FENIMORE
KAY
HARRISON
FORD

Kevin Strachan
(770) 282-5117
kstrachan@fkhpartners.com

THE EARNINGS RELEASE ADVANTAGE FOR PRIVATE BANKS

A familiar ritual commences every quarter.

Blue-chip companies publicly announce their earnings results for the quarter that ended two or three weeks earlier. Their executives hold conference calls where analysts that cover the stock ask probing questions about the results. The Wall Street Journal has a week of fodder for its front page as financial journalists glean trends from the noise.

This quarterly undertaking may seem far-removed from most community banks, even for those that are public and issue quarterly earnings releases. However, **the underlying accountability that comes from communicating your results in a narrative — and even interactive — manner to your shareholders on a quarterly basis is something more banks should consider.**

There is no requirement from the U.S. Securities and Exchange Commission that companies issue quarterly earnings releases. This is true for both private and publicly traded banks. Investor expectations, rather than any legal requirement, have made the quarterly earnings release almost mandatory because of the value it provides through regular communication to investors and other stakeholders.

The reasons why executives at public banks find value in earnings releases are also applicable to private banks. Many, if not most, private banks communicate with shareholders only once per year: when the annual report is issued (although dividend checks can be their own form of communication). **Increasing this frequency through quarterly earnings releases gives executives an opportunity to better manage expectations.** Management advising shareholders in April that they expect soft earnings due to interest rate trends could cushion the blow of an annual report that reflects several months of a previously unreported negative development. A bank's commitment to transparency in providing quarterly results could actually enhance its credibility among shareholders and potential future investors.

Reporting earnings may also have internal benefits for the bank. The exercise of preparing and reporting quarterly results enhances the focus of the board, executives and employees on the bottom line. It may also accelerate internal recognition of trends affecting those results.

These benefits apply to all privately held banks, regardless of their future plans. However, institutions expecting to conduct an initial public offering, or IPO, in the short- to medium-term often find committing to quarterly reporting early to be most beneficial. Once a bank begins the IPO process, SEC rules allow it to continue existing shareholder communications practices. **A community bank with an established practice of releasing quarterly results has an advantage in what it is permitted to release**, versus a bank with no such history. Implementing a quarterly earnings disclosure process also prepares all employees involved in areas such as financial reporting and investor relations for the new responsibilities and processes following an IPO. Without such preparation, those requirements and expectations can constitute a painful learning curve for the unprepared.

Transparency may also address an often overlooked, but significant, risk faced by private banks: ownership succession. Private banks should assume that a large block of shares will eventually need to be sold by existing shareholders or their heirs to satisfy liquidity needs. By publishing insightful earnings releases, private banks not only "speak" to existing shareholders, they establish a narrative that may be useful for future buyers of their stock. They may be able to facilitate future sales of

existing securities in a manner that avoids selling the institution.

But commencing quarterly reporting should be considered an almost-irreversible decision: starting creates shareholder expectations, and stopping is likely to incur harm that exceeds the benefit of starting in the first place. Although you may send earnings reports to shareholders, rather than posting them publicly as an SEC-reporting company would, information once released may be spread more widely — to the local or financial press or on social media. **Executives should also consider the availability of institutional resources, and consider how constrained these resources could become in the future.**

The decision to report earnings, along with its costs and benefits, should be considered in conjunction with the bank's long-term strategy. Banks considering going public or looking for ways to increase shareholder engagement may realize the biggest benefits. For management teams that are skeptical of their shareholders' desires for additional reporting, or banks with scarce resources that could be more effectively utilized elsewhere, quarterly reporting may not pass the test. One way to help the board mull this decision is by preparing something akin to a quarterly earnings release for inclusion in the board package. Adding a written narrative to the standard set of financial statements prepared for the board can give a bank an idea of the effort involved. The board can also provide feedback from the board on the utility of such a report.