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Study: Poor Governance Means Poor Performance

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By Staff Reporter

New York - Companies with the poorest earnings quality and corporate governance underperformed the S&P 500 Index by 11 percent in 2005, according to a study by independent risk research firm RateFinancials Inc.

Using the firm's methodology, RateFinancials identified more than 50 companies whose financial statements rank low in terms of the quality and transparency of earnings disclosures and corporate governance. The companies range in size from automakers General Motors and Ford to companies with comparatively little market capitalization, such as content-provider Jupitermedia Corp. and personal care product manufacturer Helen of Troy.

"We continue to establish a strong correlation between poor stock performance and companies with questionable earnings quality," said founder and president Victor Germack, in a statement. "Investors who choose to ignore these warning signs have a high probability of sustaining losses." Germack also noted that an estimated 1,200 companies restated their earnings last year, nearly double the level of 2004.

Last year, the companies on the RateFinancials' list lost 8 percent of their market value in 2005, while the S&P 500 Index gained 3 percent. At least three companies identified by RateFinancials filed for bankruptcy, including Winn-Dixie Stores, Delta Air Lines and Calpine. The value of those stocks all eroded by 89 percent or more.

A previous RateFinancials study also found that companies with poor earnings quality, aggressive accounting and poor governance standards have lower equity returns and more volatility than companies with stronger practices in these two key areas.

RateFinancials rates and ranks the financial reporting of U.S. public companies based solely on filings with the Securities and Exchange Commission. The firm's ratings focus on quality of earnings, transparency and completeness of financial reporting and corporate governance