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The National Investor Relations Institute (NIRI), a U.S.-based association of investor relations professionals, defines investor relations as, “a strategic management responsibility that integrates finance, communication, marketing and securities law compliance to enable the most effective two-way communication between a company, the financial community, and other constituencies, which ultimately contributes to a company’s securities achieving fair valuation.”

At J.P. Morgan, we believe effective investor relations contribute substantially to the success of a company’s depositary receipt program in addition to its valuation. Our depositary bank’s global IR Advisory team guides clients on employing best IR practices, with the aim of optimizing investor demand for their equity, achieving an adequately diversified shareholder base, and maintaining ready access to the capital markets over the long-term. This advisory-based approach, coupled with our bank’s strength as a global equities leader, is a powerful combination for many of our clients’ DR programs.

The 2017 edition of our IR Best Practices Guide updates the previous one, with chapters about topical issues, such as targeting Asian investors and virtual roadshows. The team and I hope that with this new edition you will discover new ways to enhance your investor relations and advance your company’s DR program.

Warm regards,

Candice Teruszkin

CANDICE TERUSZKIN
Global Head of Depositary Receipts
ESTABLISHING AND MAINTAINING AN EFFECTIVE IR DEPARTMENT
As defined by the National Investor Relations Institute, a U.S.-based association of investor relations professionals, investor relations is a strategic corporate marketing activity that combines the disciplines of communication and finance. For issuers that need to appoint an Investor Relations Officer (IRO), finding someone who has a command of both these seemingly incongruent fields can be challenging.

Isn’t hiring an Investor Relations Officer simply a matter of finding someone who has experience as an IRO in the company’s sector?

That’s certainly an option, although an issuer shouldn’t unnecessarily limit its pool of candidates. First, bear in mind that in certain markets, especially emerging markets, finding someone with these specific qualifications can be difficult. Also, there can be other qualifications to consider, depending on the issuer’s objectives.

Hiring someone from outside the sector and the investor relations field may bring a fresh perspective on the company’s equity story, investor relations activities and the capital markets.

The most important skills required for a corporate IR strategy

In addition to the candidates’ professional backgrounds, consider their skill sets and personal qualities. Suitable experience includes work in the capital markets—particularly on the buyside and sellside—corporate finance, strategic planning, sales, marketing, communications as well as law.

First and foremost, an IRO must have a strong financial acumen. An IRO must understand how financial statements are compiled and, more importantly, how the statements are analyzed and interpreted by analysts and investors. Related to this is having a thorough knowledge of how they value public companies. In addition to understanding traditional methods of analysis, such as price multiple comparisons and DCF (Discounted Cash Flow), an IRO must also be knowledgeable about return-on-capital methods.

But it’s more than just the numbers. An IRO needs to know what’s behind the numbers. In other words, what accounts for the company’s operating and financial performance and how such performance will be interpreted by the financial community with regard to future performance. The latter is important because a company’s market value is based on the collective performance expectations of investors. In addition to extrapolating past financial results to predict future performance—using a financial model—investors will assess a company’s growth strategy and competitive position and factor these into their models. So an IRO must also understand corporate strategy and, more specifically, he or she must be able to clearly articulate the company’s strategy.

Other skills a company should look for in an IRO

Strong writing skills are essential for an IRO. Usually the IRO is responsible for drafting earnings announcements as well as the script that management often uses for earnings calls with investors and analysts. Other market announcements, such as those concerning acquisitions, changes in performance guidance and other material developments, also fall under an IRO’s purview. Much of what a company communicates to the market is done in writing, so written investor communications must be clear and concise. This is the communications side of investor relations. The marketing component of IR includes development of investor presentations, the IR website, the annual report and investor fact sheets.

With respect to the sales side of IR, the ability to present to and interface with investors and analysts is another important skill, in both group and one-on-one meetings. An IRO must be able to effectively field questions and, where appropriate, link the answers with the corporate strategy and keep investors focused on how
the company is driving shareholder value over the long-term. Also, when communicating with investors in a non-public setting, an IRO and management must be vigilant to avoid disclosing material information that hasn’t already been made public.

Many investor relations activities take place simultaneously. So an IRO must have strong planning and organizational skills. Whether it’s reporting financial results, returning investors’ phone calls or making efficient use of management’s time during roadshows, virtually every aspect of investor relations is time sensitive and requires flawless execution. Being able to multi-task is even more essential for small- and mid-cap companies and for those in emerging markets, where many IROs are a one-person department. The ability to prioritize the internal and external demands is crucial for the role.

**Personal attributes that should be considered when assessing candidates**

One important attribute is diligence, of course, given the myriad activities taking place at any given time and the need to be timely and accurate. Other qualities include being judicious, self-motivated, persistent, persuasive, flexible and ethical, as well as having an innate ability to collaborate with people inside and outside the company. I would add that an IRO must also be confident, as analysts and institutional investors can be critical of a company and its management and will sometimes challenge the company’s strategy. Confidence is also needed when working with management. An IRO must be prepared to objectively share negative feedback from shareholders as well as reel in management when it begins straying from best IR practices.

**Educational or professional credentials that should be taken into consideration**

An M.B.A. can be an indication that an individual has a strong grasp of corporate strategy and is financially literate. Being a CFA or CPA can also be highly beneficial. But what is required of an IRO can vary by sector. For example, technology and engineering companies might seek candidates with scientific and engineering degrees. To further illustrate this point, a fair number of buyside and sellside analysts covering pharmaceutical and biotechnology companies hold degrees in medicine and bioresearch. So IROs with similar educational and professional backgrounds can be effective counterparts. This is why some companies should consider looking internally for IRO candidates. Employees with technical degrees and experience in operations can be highly effective IROs in certain industries, provided they possess many of the skills and personal qualities discussed. Another advantage of hiring an existing employee is you know they already fit into your company’s culture.

**Other things to consider when seeking a prospective IRO**

There isn’t a standard formula for identifying the person who would be the right IRO for your company. Take the time to review the near and long-term goals of your company’s IR program as well identify challenges the company is likely to face in the capital markets. That’s a good way to define the ideal candidate and the best way to begin a search for an IRO.

**KEY TAKEAWAYS**

- When seeking an IRO, it is not necessary to limit your search to people with corporate IR experience in your company’s sector
- There are a variety of professional backgrounds, skills and personal qualities that make an individual a suitable IRO candidate
- Essential requirements for an IRO position are a thorough understanding of finance and corporate strategy as well as strong writing, presentation and organizational skills
- As a starting point for conducting a search, review your company’s investor relations objectives and consider any challenges ahead in the capital markets
- The perfect candidate might be found inside your company
Making the transition from a private to a public company can be difficult in various ways, beyond the complexities and hard work that a public offering entails. For some companies, a major challenge is shifting senior management’s mindset from one of almost absolute secrecy to one of transparency. This change requires understanding that transparency is imperative for investors. Many of them will also insist on more information disclosure than required by regulators.

Because companies begin life as private entities, Investor Relations Officers (IROs) of newly public companies can find it difficult to persuade the CEO and CFO to spend sufficient time meeting and talking with new shareholders, prospective investors, and broker analysts to answer probing and seemingly intrusive questions about the company’s business and financials, information that had been carefully guarded before the public offering.

Just below the senior management level, an IRO can encounter problems obtaining timely information from colleagues such as division heads or those who lead the sales or operating areas of the company. Such information is either requested by an investor or analyst, or is needed to explain financial results or a material development, both of which require a public announcement. Like senior management, these colleagues are not accustomed to the information demands of the public equity markets, and they might not even understand the role of the IRO, a position not found at private companies.

Shifting the corporate culture to one of transparency can be accomplished by educating senior management and other employees on whom the IRO relies for information needed to effectively communicate with investors and analysts. With respect to management, it can be useful to explain the benefits of transparency, and for others it is important to help them also understand that certain information disclosure is required by law and that material non-public information¹ must be disclosed in ways that comply with financial market regulations.

Highlight the benefits of being a public company

With respect to securing the cooperation of colleagues, it can be helpful for the IRO to point out the advantages of being a public company that they can benefit from collectively and individually. Among these are improved access to capital, which facilitates a company’s growth; greater visibility, which helps attract new business; feedback from the capital markets that can be used to better inform decision making; and stock-based compensation that allows employees to benefit directly from a company’s growth. Generally, when employees can see the benefits of cooperating, you are more likely to receive their full support.

Provide context

Another important step in educating colleagues about transparency is explaining who the key players are in the public equity markets, namely, institutional investors and the sellside analysts who serve them. Emphasize that both make decisions based on the information they receive from the company, hence the need to publish information that is accurate, timely and clear. Regulations that apply to public companies also demand that the information meets these criteria and investors receive it simultaneously so none has an unfair advantage. Colleagues should also know that for these reasons and others only authorized employees, such as senior management and the IRO, are permitted to communicate with the investing public and media. Spokespeople and disclosure procedures are usually defined in a company’s disclosure policy.

It is also important for the IRO’s colleagues to know that public companies tend to be scrutinized by the press. While coverage by the media can help raise a company’s visibility and generate business, it can be negative, which is another reason why public communications must be carefully managed. The opinions of current and prospective customers, strategic partners, key stakeholders, and the media need to be considered when planning and implementing communication strategies.

¹Generally, non-public information is considered material if a person could be reasonably expected to purchase or sell shares of a company after becoming aware of this information
suppliers and employees are shaped by the media, in addition to those of investors and analysts. Generally speaking, good communication with investors and the media is good for a company’s stock price and business. Poor communication tends to have the opposite effect.

**Explain the IRO’s role**

Explaining the role of an IRO will provide additional context that will help your colleagues understand how they can best support you. As well as describing the IRO’s responsibility for publishing financial results and for publicly announcing other material developments to investors, shed light on how you serve as a liaison between senior management and the investment community. Let your colleagues know that the myriad questions you will be asking them come from (or you are anticipating) investors and analysts who demand, and are entitled to, prompt answers.

Also explain to them that you will have many questions about the financial statements, the answers to which are used to explain the financial results and other performance measures in interim earnings reports (usually in the form of a press release) and the annual report. Emphasize that investors need more than the numbers; they also need to know what accounted for them. Those who head divisions, sales and marketing, operations as well as other areas of the company will be asked for details that will allow senior management and the IRO to effectively explain what drove or hindered performance and what the most recent earnings report means with respect to the effectiveness of the company’s strategy and its future performance. The earnings conference call—during which management discusses the company’s financial results and answers investors’ and analysts’ questions - is another illustrative example you can use to educate your colleagues about information demands that must be met. Invite your colleagues to listen to these calls.

Many companies provide some form of performance guidance. In the interest of preserving investor trust in senior management as well as the company, it is crucial to publish performance forecasts that are reliable. This is another area where the IRO and senior management will rely on colleagues for accurate and timely information. If investor expectations are set higher than what the company actually produces in terms of financial results, trust will be eroded, and this can have long-term consequences for a company’s market valuation.

An IRO is also responsible for marketing the company to prospective institutional investors, primarily through non-deal roadshows. This effort mostly centers on explaining the company, the markets in which it operates, its competitive advantages and strategy to grow the company over the long-term. Such conversations with investors require the IRO, as well as senior management, to be fully informed and current on virtually every aspect of the company’s investment proposition. Here again, the IRO will rely on colleagues, so explaining this marketing role will help win their cooperation in securing needed information.

**Education leads to cooperation**

Becoming a public company places additional demands on the CEO, CFO and other members of upper management. By helping them understand the importance and benefits of transparency, the IRO can quickly secure their cooperation in delivering accurate, timely and clear information to the financial community and in building strong relations with investors and analysts.

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**KEY TAKEAWAYS**

- Achieving a sufficient level of transparency can be one of the difficulties in making a successful transition from a private company to a public one
- Educating upper levels of management about the information requirements of investors and analysts and the benefits of good investor relations can facilitate a complete transition
- Highlighting the advantages of being a public company is a good first step to secure the cooperation of colleagues
- Providing context can facilitate your colleagues’ comprehension of the basis of information disclosure and why it must be carefully managed
- Explaining the investor relations function is another effective way for an IRO to win support within the company
The challenge of securing an appropriate budget

An investor relations department plays a vital role with respect to a company's financial strategy and has a myriad of responsibilities. But like any other area of a public company, it must abide by a budget. In the wake of the most recent financial crises, many IR budgets remain under pressure. For a company that is about to go public, creating an initial budget that sets aside sufficient funds can be especially challenging. In order to make strong and enduring first impressions with public equity investors, the senior management team and investor relations officer must travel frequently to meet with them. Also, the IR department must have adequate resources to ensure that investor communications are effective from the first day of trading. For the IR departments of existing public companies, the challenge is increasingly having to contend with budget cuts or adjusting to flat budgets amid rising costs.

