

THE USE OF ALTERNATIVE PERFORMANCE MEASURES IN FINANCIAL INFORMATION

PRACTICE OF EUROPEAN LISTED COMPANIES AS AT 31 DECEMBER 2016

EFRAG User Panel/TEG joint meeting – Brussels, 16 March 2019

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BACKGROUND

CONTEXT OF DISCUSSION ON APMS

**ESMA
Guidelines
effective
July 3, 2016
+
17 Q&As**

**IASB research project
on Primary Financial
Statements**

- Promote usefulness and transparency of APMS. Prospectuses, financial reports and market disclosures in scope
- Principles addressing the labelling, calculation, presentation and comparability
 - **Keywords: disclosure, presentation, reconciliation, explanation of use, prominence, comparatives and consistency over time**
- Compliance monitoring by National regulators under Transparency, Prospectus or Market Abuse Directives
- Inconsistencies observed in practice for the statement of profit or loss
- **Examining possible changes to primary financial statements, such as including a defined subtotal for operating profit + another management measure**
- Presenting the results of 'integral' associates and joint ventures separately of 'non-integral' associates and joint ventures
- Examining use & labelling of alternative performance measures (e.g. non-recurring)

IAS 1 REQUIREMENTS FOR ITEMS « ON THE FACE »

Additional items to be added on the face

- Relevant to understand financial position or the entity's financial performance
- Calculated and presented in an unbiased fashion

Presentation

- Subtotals include IFRS items, presented and labelled in a clear and understandable way, consistently presented from period to period

Prominence

- Not displayed with more prominence than subtotals and totals required by IFRS Standards

Operating profit

- 'Operating profit': misleading if items of an operating nature (e.g. business combination impacts, depreciation of assets or inventory write-downs) are excluded

Extraordinary items

- Do not present extraordinary items and use meaningful labels, e.g. items affecting more than one period rarely can be non-recurring such as most of the restructurings costs or impairment losses

Benchmarking analysis on current use of APMs in financial reporting

- Investigating commonalities at segment level
- IAS 1 and ESMA requirements as reference points
- Categorising APMs into “presented on the face”/”direct”/”indirect”, based on the degree of reconcilability with GAAP measures

Financial information analysed

YE16 Financial reports



Press releases

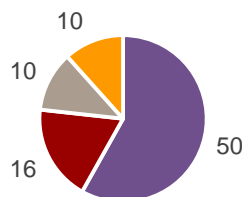


Investor presentations



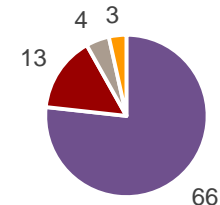
Scope of listed entities analysed

4 samples



- EUROSTOXX 50 (initial benchmark sample)
- UK (STOXX Europe 50)
- STOXX Europe Mid 200
- STOXX Europe Small 200

4 segments



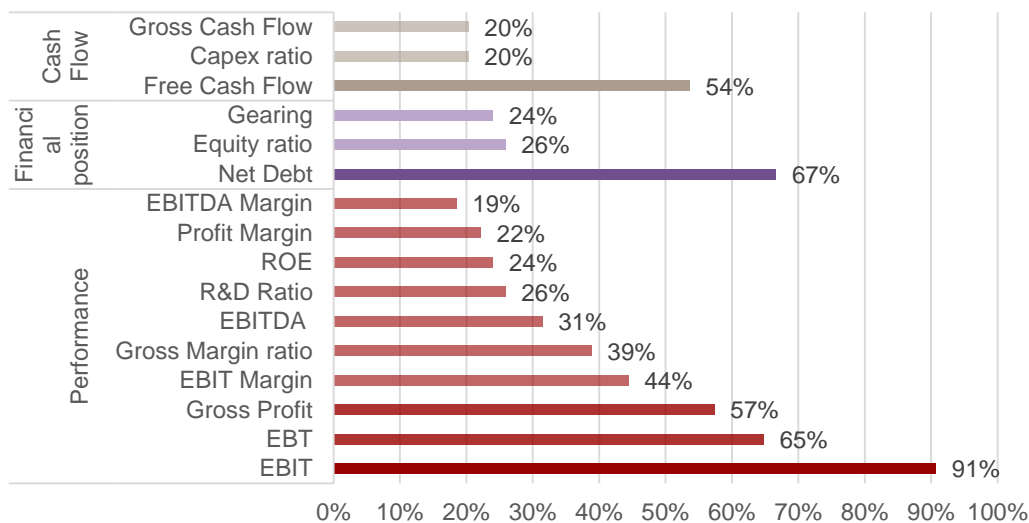
- Industrial
- Banking
- Insurance
- Real Estate



**LIST OF APMs
COMMONLY
USED BY
SEGMENT AND
THEIR
PRESENTATION**

INDUSTRIAL SEGMENT (1/2)

