



PANEL ON ESEF

NICOLAS D'HAUTEFEUILLE & JEAN-BAPTISTE BELLON
ANALYSTS MEMBERS OF EFFAS

ESMA/ EU
Bruxelles 5 June 2018

EXECUTIVE SUMMARY:

CAN ESEF HELP TO TRANSFORM SCORING FROM AN ART INTO A SCIENCE?

DISCLAIMER: THIS PRESENTATION IS OUR PERSONAL OPINION

- (1) Financial analysis is not scoring:** limited scope for input cost reduction because the focus is on projections (ie making growth profitable)
- (2) ESEF & XBRL could become useful tools:** huge interest for using “big data” to improve benchmarking & scoring
- (3) But value of BIG DATA is driven by TAXONOMY:** AI and other cobot cannot make non standard adjustments
- (4) ESMA must enlarge “back testing” to the use of big data:** back testing will open the “black box” and improve feed back from users
- (5) Stronger input from users through a “financial lab”?** Europe must build more efficient methodologies to industrialize the scoring process

1. BIG DATA & COST REDUCTION?

Scoring is not the stronger focus for investment professionals (ie portfolio managers and analyst)

- **Added value focus more on reliability in projections based on they own financial models**
 - Estimated time spend to crunch data: between 5% and 10% of the typical work load
 - Work load more intense at inception of the coverage: due diligence on metrics is a first building block toward proprietary model
- **Big data usage based on historical metrics is key for passive asset management, quants and investment bankers**
 - Analyst employed for such purpose spend more than 2/3 of their time in number crunching
 - M&A modelling to brainstorm on “what if” scenarii)

XBRL and ESEF is a progress to outsource “maintenance work” for comparison purposes (BENCHMARKING)

- Some company (usually large one) already provides their accounts (primary statement and segments) in excel format which are easier to plug into financial model
- Competition between the major data providers should include their capacity to apply standard restatement in order to filter the information (avoid short term “noise”)

FINANCIAL ANALYSIS WILL REMAIN MORE AN ART (IE RATING IS NOT SCORING)

2. ESEF IS A TOOL BUT ITS VALUE IS LINKED TO THE QUALITY OF THE DATA

- **TODAY:** existing providers are not using consistent methodologies: reliability of benchmarking based on non adjusted metrics is uncertain
- **TOMORROW?** a global data base could provide a cheap, relevant and reliable source of data for working on investment themes and give ability to asset managers to define instantly key factor exposure: this is a attractive tool to select return drivers or to update risk sensitivity

ESMA, the FRC and the SEC should WORK TOGETHER to improve the ability to share big data

- The initial focus by ESMA on Primary Financial Statement for listed issuers based on IFRS taxonomy is a first step
- Digitalization does not require building a global platform but the need is to normalize **TAXONOMY** because big data based on non adjusted metrics will be detrimental for the value of European issuers and their access to the global markets

BIG DATA will improve stability in financial markets only when benchmarking between US and European listed companies will become more efficient & reliable

3. VALUE OF BIG DATA IS DRIVEN BY TAXONOMY

TODAY: usage of XBRL or iXBRL is mostly done in Europe for compulsory reporting

1. Computation of taxes or social charges (company individual account reporting as in UK or as the SBR system in the NL)
2. Prudential use in the European banking system (reporting to ECB Finrep and Corep)

In both cases, taxonomy is clearly determined by the responsible Authority: no need to adjust information

TOMORROW: digitalization of the scoring process for listed company is jeopardized by the fact that accounting standards are still a “black box”

- Divergence between IFRS and US GAAP: IFRS 16 as a business case
- IFRS is currently not prescriptive enough and generate many differences in format for P&L
not enough details in IAS 1 Balance Sheet (industry specific presentation) or CFS (option left on interest and tax in operating CF or not).

ESEF requires more convergence to be sure that accounting data can be used as facts: **SCORING MUST BECOME A SCIENCE TO OPEN THE BLACK BOX**

4. BACK TESTING TO MAKE SCORING “CLEAR AND SIMPLE”

The conceptual framework applied by IASB should be tailored on the metrics used by users (ie equity and credit analysis, regulator & management) to structure data and Primary Financial Statement :