Making sure that IR's importance and value are clearly understood and defining which IR tools and activities are going to have the greatest impact are the best ways to obtain a budget that will enable an IR department to succeed.

Ensure that IR's value is understood

The value placed on IR varies across companies. For example, the CEOs and CFOs of companies that regularly employ stock to make acquisitions are well aware that an optimal share price—one that reflects a company's intrinsic value—means they have a strong acquisition currency at their disposal for M&A deals. They know that effective investor relations contributes to this purchasing power, as it helps investors appropriately value a company and can lower risks associated with poor investor communications. At other companies, however, the benefits of investor relations are less obvious, potentially leading senior management to undervalue IR and constrain its budget. Therefore, it is important to educate management about how investor relations supports the company's financial strategy.

Equity is a big part of most public companies' capital structures. Management needs to know—or be reminded—that effective investor relations helps optimize market valuation, which can result in more funds being raised from follow-on and rights offerings. IR helps drive a company's market valuation by maximizing investor demand for its shares/depositary receipts and by effectively communicating the company's investment proposition. Meeting these goals means having sufficient funds for important IR activities like roadshow travel, broker conference attendance and investor days, as well as for information resources, such as investor databases, market data and shareholder IDs.

Therefore, the context of budget discussions with senior management should be the company's market valuation and positioning the budget as an investment in strengthening the company's standing in the capital markets. In other words, investing in IR helps maintain ready access to capital on favorable terms. When making your case for a desired budget, it can also be helpful to remind management that they and other employees who are partly compensated with stock or options directly benefit from a fair market valuation.

Sound investor relations is also a fiduciary duty to shareholders, as anything less could lead to a valuation discount relative to sector peers and/or a company's intrinsic value. Accordingly, management should be aware that the board of directors could receive complaints from shareholders if investor relations is poorly executed over time. And because members of the investment community talk with one another, an unwelcome reputation can develop eventually. Like investors, sellside analysts also rely heavily on clear and regular communication with senior management and the IRO. Therefore, a company with a reputation for poor investor relations runs the risk of losing existing or potential research coverage. Limited coverage can be detrimental to a company's market valuation because the institutional sales forces of brokers help drive demand for its shares and DRs.
Emphasize a judicious approach to spending

When discussing your IR budget with the CFO, emphasize that you have taken a disciplined approach to it and that funds will only be spent on resources and activities that will have the greatest impact. In this vein, explain the ways in which you will limit spending. If you have determined that the cost of marketing your company to retail investors outweighs the benefits in terms of incremental market valuation, point this out to management.

Performing targeting analysis lets management know that money as well as the time they spend on roadshows will be worthwhile. Highlighting some of the ways you are lowering costs—for example, producing a 20-F wrap instead of a glossy annual report—also conveys budgetary discipline. Illustrating disciplined spending as well as underscoring IR’s strategic benefit can lead to an optimal budget.

KEY TAKEAWAYS

• An IR budget can be unduly constrained if management does not fully understand the important role that investor relations plays in a company's financial strategy

• Effective IR helps optimize a company's market valuation by maximizing investor demand and by effectively communicating its investment proposition. Accordingly, emphasize to senior management that IR helps maintain ready access to capital at a favorable price

• When discussing a budget with the CFO, stress that a disciplined approach was taken and that funds will only be spent on resources and activities that will have the greatest impact
Investor relations requires considerable resources, both in terms of time and money. As is the case with other uses of corporate resources, a well-managed company needs to measure its return on investment. There are various methods that can be employed, although not all measures are direct corollaries and the data needed to make certain assessments can be limited. Gauging the effectiveness of a company’s investor relations is never a precise science and thus challenging.

New investors

For many companies, attracting new investors is one of the most important objectives of an IR department. Tallying them and the value of their investments each year are obvious metrics, but the availability of ownership information that evidences purchases can be very limited in some countries. In the U.S., quarterly 13F filings that investors make with the U.S. Securities and Exchange Commission can tell you which investors bought (or sold) your company’s ADRs. In other countries, however, such information is not as readily available and requires the resources and expertise of Shareholder Identification firms.

Increases in share and DR liquidity make it easier for institutional investors, particularly large ones, to build or reduce their position in an issuer. Accordingly, trading volume is an important measure for assessing the IR department’s performance. Generally, the more meetings and calls they hold with investors the more likely liquidity will improve. However, like other metrics, there are a variety of other factors that have an impact, such as trading conditions in the overall equity market. The IR department, though, should not be solely judged on the number of new investors it has managed to attract through meetings and telephone calls. Equally important is the quality of the investors it has attracted. Medium—and long—term holders are ideal, while high-turnover managers are not, generally speaking. Accordingly, avoid spending too much time with the latter category of investors, especially management’s time. Also, when using brokers to arrange non-deal roadshows, be mindful that they tend to favor high-turnover institutions because these investors generate more trading commissions.

The quality of investor meetings should also be monitored. When senior management’s time is used, investors should be engaged in a substantive conversation with them about strategy and competitive advantages, for example, not asking basic questions about the company’s business. Although the quality of meetings cannot be measured quantitatively, the types of questions an investor asks are the best gauge. After a meeting, an IRO can expect management to express how satisfied they were with it. The same should be applied to brokers, and those who arrange quality meetings should be rewarded with future roadshows.

Ownership mix

Some companies seek an optimal mix of shareholders. Accordingly, investor relations can be judged on its ability to attract and maintain certain percentages of foreign investors and/or DR holders as well as medium- and long-term holders. Concentration of ownership is also an important measure because swift selling by one or several shareholders with large positions can result in a rapid fall in the stock price. This is one reason why an IRO must continually cultivate new buyers, as they can step in and absorb any sudden supply of shares in the market.

While an IRO cannot prevent an investor from acquiring a large stake in their company, he/she can set the stage for future demand when it is needed. Remember, investors often need several months (sometimes longer) to analyze and get comfortable with a company and its management. In other words, do not wait for the stock price to drop before looking for new investors. The geographic distribution of shareholders can also be important; as a company becomes less dependent on a limited number of capital markets, its ability to raise capital in the future is enhanced and at potentially more favorable terms.
Investor feedback

Obtaining investor opinion regularly is one of the best ways to gauge an IR department’s effectiveness. It also helps the IRO understand how investors and sellside analysts are valuing the business and uncover any misperceptions or information gaps that might exist. As part of a perception study (a comprehensive means of gathering feedback), the firm conducting the study should ask shareholders and analysts how satisfied they are with your company’s investor relations and how it could improve. Areas to discuss with investors are management and IRO availability and responsiveness, transparency and access to company information.

If prior perception studies had indicated information gaps or misperceptions, your next perception study should seek to determine if investors are now sufficiently informed and/or if any misperceptions have been corrected. Such findings would indicate whether the IR department had taken the necessary corrective actions.

Sellside coverage

A broker’s research and institutional sales force can drive significant investor demand for an issuer’s shares and DRs. Although a broker’s decision to cover a company is mostly economically driven, namely potential trading commissions, the IR department can influence this decision. Good investor relations can help with regard to increasing sellside coverage. Therefore new coverage by a broker which can be attributed to efforts by the IR department to initiate and build a relationship with the analyst should be tracked.

Stock price not a suitable measure

Some companies mistakenly judge their IR department on changes in the stock price. This is inadvisable because the influence of IR cannot be isolated among the myriad factors that affect a company’s stock price, such as the company’s financial performance and conditions in the capital markets. Nonetheless, the company’s market valuation should always be at the forefront of an IRO’s mind. Specifically, is the company undervalued relative to its intrinsic value and peers market values? That is not to say that market valuation should be used as a performance measure for the IR team. Rather, a low relative valuation may indicate there is insufficient demand for your company’s shares and DRs or that the investment community does not fully understand and appreciate its investment proposition. And this is where the aforementioned performance measures can guide an IRO—they can indicate where problems exist and thus allow the IR program to be effectively recalibrated in order to close a valuation gap.

KEY IR MEASURES

Quantitative measures

- Number of new investors and the value of their share and DR holdings
- Share and DR liquidity
- Percentage of low- and medium-turnover institutions vs. high-turnover institutions
- Concentration of ownership
- Geographic mix of ownership
- New analyst coverage attributable to IR efforts

Qualitative measures

- Quality of investor meetings
- Shareholder and analyst opinion of investor relations
- Changes in investors’ perceptions and their understanding of the company
The theoretical advantage of providing more information than required

As a public company, an issuer must comply with the information disclosure requirements of securities regulators, principally national government agencies, such as the U.S. Securities and Exchange Commission (SEC), and stock exchanges. In addition to the various types of information that must be publicly disclosed by a company, regulators require that financial and operating results be reported with certain frequency, such as quarterly or annually. In the U.S., an example of the latter would be the Form 20-F that is filed each year with the SEC by a foreign private issuer.

Interestingly, some companies elect to publicly disclose more information than required by regulators. The senior management and boards of directors of these companies typically choose to do this because they believe that incremental disclosure can improve the financial community's understanding of their business and thus value it more accurately. In other words, they believe that increasing investors' and analysts' knowledge of their company will translate - over the long-term - into a market valuation that more closely reflects its growth potential and economic value. This philosophy hinges, in part, on the theory that providing more information can lower the risk premium that investors assign a company. It means that investors would be willing to pay higher multiples of earnings and cash flow when purchasing a company's stock or depositary receipts, resulting in a higher market valuation.

Of course, a company's competitors also might like to see it disclose more information publicly, as they could potentially use the additional information to their advantage. Any company contemplating increased disclosure should consider this potential drawback.

Methods to identify incremental information for disclosure

There are two principal methods that can be used to determine what additional information a company could make public. The first is to simply ask shareholders and analysts what other information they would like to obtain from the company that would benefit their analysis, and then compile their feedback to assess which additional metrics could be disclosed. An Investor Relations Officer (IRO) can either ask them informally during a conversation or via email, or pose the question as part of any formal means of obtaining feedback from the investment community, such as a perception study.

Another method is to perform a disclosure benchmarking analysis. Here the IRO compares the company's disclosure with that of its sector peers. It is generally recommended that the universe of peers includes companies from around the world, particularly those domiciled in countries known to maintain high disclosure standards.

You can also ask investors and analysts which companies they believe offer the best levels of transparency. Each line item in the company's financial and operating statements, and in other forms of information disclosure, is compared with those of the chosen peers in order to identify information gaps. An example would be discovering that a peer or several peers disclose EBITDA at a division level versus just the corporate level at your company.

A comparison is also made with regard to the frequency with which peers provide certain information. For example, a number of peers might publish a particular measure or all of their financial and operating results on a quarterly basis even though regulations only require them to do so bi-annually. In addition to reviewing peers' earnings press releases and annual reports, be sure to examine all of their regulatory filings to get a complete picture of what they disclose and with what frequency.

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1 To learn about perception studies, please refer to the chapter on this subject
How to conduct the benchmarking analysis

One way to perform the benchmarking analysis is to use a spreadsheet to compile the findings from reviews of the peers’ disclosure documents. Place each financial and operating measure at the beginning of each row of the spreadsheet and place your company’s name at the top of the first column followed by the names of each peer at the top of each column to the right. For your company and each peer, place an ‘X’ in the corresponding cell where each performance measure is disclosed; using the income statement as an example, place each line item at the beginning of each row, starting with revenue, moving down the income statement, and ending with earnings measures. After completing this process for each disclosure document, you can easily compare what information your peers disclose with what your company makes publicly available. It should be noted that you might discover that your company is more transparent than its peers.

Using the results of the analysis

Either of the above methods can be revealing, although employing both would likely produce the most insightful results. The findings of the disclosure analysis are presented to the chief financial officer and may be presented to the board’s audit committee, which is responsible for overseeing a company’s financial reporting process, among other activities and processes related to ensuring the accuracy of financial information. As is the case with any decision regarding the public disclosure of company information, be sure to consult qualified legal counsel.
Prepared for your annual shareholders’ meeting.

Know in advance where your shareholders stand on your company's corporate governance practices.

Careful advance planning is the surest way to achieve a successful annual shareholders meeting (AGM). As an emerging best practice, issuers are increasingly reaching out to major shareholders to obtain their views on the company's corporate governance practices. Identifying major shareholder concerns in advance of the AGM can help avert problems at the meeting and avoid unexpected outcomes.

To maximize effectiveness, key shareholders should be approached by an issuer before drafting begins on resolutions that will be considered at the AGM. For example, if an AGM is typically held in the spring, an issuer may want to initiate shareholder outreach during the previous autumn. In addition to helping the company understand the ways in which its corporate governance could improve, the resulting feedback can aid the board of directors in its consideration of what to include on the AGM agenda and on how to best communicate those resolutions to shareholders. Also, the issuer may gain some insight into improving corporate governance generally.

Shareholder feedback on corporate governance is usually gathered via telephone by the corporate secretary or Investor Relations Officer. At some companies, this task is shared by both. It is advisable that the phone call be made by the person who has an established relationship with the appropriate contact at the shareholder.

