

Investors and the weather

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[stag_intro]As financial reports are disseminated quarterly and stock performances analysed in real-time to investors, there is one determinant that the majority of companies are providing incomplete, misleading, or obscure information for. Worse, they are conveniently blaming disappointing financial results on it, and yet not employing the appropriate risk management strategies to address it. Investors deserve better. [/stag_intro]

The Chief Financial Officer in providing second-quarter results, including a profit decline of 4%, is asked to explain the disappointing results. His answer? “I hate to use the weather, but a lot of it was the weather.” “We are an industry that is susceptible to weather,” he explained further.

If you are thinking this is a mom-and-pop operation, a start-up, or a tourism operator, you would be wrong on all counts.

In fact, this industry leader is a multinational company employing 129,200 employees, with 250 manufacturing centres producing and distributing its portfolio of 3,500 products in over 200 countries around the world, in operation for 128 years. Last year, its net operating revenues were \$45,998 million, having sold 28.6 billion unit cases of its products. Its stocks trade on the NYSE exchange for \$40.60, and its investors include the ranks of Berkshire Hathaway Inc., the Vanguard Group, Inc., State Street Global Advisors (US), and BlackRock Institutional Trust Company.

Yet, despite all this stature, Coca-Cola, the world’s largest beverage company, did indeed echo the age-old excuse of “blame it on the weather” in July 2013, and apparently investors were expected to simply accept weather is beyond the control of this global leader. But this is not to name and shame Coca-Cola, as investors seem to be expected to simply accept that weather is beyond the control of pretty much any company in any industry in any country, judging by the frequency with which members of the C-suite cite the weather when they deliver disappointing results, of which Coca-Cola is just one example.

Here are a few highlights of this past year’s filed financial reports from other heavy-hitters in industries as diverse as beverages, manufacturing, energy, retail, and construction across Europe and North America:

From a leading global brewer: “Own beer volumes in Belgium declined by 7.2% in 3Q14, and were marginally down in 9M14. The result for the quarter was driven by very poor weather in July and August, against a difficult weather comparable....” Anheuser-Busch InBev, 31 October 2014, Brussels, Belgium

From a manufacturer of industrial packaging operating in more than 50 countries: “Gross profit decreased to 18.0 percent of net sales for the first quarter of 2014 from 18.5 percent of net sales for

the first quarter of 2013 primarily due to adverse weather related conditions in North America.” Grief, 26 February 2014, Delaware, USA

From a multinational electric utility company: “Revenues for the Energy Europe Business Line amounted to EUR 25,697 million, down -17.9% on a gross basis. This decrease is mainly explained by the impact of weather conditions on gas sales (first nine months of 2014 having been particularly mild in Europe and notably in France, while 2013 had been particularly cold)...” GDF Suez, 30 September 2014, Paris, France

From a luxury goods manufacturer: “North America, strongly impacted by the unfavourable weather conditions, recorded a Revenue increase of only 2% in the first three months of 2014.” Salvatore Ferragamo S.p.A., 13 May 2014, Florence, Italy

From the leading independent wholesale distributor of building products in Canada: “Taiga’s Fiscal Year 2014 sales up by 5.4%, but earnings down by 51% due to margin pressure and Q4 weather.” Taiga Building Products Ltd., 27 June 2014, Burnaby, Canada

In one way, each of these companies is right: the weather plays a predominant role in affecting sales and profits in the majority of industries. In fact, weather can explain 40% to 85% of the changes in demand in certain sectors’ activity. Looking to the above-mentioned companies, it can be noted that other than finding a common defence for profit losses in weather conditions, there is no explanation as to the exact performance component that is linked to weather. Each company acknowledges that it has suffered as a result of a defined risk, the weather, but not one of them explains exactly what that risk is in precise terms. All that the investor is told is that the weather was “adverse”, “unfavourable” or “difficult”.

For the diversity of the risk that weather imposes for each industry, investors and shareholders are not provided any precision and detail in financial reports of the specific relation between the weather and sales, profits, or production costs. More importantly, they are not provided with information on how companies will mitigate these weather-related risks. In light of international acceptance of climate change, and its resultant future climate variability, including increased weather volatility and weather extremes, these weather-related risks are only going to get worse, and investors need to know the exact correlation between weather and performance.

Fortunately, this is possible today, using advanced numerical forecasting techniques, data assimilation, interpretation and post-processing model outputs. The relationship between a company’s performance indicator (such as sales volume, cost of production, net income) and any weather parameter can be identified and measured to the precision of a one degree in the temperature, one millimetre of precipitation, or one meter per second of wind. Using historical records of meteorological data, companies can then gather precise weather sensitivity over days, months and years, in order to determine average, minimum and maximum gains or losses sustained by weather variations. This correlation can be made at the level of a product, product family, company or sector, by geographic region or globally.

For example, in Coca-Cola Company’s 2014 Annual Reports to Shareowners, the company noted that it is particularly vulnerable to the vagaries of the forecast due to the seasonality of its product. Unusually cold or rainy weather during the summer months may have a temporary effect on the demand for their products and contribute to lower sales, which could have an adverse effect on its results of operations for such periods. Similarly, the Company notes that adverse weather can affect the raw materials it sources. Freezing weather or hurricanes in central Florida may result in shortages and higher prices for orange juice and orange juice concentrate throughout the industry. For both the seasonality of consumer preference for beverages and the effect on shortages and prices of its raw materials can (and has) been modelled, and this information can be passed on to investors. So, why isn’t the company being more exact in its analysis of the risk for investors?

More importantly, having determined their weather-related risk, companies can do something about it. They have the option of purchasing index-based weather insurance to protect themselves against the financial impact of weather anomalies, through predefined payments based on the occurrence of specific weather conditions. The cover is designed to compensate exactly or partially the losses associated with unfavourable weather conditions. The compensation may be fixed when the weather index exceeds a predefined value or progressive if the losses caused by the weather increase in line with the index value. Unlike traditional insurance, index-based weather insurance demands no field loss assessment or other administrative procedure.

Investors today need no longer accept a vague business report, in which the weather is blamed. Business performance can be (and is) linked to the weather, and Meteo Protect provides the weather risk management consultancy services to provide a precise weather risk assessment for each company, including a financial analysis of weather sensitive businesses, financial communication and reporting of weather risk, and analysis and management of a portfolio.

Having provided this analysis, Meteo Protect can provide the insurance product that assures that the company is compensated if the weather is inclement, and the company be compensated for the resultant impacts upon its sales volume, cost of production, or net revenues, so that the business report is not only comprehensive and precise, but the profits and losses not affected. It is not only a matter of time before investors and shareholders demand this information, but that companies are penalized for not providing it, and rightly so.