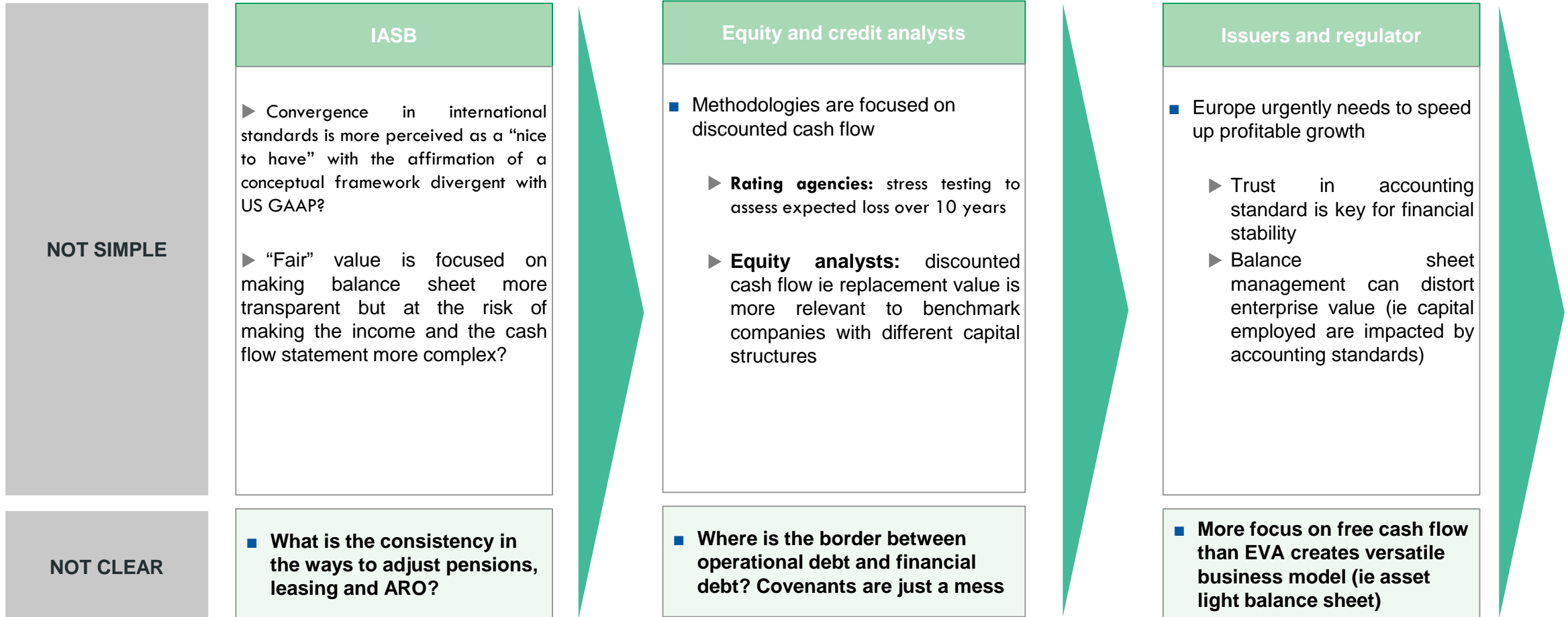
- 1. Inclusion of segment data:** understanding trend in marginal return for capital employed by business unit is the key issue to assess if growth is profitable
- 2. Ability to “clean” cash flow and to adjust debt:** key to make stress testing
- 3. Incorporation of parent company data** and main non consolidated affiliates: what are the costs to upstream cash flow to pay back debt and distribute dividends?
- 4. More convergent industry standard as a way to regulate non gaap?** Non Structured data and MD&A : PDF is fine for the time being, ESMA could envisage field test and impact study to judge the cost/benefits

Bigger use of BACK TESTING is urgently needed to make scoring “CLEAR AND SIMPLE”

5. A FINANCIAL LAB COULD ACT AS A THINK TANK TO IMPROVE CONCEPTUAL FRAMEWORK

- (1) ESMA sharing big data through easy and cheap one point of access (as Edgar) will be efficient if users switch to more sophisticated financial models which could be shared as “templates” to industrialize scoring
- (2) The LAB could work with association of users to improve taxonomy holding & monitoring (urgent need to improve accounting standards)
- (3) The LAB could act as a “go between” with academics on the definition of key metrics to score financial performance from the accounts (EBITdA(R), FCF, Net Financial debt, etc)
- (4) The promoters of iXBRL and XBRL should make the POC that ESEF will work on investment processes
- (5) Impact study before moving to second step, after primary Financial Statements

IFRS 16 AS A BUSINESS CASE



▶ The conceptual framework must be global and improve the ability to fund more efficiently profitable growth in Europe