While the portfolio manager is an issuer’s main institutional investor contact, it should be noted that portfolio managers often do not have voting authority. Rather, a designated decision maker may be assigned that task with some institutions even maintaining voting committees. These decision makers can be difficult to identify and reach, which is one of the reasons proxy solicitation firms, which can help a firm target their communications to appropriate investor contacts, are retained by issuers. Other institutions rely on guidance from vote advisory firms, such as Egan Jones, Glass Lewis & Co., Proxy Governance and Risk Metrics Group (formerly ISS), to make their decision and, in some cases, even cast their votes, which may preclude the need for reaching out to these shareholders.

With regard to vote advisory firms, be sure to review the commentary that accompanied previous vote recommendations, before embarking on an outreach program. Also recommended is a review of governance ratings issued by Risk Metrics Group (e.g., Governance Risk Indicators, or GRId) and other advisers, such as Governance Metrics International and the Corporate Library.

There are several other things to consider before seeking shareholder feedback. A call to obtain a major shareholder’s opinions about your company's governance practices should not be the first time the investor is contacted, generally speaking. Also, and perhaps most important, the board of directors must be prepared to seriously consider any changes requested by a shareholder whose opinions have been solicited. In other words, some opinions might surprise the board and any unwillingness to address substantive governance concerns is likely to reduce goodwill with those shareholders. If the board ultimately does not agree with the shareholder’s recommendations, a follow up discussion with the investor to explain the company’s stance is advisable. Finally, if you are unsure of your abilities to solicit shareholder opinion effectively, consider consulting a proxy solicitation firm.
The National Investor Relations Institute (NIRI), a U.S.-based association of investor relations professionals, recently released the results of research that it conducted among senior U.S. IR officers. The research, which was gathered through focus groups, explored the subject of IR officer communications with the Board of Directors. The number of public companies that actually employ this practice is unknown, but anecdotal evidence suggests that corporate boards benefit from receiving IR-related information. Additionally, exposure to board directors can be a rewarding experience for IROs and help advance their careers.

Given the Board of Directors’ fiduciary duty to shareholders—governing a company’s senior management to ensure that it deploys shareholder capital appropriately and effectively—it stands to reason that directors periodically receive some of the information that an IRO delivers to the CEO and/or CFO (at some companies, the CEO is also the board chairperson). Some of the types of information reported to the board are share price performance, the main factors impacting market valuation, consensus estimates, major changes in ownership, and top shareholders’ current opinions of the company. The latter can be particularly valuable because boards usually only learn shareholder views at the annual shareholders’ meeting. Knowing prevailing shareholder opinions ahead of the annual meeting can be useful because it can help the board prepare in advance to respond to issues that are likely to be raised at the meeting and lessens the likelihood of unwelcome surprises. Shareholder opinion along with other IR-related information can be delivered to the board via a written report or presented by the IRO or a member of the senior management team.

The decision to provide IR information would be made by senior management or might be at the direct request of the board itself. If briefing the board is not a current practice at your company, consider suggesting it to senior management. The frequency of reporting this information is another decision that needs to be made. According to the findings of NIRI’s focus groups, one of the advantages of having the IRO report to the board is that he or she regularly communicates with investors and sellside analysts and, therefore, can give color to the reported information, particularly with regard to the opinions of top shareholders and those of influential sellside analysts.

In the box below is a list of information an IRO and senior management could consider sharing with their company’s board of directors. This is not an exhaustive list and the information needs of boards vary by company, of course. Also, be careful not to inundate the directors with too much information, as a number of the participants in NIRI’s focus groups cautioned. Generally speaking, what is most important is alerting the board to emerging trends that could materially impact shareholder equity.

<table>
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<tr>
<th>IR INFORMATION THE BOARD OF DIRECTORS MIGHT FIND USEFUL</th>
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<tr>
<td>• Share and ADR price performance relative to peers and key indices</td>
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<td>• Key factors that affected prices</td>
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<td>• Key valuation multiples compared to peers</td>
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<td>• Substantial buying and selling activity by top shareholders</td>
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<td>• Significant changes in the composition of the shareholder base, in terms of investment style and geographic distribution of ownership</td>
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<tr>
<td>• Consensus estimates and broker ratings</td>
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<td>• Summary of opinions of top shareholders regarding the corporate strategy, company’s operating environment, company’s competitive strengths and weaknesses, the management team, etc</td>
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<tr>
<td>• Summary of influential sellside analysts’ views</td>
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2 To learn more about this subject, please refer to the chapter entitled Preparing for Your Shareholders’ Meeting
Transactions such as IPOs and acquisitions move investor relations beyond traditional activities and present unique challenges. Just as football fans expect their team to raise their game on the World Cup stage, stakeholders in a company look to the management team to intensify its efforts in special situations. Corporate transactions such as capital raisings, acquisitions and hostile bid defenses are business defining moments. And there is no question that a positive outcome owes much to management’s performance at the height of the campaign to win investor support.

Planning ahead

Success, though, rarely happens in an instant. It originates from an executable plan and hard-earned experience. National football teams gain their place in the World Cup tournament by playing at a high level over a sustained period of time. And winning the favor of a team’s manager requires consistent performance by players throughout the season. Effective investor relations also takes practice and persistence. A company that is well-organized, that has a track record of effective communication and is knowledgeable about the challenges ahead, will be much more keenly received by the investment community at the onset of a transaction. Many elements of IR preparedness are common to all transactions. However, the resurgent focus on IPOs and M&A activity make these useful areas for discussion.

IPOs

With volatility making the choice of when to tap the equity markets a difficult one, private companies may be tempted to rush the transition to public status at the expense of key preparations. In the run up to pricing there are numerous demands from bankers, lawyers and auditors. However, alongside the many hours dedicated to due diligence and the prospectus, IR deserves marked attention.

Here are eight essential tasks typically required to build an effective investor relations infrastructure and successfully announce to the world that a new public company has arrived.

• Decide who will manage the investor relations function – The most effective IROs work directly with top management.

The professional experience of the IRO will be driven by the specific nature of the business. For example, in highly regulated sectors such as banking and pharmaceuticals strong sector expertise is an advantage. Above all, an IRO must have a strong financial acumen and understand the nuances of corporate strategy.

• Develop a disclosure policy – This should describe the information that will be communicated by the company in an orderly fashion on an ongoing basis. An important part of the policy will be the company’s authorized corporate spokespeople: a small group of individuals (typically the CEO, CFO and IRO) who are trained on what they are permitted to disclose to ensure message consistency and comply with regulations. Bearing in mind the more stringent financial reporting requirements upon a listed company, a comprehensive assessment should also be made on whether any changes in accounting policies or additional disclosure notes are required.

• Determine your guidance approach – It is said that economists give their predictions to a digit after the decimal point to show that they have a sense of humor. Producing reliable earnings forecasts consistently can consume much time and effort. Careful consideration should therefore be given to what amount of forward-looking information the company will provide to the market, in what form and with what frequency (quarterly, bi-annual or annual). This may include projections on revenue, margin, EBITDA and net income. Naturally, the visibility a company has into its future financial results will largely shape the level of its guidance.
A decision must also be taken on whether to provide range or pinpoint forecasts and how frequently to update guidance during the year.

- Target investors to focus on after the IPO - One of the priority questions a company needs to address is what kind of shareholders will it seek to attract and from where. A company must continually cultivate new investors in order to maintain an optimal valuation level. This is especially true during periods of distress. Investors need considerable time to understand a company, so don't wait until the stock price falls or capital is needed to start targeting and talking with prospective investors. Targeting also facilitates building an optimal shareholder structure by focusing IR efforts on investors whose portfolio holdings and characteristics are compatible with the fundamentals of your company. Factors used to evaluate investors include investment style, peer holdings, portfolio fundamentals, rate of portfolio turnover and geography, to name a few.

- Build an IR website that will impress investors and help fulfill most of their information requirements - As a public company, the IR website will be the face by which investors initially assess the professionalism of the business. Investments are all about information and investors need various forms of information to conduct their analysis and ultimately value the company. The website can be an accessible and efficient way of delivering this information. However investors don't want to wade through irrelevant information or overly complex sites. Importantly, the website must be ready to go live on the day of IPO pricing.

- Compile investor materials - A pre-packaged set of materials can neatly communicate key information on your business with minimum fuss. Management biographies, an investor fact sheet, FAQs, recent press releases (and a brief corporate video if the budget permits) can answer many of the fundamental questions that investors and the media will want answered.

- Perfect the investor presentation - An effective presentation will capture how market value and/or dividend growth will be delivered over the long-term. A company should begin structuring and practicing its presentation (including Q&A) well in advance of the roadshow, striving to continually refine and improve it. About ninety percent of information conveyed in a presentation is auditory-visual. Less than ten percent is text, according to educational psychologists. So it’s important that the management team has an opportunity to polish its public speaking skills.

- Celebrate the listing day - This is the start of a new phase in the company's evolution and deserves to be recognized as such. To publicize the event, a company may hold an IPO ceremony at the stock exchange and the IRO can consider an investor lunch with key industry analysts and fund managers. Consider an employee celebration too, which can be a significant morale booster.

Given the amount of preparation involved, the shift from private to public should be regarded as transformational, rather than a one-off financial transaction. Sustaining momentum after listing day requires renewed effort and focus to ensure the business reaps the benefits of its new status, whether it’s by stimulating equity analyst coverage, reporting success or sensibly guiding on expectations.

“IT’S FAR BETTER TO BUY A WONDERFUL COMPANY AT A FAIR PRICE THAN A FAIR COMPANY AT A WONDERFUL PRICE.”
- WARRREN BUFFET

M&A

IROs are not often part of the negotiating team for corporate deals. It is for management and financial advisers to decide the strategy for doing the deal, the funding structure and the integration plan. The job of the IRO is to effectively communicate to shareholders the merits of a deal and play a constructive role in the ensuing debate.
Measuring and communicating worth

A key question in any transaction debate is price. But it’s not always clear if the offer price represents value. In 1867 the United States purchased Alaska from Russia for $7.2 million. At the time, many objected to the high price and uncertain prospects of earning a return. In fact, Alaska has paid for itself many times over with its natural resources as well as seal and whale trade of the past.

Price is important to shareholders of the buyer and is invariably the most critical aspect of the debate to shareholders of the target company. More often than not the latter will vocally dismiss an offer, while leaving the door open to a higher bid. That is evident in such high-profile takeovers such as Cadbury’s recent defense against Kraft and Anheuser—Busch’s initial rebuffal of InBev.

In fact, among financial audiences, most discussion points ultimately seek to examine whether it’s a good price. In preparing to announce a sale or acquisition, therefore, the investor relations team needs to take price into consideration as a fundamental concern and be able to persuasively justify it.

Analysis and assessment of valuation will be based on both financial and non-financial indicators. An investment banker’s opinion on fair value and the language they use in presentations to the company board can be borrowed by the IRO to shape investor messages. The IRO should be prepared to discuss valuation measures, like EBITDA multiples or book value, to help tell the story to well-informed investors.

Share price comparisons are also commonly used to offer perspective. Typically, people look at the ‘premium’—the percentage the offer stands above the last price at which the target company’s stock traded. A stock’s 52-week high is also a frequent benchmark used in negotiating and communicating deals.

Of course, it’s not always just about price. In the biggest media deal of 2009, Walt Disney acquired Marvel Entertainment for $4 billion. It was a ‘full price’ offer, meaning that it was at the high end of the valuation spectrum at a tough time for the entertainment industry. It even prompted S&P to place Disney’s credit rating on its negative watchlist. Significantly, however, the deal was framed to address a key area of concern among investors: giving Disney more exposure to the young male demographic. The message emphasized a strong industrial logic that plainly justified the expense.

M&A is often talked about in terms of delivering ‘strategic benefits’, ‘synergies’ and ‘shareholder value’. However, words like ‘strategic’ often make investors wary. Investor communications should always seek to explain, clearly and logically, that a deal presents compelling financial rationale both now and in the future. Generally, shareholders like to hear that an acquisition is earnings-neutral or accretive this year or next.

Consider the context

In its takeover of the Dutch lender ABN Amro, the RBS-led consortium paid three times book value, which at the time was already expensive for a bank based in an economically mature European country. RBS was later criticized for overpaying at the top of the market. Transactions should always be considered within a time context, notably the stage of a business cycle. A business problem requiring an action today will often have a different action if it were to be tackled in the future. A seller may be more willing because cash is running out. Likewise, a buyer may be attracted to depressed prices and rationalize an expectation for economic return based on cyclical recovery.

All in the timing

M&A often requires timely decisions, for example, in the case of buying the shares of the target company in the stock market. When a potential deal is leaked, competitors may be motivated to take over the deal or to drive up the price.

