would also be very keen to know what each division is doing and how profitability is. Category or product wise information is quite relevant in a multi-product/brand company, its market share or its profitability and what the contribution is to the profits. To some extent, it may be sensitive information, but nevertheless these figures are available off the record from various sources.

*...and so are collaborators and lineage...*

Information on parent and collaborators for multinationals is very important. Multinationals in India could learn from its parent company on how they make their annual reports. There is a sea change, just too vast especially, when we look at the information that an American Company has to provide to investors versus what its Indian subsidiary does.

A company may take some management decisions during the year, for example on the sale of a particular division, which would require some explanation:

- *why it did it*
- *what impact it had or would have in the future*

Infosys did it in 1996 when the GE contract was taken away from it.

Consolidation of accounts is part of the Company Law bill and will work wonders if companies do give it voluntarily like WIPRO does. Some companies are also sharing FAQs and shareholder information, for example Cheminol Drugs. The company did very badly in a particular year and there was question and answer session with the Managing Director, Mr. Prasad, on why the company had performed so badly. In this way negative information at least gets diluted.

*...timely preparation* Corporate governance report is another new concept that

*and dispatch of the annual reports...*

some companies have started. This could consist of simple things like:

- *how many directors are executive versus non-executive?*
- *how many directors attend the board meeting in the first place?*
- *what kind of profit-sharing do the directors have?*

These can be tackled in the report. Most importantly the annual report should go to the investors at the right time, two months after the closing of the financial year would be a good time.

*...quarterly results...*

Poor quarterly results always get tucked away in some corner of an obscure newspaper and are difficult to find it. Quarterly results also reach on time, companies practise the just-in-time principles here as against their inventory and suddenly at the end of the month you see some 300 odd companies bringing out results. It is more important to meet the press and analysts when the going is tough.

Companies also have a habit of comparing apples for oranges - sometimes a six-month result is compared to a nine-month result and sometimes expenditure, pre-operating expenditure is brought in. Even the quarterly result could have a short commentary of operations and the impact of any major change the company has gone through in that quarter. These would be very relevant. Notes could also be put in at the end of quarterly notes. Balance sheet data should be available if not in advertisement form, at least given later on request. This will indicate, for example, increasing employee costs or VRS costs. All this information given by a company is very relevant to the analyst.

The other qualitative information that companies need to share is:

- *data on operating performance*
- *market shares - specially for the multinationals*
- *division-wise performance and profitability*

*...and industry trends are relevant...*

Companies should also provide information on the following:

- *How management views competition in the short term and the long term?*
- *New products in the market and the performance of the product in the face of competition?*
- *What the trend in advertising expenditure is going to be?*
- *How technology is going to change the industry?*

The next part is Media and Analysts. There is a trend by which company executives, who are slick and smooth, end

up meeting the analysts and media community. It would however be more beneficial if companies bring out a cross section of people across divisions and across functions to meet with the media and the analysts. This will add a lot of value to analysts and media.

Investors have been moving of late for plant visits once in a while, but more companies can take undertake this. Companies should acknowledge that something is on. If Glaxo and SmithKline Beecham can say that merger talks are on, why can't Indian companies talk about their friendly merger talks, it just brings information faster to investors. There are also many instances when a company denies the story, a correction is then carried and then the story turns out to be true later. PR people on the other hand have a problem of promising a lot more than they can deliver. As far as personal experience goes, if an interview is scheduled, this week and if it doesn't happen, I would like to know that as soon as possible.

Some other random thoughts on what companies can do is to have toll-free telephones for investor services which is allowed by MTNL. The internet will turn out to a very important information disseminator very soon and internet can be as interactive as on-line. Companies should identify a person in each major city to tackle the investors, mainly the small investor who always has problems. The big investor always gets the information he wants. An investor who is not an investor but a potential investor like a capital fund manager would get to meet the Managing Director, but would a small investor gets that kind of information.

What is very important for everyone to remember is that shareholders are the owners of business. Treat them like owners and if they have right to information then it should be given to them.

#### **QUESTION & ANSWER**

*Which of the two approaches – growth or value approach would be more suitable or whether it was specific to industries?*

Mr Bhatt replied that a mix of both was suitable. Growth is good today for software or FMCG. But value may be the better indicator for cement stock. It would also depend on the industry and the conditions in the industry.

*One most common complaint against analysts is about their herd mentality. What is...*

Mr Bhatt agreed that there was a lot of herd mentality, but that it is not unique to India as it is also known to occur in Wall Street.

*mentality. When stock is going good, you find recommendations for strong buys and vice versa when it is not so?*

*What does a PR person or company need to be careful about when they interact with media. What are the kinds of things that can be misinterpreted, misconstrued or misreported? As there are enough instances where companies have shared information & have actually got into trouble because of coming out clean.*

Responding to the first part, Mr Bhatt replied that there were problems with the "off the record" and "on the record" statements. Some journalists have gone ahead and printed "off the record". So the PR person has two options: not to send information or trust the person. But he quoted personal experience saying that companies have tried to hide more things than possible.

Answering the second part of the question, Mr Bhatt said that coming out clean with the media usually doesn't get a company into trouble – however, it could have happened on a particular news story.

*(Excerpted from the presentation made by Niraj Bhatt, Assistant Features Editor, Smart Investor Business Standard, at PR Pundit's workshop – The Contemporary Portfolio, held in Mumbai on March 17, 1999)*