CTC Investor Relations

Market News

November 2016

A monthly review of IR developments for our clients and friends. . .

Directors split on non-GAAP regulations

Most directors of public companies think non-GAAP measures more accurately portray their results. But according to a survey published by accounting firm BDO USA, directors are evenly split on whether regulators should give more guidance on how non-GAAP numbers appear in financial statements. The half favoring additional guidance point to EBITDA measures as their biggest concern about possibly misleading investors, followed by restructuring costs, equity-based compensation and acquisition integration. Two-thirds of the participants think investors would have more confidence in non-GAAP financials if they were required to be audited prior to disclosure. Meanwhile, the SEC appears to be taking its crackdown on excessive non-GAAP reporting to a new level. The Wall Street Journal says several public companies have been advised that the SEC's enforcement division is looking specifically at non-GAAP reporting by several large companies.

Proposed 'universal ballot' would boost dissident odds in capturing board seats

Last week the SEC voted 2-1 in favor of a proposal that would require companies give shareholders a single proxy ballot that lists all candidates in a contested board election. Currently, shareholders receive two sets of ballots in contested elections, each featuring a rival slate of board candidates. The universal ballot would make it easier for investors to split their votes. Under existing rules, shareholders must attend the annual meeting in person to vote for candidates on both slates. The proposal must go through the comment period and be voted on a second time before becoming law.

ISS sets new standards for 2017 shareholder votes

Advisory service Institutional Shareholder Services Inc. (ISS) has proposed new principles to its clients for 2017 shareholder voting, based on its annual survey. For U.S.-listed domestic companies, ISS is proposing that shareholders vote against directors at companies that significantly restrict shareholders' ability to amend bylaws, and against directors at IPO companies with multiple share classes with unequal voting rights unless the unequal provisions expire within a reasonable time. ISS also wants companies listed on US exchanges but incorporated elsewhere to limit their share issuance powers and conform their executive compensation rules to U.S. standards. ISS is seeking comments on its new proposals through November 10.

Investors confident ranks high for audits and the capital markets

The Center for Audit Quality's Main Street Investor Survey found the highest degree of confidence in investing in U.S. publicly traded companies since the 2008 recession. Seventy-nine percent of American investors said they are confident in U.S. capital markets, while 81 percent indicated they have confidence investing in U.S. publicly traded companies. Three-quarters of them were confident in audited financial statements, while 77 percent had a high degree of confidence in independent audits.

Corporate debt continues to pile up

Buoyed by low interest rates and healthy liquidity, investment-grade U.S. companies are piling up more debt than their earnings justify. The trend to increase leverage continued unabated through mid-2016. The ratio of median debt-to-EBITDA for U.S. investment-grade companies climbed to 2.6 at the end of June 2016, up from 1.8 ten years ago according to credit rating agency Moody's. Further contributing to the spiraling debt, corporations are feeling pressure to allocate more of their earnings toward paying dividends, as yield has become an important consideration for investors in the low-rate environment. Moody's points out that this trend has cut the proportion of earnings converted into free cash flow, and with it, financial flexibility.

Likeable symbols earn premium prices

Likability and the ability to pronounce a stock symbol has positive impacts on the value of a company, according to a study published in the October *Journal of Financial Marketing*. Undergraduate business students at the University of Central Florida rated three-letter symbols from 1,959 publicly traded companies as on how much they liked them and how easy they were to pronounce. They found that between 1982 and 2011 the favorable companies traded 1.3 percent higher. While that doesn't seem like much, the study's author points out that for identical companies having $1 billion of assets, the one with the likeable symbol value would appreciate $13 million more than another with a less favored symbol. The study also found that stocks with more-likable symbols trade at a higher rate.

SEC breaks enforcement records in 2016

SEC Chair Mary Jo White proudly proclaimed that her agency had filed 868 enforcement actions related to financial reporting misconduct in fiscal 2016 ended September 30, a single-year high. The year saw the most cases involving investment advisors and investment company violations, with 160, and the most actions related to the Foreign Corrupt Practices Act at 21. A record $57 million was distributed to whistleblowers. Judgments and orders yielded more than $4 billion in disgorgements and penalties in fiscal 2016. "By every measure the enforcement program continues to be a resounding success, holding executives, companies and market participants accountable for their illegal actions," White said.

Fighting fire with fire

The Financial Industry Regulatory Agency (FINRA), NASDAQ and the London Stock Exchange are testing whether artificial intelligence software can replace algorithms to detect patterns of trading data that may signal manipulations. The sheer volume of data has become overwhelming for the algorithms method. FINRA alone monitors roughly 50 billion market events a day, which includes stock orders, modifications, cancellations and trades. Algorithm methods look for about 270 patterns to uncover potential rule violations, creating many false alarms on the way. Artificial intelligence will look beyond set patterns, learning new patterns as they develop to better understand which situations warrant red flags. Artificial intelligence surveillance software is set to debut in 2017.

SEC rule would set new fund liquidity requirements

New SEC rules regarding disclosure and holdings are intended to ensure liquidity in the asset management industry. Funds must better assess, manage, and periodically review their liquidity risk, defined as the risk that a fund could not meet a large redemption request without significantly diluting other investors. This rule will require a fund to determine a minimum percentage of its net assets that must be invested in highly liquid investments, show it can respond to a highly liquid investment minimum shortfall, and prohibit funds from purchasing additional illiquid investments if more than 15 percent of its net assets are illiquid.

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