Prior to announcement, information about the deal should be restricted to a small circle on a ‘need—to—know’ basis. Of course, a company needs to balance confidentiality with disclosure obligations. It is therefore essential for the IRO to advise on identifying when is the right time to make the M&A announcement to the public, taking into consideration the threat of market speculation or unusual trading activity. There is no bigger risk than letting the rumor mill fill an information vacuum, while clarity in communications can have a huge positive influence. Successful bid communications minimize uncertainty among shareholders at all stages in order to sustain their understanding and support.
The human factor

Company leaders play a vital role in successful M&A. A recognized, respected leader assuming a visible role can be a comforting anchor during change or instability. For example, former CEO of the London Stock Exchange, Clara Fuse was widely applauded for inspiring a sense of purpose and coherence in the robust takeover defense against rival stock exchanges. The IRO has an important role to play in helping craft a leader’s words and behavior so they resonate with shareholders and in facilitating timely access to the leadership team. Yet, the IRO must also make sure of their own accessibility, given the proliferation of shareholders and demands placed on top management’s time.

A final thought

Getting communication right helps to mitigate other M&A risks, such as loss of key talent, diminished productivity and political or regulatory scrutiny. Investors know that employee and customer satisfaction with a deal can often be as important as the right strategic fit in connecting two companies and creating value. So IROs should counsel management to think deeply and communicate around issues affecting all constituencies.

PRACTICAL TIPS ON TRANSACTION IR

- Become familiar with the transaction and strategic benefits early on so that you can begin crafting the communications package with spare time to make inevitable revisions
- Run a campaign. Create timetables, identify your audiences, recognize the risks, and define your tactics and resources
- Prepare an exhaustive question and answer document to respond to challenging questions that will inevitably be asked. The investor presentation and press release will emerge from that exercise
MAKING A STRONG FIRST IMPRESSION VIA THE INTERNET

An IR website is an essential tool for most investor relations practitioners, but it often assumes even greater importance for IROs charged with promoting their company’s Depositary Receipts (DRs). Creating a stellar IR site inspires confidence in your company’s investor relations and quickly and easily satisfies most international investors’ information requirements.

First impressions count on the Internet, just as they do in daily life. Many portfolio managers, analysts and retail investors will make their initial judgment about a company, and its ability to effectively communicate with investors, based on the IR site.

Remember that the quality and user-friendliness of an IR website can influence investors’ perceptions of a company and even its management, not just the IR team. If an investor or analyst goes to the IR section of an issuer’s website and has difficulty finding—or can’t find—information required to conduct his or her analysis, this ultimately diminishes the company’s credibility and, therefore, decreases the likelihood that a potential investor will eventually take a position. This will also be to the advantage of competitors who maintain high-quality IR sites.

For DR issuers, an effective IR website is an indispensable marketing tool and means of information delivery. Operating an IR website that is easy to navigate and contains most of the information needed by investors and broker analysts is especially important in the DR context, given the time differences that can exist between market participants and a DR issuer’s home market. An English version of the IR site is almost obligatory for a DR issuer, as English is the international language of finance as well as business.

For companies promoting their DR programs to individual investors, the IR site is also a vital marketing channel. In a July 30, 2008 survey conducted for the U.S. Securities and Exchange Commission (SEC), 38% of the 1,000 participating U.S. households cited individual company websites as the primary place where they seek investment information on the Internet. Corporate sites ranked highest, above private financial investment sites (24%), Yahoo.com (9%) and news/newspaper sites (8%). An effective IR site also saves an IR team valuable time, as individual investors are less likely to call in search of information if it can be readily accessed on the site.

Essential elements

Through a well-designed and carefully considered website, a company can highlight its DR program for retail and institutional investors alike. A best practice is to outline the issuer’s investment thesis on the opening page of the IR site, highlighting both the company’s strategic vision and initiatives, as well as key performance indicators that demonstrate a track record of success. This synopsis need not be lengthy or overly technical, but there should be at least one paragraph summarizing the company’s business and investment case. You simply can’t assume that U.S. investors know your company and its investment proposition. The goal here is to quickly secure an investor’s interest and encourage him or her to further explore your company as a potential investment. This information can also take the form of an introductory letter from the company’s chairman or chief executive officer. Graphs are the best way to communicate financial performance and potential.

Other important elements of a world-class IR site include current and archived annual reports, press releases, regulatory filings, webcasts, information on the management team and board of directors, as well as information on corporate governance.

It is also important to provide information unique to the DR program, such as the DR price, and not just the price for ordinary shares. IROs should furnish a straightforward explanation of the basics of their DR program, including where the DR trades and related data, such as the DR’s average daily trading volume. Supplying such information is important not only in terms of meeting investors’ information requirements, but with regard to making them aware that depositary receipts are a means of investing. The IR website is a simple way to give a DR program visibility and aid liquidity.
IROs should include their contact information, listing both a phone number and an e-mail address. If someone’s looking to contact you, it’s for an important reason, whether it’s an institutional shareholder who wants to set up a meeting or an individual investor who has a problem. Being accessible is one of the cardinal rules of investor relations, particularly when a stock is under pressure.

What information should be available on a company’s IR website? The primary benefit of websites is that they enable a company to make virtually every form of investor information available at little cost. Of course, posting too much information on a website can make searching for specific information daunting and frustrating for users. All information should be properly compartmentalized and placed in locations where an investor or analyst would look for it intuitively. Benchmarking your IR website against those of peers or companies recognized as IR leaders, such as BP and GE, is one way to decide what information to post, for companies that wish to be selective.

Finally, make sure your IR site is user-friendly. Forcing investors to spend time searching for the IR section can frustrate them, making a bad first impression. The IR section and DR information should be easy to locate, and ideally the former should be reachable via the top navigation bar on a company’s homepage or from a prominently displayed “about us” button.

Some DR issuers are focused on other aspects of investor relations but neglect their IR websites, which often haven’t been improved since their initial design. We have the expertise to help our issuers enhance their sites, with the aim of attracting investors outside their home market.

Distinguishing your IR site with technology features

Webcasts have become commonplace, but technology allows for other types of information delivery as well. Consider featuring a corporate video explaining the company’s strategy, operations and products on your DR site? Producing videos can be expensive relative to other communications materials, but this medium appeals to investors as they can quickly grasp the investment story. An issuer’s investment case can be delivered within minutes, using eye-catching moving images and graphics while showcasing senior management talking about the company and their vision.

Some companies feature a download manager on their IR website, a new technology feature that enables investors and analysts to click on documents and designate them to be downloaded later, much like a “shopping cart” feature on commercial websites. By capturing documents to be downloaded simultaneously after an information search has been completed, visitors tend to gather more information and the company holds the visitor’s attention longer.

Other attractive technology features include RSS newsfeeds, interactive financial data and podcasts of investor events, such as earnings calls and webcasts, which can be downloaded to an MP3 player and listened to or viewed at the user’s convenience. As an additional convenience, some issuers post Excel-based spreadsheets on their IR sites, which can be downloaded directly into the user’s own spreadsheets, as opposed to transcribing financial data from Word- or PDF-based documents.

It is important not to forget the technology basics of IR websites, such as enabling investors and analysts to subscribe for and receive information via e-mail. E-mail alert subscriptions allow investors to receive new press releases, event invitations and notifications. Pushing information out to investors—rather than waiting for them to request it—ensures that they receive it and helps keep your company at the forefront of their minds. Be sure to feature the alert subscription function in a prominent location on the IR website. Also, consider collecting the names and e-mail addresses of information subscribers and using this as part of any investor-targeting analysis. Companies have also begun to track and analyze subscription data, learning where institutional investors are domiciled—information that can be valuable when planning roadshows or choosing among equity conferences.

Knowing when enhancements are needed

IR websites are usually the result of information being added in an ad-hoc way over time, with only minor—and at times
disjointed—adjustments to the site’s organization and usability. In such cases, consider taking a step back and conducting a thorough review of an IR site’s content, organization, technology features and ease of use. For companies that lack the internal resources to conduct such a review, there are consultants offering these services. She adds that some also serve as website hosts and even upload new information on behalf of the company, ensuring that site content remains current.

Making as much information as possible readily available to investors is the ultimate goal of IR websites. For investors and analysts new to an issuer, an effective IR site immediately conveys a commitment to high-quality investor relations, which is particularly important for companies domiciled in nascent capital markets. As both an information delivery and marketing tool, IR websites are a cornerstone of world-class investor relations.

**KEY TAKEAWAYS**

- Be mindful that the IR website is often the first impression investors and analysts will have of your IR team, and even the company and its management
- When enhancing an IR site, in addition to content, consider how information is organized, what technology features could be employed and the site’s overall ease of use
- Don’t assume visitors to the IR website understand your company’s investment proposition. On the opening page of the site, give a summary of your company’s equity story, highlighting the strategic vision and initiatives, as well as key performance indicators
- Give your company’s DR program visibility via the IR website by supplying information such as where the depositary receipts trade, their price and average daily trading volume
- Stay abreast of technology features upon which investors are coming to rely, such as information download managers, podcasts and e-mail alerts
CREATING EFFECTIVE INVESTOR PRESENTATIONS

Similar to an IR website, an investor presentation is one of the first impressions that analysts and portfolio managers will have of a company. But for many IROs it can be challenging to create a presentation that clearly articulates a company’s investment proposition.

The most common problems with investor presentations

Most slide presentations are quite good, but some are ineffective in terms of clearly communicating why an investor should consider investing in a company. The most common problem is a presentation that contains far too much information for its purpose: securing investors’ interest and convincing them that they should research the company and eventually invest in it. While investors always appreciate information, too much of it can cloud the investment picture, which at its core is the strategy to grow a business over the long-term. In other words, a presentation that contains excessive detail doesn’t allow investors to synthesize all of its content and see the investment opportunity; there is no clear narrative of the equity story.

Corporate strategy should be the focus of an investor presentation

Investors want to understand the growth strategy and the strategic initiatives that are either underway or will be implemented. Ultimately, investors want to know how the company will drive revenue, earnings and cash flow over the mid- to long-term. They want to understand how management is going to invest their capital and what the expected return on this investment is likely to be.

How an investor presentation should be structured

It is helpful to remember that analysts will model your company. So when developing your presentation, think in the context of a financial model. An effective investor presentation provides a narrative that walks investors through the income statement, from top to bottom and, in some cases, through the balance sheet, from left to right.

Information that an investor presentation should contain

While the information content will vary from one company’s presentation to another’s, what needs to be conveyed to investors is basically the same, almost universal: to comprehend the investment opportunity, investors need to understand the opportunities that exist in a company’s markets, how the company is positioned within these markets, and the strategy and assets that are being deployed to exploit those opportunities. With regard to the markets in which a company sells its products and services, presenting third-party data is typically more effective for making an investment case. Also, trends are most relevant to investors, as they are concerned with the future, with forecasting it.

Accordingly, an investor presentation should not focus on past results, generally. Consider limiting such information to key financial and operating measures, which help establish management’s track record.

Optimal length for an investor presentation

Generally, investors have very short attention spans. Time is of the essence when delivering your company’s equity story. One should aim to hold the audience’s attention for the duration of the presentation, but the first few minutes are most crucial. If you haven’t gotten their attention at the outset, the audience may not remain attentive long enough to grasp and retain the investment thesis. So within the first two or three minutes of the presentation, management (or the IRO) need to give investors a snapshot of the investment opportunity the company offers. An initial slide that briefly summarizes the investment thesis is recommended—four or five brief bullet points that capture the company’s investment case. The presentation should also end with basically the same slide in order to reiterate these key investment messages; in other
words, “These are the top reasons why our company is a good investment.” Once you’ve secured the investors’ attention, you can delve into some details, the information which supports the investment case. In total, the presentation shouldn’t run any longer than 20 or 25 minutes. Generally, that translates into roughly an equal number of slides.

Regardless of a company’s size or complexity, the objective of an investor presentation is not to make investors experts in your company but to illuminate the investment opportunity for them. For investor’s who are relatively new to your company—those attending an equity conference or group luncheon, for example—the goal is to secure their interest, as mentioned earlier. For investors who are already somewhat familiar with your company, the aim would be to reiterate or synthesize the investment opportunity for them and close the deal, so to speak; compel them to call their trading desk at a later time and place a buy order. Also, bear in mind that you need to leave time for investors’ questions. In most one-on-one investor meetings a presentation isn’t usually used, at least not from start to finish. Generally, most investors prefer asking questions and having a dialogue with management.

How do you know the investor presentation is effective?