Most frequently used direct APMs
Large industrials

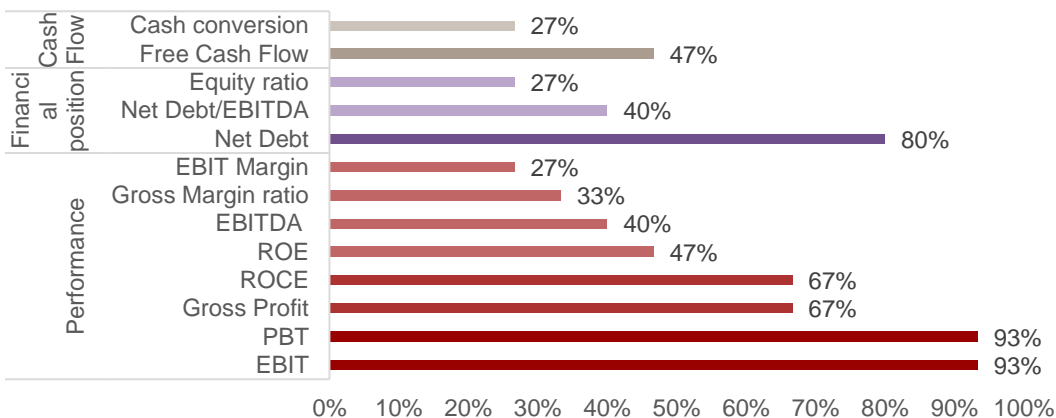


n=51

EUROSTOXX 50:
No significant changes observed vs. last year

Consistency not analysed for new samples

Most frequently used direct APMs
Small and Mid-Caps

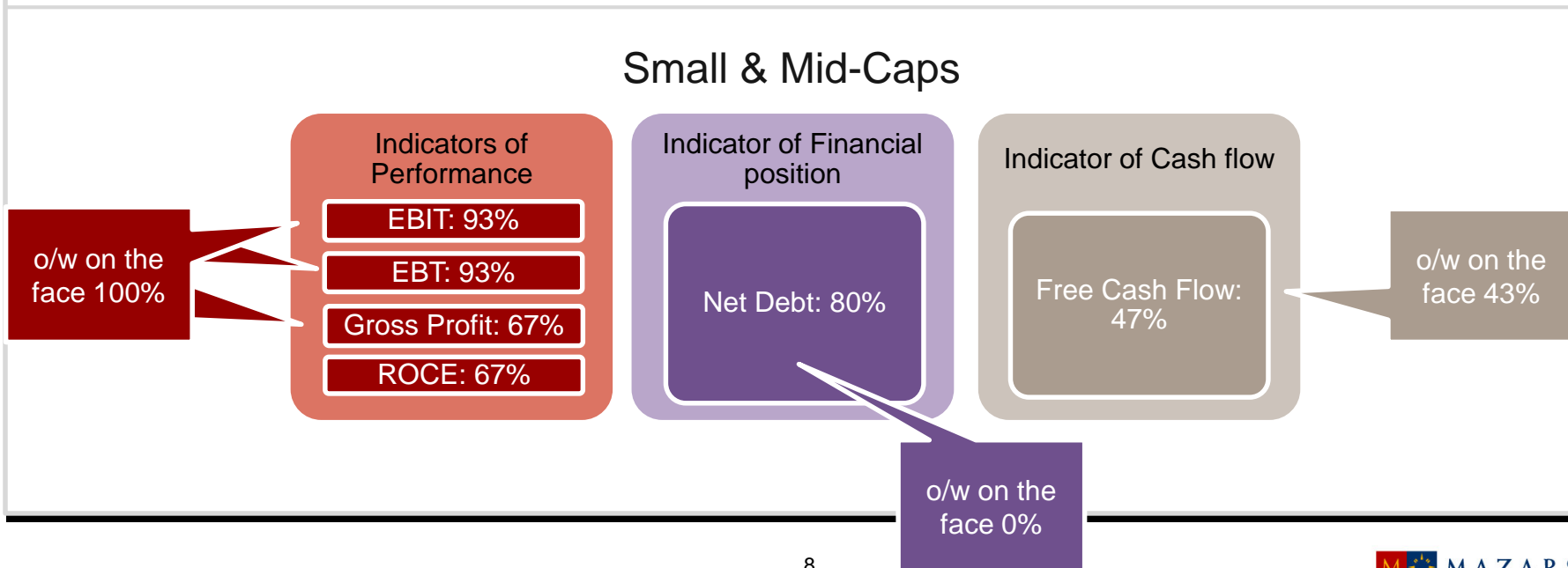
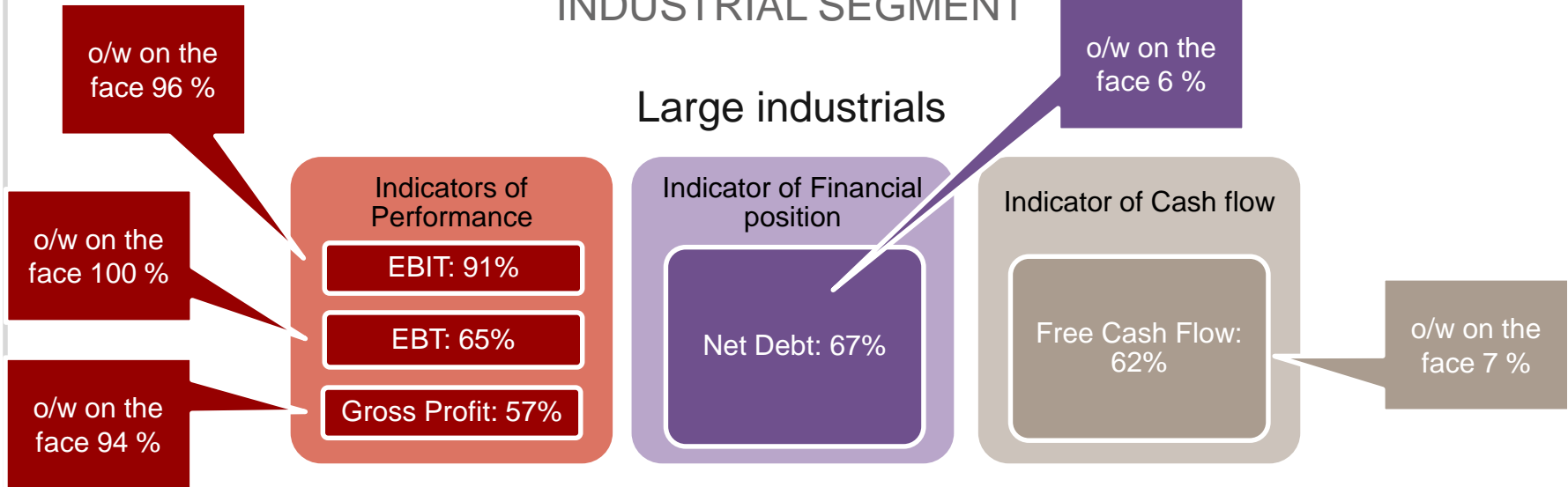


n=15

	Euro-stoxx 50	UK	Small & Mid-Caps
Average number of APMs	17.1	10.7	17.3
Range	7 – 37	7 – 15	8 – 19

INDUSTRIAL SEGMENT (2/2)

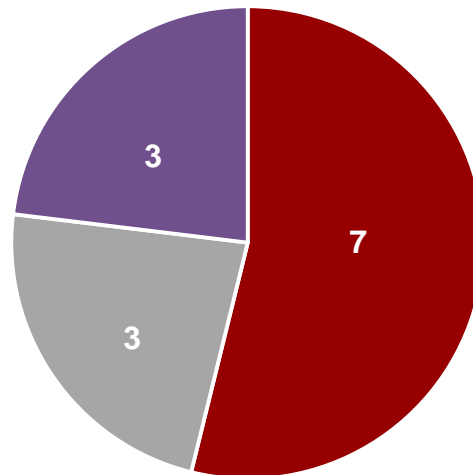
INDUSTRIAL SEGMENT





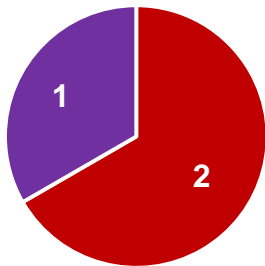
THE SAMPLE OF BANKS

Sample Composition



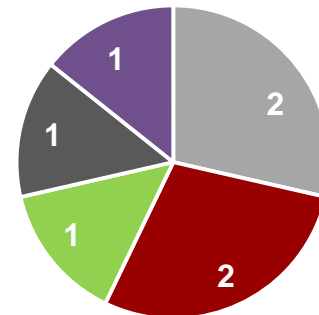
■ Eurostoxx 50 ■ Eurostoxx 200 ■ GB banks

