The annual letter to shareholders is the ideal opportunity for a CEO to demonstrate his or her leadership skills to investors and analysts. ‘After reading a good letter to shareholders, you will feel like you just had a meeting with the CEO,’ says Laura Rittenhouse, president of New York-based andBeyond Communications and an expert at penning and editing chiefs’ letters.

Three of the best...

A strong letter is clear, engaging, informative and candid. Wayne Leonard, CEO of New Orleans-based Entergy, achieves this with a forthright letter that acknowledges the impact of hurricane Katrina on Entergy’s business and employees and sets a blueprint for what the company needs to achieve next.

Many CEOs talk up the value of their employees, but rarely do they sound as genuine as Leonard: ‘Our employees performed thousands of individual acts of courage and ingenuity that made our darkest moment truly our finest hour,’ he writes.

Beyond his sincerity, Leonard is upfront about Entergy’s 2005 numbers and sets out a clear recovery plan. In discussing federal and state funding, he points out that the money will be used to assist customers, not shareholders. He also lays out an easy-to-digest plan to restore Entergy’s ‘financial flexibility.’

Granted, it’s lengthy – weighing in at nine pages – but if you take the time to read Jeff Immelt’s 2005 letter, you learn a lot about GE. This letter achieves the ultimate goal of demonstrating leadership by giving a very thorough report on GE’s results and communicating Immelt’s outlook on its various businesses. Here Immelt talks about how GE’s strategy works to achieve the company’s growth objectives and lays out a series of expectations that provide the reader with a good understanding of GE’s businesses and prospects.

The theme of the letter – and the annual report – is ‘big’, and Immelt does a good job of revealing the handicaps as well as the benefits of GE being a large, complex corporation. ‘Size can insulate a company from failure until it is too late to change,’ he writes. What comes across here is a hands-on CEO who is realistic about the challenges and opportunities of his business.

Taking a page out of Warren Buffett’s book, 2005’s message from Sears chairman Edward Lampert addresses controversial financial issues head-on. Following a discussion of the merger integration with Kmart, Lampert launches into why he believes same-store sales are not the best metric to measure a retailer’s financial performance. He then tackles the contentious issues of share repurchases and pension liability. ‘While most observers focus on repurchases as a way to return cash to shareholders or to offset the dilution from options, [they have] other consequences as well,’ he writes.

This letter demonstrates respect for its readers by outlining issues that are relevant to the company in an efficient and frank manner. Lampert is able to talk specifically about Sears’ business and uses the letter to raise topics that many companies purposely avoid.
Adrienne Baker looks at a sample of the best and worst letters to shareholders from 2005 annual reports

‘It is my view that the shareholder letter is read because it is a window on leadership and a reflection on the culture and how the leader intends to nurture that culture,’ she adds. It’s critical that this letter not become a lost opportunity for companies. In preparation for the 2006 letter, here are some examples of well-executed – and poorly written – letters from 2005.

...and three of the worst

The writing style of Richard Parsons’ 2005 letter to shareholders is very generic, with broad statements that could easily apply to any business. ‘With a workforce drawn from all walks of life, we have the expertise and insights to create a broad array of products and services for more culturally diverse marketplaces,’ he writes.

Since 2001, the number of words used in Time Warner’s annual letter has increased by 50 percent, notes Rittenhouse. This is not necessarily a bad thing if the words have meaning and insight, but Parsons’ words don’t resonate or engage the reader. ‘We are also building businesses to reach growing consumer groups,’ he writes. ‘In 2005, for example, Turner Broadcasting’s Adult Swim began its first year as a stand-alone network, and it achieved higher ratings among young adult viewers than any of the major broadcast networks.’

Most readers are unlikely to understand what ‘Adult Swim’ is, and what exactly does Parsons mean by a ‘growing consumer group’?

In 2005, Boeing CEO Harry Stonecipher resigned after just over a year in the position when his relationship with a female executive came to light. Current CEO Jim McNerney stepped in to revive the beleaguered aerospace giant, but he doesn’t use his first letter to tackle the company’s culture problems effectively. This could be an opportunity to revive the reader’s confidence in Boeing’s leadership but, as with Time Warner, Boeing’s message to shareholders is full of platitudes with little meat to back them up. ‘We can “play bigger” as a team and make the whole add up to more than the sum of the parts,’ writes McNerney.

There is lots of discussion throughout about what the new CEO would like to do with the company, but very little focus on what needs to be fixed. This is a classic example of a letter that tells but fails to show.

Written in a conversational, Q&A style, Cigna CEO and chairman Edward Hanway’s letter to shareholders fails to instill trust in the reader. Hanway kicks off by claiming the company has had a very good year in 2005, but total revenues at the Philadelphia-based benefits provider are down for the first time in five years. The earnings per share figure is also down. A letter that glosses over the facts will immediately put off analysts and investors who are familiar with the company.

Hyperbole rather than clarity characterizes Hanway’s responses throughout the letter. ‘We believe that the shift to consumerism will require benefits providers to take a more active and holistic approach to health care,’ he writes, in answer to a question about the effect of consumerism on healthcare. Both the question and the response do little to enlighten the reader on the trends driving changes in this industry.