Look at your audience while you or management are speaking. Are they paying attention to you? Is anyone skipping ahead to the other slides in the presentation? Also, obtaining investors’ feedback after conferences or group presentations can indicate how well you have communicated the equity story. In fact, market intelligence should be used to inform the development process. Investor opinions and other forms of market intelligence help you determine what information is critical for investors in their decision making—what is most relevant to them. The process is very similar to market research for consumer products; once you understand consumers’ preferences and buying behavior, you’re in a better position to craft an advertising campaign, let’s say, or other forms of marketing communications. Similarly, it’s important to understand what investors think about your company. Ideally, you would gather some market intelligence prior to meeting with investors—what I refer to as real-time feedback. In addition to aiding the presentation’s development process, this information helps prepare the IRO and management for questions you might not have otherwise expected.

Other common problems with investor presentations

Excessive images, graphics and animation effects can be distracting. While these are helpful to illustrate certain aspects of your company’s investment thesis—such as a core technology—too many can overwhelm the key investment messages. You want investors and analysts to be listening to management, hearing the narrative that explains how the company will drive shareholder value. That’s how you ultimately win investors’ trust and confidence, and how you attract their capital. Remember, it is management who sets the strategy, leads its implementation and allocates shareholders’ capital.

Delivering the presentation

While the slide presentation is important, the person who delivers it ultimately determines its effectiveness. A company can have a perfect investor presentation and a compelling investment case, but if the presenter doesn’t convey credibility and the right measure of enthusiasm for the company and its growth prospects, the opportunity to win investors’ capital will likely be lost. Credibility and a passion for the business either exist or don’t—neither can be taught, obviously. But for some executives, presenting doesn’t come naturally. For them, presentation training is a must. Also, rehearsing a presentation is always recommended, whether an executive is a skilled presenter or not. A great deal of work often goes into getting a company in front of potential investors, so you need to make the most of the opportunity and make the strongest first impression possible. A poor first impression, by the way, can be long-lasting and difficult to correct.
Other considerations when developing a presentation

As with other forms of investor communications, the presentation should set investor expectations appropriately. Doing so will help preserve the credibility of management and the company over the long-term. That means being candid about the challenges that the company faces, and not just presenting its opportunities. Without credibility you can never gain investors’ trust and build confidence in what you’re saying about your company’s future. And once lost, re-establishing credibility with them can take a very long time.

KEY TAKEAWAYS

- Too much information often does not allow the investment thesis to clearly emerge from an investor presentation
- The primary aim of an investor presentation is to explain management’s strategy to grow revenue, earnings and cash flow over the mid- to long-term
- Market intelligence is important to the development process of presentations
- Consistent with other investor communications, a presentation should set investor expectations appropriately
The annual report is one of the most important forms of investor communications. Beyond the regulatory reporting requirements that it fulfills, the annual report plays a vital role in helping shareholders appraise the value of their investment. It is also an effective marketing tool to attract new investors. Although the information requirements of regulators and investors vary by country or region, the principal communication goals of an annual report are basically the same.

**The annual report’s primary goals**

Above all else, the annual report should help shareholders (and other key stakeholders) understand your company’s performance and progress during the previous fiscal year. This forms the basis for assessing your company’s future and ultimately arriving at an estimated valuation that enables current and potential investors to make a buy, sell or hold decision. Past surveys have shown that for the majority of investors the annual report has a substantial influence on their decisions. Of course, other forms of communication also influence investors, such as interim reports and conference calls, regulatory filings, and meetings with management.

For some issuers, the annual report is used to influence other important constituents outside the financial world, such as customers, current and prospective employees, strategic partners, regulators, community leaders and the media. In other words, it can be used to help win new business, attract talented workers and educate other non-investors who can have a substantial impact (positive or negative) on a company’s business.

In order for an annual report to be an effective communications and marketing tool, a fine balance must be struck between being comprehensive and concise. The latter is important because the aforementioned audiences are almost continuously bombarded with information from other companies competing for “share of mind.” The fight for their attention requires first securing it and then delivering your key messages during the usually fleeting moment your annual report holds their attention. “Less is more,” in other words. Not only will key messages be lost in a report that is dense and lengthy, the company’s annual performance will likely be less comprehensible too.

Of paramount importance, of course, is that information contained in the annual report should accurately reflect performance, the operating environment and the company’s financial condition. It should also be consistent with other investor communications, complementing and supplementing other information sources, particularly the corporate website.

**Keep your audience in mind**

The best way to ensure that your annual report is sufficiently concise and informative is to continually ask yourself and others involved in the development process how useful and relevant the information will be to investors. This requires understanding their opinions of your company (and the investment process generally). A company that regularly obtains candid feedback from investors knows what they consider to be its strengths and weaknesses as an investment and is in the best position to produce an annual report that will effectively reinforce their original decision to invest (or to invest more capital in the company) as well as address any concerns that have arisen since then.

Readers of the annual report will range from those who are completely new to the company to those who are knowledgeable longstanding shareholders. Ideally, the report should be written in such a way that someone without specialist industry or financial knowledge can benefit from reading it too. With respect to current shareholders, key messages will be reinforced and, if the annual report is organized well, they will be able to readily find within it the specific information they need.
Content and structure of the annual report

Apart from what is required by regulators, the key sections of an annual report typically include the following:

- Financial highlights and a brief list of important events
- CEO and/or Chairman’s letter(s) to shareholders
- Management’s Discussion and Analysis (MD&A)
- Financial statements
- Auditor’s report
- Corporate governance

Highlights

Ideally, this section—usually one or two pages containing trend graphs of key financial measures and a list of various strategic initiatives that were executed during the year—is intended to catch the attention of investors new to the company and compel them to read more about it as a potential investment. For shareholders, it gives them a quick snapshot of the company’s annual performance and how their capital was further invested by management.

Letter to shareholders

This part of the annual report gives the CEO and/or Chairperson the opportunity to present a concise and cogent overview of the company’s performance during the year, what accounted for this performance (particularly with regard to the corporate strategy), how the company is responding to marketplace conditions, and what all of this means with respect to its competitive position, financial condition and outlook. Understanding the strategic direction of the company and the mindset of management are the main reasons investors read the letter to shareholders. So it is best not to approach the letter as a perfunctory introduction to the annual report, as some companies do. Also, be mindful that the first few sentences will set the tone for the letter and the annual report.

A thoughtful and well crafted letter to shareholders will help convey that the company is well managed and governed. Specifically, the letter should give shareholders the confidence that management has a strong grasp of the operating environment and has the appropriate strategy in place to effectively deploy the company’s assets in order to best capitalize on market opportunities, address challenges and achieve stated goals. In effect, the letter explains how management is driving revenue, earnings and cash flow to maximize the return on equity over the long-term. It is important to be candid about the challenges that your company faces (but be careful not to overemphasize them). A lack of candor can give some investors the impression that management is concealing or ignoring problems.

Usually, throughout the annual report a theme or themes are conveyed that reflect a company’s strategic direction. For example, the themes of GE’s 2009 annual report are “reset” and “renew”, reflecting the company’s various plans and initiatives to effectively respond to the far more challenging business environment that emerged from the global financial crisis and to eventually restore its financial performance. For another company, the theme might be accelerating growth, diversifying the business, or expanding overseas. The report’s cover or, letter to shareholders, is where such themes first appear as brief investment messages. Subsequent pages reiterate and expand upon these themes and messages by providing more detailed information that supports them.

In addition to reviewing key performance measures and strategic initiatives, such as acquisitions, key product launches and divestments, consider devoting part of the letter to a discussion about how the company manages its risk.

While it is important to keep the letter concise, be careful not to limit it to high-level subjects alone. Help make the company’s investment thesis tangible by explaining how certain key products and services are performing in terms of market acceptance and competitiveness. Or, for example, explain how efficiency is improving at operating levels.

If the roles of CEO and chairperson are separate at a company, the latter’s letter should seek to maintain investors’ confidence in the board of directors’ ability to oversee management and protect shareholder interests. In other words, emphasize what makes the board strong stewards of the shareholders’ investment—list board committees, the metrics they focus on, and how they conduct their due diligence. Consider highlighting board evaluation procedures too.
Examples of good shareholder letters can be found in the annual reports of Berkshire Hathaway and J.P. Morgan.

**MD&A**

This section is the heart of the annual report and the focus of most investors. Remember to be mindful of regulatory requirements that would be applicable here too. Management’s Discussion and Analysis provides a detailed explanation of what accounted for the company’s performance during the year. In addition to explaining operating results, such as revenue, expenses, cash flow, earnings and financial condition, the MD&A covers key industry trends, market risk, major investments (or divestments), R&D, foreign exchange, suppliers, competing products and services, risk management, and anything else that has a material bearing on a company’s performance.

In recent years, companies have paid more attention to the ‘forward looking information’ they include in their annual reports. However, with such information care needs to be taken; when giving some indication of future prospects, avoid making unrealistic statements that could mislead investors and therefore expose the company to legal risk or compromise the credibility of senior management. Companies that are adept at presenting forward-looking information tend to concentrate their efforts on talking about their plans for the future in the context of opportunities and threats that they currently see in their markets.

**Financial statements**

Here the company’s consolidated financial statements are presented—income statement, cash flow statement and balance sheet. Consider making the company’s performance more readily apparent by including the percent changes between the reporting periods.

**Auditor’s report**

Usually a page in length, the report confirms that an independent audit has been conducted and that in the opinion of the auditor the financial statements present fairly, in all material respects, the financial position of the reporting company (regulatory requirements for this area of the annual report also vary across markets).

**Corporate governance**

It is common practice to list a company’s board of directors in an annual report. In addition to noting their affiliations, consider including their professional biographies. Among a board’s primary responsibilities is vetting management’s strategic decisions, such as mergers and acquisitions or the penetration of new markets. Accordingly, investors increasingly want to know what combination of experience, skills and talents make a board an effective steward of their investment. Providing brief information about the board’s committees (e.g., audit committee) and indicating the members of each is also useful information for investors.

**Other information to consider**

Devote some space to reviewing your company’s products and services. This information will make your company more tangible to the reader and help illustrate the business model and how it is delivering value to its markets in ways that will drive revenue, earnings and cash flow over the long-term.

Innovation is how most companies maintain their competitive advantage. Accordingly, an annual report should contain information about R&D investments and activities. For companies whose investment proposition does not hinge on technology, highlighting innovation can be describing or showing (see “Annual report formats” on the next page) novel approaches to delivering services or producing products. Brief case studies featuring products or customers can also help bring the intangible aspects of your business to life.

Also consider profiling executives who play a key role at your company in addition to the CEO. For example, the head of marketing and merchandizing at a retailing company or the head of R&D at a pharmaceutical company are central to the success of their employers. A profile can take the form of an interview. With online HTML-based annual reports, the profile can be video-based, thus allowing illustrative moving images and animated graphics as well.

At some companies, Corporate Social Responsibility (CSR) is an integral part of how the company is managed. Consequently some choose to include CSR information in the annual report, rather than publishing a separate one about CSR policies, activities and measures.
Assembling and organizing the report’s content

Although the Investor Relations Officer is often responsible for and usually leads the development of the annual report, there are many people involved in the process. They often comprise a committee that meets regularly and typically includes other members of the finance department, people from the corporate communications and legal departments and, for online versions of the report, the website team of the marketing department. During various stages of the development process, other people will become involved, such as the CEO, CFO and chief legal officer. Everyone contributes their own perspectives on the business, its performance and future, and ultimately what needs to be communicated to the company’s key stakeholders. To this end, it is important to listen to them, senior management in particular, to ensure that the year’s performance is clearly and sufficiently explained and that key investment messages are effectively delivered.

To make them clearly visible, key messages often stand alone in the early pages of an annual report, frequently in the form of headings to pages and sections. Messages bear repeating to ensure they are absorbed by stakeholders. So as not to bore the reader, though, it is best to use variations of these messages, in terms of how they are stated and how and where they appear. The simplest way to accomplish this is to embed the messages in the body of text. The real task is to make the report readable. Narrative is how you communicate. A readable narrative is how you retain good shareholders and attract new ones.

Again, it is important for the annual report to be concise. So limit information to that which best explains the year’s performance and your company’s investment thesis. Endeavor to use “Plain English”. To help the reader digest all of the information, organize and segment it in ways that show how the various parts of the business are growing revenue and earnings. For example, compartmentalize information by business division, geography, technology or product line, and explain how each is contributing (or is expected to contribute) to the top and bottom lines of the income statement. Also prioritize the information in order of importance. Create a narrative that walks the investor through the business. To avoid dense and lengthy text, use bullet points and segment information using text boxes and different colors schemes.

Annual report formats

Online annual reports are becoming increasingly common, although U.S.-listed companies are legally required to make printed versions available to those shareholders who request them. The advantages of online reports are numerous. In addition to saving considerable money (about one-tenth the cost) by avoiding printing costs, online versions are considered environmentally friendlier as they avoid the use of paper and shipping.

