Where is the 'Global' in Your Financials?

Panelists:
Michael Kesner, Leader, National Compensation Practice, Deloitte Consulting
Tavis McCourt, Managing Director and Analyst, Raymond James
Zachary Rosenstock, CFA, Senior Equity Analyst, Segall Bryant & Hamill
Terri Anne Powers, Director, North American Investor Relations, Veolia Environnement

Moderator:
Heather Wietzel, Senior Director, Lambert, Edwards and Associates

Key Takeaways

- **Foreign exchange volatility is at its third-highest level in two decades.** Currency fluctuations can have a significant effect on assets, liabilities and equity beyond the effects that flow through the income statement. Many companies grapple with how to communicate currency volatility in a way that is transparent and meaningful.
- **FX or structural weakness?** When currency fluctuations reduce financial performance, the first question analysts ask is whether the changes in the balance sheet reflect a structural weakness in the underlying business. Currency transaction risk occurs when sales are denominated in a foreign currency. These sales must be converted to U.S. dollars before they can be recorded. Currency volatility can put pressure on product pricing and margins, reducing revenue but not necessarily market share, said Tavis McCourt of Raymond James. Investors are much more concerned if a company is losing market share because of pressure from a local competitor.
- **Financial presentations need to help investors understand companies operating in multiple currencies.** Veolia Environnement operates in more than 45 countries and therefore, its costs are also local – so the company only faces translational currency impacts. To show the impact of currency fluctuations for improved comparison and disclosure, Veolia presents the impact of currency on certain P&L metrics via standalone impact as well as figures presented on a constant currency basis. In quarterly reports, Veolia presents an appendix of currency movements in its main markets to help analysts and investors gauge which currencies are the most material to the company. Veolia also presents the percentage of debt denominated in foreign currency to help analysts and investors gauge the impact of currency fluctuations on debt balances.
- **The impact of foreign currency fluctuations on financial outcomes and incentive plans presents management with a particularly thorny challenge.** Management and boards have considerable discretion in making adjustments to financial performance that is applied to the executive incentive compensation formula.

  "You can't [allow currency effects to] double bonuses when earnings are down, regardless of why," said Michael Kesner, Deloitte Consulting's national compensation practice leader. He went on to suggest that incentive plan compensation and bonus disclosures reconcile the differences between GAAP and adjusted earnings. Companies must be more transparent about disclosing the incentive pay formula, or it will raise red flags with investors.

– Bess Gallanis