Geographical Composition of Eurostoxx 200



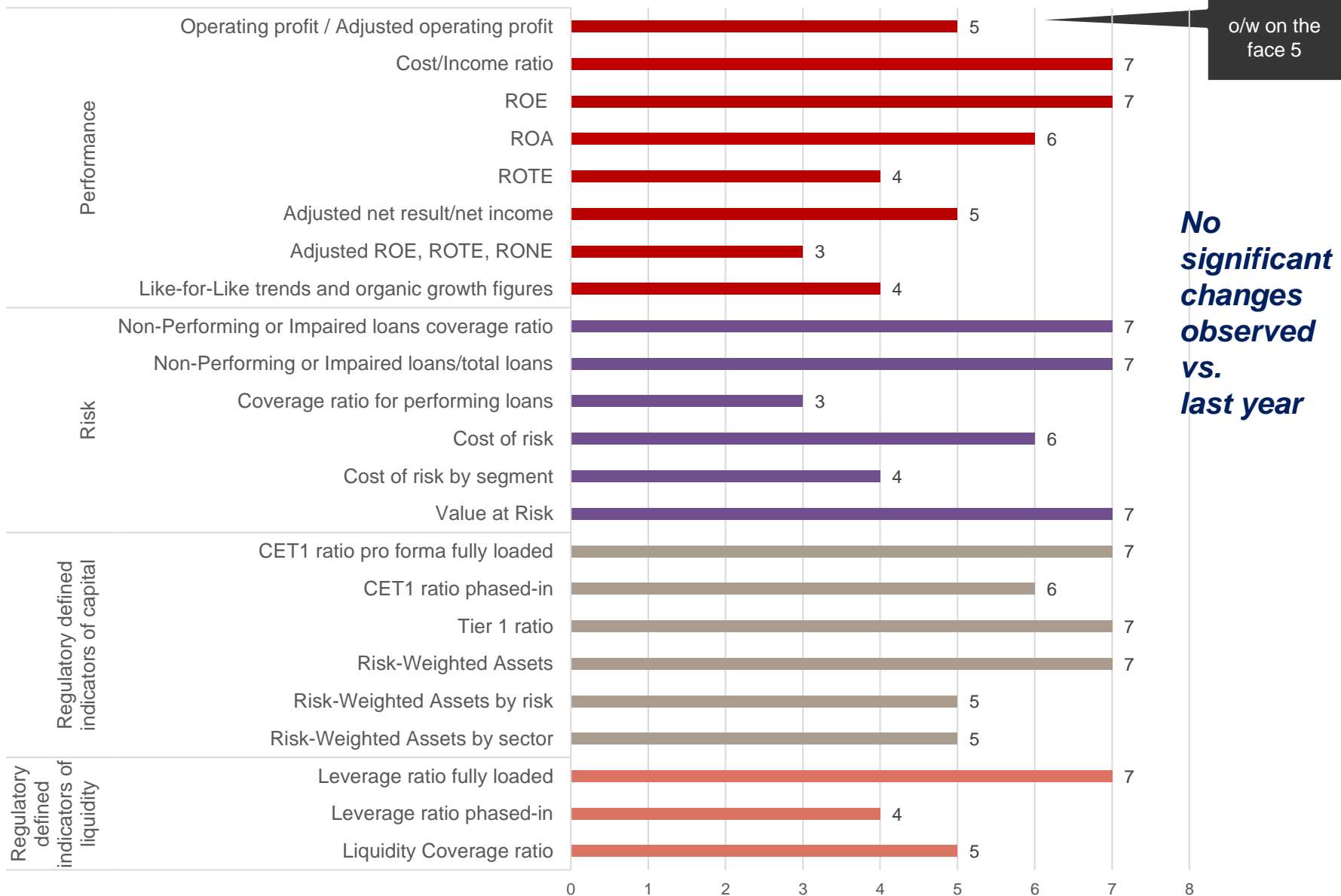
■ Spain ■ Czech Republic

Geographical Composition of Eurostoxx 50

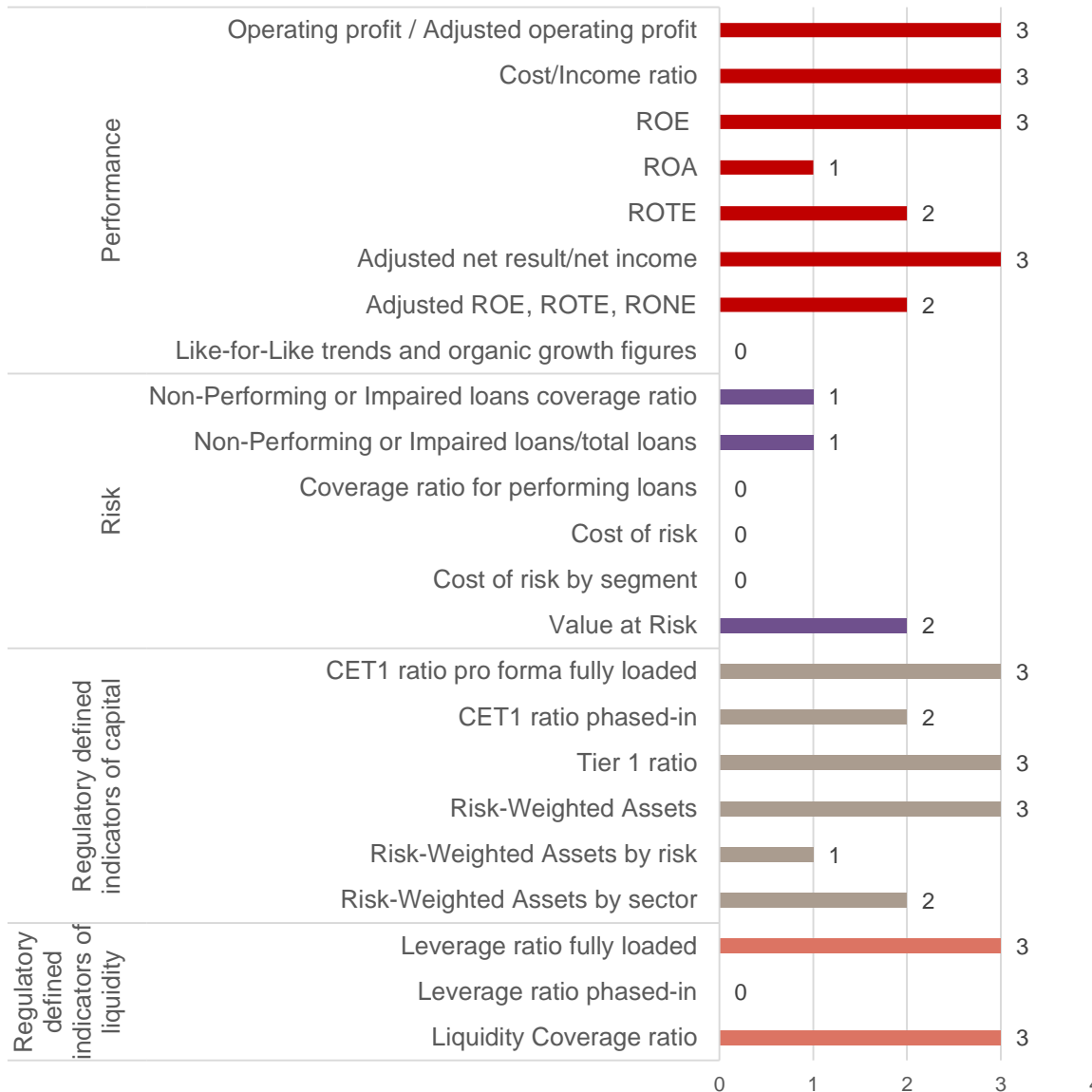


■ Spain ■ France ■ Italy ■ Germany ■ Netherlands

BANKING SEGMENT – EUROSTOXX 50



BANKING SEGMENT – UK BANKS



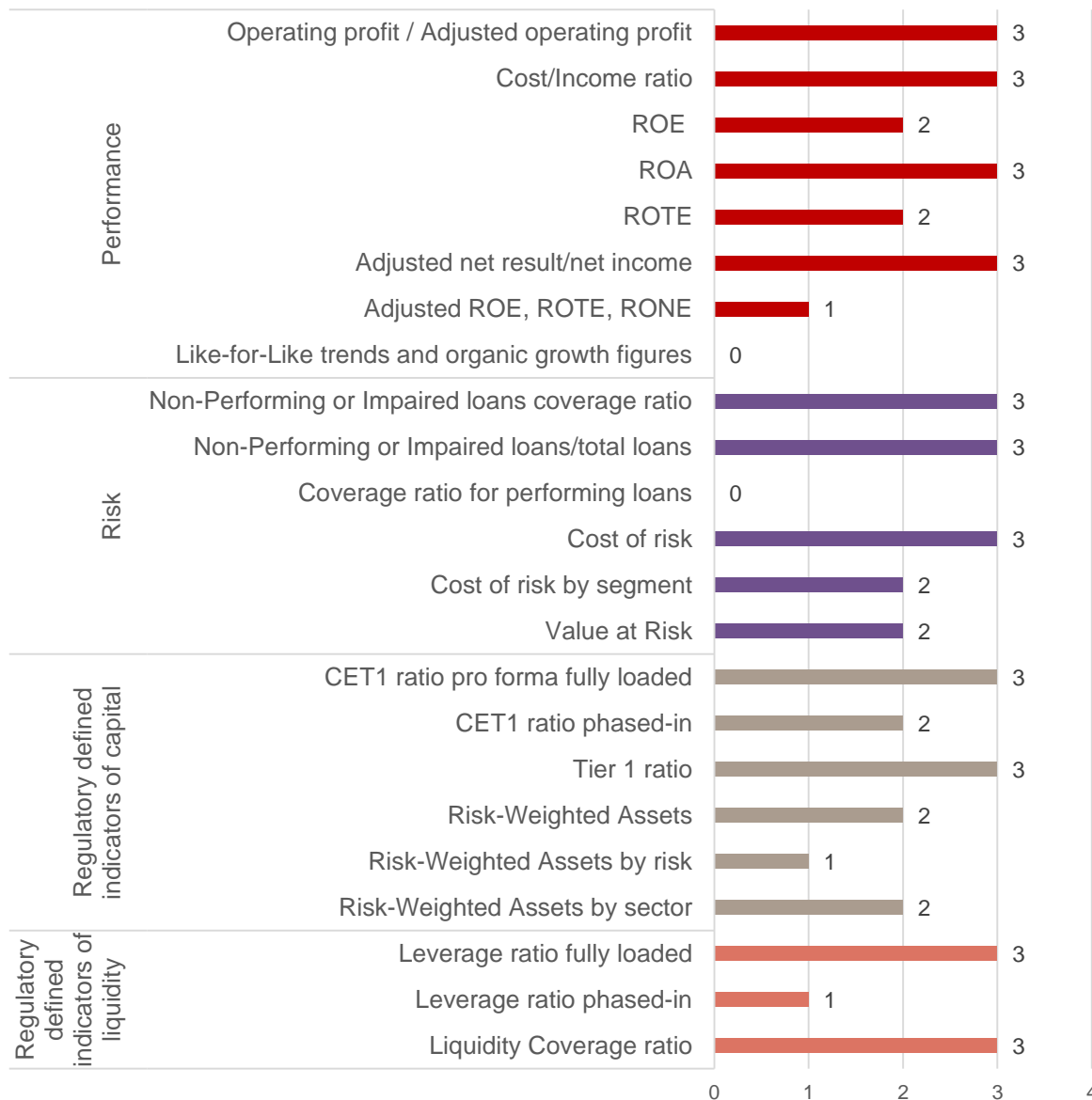
o/w on the face 3

The indicators used are substantially the same as for the EU big cap.

Less indicators of asset quality are used, probably reflecting the lower scale that the non performing issue has compared to other EU geographies.

Leverage-ratio «phased-in» not used in this sample.

BANKING SEGMENT – EUROSTOXX 200



o/w on the face 3

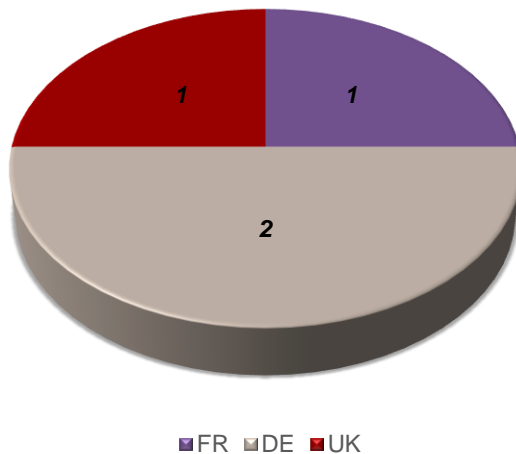
We do not observe a different approach to the use of APMs in the small/medium CAP compared to the big ones.

The indicators used are substantially the same as for the big cap.

