The Higher Cost of Less Information

Allowing companies to report earnings every six months could make markets more volatile and raise the cost of capital for business

BY JUSTIN LAHART

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When he tweeted about reducing how often companies report earnings, President Trump said that business leaders had told him it was a good idea. Investors—the people who own the companies that the executives lead —probably don’t agree.

Donald J. Trump
@realDonaldTrump

In speaking with some of the world’s top business leaders I asked what it is that would make business (jobs) even better in the U.S. “Stop quarterly reporting
& go to a six month system,” said one. That would allow
greater flexibility & save money. I have asked the SEC
to study! 7:30 AM - Aug 17, 2018

The SEC has required companies to report quarterly results since 1970, and over the years the
fuss around each quarter’s numbers has devolved into something of a circus. Instead of focusing
on the numbers, many investors play a guessing game of whether companies performed better
than expected and they analyze every utterance of executives on the ritual conference calls.

The criticism of giving quarterly earnings reports is that they contribute to a myopic focus on the
short-term results that is detrimental to companies’ long-term success. Indeed, a recent
paper [link] in The Accounting Review found that when companies reported more frequently
they invested less in their businesses.

Executives might want to say as little as possible but investors want to know as much as possible
about the companies they own. Longer lags between financial reports would make investors view
stocks as riskier, since a lot more can happen in six months than in three months. Stocks would
eventually reach the same place, it would just take longer and the short-term moves would be
bigger. This ought to lead, all else equal, to stock prices a little lower, and companies’ cost of
capital a little higher.

A 2011 paper in the Journal of Accounting and Economics examining the period from the early
1950s, when companies were only required to file annual reports, to the 1970s, when they were
required to report quarterly, found that companies cost of capital was lower when they reported
more frequently.

A six-month lag between reports could also make for a less level playing field among investors.
Some, like corporate insiders or investors who had access to specialized information like credit-
card data, would have longer periods where they had insights into company operations that
others didn’t.

Another problem is that less frequent reports would make financial chicanery harder for
investors, and regulators, to spot, says Howard Schilit, founder of accounting-analysis firm
Schilit Forensics.

Mr. Schilit isn’t surprised chief executives would be in favor of reporting results less
frequently—“Of course the companies want to do what they want to do and have fewer
restrictions,” he says. “What should matter is what’s good for the investors.”

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