The greatest advantage, though, are the various electronic communications tools that web-based technologies, such as flash technology, offer. Such features help convey the value of intangible assets, such as management talent, innovation and brand equity. For example, HTML-based annual reports (which are distinct from the static pdf-based versions found online) allow the reader to view video statements by the CEO, to click on financial figures and hear explanatory comments by the CFO, watch and listen to the head of marketing explain a new branding campaign, or view a video that demonstrates a new product or technology. Animated graphs and charts make trends more readily apparent and can make financial and operating data easier for the reader to comprehend.

Some of the advantages of HTML-based annual reports are quite simple, such as the ability to obtain certain information faster. Links to regulatory filings, to more detailed information about certain aspects of the company, or to third-party industry data can also be made available through this format. And for the Investor Relations Officer, the level of usage and what is being viewed is valuable information that can be captured and used to refine future reports as well as other investor communications. A good example of an HTML-based annual report can be found on the investor relations website of Life Technologies.

Depending on the regulatory jurisdiction in which a company’s securities trade, a “wrap” can be produced in lieu of a printed
annual report. For foreign issuers listed on a U.S. stock exchange, a wrap is the Form 20-F with a glossy cover, a letter to shareholders and perhaps a page or two of the year’s operating and financial highlights. While a wrap is a low-cost alternative, it might not be as effective if the regulatory filing is not written in a “Plain English” style, containing lengthy, legal text. If the annual report is not aimed at investors alone, bear in mind that the IR department could share the cost with other departments (e.g., sales and marketing).

Look and feel of the annual report
Generally, an annual report should conform with the company’s corporate brand architecture, with respect to the report’s color palette, the font of its text and other forms of style. Bear in mind that investors will be familiar with the corporate website and have probably seen your company advertisements or marketing collateral as well. Accordingly, be sure to include your company’s marketing department in the design stage of the development process to help ensure consistency in design across all communications materials.

Give some meaningful time and thought to the cover of your annual report. The image(s) and/or text on the cover should reflect the report’s core themes and investment messages, to help capture the essence of the company and its future. If you choose an image for the cover, it should help clearly identify the company with respect to its core activities and strategic direction.

Producing the annual report on time and within the budget
Regulatory deadlines must be met, of course. However, timeliness also reflects well on the management team and IRO. Start the development process as early as possible; for companies whose fiscal year coincides with the calendar year, many get started in September. Employ a timeline that sets deadlines for the various stages of the development and production processes and that clearly identifies who is responsible for each activity. Be mindful that the latter includes people outside your company, such as designers, printers, photographers and videographers. Also, be sure to build in sufficient time for review by the legal and compliance departments and approvals by senior management and the board of directors. If you are completely new to creating an annual report and internal marketing resources are limited, consider appointing a design firm that specializes in this field.

As with any other key part of the investor relations program, the publication date of the annual report should be set well in advance as part of a company’s financial calendar.

Additional things to consider
Spend as much time as possible with the senior management team to understand what they think is most important to say about the year’s performance. Use this information and what you know about investor opinions of the company to define a core theme or themes for the annual report and to create, refine or reinforce a set of key investment messages. Next, create an outline for the report’s content, which helps ensure that information is logically organized and flows well and that key investment messages are effectively delivered. In the same vein, include a table of contents at the front of the annual report; for readers who lack time to read all of the report, this will help them easily locate the information they need most.

Producing an annual report is a challenging and time-consuming process that involves many people already very busy with their regular responsibilities. So it can be helpful to periodically remind them (and yourself) that the quality of the annual report reflects the quality of management, the board of directors, the IR department and the company. For many companies, it is the single-most important public communication every year.
KEY TAKEAWAYS

• The annual report helps shareholders understand a company’s performance and progress during the previous fiscal year.

• An annual report should accurately reflect a company’s performance, operating environment and financial condition, and should be consistent with other investor communications.

• Understanding investor opinions about your company is a good first step for developing an effective annual report.

• Limit information to that which best explains the year’s performance and your company’s investment thesis.

• The letter to shareholders and MD&A are considered the most important sections of the annual report.

• Understanding the strategic direction of the company and the mindset of management are the main reasons investors read the letter to shareholders.

• It is important to listen to senior executives of the company to ensure that the year’s performance is clearly and sufficiently explained in the annual report and that key investment messages are effectively delivered.

• Electronic communications tools that can be employed using HTML-based annual reports help convey the value of intangible assets, such as management talent, innovation and brand equity.

• Start the development process as early as possible and build in sufficient time for reviews and approvals by senior management, the board and legal department, among others.
INVESTOR COMMUNICATIONS

CONDUCTING AN INFORMATIVE EARNINGS CONFERENCE CALL

The essence of the earnings conference call

Investors and broker analysts greatly value earnings conference calls that are truly informative. Such calls further their understanding of your company and, ultimately, help them better forecast its earnings potential. An effective earnings call is one where the senior management team clearly and concisely elaborates on the information contained in the company’s earnings press release. The CEO and CFO expand on this information through prepared remarks and during the question-and-answer period of the conference call.

The core objective of the earnings call, which typically runs for 45 minutes to an hour, is to further explain (beyond the earnings press release) what accounted for the most recent financial and operating results of the company. Think of the call as a spoken version of the MD&A\(^1\) section of an annual report. Management’s explanation of the results helps investors and analysts better understand the health of your company’s business, the market conditions in which it operates, its competitive strengths (and weaknesses), and what the most recent performance results mean with respect to future earnings and to annual performance guidance (if given by the company). In other words, this process helps them improve their forecasts of revenue, earnings and cash flow, and ultimately make more informed investment decisions. However, while it is important to give details, be sure to help investors understand the “big picture” at the same time.

To this end, at the beginning and conclusion of management’s remarks give a brief summary of what the results mean for your company’s overall long-term investment proposition. More specifically, link the results with the company’s long-term strategy and key business initiatives—which aspects of the strategy are working, which are not, and why? Does the strategy need to be recalibrated? Are major business initiatives proceeding according to plan? What revenue or cost initiatives might be implemented in light of the company’s most recent financial performance? While much of this type of information is contained in the earnings press release, the forum of an earnings call allows management to give color to it as well as provide a clearer picture of the company’s recent reporting period and its long-term outlook. With respect to the latter, a well-executed conference call can help prevent investors and analysts from overreacting to recent problems that senior management expect to be short-term.

Thorough preparation increases the chance of success

The quality of an earnings conference call generally reflects on the quality of the management team, so preparation and attention to details are essential. This is especially true for companies that have recently gone public, as the conference call will be senior management’s (and the IRO’s) first time reporting to public investors as well as the broker analysts who influence their opinions; bear in mind that first impressions can be strong and lasting. A well-executed earnings call will go a long way toward assuring the investment community, upfront, that management will keep it informed. This is an important first step in building trust with investors and analysts, a cornerstone of investor relations.

Due to the timing of an IPO, some newly-listed companies will have little time to prepare for their first earnings conference call. In such cases, the IRO will have to do the preparatory work while senior management is on the deal roadshow, or rely on an external IR advisor to do it.

A good starting point for making conference call preparations is to include them in a timeline for publishing your company’s financial results. Additionally, make sure that everyone who must participate in each of the preparatory steps has these in each of their business calendars. This would include activities like developing a slide presentation and script, drafting potential questions from investors and analysts, rehearsing the conference call, and reviews and approvals by senior management and the legal department.

Presentation slides and script for the earnings call

Many companies utilize a slide presentation for their earnings conference call. The presentation and earnings call are “webcast” via the internet. Presenting key points, graphs and charts in the presentation can facilitate the CEO’s and CFO’s

\(^1\) Management Discussion & Analysis
explanation of the performance results and help increase
investors’ and analysts’ comprehension of the information.
However, the presentation should be concise, with only the
most essential information featured in each slide. Too much
information means some conference call participants will read
the presentation more than listen to management.

It is not uncommon for newly-listed companies to use the slides
from the IPO roadshow presentation as a basis for creating the
presentation for their first earnings conference call. However,
when creating it, they should be mindful of any information
that has changed materially and be careful to adjust the
presentation accordingly.

Not all companies use a script for their earnings calls; however
it is considered a best practice. Using one helps ensure that
management’s explanation of the financial results is clear
and reduces the likelihood that a remark is misinterpreted by
an investor, analyst or journalist; this is particularly true for
executives who are not native English speakers. A script also
helps ensure that key investment messages are conveyed by
management during the course of their remarks.

Generally speaking, the structure and flow of the conference
call script should be mostly consistent with that of the press
release. Prior to the earnings call, the IRO, CEO and CFO
should sit in the conference room that will be used for the
earning call and rehearse the script in conjunction with the
slide presentation. The IRO should give feedback during the
rehearsal. All of this helps ensure that management’s remarks
are spoken clearly and come across naturally. Transitions
between speakers and use of the presentation will be
smoother too. Prepared remarks should not run longer
than 20 minutes, unless there is something particularly
unusual about the reported results or the company is complex
in nature. Regarding the latter two instances, other members
of the senior management team should be in the room during
the conference call, as they could be in a better position to
answer questions related to their specific work at the company.
It is not uncommon for the CEO or CFO to ask a division head
or the head of sales and marketing, or the person who leads
R&D, to answer a question asked by an investor or analyst.

The Q&A period of the earnings call

During the question-and-answer session, the second part
of the earnings conference call, investors and analysts are
invited to ask the senior management team questions. This
is another opportunity to help deepen their understanding
of your company. Call participants typically ask management
to elaborate on their explanation of the results, and the
information they seek can be quite detailed. Accordingly,
check with your legal counsel to make sure that divulging
material information not contained in the press release
would not constitute selective disclosure that could violate
securities regulations.

Often it is the sellside analysts who ask the most questions
and for the most detailed information. This is because they will
make even the smallest adjustments to their financial models
in order to fine tune their earnings estimates. In the U.S. equity
market, estimates are made on a quarterly basis, consistent
with the frequency of reporting required by the U.S. Securities
and Exchange Commission.

Your teleconference service provider should provide you,
via the internet, the names and affiliations of investors and
analysts who have indicated they wish to ask a question. The
IRO can then instruct the teleconference operator who can
ask a question during the time allotted for the call. Influential
analysts and major shareholders are usually given preference.
This is one reason to arrange a “com-line,” which is a separate
phone line that allows the IRO and operator to talk privately.
This line can also be helpful if technical problems arise during
the conference call.

It is important to try to anticipate the questions that could
be asked on the earnings conference call, particularly
difficult ones. Drafting in advance a set of potential questions
and answers to them helps senior management respond
to questions more clearly and concisely. If an executive is
inaarticulate or sounds flustered when answering a question,
investors, analysts and journalists might interpret this to
mean that he or she is not sufficiently knowledgeable about
the business or has concerns about the area of the business
to which the question relates. If a question is unclear, do not
hesitate to ask the investor or analyst to repeat or clarify it. If you are unable to answer the question, tell the person that you will call them later with the information they need; never make up an answer to a question.

Although rare, an investor could ask a question or make statements that are not relevant to the earnings call, perhaps with the intention of being disruptive. As such, it is generally inadvisable to take questions from investors with whom the IR department is unfamiliar. Consider calling the investor after the conference call to answer their question and to learn about them. If you are concerned there will be more questions than time permits, advise participants at the start of the conference call that each participant will be limited to three questions. If there is something unusual about your earnings announcement, such as significantly missing earnings or revenue guidance, consider extending the Q&A period to ensure that as many concerns are addressed as possible. Journalists should not be allowed to ask questions, in order to leave sufficient time for questions from investors and analysts for whom the earnings call is primarily intended. Also, a separate conference call can be arranged for the financial press.

If your company reports after any of its sector peers, listening to their earnings calls can give insight into the questions that investors and analysts might ask on your conference call, especially matters related to conditions and trends in your company’s sector. Developing a Q&A also helps ensure that the IR department gives answers that are consistent with management’s, when the department later receives phone calls from investors and analysts who were unable to attend the conference call.

Feedback improves preparation

A few weeks prior to the earnings conference call, consider calling key investors and analysts to ask them what key issues they would like management to focus on during their remarks. In addition to helping keep the conference call focused, this feedback can be used to develop the Q&A document discussed above. Also, obtaining feedback after the call can identify areas where future calls could improve and can be useful in preparing for non-deal roadshows that often follow earnings calls.

After the earnings call

A recording of the conference call should be made available, along with the slide presentation, on your company’s IR website. Most companies make these available on the website for one year. Be sure to consult your company’s legal counsel about how long an earnings call should be archived in order to comply with any applicable regulations.

Some companies also post a transcript of the conference call. If your company chooses to post transcripts on its website, be sure to review each of them, as they are created by the teleconference provider. For IROs new to earnings conference calls, these transcripts can provide instructive insights. They can also reveal some of the investors who attended your peers’ earnings calls.

Making your company’s earnings call available via podcasting is a best practice too. It allows investors and analysts to access it at their convenience, thus increasing the likelihood they hear management’s explanation of the most recent earnings results.