The indicator of «like-for-like is missing, reflecting the more simple group structure of the small/medium cap.

THE SAMPLE OF INSURANCE ENTITIES

Our analysis covered the 3 insurance groups included in the EUROSTOXX 50 index plus a UK company. 1 entity operates life-only business, while the other 3 are active on both life and non-life.

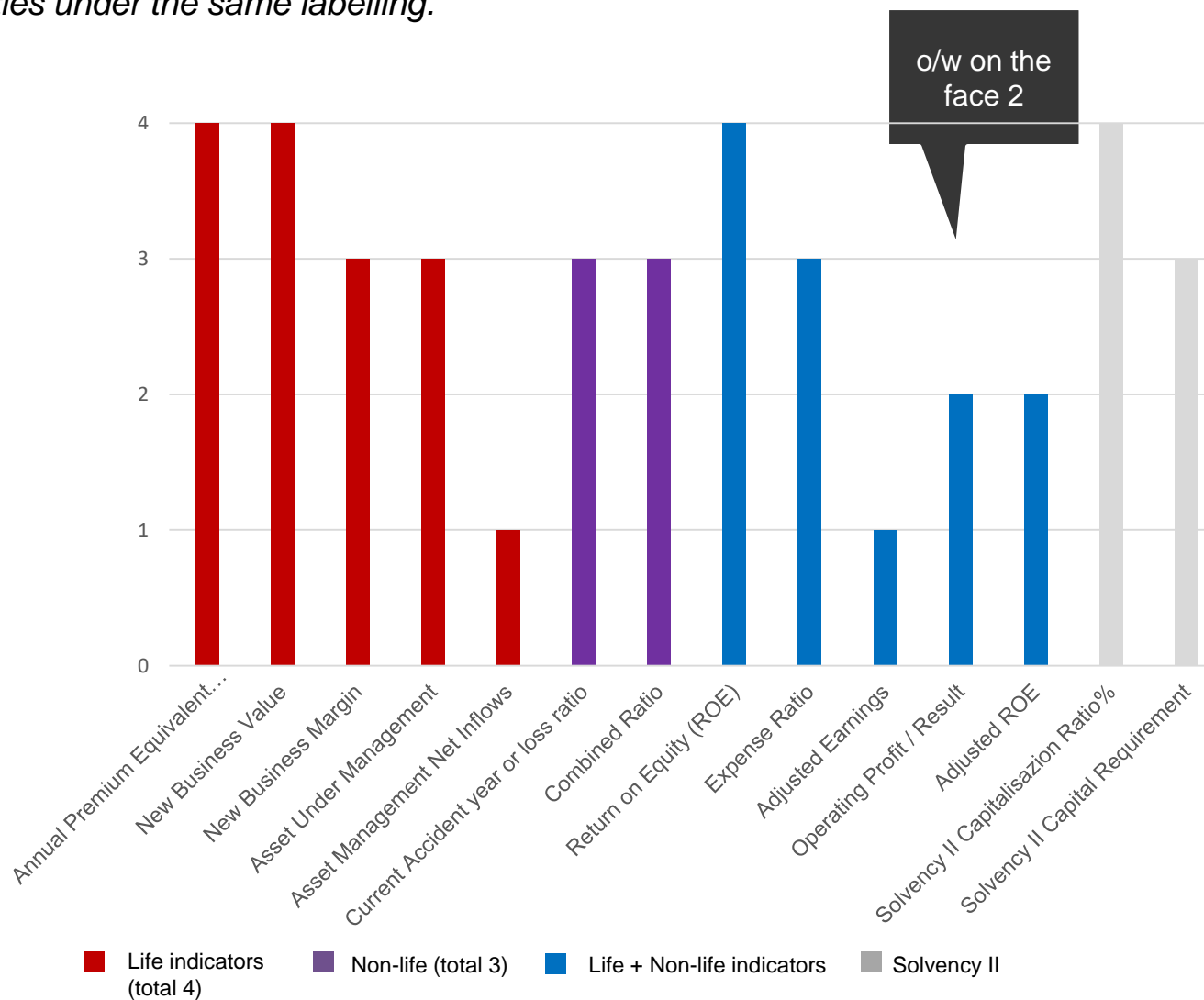


Sub-segment relevanceSSol	Indicator
Life only	Annual Premium Equivalent (APE) New Business Value New Business Margin Asset Under Management Asset Management Net Inflows
Non Life only	Current Accident year or loss ratio Combined Ratio
Both Life and Non Life	Return on Equity (ROE) Expense Ratio Adjusted Earnings Operating Result Adjusted ROE
Solvency II	Solvency II Capitalisation Ratio Solvency II SCR

Life and Non-life businesses represent two different segments that are monitored using different indicators.

