STANFORD BUSINESS GRADUATE SCHOOL OF

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GUIDE TO INVESTOR REPORTS FOR EARLY CEOS

INTRODUCTION

While most every early CEO knows they should communicate with their investor group, often they struggle with the question of "how often and how much?" The result is generally, "not often enough, and too much". This white paper offers best practices for investor reporting, so that you can focus on running your company and knowing you're presenting investors with the most professional face of both you and your company.

UNDERSTAND YOUR AUDIENCE

For most of your investors, you are one of ten to twenty startup investments, of which startups might be only 20% to 50% of their investment portfolio. That does not mean you are not important, but it does mean there is only so much you can expect your investors to retain and remember about your company.

That means your report should stand on its own—meaning you cannot expect the reader to recall original deal facts, what you told them last quarter. As well, the best reports present data and information with context. For example, include the quarter's EBITDA with comparison to last year and budget; present the balance sheet in the context of prior months; or include with your sales pipeline perspective on what a good or bad pipeline looks like.

At the same time, consider the likely questions on the mind of your reader. They can't buy more or less of your company, like a public stock, and they know they are with you until the bitter, or sweet, end. Therefore, they're probably thinking just these four things:

- Am I glad I invested in this company?
- Is there anything they need from me?
- Is the CEO getting the job done?
- What are the company's priorities?

David Dodson, Lecturer in Strategic Management, prepared this note as the basis for class discussion.

For this reason (and out of courtesy of their time) the best reports avoid lots of data and raw facts, and instead curate the information, presenting only the essential material. It's best to avoid taking your investors on a treasure hunt, asking them to dig through charts and tables and elaborate graphics, in order to get answers to their questions.

Finally, remember that most investments operate on the same quarterly cycle. That means whether it be reports from hedge funds, real estate partnerships, venture deals, as well as investments in Stanford MBAs, your investor is likely getting a small avalanche of quarterly reports at the same time you are sending them yours. Show respect by presenting your material in an economical and concise manner—remember the adage: "If I had more time, I'd have written you a shorter letter".

OUTLINE OF AN EFFECTIVE QUARTERLY REPORT

While there is nothing sacrosanct about this particular outline, it's certainly one that most of your investors will find effective.

1. Recap the original transaction in the form of a simple sources and uses table, with the assumed EBITDA or relevant valuation metric:

Sources			**Uses**		
Senior debt	4.3	2.0x	Cash purchase price	14	6.6x
Seller roll	2.3	1.1x	Cash to B/S	0.5	0.2x
Investor equity	8.2	3.9x	Fees	0.3	0.1x
Earn out	3.0		*Earn out*	3.0	
Total	**14.8**	**7.0x**		**14.8**	**7.0x**

2. Short description of the company:

   "Johnson Environmental picks up recyclable materials, such as cardboard or plastic from food processors, cleans and sorts the waste product, and then delivers the refined product to paper and plastic product manufacturers. The company charges the generator of waste product a set monthly charge and rents receptacles on three-year contracts."

3. 150-word executive summary, essentially answering the question, "How are we doing?":

   "After a difficult second quarter due to the loss of our largest customer and an unexpected increase in health insurance expense, both sales and margin improved leaving us likely to hit our original forecast…"

4. Table with key performance indicators (KPI), which may include some financial information, but captures important operating indicators not found in the standard financials:

	Q3 Actual	Q3 Budget	Q3 LY	Variance Budget	Variance Last Year	YTD Actual	YTD Budget	YTD LY	Variance Budget	Variance Last Year
Patient Visits/Day	13,421	12,750	10,981	5%	22%	45,900	47,048	32,943	-2%	39%
Revenue/Patient	876	940	880	-7%	0%	2,996	3,102	2,772	-3%	8%
New Patients	127	200	98	-37%	30%	434	588	335	-26%	30%
% Private Pay	77%	75%	64%	3%	20%	79%	75%	67%	5%	18%
Cash Balance	785	600	137	31%	473%	785	600	137	31%	473%
EBITDA	468	400	297	17%	58%	1,601	1,476	891	8%	80%

5. Note that all of the information is presented in context to last year and budget. As well, don't move the goal posts from quarter to quarter. While it's okay to swap out KPIs from time to time as your company evolves, generally speaking report consistent information.