Scheduling your earnings call and inviting the investment community

Ideally, the earnings conference call should be held the day the earnings press release is distributed to the investment community. That way anything in the press release that might be misunderstood or misinterpreted can be clarified sooner rather than later, through the conference call. Earnings calls are typically held before or after the stock market closes, although this practice is becoming less common. The time zones in which your investors operate also need to be taken into account. Also, determine when your company’s competitors will hold their earnings call, as some of your investors and covering analysts may wish to listen to both calls.

Be sure to use a conference call provider that specializes in earnings calls and that utilizes operators who are bilingual. If your company hosts two conference calls—one in your native language, the other in English—the IRO should monitor both calls to identify any disclosure of material, non-public information on one call but not on the other. In such a case, the company should issue a press release containing this
information. If simultaneous translation is utilized, the IRO should monitor it for accuracy and make corrections as necessary. Consult your company’s legal counsel with respect to both matters.

Use as many communication channels as possible to distribute the earnings call invitation and be sure to update your investor and analyst list regularly. This helps maximize the number of investors and analysts who are notified and access the call. In addition to email and your company’s IR website, consider using social media channels such as Twitter. Be sure to include in the earnings press release the date, time and phone numbers of the conference call. All of the above should also include an internet link for the webcast of the earnings call.

The value of an informative earnings call

A well-executed earnings conference call helps investors and analysts see the business as management sees it, and increases the likelihood that they value your company close to its intrinsic value.

On a more practical level, it can also result in senior management (and the IRO) spending less time answering questions from individual investors and analysts after your company’s financial results have been published.

**STRUCTURE OF A TYPICAL EARNINGS CONFERENCE CALL**

- At the scheduled start time, the teleconference operator welcomes the participants and explains that after management has finished its remarks, the operator will individually introduce, during the Q&A period, investors and analysts who have questions
- IRO introduces him or herself and the members of the management team who are participating on the conference call. Any required legal disclaimers, such as the Safe Harbor Act, are stated at this time
- CEO and CFO make their prepared remarks, respectively
- Operator announces and begins the Q&A session, which runs until the conference call is scheduled to end or until the last question is asked
- CEO or IRO thanks the investors and analysts for participating and invites them to call or send an email if they have additional questions
CONDUCTING AN INFORMATIVE EARNINGS CONFERENCE CALL

KEY TAKEAWAYS

• By clearly and concisely elaborating on the information contained in an earnings press release, senior management can further investors' and analysts' understanding of the company via an earnings conference call.

• An important objective of the earnings call is to link the financial and operating results with the company’s long-term strategy and key business initiatives.

• An informative conference call can help prevent investors and analysts from overreacting to recent problems that senior management expects to be short-term in nature only.

• For a company that has recently gone public, its first earnings call is an important first step in building trust with investors and analysts.

• Webcasting a presentation as part of the earnings conference call can facilitate senior management’s explanation of performance results.

• Using a script for the earnings call helps ensure that senior management’s explanation of the financial results is clear and reduces the likelihood that a remark is misinterpreted, especially when they are not speaking in their native language.

• Anticipating potential questions from investors and analysts helps prepare senior management for the Q&A period of the earnings call.

• If a question is not clear, do not hesitate to ask the investors or analyst to repeat or clarify it.

• Gathering investor and analyst feedback prior to and after the earnings call enhances preparation and improves future calls.

• Be sure to use a conference call provider that specializes in earnings calls and that utilizes operators who are bilingual.
From a marketing perspective, the business and financial media can be highly efficient channels to broadly and effectively deliver a company’s investment story across multiple segments of the capital markets.

Savvy IR professionals understand that the effective use of media relations can help bolster their investment story and deliver it to a wider audience. At the same time, they are well-aware of the challenges inherent in working with the business and financial press. While media relations is substantially less expensive than advertising, where the cost of a single full-page ad in a major business publication can exceed $50,000, a company has little or no control over what a journalist actually writes or edits out of an interview. If the press is less controllable or predictable than other communications channels, why should media relations be a component of an investor relations strategy?

First, the business and financial press deliver important coverage of global markets and individual company performance, information relied upon by virtually every investor making portfolio decisions. Print, broadcast and internet media cast a wide net: watched and read by institutional and retail investors alike, the news media is a highly efficient way to simultaneously reach most buy- and sell-side professionals and the more than 80 million individual investors in the U.S. alone.

Second, the very independence of the news media is the reason it can serve as an effective third-party endorsement of a company, in much the same way the sellside does.

Whether you are beginning to develop your IR strategy or refine it, you need to understand your media options. While one might naturally gravitate to obvious media outlets like CNBC, The Wall Street Journal or the Financial Times, the competition to receive coverage by them is fierce. However, there are many other potential media channels you can leverage to raise your company’s visibility and deliver its investment story. How can you identify and capitalize on media opportunities? What are the potential risks? And, most importantly, how can you get started or increase your exposure via the press?

The opportunity and process

As part of an integrated investor relations strategy, a properly executed media relations program raises visibility—putting your company on the radar screen of institutional and retail investors and potentially seeding demand for your shares over the long-term. That said, generating such visibility requires consistent focus and dedication.

Unless your company experiences some extraordinarily positive or negative event that demands to be reported, gaining media coverage—and maintaining it over time—requires developing and sustaining relationships with reporters and editors by consistently giving them the stories and information their readers, viewers and listeners demand.

Just as a company develops a business and IR strategy, you will need to create a media strategy and plan. Further, your management team must be willing to commit their time to media relations, making themselves available for interviews and the preparations required beforehand.

The strategies and tactics employed by companies to win media coverage vary, but the fundamentals of each are generally similar.

Identify and develop your story ideas

Journalists and editors value business partners who have a clear story. Identify your company’s niche, pinpoint within your company compelling stories that make good ‘headlines’, and then be prepared to “pitch” a story idea quickly and concisely (via either email or telephone). To begin the process, consider:

- Does your company have an interesting investment story that will be relevant to the average investor?
- Is your company a leader or influencer within its sector?
• Can management share a fresh or innovative business lesson?
• Has your company overcome a significant business challenge?

Some examples might be technology leadership (think of Google), an innovative business model (such as eBay) or a company with a unique culture that drives performance (e.g., GE). A newspaper, wire service or broadcast outlet wants to be the first among competitors to deliver this type of information to their audience.

On the other hand, you may be fortunate enough to have a CEO or other leader who is either charismatic or has developed innovative solutions to manage the company. Prized for their entertainment and educational value, respectively, articles or broadcast interviews profiling such managers serve to heighten your company’s visibility as well as convey various aspects of its investment proposition.

Be a resource
What insight can your company’s management offer a reporter? Management may be able to provide subject-matter expertise on a particular industry, trend or topic, or they could offer valuable perspective on the potential impact of current events. Often, your company will gain the visibility you desire—among investors as well as other reporters seeking expertise and quotes—by becoming a recognized, quotable authority and “go to” source for the journalist. The latter could lead to your corporate story itself being published or broadcasted.

Work your way up
Start with smaller media outlets such as trade publications, widely read by sellside analysts. Focused on particular industries, these publications are generally friendly toward management.

Given their relatively narrow scope, they are continually hungry for stories and information sources.

News wires, such as Bloomberg, Dow Jones and Reuters, are also good options, particularly for reaching institutional investors. Increasing competition among the wires and rapid news cycles create a huge appetite for fresh information. Also, stories produced by the wires are regularly syndicated, sometimes appearing in major publications.

Focusing initial efforts on smaller outlets not only provides good practice opportunities for companies new to media relations, but can also limit potential harm to their reputations in the event mistakes are made. Using these channels is also a practical way to test the media’s appetite for your investment story or to hone it.

Sell your story with skill
When you are prepared with a compelling story and the fundamental skills required to pitch it, you can expand your horizons to the mainstream U.S. business and financial press. However, you will face fierce competition as you seek to secure coverage. Journalists and editors are constantly bombarded with emails and phone calls from companies, including your competitors, claiming to have interesting stories to share.

Be prepared, again, to be concise. Deliver your story in the first few sentences or seconds, treating the reporter as if he or she was a reader or viewer.

If your “headline” doesn’t grab and hold their attention, they will move on to the next potential story.

This is the point at which you may wish to enlist the help of a media relations agency whose experience and relationships can be leveraged to secure an interview. An agency may have advance notice of key themes or topics of future publications or broadcasts, or understand which type of story would interest which journalist. Going further, the best agencies will use their business and financial acumen to identify a good story within your company and articulate it in a compelling way to reporters.

The upside and downside of media exposure
No matter where you are on the media continuum, planning and preparation is essential to ensuring clear and consistent delivery of your investment story and its underlying key messages.
Media training will help your key spokespeople properly prepare for interviews by arming them with the skills to answer questions or redirect them in such a way to assure your core investment thesis is conveyed.

Rehearsals will prepare your management for the types of questions likely to be asked. In fact, while important for any media channel, rehearsals are absolutely essential for broadcast media. Posture, gestures and other forms of body language have as much impact on the viewer as the spoken word.

Awareness of potential pitfalls is important. The information your spokesperson presents will be combined with that of other sources and with independent research, both of which may bolster or invalidate the points that he or she has made. Part of preparation is considering how remarks might sound if taken out of context, or whether an answer may be used in unanticipated ways. Above all, what a spokesperson says must be consistent with what has already been communicated to investors via other channels, such as earnings releases and conference calls.

Communications protocols (as part of an IR Disclosure Policy) for interacting with the press will ensure that your company communicates consistently, preventing the unintended distribution of mixed, or conflicting, messages to investors and potentially causing an erosion of management’s credibility.

Finally, no media relations strategy is complete without a crisis communications plan. The absence of such a plan—or not deploying one effectively—is likely to make a crisis appear worse in the investing public’s eye. Being prepared to communicate effectively during a crisis can help limit the severity and extent of any negative coverage and may make a significant difference in the opinions of investors, customers and other key stakeholders. By sharing pertinent information in an open and timely manner—and therefore appearing in control of the situation—your company may gain the time it needs to overcome a crisis.

Focus on the benefits

While media relations is not without risk, a successful program can raise your company’s visibility and engender favorable views among investors as well as customers, prospective business partners and employees, among other constituents. In particular, your company’s presence in the press can strengthen its brand and boost employee morale, while positively impacting market valuation over time. Those valuable outcomes are well worth the time and effort required to make media relations an effective component of an IR program.

KEY TAKEAWAYS

- Media relations is an efficient way to reach and positively influence large numbers of investors in the U.S. and other capital markets
- The press can serve as a credible endorser of a company’s investment proposition
- Thorough planning and careful preparation are needed to effectively employ media relations
- Include in your company’s Disclosure Policy formal protocols for communicating with the media
Social media, such as Facebook, Twitter, Flickr, YouTube, blogs and message boards, have become an integral part of product and service marketing. But should public companies use social media as a channel for investor communications? One thing is certain: The buyside and sellside are increasingly using in their research process information about issuers that has been gleaned from social media channels. In a way, investors and analysts who consult social media are trying to get an information advantage and are not relying on company information and traditional news sources alone. One advantage is time—news of corporate developments can emerge sooner via alternative information channels, such as social media. Market-moving news about public companies is traveling at an ever faster pace and sometimes it is inaccurate.

Social media as an alternative information source

According to a 2014 survey of institutional investors and sellside analysts, conducted by the Brunswick Group, the investment community continues to look to companies as their primary source of information when making investment decisions and recommendation. However, according to Brunswick, investor and analyst interaction with digital media continues to increase in nearly all categories and deeper online engagement continues to drive investment action. The survey’s key findings include:

- 70% of investors believe the role of digital media will play a greater role in their future investment decisions
- 29% of investors are proactively following up on leads they initially found on micro-blogging services, such as Twitter
- Investors ranked information direct from companies higher than any other information source
- 35% of investors listed real-time subscription services, such as Bloomberg, as becoming more valuable for their work, compared to 22% in the last survey. Other information sources were ranked in the following order: analyst research, primary market research, online business media, print business media and digital media

Based on the findings of the survey, blogs are the most frequently used information sources among all social media. There are too many to list here, but an illustrative example is The Business Insider, a blog written by Henry Blodget, a former top ranked sellside Street analyst. Others include influential blogs aggregated on the Seeking Alpha website and postings on StockTwits.com. Following blogs were micro-blogging services, message boards and social networking sites.

Should social media be used for investor communications?

Because disclosure regulations vary by country and stock exchange, your company’s legal counsel should be consulted to determine if and how social media could be used for investor communications. In other words, there is not a single legal standard for depositary receipt issuers.