INSURANCE SEGMENT

No significant changes observed vs. last year, except for Solvency II ratio, that is now disclosed by all the entities under the same labelling.

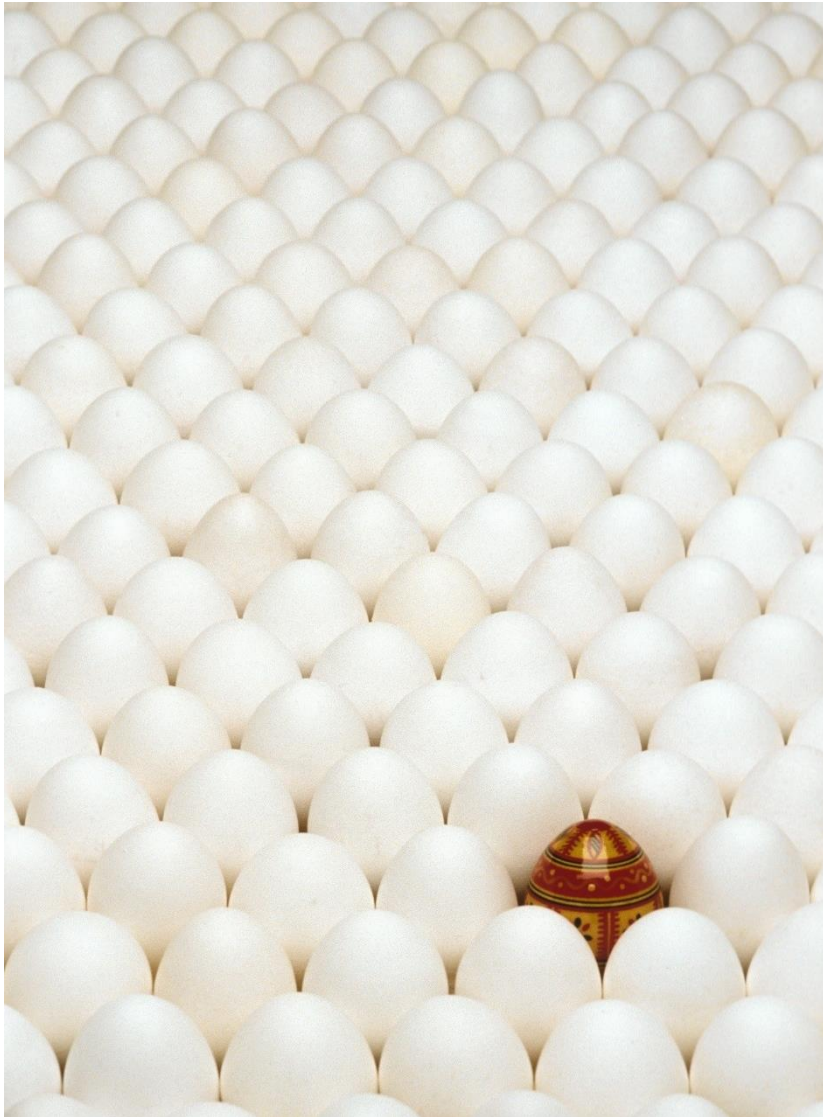


One insurance company presents 3 different indicators: "Net operating income", "Underlying earnings" and "Adjusted earnings", the first is presented on-the-face of primary statements and the second and third presented on a managerial detailed income statement.

CONSISTENTLY ACROSS SEGMENTS & SAMPLES: OCI ITEMS NEVER USED NOR COMMENTED

- None of the entities comment OCI in their management commentary, in the press release nor in the presentation to the analysts
- No APMs were presented with reference to components of OCI in the documents analysed

EUROSTOXX 50: No changes observed vs. last year

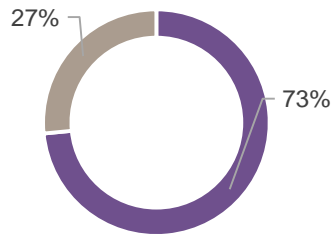


SELECTED FINDINGS ON KEY APMs

DIVERGENCES IN EBIT CALCULATION AND LABELLING - 1/5

LARGE INDUSTRIALS

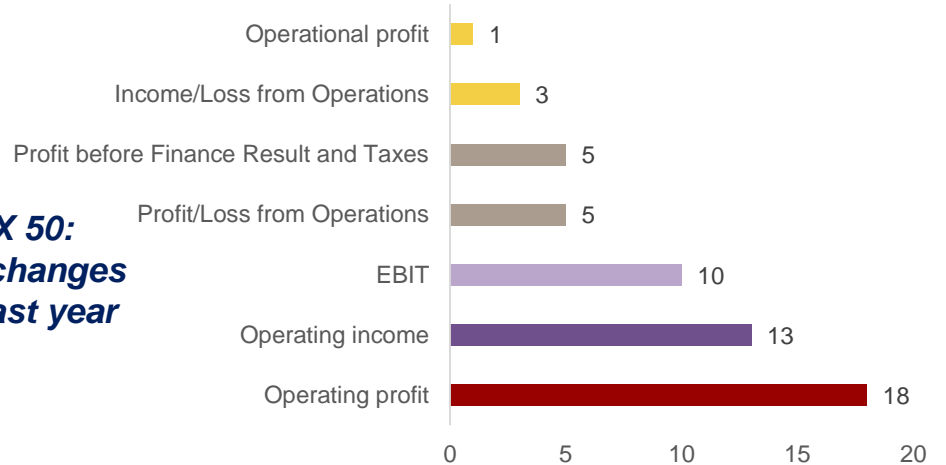
Calculations of EBIT Large industrials



EUROSTOXX 50:
No significant changes
observed vs. last year

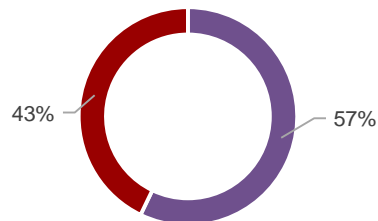
- EBIT excluding "Share of profit/loss of equity-accounted investments"
- EBIT including "Share of profit/loss of equity-accounted investments"

Labelling of EBIT Large industrials



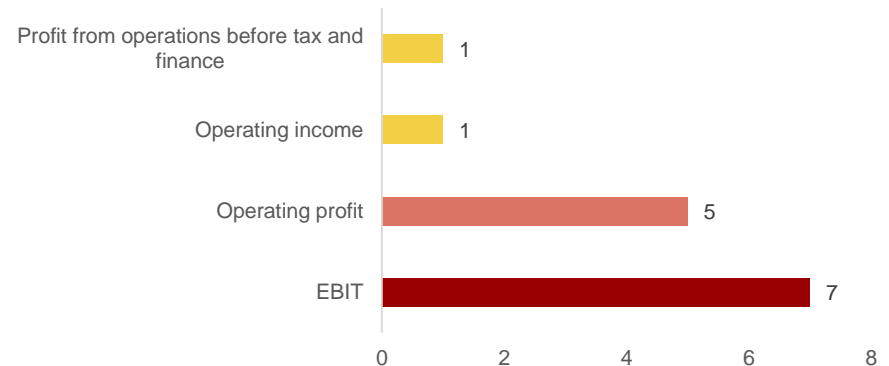
SMALL & MID – CAP INDUSTRIALS

Calculations of EBIT Small & Mid-Caps



- EBIT excluding "Share of profit/loss of equity-accounted investments"
- EBIT including "Share of profit/loss of equity-accounted investments"