6. Standard financials. Always to include the balance sheet and the cash flow along with your income statement. Present this in your report, and not as an excel attachment.

   Below each financial statement, include roughly 100 words of commentary answering questions that are likely to be raised by the information; but do not restate what is clear in the financials (e.g. "EBITDA increased 17% to $468,000…").

   For each financial report, consider using these two formats:

   Comparison Format

	Q3 Actual	Q3 Budget	Q3 LY	Variance Budget	Variance Last Year	YTD Actual	YTD Budget	YTD LY	Variance Budget	Variance Last Year
Revenue	2,345,009	2,509,160	2,251,209	-7%	4%	7,269,528	8,029,311	6,866,186	-9%	6%
Cost of Goods										
Labor	539,352	631,042	496,204	-15%	9%	1,671,991	2,019,334	1,513,422	-17%	10%

   Trend Format

	Actual									Projected			
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
Revenue	807,725	791,571	807,402	791,254	807,079	790,938	806,756	790,621	806,434	800,000	810,000	820,000	9,629,781
Cost of Goods													
Labor	185,777	182,061	185,703	181,988	185,628	181,916	185,554	181,843	185,480	168,000	170,100	172,200	2,166,250

   This same presentation would hold true for the balance sheet and income statement, with the obvious exception that YTD and quarterly is the same for balance sheet data.

   Then below each set of financial statements, offer commentary on the Income Statement, Balance Sheet, and Cash Flow Statement:

   "While we continue to improve over last year, our inability to on-board new customers in our Birmingham location has led to a negative variance to budget. While our Atlanta and Nashville offices are ahead of plan (8% and 3% respectively) Birmingham is 13% below budget…"

7. 350 to 500 words of general thoughts, focusing on key initiatives, what keeps you awake at night, what you need from your investors, or important developments. If

there are exceptional issues like an acquisition or debt recap, that should be in a separate section.

8. Appendix with standard reference items
   a. Organization chart
   b. Cap table with shares
   c. List of board of directors
   d. If appropriate, definitions of non-obvious terms (e.g. how attrition is calculated, acronyms, explanation of key operating indicators)

GENERAL TIPS FOR BEST PRACTICES

1. Make sure the quarterly report is self-contained in one complete pdf report for your investors and avoid multiple attachments. If your investors like to have an excel version of the financials, have that as an optional attachment, but not part of the basic report.

2. Avoid jargon. You live with the industry day-to-day, but your investors do not. Use acronyms, industry terms, and nicknames sparingly, and where absolutely necessary offer a definition.

3. There's no reason to repeat the content of your report in the body of your email – as it often just requires your investors to read the same thing twice. Simply write in the email: "Please see attached third quarter report for Fisk Performance Company."

4. For variance analysis, use the negative sign for unfavorable comparisons and the positive sign for favorable comparisons—that way your investor can quickly pick up the essence of the comparison.

5. PowerPoint is convenient for the author, and generally hell for the reader! Don't dump unlinked data points, and complex graphics, and expect us to figure out what it means. Remember this rule: write how you speak.

6. Be careful about the use of graphics, unless it truly enhances the message. Often all those arrows and colors and shapes create confusion for your reader rather than simplify the message.

7. Use your senior finance manager for much of the work. You should delegate most of the quarterly reporting, such that your role is principally the 350-500 words of commentary, while the financial presentation, as well as the repeated material (deal summary, cap table, etc.) is performed by your staff.

8. Present the bad news without spin, and confidently. You may not be used to bad news, but your investors are. They will greatly appreciate frankness and straightforward description of the bumps in the road, and any spin only reduces their confidence in you.