

The Most Candid CEO

Selena Maranjian

July 2, 2009

You know that when [looking for companies for your portfolio](#), you should consider some key qualitative factors, such as competitive advantages and the [quality of management](#). Unfortunately, it can be hard to determine management's quality. But one place you can learn about character is by reading CEOs' letters to shareholders.

One analyst, Laura Rittenhouse, actually uses these letters to prepare an annual survey of CEO candor. The 2008 results were recently released, and this year's top three CEOs were Christopher Connor of **Sherwin-Williams** (NYSE: [SHW](#)), Wayne Leonard of **Entergy**, and **3M's** (NYSE: [MMM](#)) George Buckley. Meanwhile, among the least candid were **Citigroup** (NYSE: [C](#)) CEO Vikram Pandit, **Humana's** Michael McCallister, and Rex Tillerson of **ExxonMobil** (NYSE: [XOM](#)).

The how and why

What would put a CEO near the top or bottom of the list? Rittenhouse looks for things like jargon, cliches, spin, and other confusing language, which she refers to as "fog." Her measure of fog rose 12 percentage points in 2008, with 80% of letters having highly confusing statements, while only 16% of letters provided "meaningful near-term direction."

Candid CEOs give shareholders an honest review of company performance, even when things aren't going well. But candor among CEOs may also be an indicator of good prospects for future performance as well. For instance, compare how the top companies of the 2007 list did against the bottom-ranked ones:

Company	2007 Candor Rank	2008 Return	Percentage Points Better (or Worse) Than the S&P 500
Eaton	#1	(47%)	(8)
Entergy	#2	(28%)	11
Wells Fargo	#3	2%	40
Novartis (NYSE: NVS)	#4	(6%)	33
Target (NYSE: TGT)	#5	(30%)	8
News Corp.	#96	(54%)	(16)
Estee Lauder	#97	(28%)	11
Boeing (NYSE: BA)	#98	(49%)	(11)
ServiceMaster	#99	N/A*	N/A*
Humana	#100	(51%)	(12)

Source: Yahoo! Finance. *ServiceMaster became a privately held company in 2007.

What CEOs said

Strong CEOs don't shy away from bad results, but they do address what steps they'll take to solve problems. For instance, Sherwin-Williams CEO Christopher Connor said, "We are not satisfied with our results over this past year, but the decisive actions we took in response to rapidly deteriorating market conditions made us a stronger and more competitive company. ... As a result, we gained share in most segments of the market."

Meanwhile, George Buckley of 3M was also rather frank in his most recent letter: "I want you to be reassured that no matter how long its duration, 3M is well prepared to overcome the economic difficulties that face us all." He outlined plans for layoffs that would number "as many as necessary but as few as possible," as well as how the company has "used furloughs, pay cuts, overtime bans, mandatory vacations and stringent incidental cost control to limit the number of layoffs, but in the end some were needed." Despite all his discussion about belt-tightening, he remained optimistic: "In a 5% recession there is still 95% of the business left and winning an increasing share of that business has to be our focus."

And the not so impressive ...

Meanwhile, the latest letter to shareholders from Citigroup's Vikram Pandit offered many vague statements that probably didn't reassure investors, who've seen their shares fall sharply. The letter's four "enduring truths" didn't exactly show that the company is ready to move beyond its past mistakes -- especially the company's commitment to "our rich legacy of innovation." Some might point out that a little too much financial innovation got them in trouble in the first place.

Similarly, ExxonMobil's shareholder letter makes broad claims without much detail. CEO Rex Tillerson says that "ExxonMobil is improving energy efficiency and taking effective steps to curb emissions in our operations." On the surface, that sounds wonderful, but Tillerson wasn't clear about how the company is doing this, and he didn't offer statistics to demonstrate just how effective its steps have been.

So, next time you're looking into a company, read its CEO's letters to shareholders and see what they really tell you. More candor can translate into better returns.

[Legal Information](#). © 1995-2009 The Motley Fool. All rights reserved.