Labelling of EBIT Small & Mid-Caps

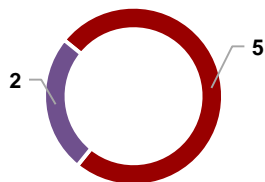


DIVERGENCES IN EBIT CALCULATION AND LABELLING - 2/5

No significant changes observed vs. last year

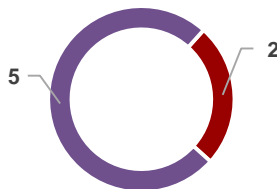
BANKING SEGMENT – EUROSTOXX 50

Share of profit or loss of investments accounted for using the equity method



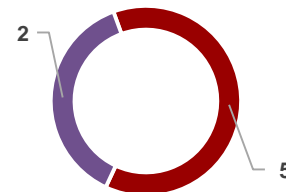
- Included in Operating Income
- Excluded from Operating Income

Loan loss provisions presentation



- Included in Operating Expenses
- Excluded from Operating Expenses

Integration/restructuring costs presentation



- Included in Operating Expenses
- Excluded from Operating Expenses

Impairment of financial available-for-sale assets presentation



- Included in Operating Income
- Included in Operating Expenses
- Excluded from both Gross Income and Operating Expenses

Impairment charges within Operating Expenses



Labelling of EBIT

Never identified as EBIT, but as operating income, operating margin or operating profit.

Same divergence in COST/INCOME ratio (used by all the banks)

DIVERGENCES IN EBIT CALCULATION AND LABELLING - 3/5

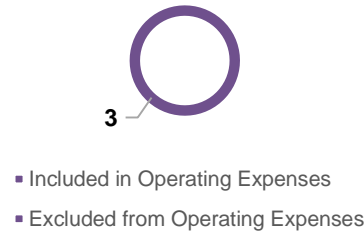
Higher level of comparability observed in items included in op. profit than the EU sample

BANKING SEGMENT – UK BANKS

Share of profit or loss of equity-accounted investments



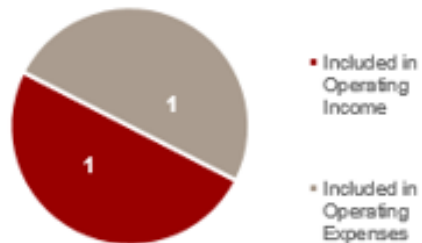
Loan loss provisions presentation



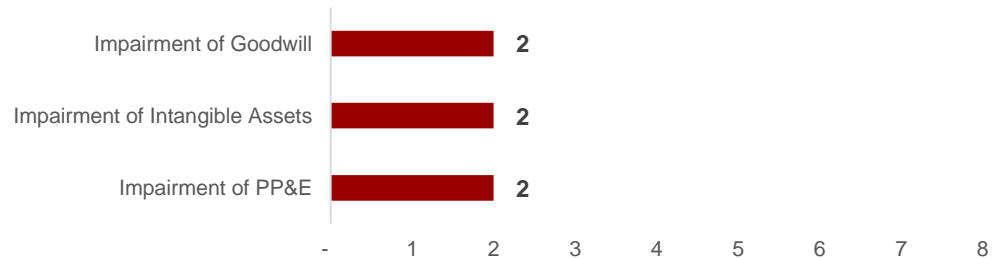
Integration / restructuring costs presentation



Impairment of financial available-for-sale assets presentation



Impairment charges with Operating Expenses



Labelling of EBIT

Never identified as EBIT, but as operating income, operating margin or operating profit.

Same divergence in COST/INCOME ratio (used by all the banks)

DIVERGENCES IN EBIT CALCULATION AND LABELLING - 4/5

The level of divergence in composition of the items and labelling observed for the big cap is applicable as well to the small/medium cap in the sample

BANKING SEGMENT – EUROSTOXX 200

Share of profit or loss of equity-accounted investments



- Included in Operating Income
- Excluded from Operating Income

Loan loss provisions presentation



- Included in Operating Expenses
- Excluded from Operating Expenses

Integration /restructuring costs presentation



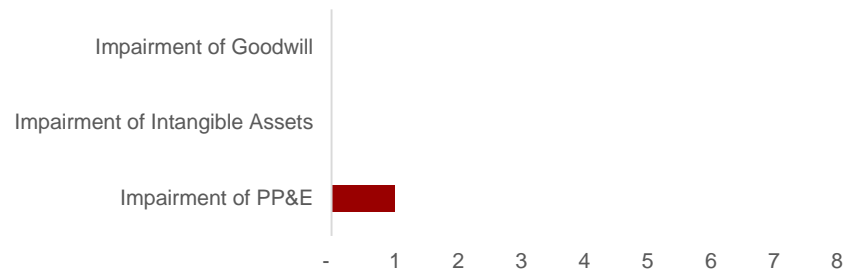
- Included in Operating Expenses
- Excluded from Operating Expenses

Impairment of financial available-for-sale assets presentation



- Included in Operating Income
- Included in Operating Expenses

Impairment charges with Operating Expenses



Labelling of EBIT

Never identified as EBIT, but as operating income, operating margin or operating profit.

Same divergence in COST/INCOME ratio (used by all the banks)

INSURANCE SEGMENT

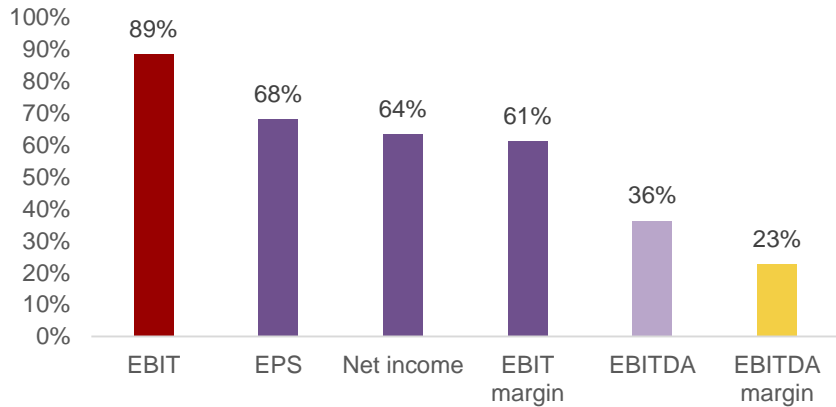
- 2 (out of 4) entities present operating profit on the face (labelled “operating result” and “net operating income”)
 - In particular, one of them presents Net operating income on the face of IFRS Primary Statement and in Managerial Income Statements. It uses also two other Indicators: Underlying earnings and Adjusted earnings, both of them on the face of Managerial Income Statements. The calculation of these elements includes:
 - UNDERLYING EARNINGS GROUP SHARE
 - Net realized capital gains or losses attributable to shareholders (+)
 - ADJUSTED EARNINGS GROUP SHARE
 - Profit or loss on financial assets (under fair value option) & derivatives (-)
 - Exceptional operations (including discontinued operations) (+)
 - Goodwill and other related intangible impacts (-)
 - Integration and restructuring costs (-)
 - NET INCOME GROUP SHARE
- 2 (out of 4) present operating profit in the notes
 - One of them has a specific definition of “EEV Operating profit”, that is: “EEV operating profit is provided as an additional measure of profitability. This measure includes EEV new business profit, the change in the value of Group’s long-term in-force business, and profit from our asset management and other businesses. As with IFRS, EEV operating profit reflects the underlying results based on longer-term investment returns.”

MANAGEMENT FOCUSES ON ADJUSTED EARNINGS, NET OF SPECIAL/ONE-OFF TRANSACTIONS - 1/4

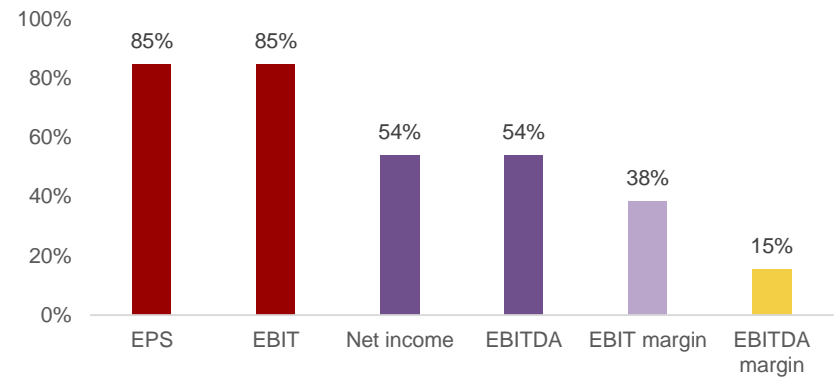
EUROSTOXX 50: No significant changes observed vs. last year

INDUSTRIAL SEGMENT

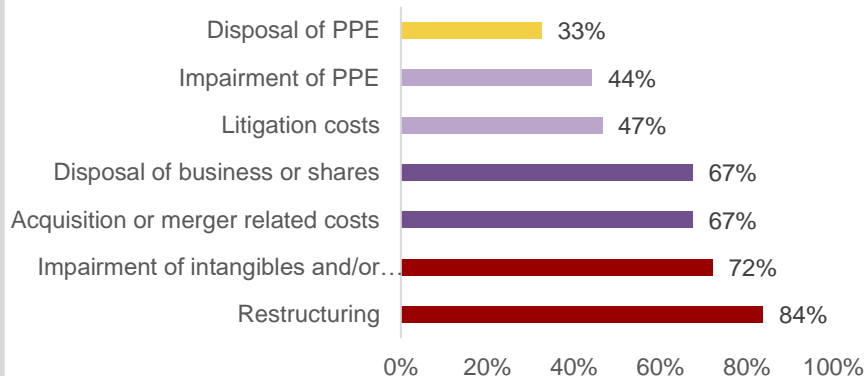
Commonly adjusted indicators of performance Large industrials



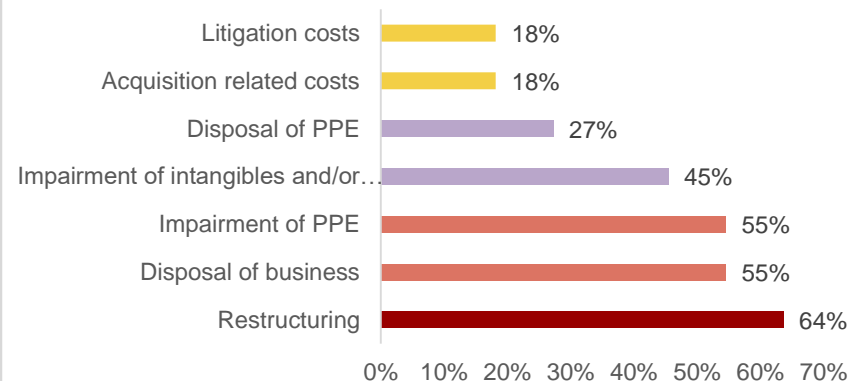
Commonly adjusted indicators of performance Small & Mid-Caps



Common reconciling items Large industrials



Common reconciling items Small & Mid-Caps



MANAGEMENT FOCUSES ON ADJUSTED EARNINGS, NET OF SPECIAL/ONE-OFF TRANSACTIONS - 2/4

INDUSTRIAL SEGMENT

Large industrials

- 39 entities out of 51 use an adjusted EBIT
 - With 15 on the face of the income statement (10 different labels)
 - 10 French, 3 UK
 - 80% of the adjustments result in positive effect
- 2 entities changed from negative to positive
- 4 French companies use the “recurring operating income label” (of which 3 follow ANC recommendation)

Small & Mid-Caps

- 11 entities out of 15 use an adjusted EBIT
 - With 4 on the face of the income statement (4 different labels)
 - 2 Danish, 1 UK, 1 Spain
 - 75% of the adjustments result in positive effect
- 1 entity changed from negative to positive

MANAGEMENT FOCUSES ON ADJUSTED EARNINGS, NET OF SPECIAL/ONE-OFF TRANSACTIONS - 3/4

No significant changes observed vs. last year

BANKING SEGMENT – EUROSTOXX 50

- 5 entities out of 7 use adjusted net result in press releases and/or presentations
 - of which 2 present also it in management commentaries and 1 on the face (“underlying result”)
- Adjustments to IFRS net result
 - disposal of an investment (5);
 - non-recurring/extraordinary items (5);
 - CVA/DVA and own credit risk (3);
 - provisions for “PEL/CEL” (2 French banks).

INSURANCE SEGMENT

- 1 out of 3 uses **Adjusted earnings**, excluding P&L on Fair Value and derivatives, exceptional operations and goodwill and other related intangibles
- 1 of the entities uses “IFRS operating result” as one of the key APMs and the nature of this indicator is equivalent to an adjusted indicator (not labelled as adjusted)

MANAGEMENT FOCUSES ON ADJUSTED EARNINGS, NET OF SPECIAL/ONE-OFF TRANSACTIONS - 4/4

The following table shows the approaches to presentation of this indicator that were observed in the 3 samples:

Frequency	Eurostoxx 50	UK Banks	Eurostoxx 200
On the face of condensed/managerial income statements and labelled “underlying” result	1	1	2
Press released and/or in the presentations to investors and in the management commentary	2	1	2
Press released and/or presentations to investors	5	3	3
Absent	3	0	0

The following table shows the items for which the reported result was adjusted respectively in the 3 samples:

Frequency	Eurostoxx 50	UK Banks	Eurostoxx 200
Results of the disposal of an investment	5	3	1
Non-recurring or extraordinary transactions or non-recurring provisions	5	3	1
“Non-economic items”, i.e. changes in own credit risk in fair value of derivatives (CVA/DVA) and financial liabilities accounted for at fair value	3	0	0
Provisions for “PEL/CEL”, a specific financial product prevailing in a given country	2	0	0
“Non-economic items” and write-downs	0	2	1
Restructuring costs	0	1	1
Contributions to single resolution fund	0	1	0

DIVERGENCES IN ROE CALCULATION - 1/2

No material changes observed from last year for Eurostoxx 50

Banks: same pattern observed for UK big cap, small/medium cap as for EU big

INDUSTRIAL SEGMENT

Large industrials

- Used by 13 entities out of 51
- 8 different formulas
 - Inclusion and exclusion of minorities from either numerator or denominator or both
 - average vs. year-end equity
- 6 different labels for the same performance indicator

Small and Mid-Caps

- Used by 6 entities out of 15 companies
- 4 different formulas
 - Adjustment for bank activity
 - Calculation on portion attributable to shareholders
- 1 label

BANKING SEGMENT

- Used by all 7 entities belonging to EUROSTOXX 50, by 2 (out of 3) entities belonging to EUROSTOXX 200 and by all 3 UK banks
- 3 different formulas
 - Inclusion and exclusion of minorities from either numerator or denominator or both
 - differences exist in the components of equity that are taken into account in the denominator
 - unclear in one case how negative reserves were considered

DIVERGENCES IN ROE CALCULATION - 2/2

No material changes observed from last year for Eurostoxx 50

INSURANCE SEGMENT

- Used by 3 entities out of 4
- The 4th entity uses Return on Embedded Value
- 3 different formulas
 - 1) The calculation of Return on Equity (“RoE”) is based on following principles:
 - for net income RoE: calculation is based on consolidated financial statements, i.e. shareholders’ equity including undated subordinated debt (“Super Subordinated Debts” TSS/“Undated Subordinated Debts” TSDI) and Other Comprehensive Income “OCI”, and net income not reflecting any interest charges on TSS/TSDI;
 - for adjusted and underlying RoE:
 - all undated subordinated debts (TSS/TSDI) are treated as financing debt, thus excluded from shareholders’ equity,
 - interest charges on TSS/TSDI are deducted from earnings,
 - OCI is excluded from the average shareholders’ equity.
 - 2) The RoE is calculated on the basis of the consolidated result, including the result attributable to non-controlling interests. To calculate the average equity for the year under review, we use the figures as at 31 December 2015 (€31.0bn), 31 March 2016 (€31.8bn), 30 June 2016 (€32.0bn), 30 September 2016 (€32.4bn) and 31 December 2016 (€31.8bn) as a basis.
 - 3) Represents the ratio of net income to the average total equity, excluding unrealized gains/losses on bonds, net of shadow accounting, at the beginning of the year and at the end of the year.

SEGMENT SPECIFIC APMs: BANKING

The table below shows the frequency of use of the two main asset quality KPIs:

Frequency	Eurostoxx 50	UK	Eurostoxx 200
Coverage ratio	All the entities	All the entities	All the entities
Ratio of problem loans (problem loans over total loans)	All the entities	All the entities	All the entities

Divergences exist in the labelling and scoping of the problem loans, as shown in the table below:

Eurostoxx 50	UK	Eurostoxx 200
<ul style="list-style-type: none"> 4 entities refer to Non Performing Loans (“NPL”): 1 Italian bank states definition is consistent with EBA’s standards and 3 banks do not clarify if reference is made to EBA’s standards; 2 French entities refer to “Doubtful Loans” and not to NPL. 	<ul style="list-style-type: none"> 1 entity refers to impaired allowances as a % of loans impaired; 1 entity refers to loan impaired charges (LICs); 1 entity refers to impaired loans as a % closing advances, provisions as a % of impaired loans and provisions as a % of impaired excluding run-off. 	<ul style="list-style-type: none"> All 3 entities refer to NPL: 1 includes also another indicator (NPA Coverage ratio); 1 reports the NPL ratio within the presentation to investors but not in the management commentary.

SEGMENT SPECIFIC APMs: INSURANCE

No significant changes observed vs. last year

INSURANCE SEGMENT

- All entities make extensive use of APMs not presented on the face of the financial statements
- APMs used mainly non-reconcilable by nature with GAAP measures, except for operating profit, adjusted earnings and ROE



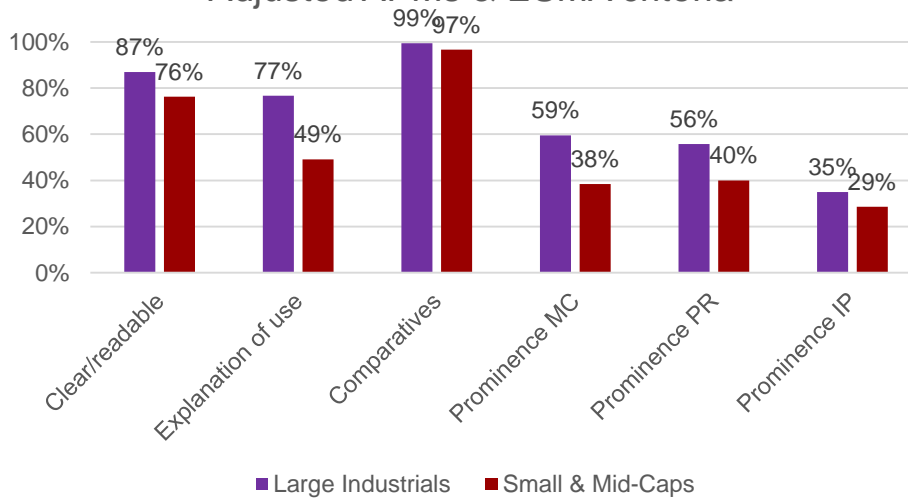
QUALITATIVE CHARACTERISTICS OF FINANCIAL INFORMATION PRODUCED USING APMS

APMS WELL EXPLAINED BUT HAVE MORE PROMINENCE THAN IFRS ITEMS

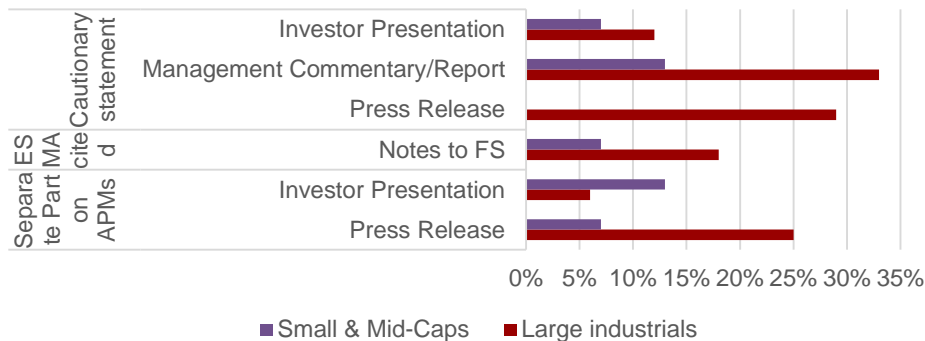
EUROSTOXX 50: No significant changes observed vs. last year

INDUSTRIAL SEGMENT

Adjusted APMs & ESMA criteria



General information - Industrials segment



BANKING SEGMENT

- Definitions presented, disclosure satisfactory
 - Many APMs are regulatory defined
- Prominence: Management commentary
 - APM and most reconcilable IFRS item stated together
- Prominence: Press release and presentation to analysts
 - Indicators affected by managerial adjustments presented with equal and in some cases more prominence than the IFRS equivalent measures

Double number of entities in the Eurostoxx 50 that have a separate section on APM compared to last year (14 vs. 7 in industrial segment and 4 vs. 2 in banking)

BANKING SEGMENT

- Comparatives for key APMs always presented
- 4 out of 7 banks belonging to Eurostoxx 50 have a separate section on APMs, remaining 3 have an Appendix/Glossary
- 1 out of 3 banks belonging to Eurostoxx 200 has separate section on APMs, remaining 2 have an Appendix/Glossary
- 2 out of 3 GB banks have a separate section on APMs, remaining 1 has an Appendix/Glossary

INSURANCE SEGMENT

- Comparatives for key APMs always presented
- 1 entity introduced a separate report on the IR website in 2016 with definitions and reconciliations of APM used
- 1 entity introduced a separate section in 2016 Annual Report on APM used
- 1 entity does not declare any change
- 1 entity declares that specific amendments to the disclosures have been done following ESMA guidance



Q&A

Links:

<https://www.mazars.com/Home/News/Latest-News3/The-use-of-APM-in-financial-information>

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