From an investor relations best practices perspective, the U.S. Securities and Exchange Commission’s (SEC) Regulation Fair Disclosure can serve as a useful guide. Reg FD, as it is commonly known, requires that material non-public information be disseminated broadly and simultaneously to the investment community. Generally speaking, social media is unlikely to achieve the goal of fair disclosure and therefore should not be used exclusively as a disclosure channel for material information. Also, it can be difficult to
determine conclusively whether some developments at a company are material in nature (see Whole Foods case below). Thus any decision about using social media for investor communications requires a great deal of circumspection.

Social media could be used to supplement legally compliant disclosure channels. For example, once material information has “cleared the market” and is definitively in the public domain, social media tools could be employed. A Twitter message, for example, could be used as an alert to let investors know that your company has announced a material development and could provide links to the official announcement.

Social media could also be used to augment the marketing aspects of an IR program. Some companies use blogs to reinforce or enhance their market position by demonstrating thought leadership in their sector. These are read by investors and analysts as well as by other key constituents, such as customers. Some corporate blogs are even directed exclusively at the investment community.

If you are considering an IR blog, it is important to remember that its content must be relevant and useful to investors and analysts. Avoid information overload and don’t stretch IR resources unnecessarily. As Sascha Bibert, senior vice president of IR at E.ON, notes, “Throwing more information at the analysts is not helpful. A company should structure its information in a way that makes it easy for the analysts to digest and use.”

How using social media for IR could go wrong

Whether it is the CEO or IRO writing a blog, training is essential, and strict regulation-compliant approval procedures and publishing protocols should be in place, as they should be for all forms of investor communications.

In August 2009, Dell Computer inadvertently posted on YouTube an interview of its CFO discussing second-quarter performance results, before the company had issued an earnings press release. By the time the company had disseminated the press release - which had to be done ahead of schedule - the stock had risen 6% on trading of 23 million shares.

In 2007, the SEC launched an informal investigation into anonymous messages, posted on a financial message board, by the CEO of Whole Foods, a publicly traded supermarket company. At issue was whether these postings were aimed at lowering the stock price of a company that Whole Foods sought to acquire. Whole Food’s case illustrates the importance of exercising care when using social media for investor communications.
IR BEST PRACTICES FOR SOCIAL MEDIA

Even well-intended use of social media could backfire and therefore necessitates careful planning for implementing it for IR purposes. Here are some tips to consider:

• Review your company’s disclosure policy to see if it is current with regard to social media

• Periodically remind employees that information disclosure is limited to designated personnel and that they should not talk with journalists or blog about the company unless authorized to do so

• Don’t ignore social media. Monitor what is being said about your company, especially commentators who could influence your company’s stock price. Software tools such as StockTwits Desktop monitor various information sources, including traditional media outlets, and help streamline the monitoring process. There are also monitoring services such as Sysomes

• Talk with your company’s media relations department about reaching out to influential bloggers, with the aim of influencing their views

• Keep abreast of new communications technologies and their implications for IR

• Make sure legal counsel reviews and approves the use of, and procedures for, using social media for investor relations purposes
INVESTOR MARKETING
In the global competition for investment capital, DR issuers increasingly seek opportunities to attract quality investors and diversify their shareholder base. Whether your company has a DR listed on a major stock exchange or a Level I ADR trading over-the-counter, employing a focused investor targeting strategy will help acquire and retain long-term shareholders, which can reduce short-term price volatility, increase DR ownership and improve your company’s market valuation over the long-term.

A successful targeting program allows Investor Relations Officers to first identify the most likely buyers from among the tens of thousands of institutional investors that make up the global equity markets, and then prioritize marketing efforts in order to make efficient use of corporate resources devoted to IR. Effective targeting enables an IRO to balance the limited time available from both senior managers and the IR team.

As an investor relations professional, your principal goal is to tell the right story to the right audience for maximum impact on your company’s market valuation. Investor targeting is focused on the latter part of this equation, helping create a better alignment between the shareholder base and the company’s fundamentals.

A company must continually cultivate new buyers. The analysis required to value a stock typically requires a great deal of time, and most investment managers like to follow a company and its management over time before making a buy decision. Consequently, an IRO shouldn’t wait for valuation problems to arise to begin searching for investors to replace those leaving the stock.

While targeting is a continuous process, there are five key steps:
1. Understand where your company is positioned relative to competing stocks
2. Identify underweight shareholders
3. Identify potential new investors
4. Develop an IR marketing plan and calendar
5. Measure progress

Within each step, a series of activities help IROs more clearly understand their prospective investor audience. Knowing your audience helps you shape a more focused investment thesis, the other key component of a successful IR program.

Understand where your company is positioned relative to competing stocks

Start by assessing where your company lies along the value and growth spectrum of the investable equity universe. You will want to assess your market valuation relative to competitors, utilizing key metrics such as Price/Earnings or Price/Book ratios. In addition, if you determine that your company is a “growth” play, understanding how your potential earnings growth compares to your competitors’ earnings potential is essential. On the other hand, if your company is a “value” play, it is important to recognize that your dividend yield will be a key return measure for potential, as well as existing, investors. These assessments will provide the basis for an investor targeting strategy that would be appropriate for certain types of investors. It is also important to understand how your company’s market cap and geographic region would be considered by potential investors. Investor research and sellside reports can provide valuable perspective when conducting the above analysis.

Next, evaluate the composition of the current shareholder base to understand the portfolio characteristics (e.g., investment styles, turnover, etc.) of this ownership and the desired degree of diversification. For example, broadening a highly concentrated shareholder base may foster stability in the share price.
Or, if the weighting tilts towards high-turnover investment managers, such as some hedge funds, targeting efforts may focus on cultivating long-term oriented investors. The challenge is to find the right mix of shareholders—you should seek to attract some short-term investors, with the aim of fostering liquidity in your stock, balanced with securing enough longer-term investors to help mitigate price volatility.

**Identify underweight shareholders**

Before applying the above analysis, examine your shareholder base again to identify underweight investors. These are shareholders that should own a greater number of your company’s shares, based on their holdings of peer assets. Such investors are a natural target, as they are already familiar with your company, yet are often overlooked by IRs who are unduly focused on top shareholders. Underweight investors are easy targets for an IR program, but how can you persuade them to take a more significant position? The answer lies in redirecting some of your attention to them and, in doing so, ensuring that you are effectively communicating your company’s investment thesis.

**Identify potential new investors**

Investment strategies vary among investment managers. Each manager has its own specific criteria. You can use publicly available information, such as 13F filings, and private information sources to understand their investment styles, regional focus, and preferred investments.

Software tools available from IR vendors can supplement and facilitate your analysis to identify those investors that are likely to be interested in your company’s investment proposition. Once complete, your targeting analysis will identify prospective investors who:

- own shares of your peers—those that operate in the same industry, have similar fundamentals, or are located in your geographic region.
- constitute the largest holders of DRs in your region, but have not invested in your company.

The next challenge is to locate the appropriate analyst or portfolio manager at each target institution. Bear in mind that Buy side analysts could be based in the region they are responsible for covering, even though the investment decision is made by portfolio managers in a different location. Consider consulting your company’s advisors and brokers to identify the specific person who should be contacted, which can save considerable time and increase the effectiveness of your marketing efforts.

**Develop an IR marketing plan and calendar**

For DR issuers, a focused marketing plan is extremely important, as geography presents another significant challenge to remaining at the fore of investor’s minds. Begin by tiering target investors according to total assets under management. Investors are commonly classified as Tier I, Tier II and Tier III, from largest to smallest. (passive investment managers are classified as Tier IV investors). Next, prioritize the investors within each tier, based on their importance (is this firm an existing shareholder or have they expressed interest in your company?), relative size, location and other key factors. Prioritizing targets gives you a strong foundation for a focused IR plan.

After prioritizing target investors, develop a plan of action to contact the appropriate person at each firm and build this plan into an IR calendar, one that should allot sufficient time for non-deal roadshows for senior management and the IR team. For example, you may wish to contact prospective investors by email or mail, providing an investor kit that contains your annual report, recent press releases, and other salient information. This is an efficient way to generate interest in your company and gauge how receptive target investors are to your investment thesis. Correspondence should be followed up with at least one phone call, as competition for investment capital is fierce.

Naturally, in-person meetings will be the centerpiece of your IR strategy. Once you have prioritized regions or cities, establish a schedule that allows interested investors to meet with senior management or members of the IR team. These meetings are particularly effective with investors located outside the major investment centers, as they are often overlooked during roadshows and thus appreciate the extra effort and travel undertaken by the company.
Meetings with large existing holders or Tier I investors require senior management’s presence. Institutional investors frequently rate in-person meetings with senior management as the single most important component of an issuer’s investor relations program.

You can also invite groups of target investors to tour your headquarters and major operations centers or to meet with members of the management team at an off-site location, such as a hotel. This approach maximizes management time while giving investors a broader view of how the company is run and also provides greater insight into some of the intangible assets that also make up your company’s value.

**Measuring progress**

With your IR plan activated, it is important to track and measure its progress. As a first step, incorporate metrics into the annual IR plan. Establish specific goals, such as the timing and number of senior management non-deal roadshows, the total number of investor meetings, as well as the key broker sponsored conferences you plan to attend each year. Incorporate specific action steps, such as updating investor presentations and maintaining or upgrading the IR section of the company website. Keep a record of each meeting, including notes on feedback provided by investors during conversations and on the topics covered, all of which will be invaluable when preparing for future meetings.

Many IR teams set targets for the desired diversification of their firm’s shareholder base. IR should establish goals for ownership by region and mix of shareholder types, as well as targets for growth and liquidity in the DR program, and develop an action plan in conjunction with the depositary bank to achieve these goals. Institutional databases provide valuable tools for tracking over time the composition of your shareholder base and which allow the IR team to monitor buying and selling by targeted firms. There are other sources that can yield insightful information, such as holdings uncovered by third-party shareholder identification services.

With regard to delivering the “right story,” you use your hard-won knowledge about target investors to better articulate your company’s investment thesis. As part of the evaluation process, it is important to assess how effectively your story has been delivered. Gather feedback from the investors you have met to gauge whether your investment story is clear and if it resonates with them. Use this feedback to refine your investor presentation and other forms of investor communications. It is also an opportunity to reveal information gaps, which can lead to a valuation discount.

Measuring the progress of the IR marketing plan also allows IROs to continually improve their investor targeting efforts. Setting clear objectives and goals provides a framework to measure the effectiveness of your targeting. It is a continual process. The pay off, though, is an investor base that is adequately diversified, which helps strike a balance between enhanced trading liquidity and short-term price stability.

**PRACTICAL TIPS FOR UTILIZING THE RESULTS OF TARGETING**

To secure meetings with institutions that your targeting analysis has identified as potential investors, an IRO has a wide array of options:

- Leverage brokers that cover your company, as well as IR firms, to organize roadshows to your priority regions. Using multiple brokers will help you cover a greater number of investors.

- Attend broker-sponsored investor conferences, where you have the opportunity to meet numerous investors individually during breakout sessions.

- Launch an “IR Only” roadshow to share your company’s investment story with prospective investors and determine if a meeting with senior management is warranted.
Not all hedge funds are the same

Much is written and said about hedge funds in the business and financial press. Hedge fund managers are often portrayed as shrewd investors who earn fortunes by making fast trades, shorting stocks, and shaking up the management teams and boards of public companies. Activist oriented funds, such as Greenlight Capital, Pershing Square Capital Management and Third Point, which have pressed for major changes at well-known companies like Apple, SONY and Yahoo, are widely covered by the media. Coverage of their activities tends to reinforce misperceptions and negative opinions of hedge funds. Consequently, senior management and Investor Relations departments tend to treat all hedge funds with suspicion and shun them. But not all hedge funds should be avoided. Indeed, some can be beneficial as shareholders.

Why hedge funds can be good targets

As is the case with other categories of institutional investors, investment strategies vary among hedge funds, as well as within them. While one hedge fund might employ an activist strategy another might be a pure value investor. Hedge funds also vary with regard to the assets in which they invest. In addition to stocks, they may invest in bonds, commodities or currencies, for example.

Short selling is among the greatest concerns companies have about hedge funds. However, hedge funds that undertake short sales might do so for hedging purposes only, instead of trying to generate an investment return alone. Also, a meeting with a hedge fund won’t necessarily lead the firm to short your company’s stock or sell additional shares short. On the contrary, a meeting could convince the firm not to sell your shares short or perhaps take a long position. Theoretically speaking, convincing an investor not to sell your company’s shares short has as much value as persuading the firm to buy shares. Most hedge funds, in fact, are long-only investors and some hold their positions for considerable periods of time. Moreover, the duration of lock-in periods of capital that hedge funds invest on behalf of their clients continue to expand, helping reduce portfolio turnover that can lead to share price volatility. For all of these reasons, hedge funds can be beneficial as shareholders and are therefore worth meeting during roadshows and at equity conferences. However, they should be carefully targeted as you would with any other type of investment manager, such as mutual funds, asset management firms and pension funds. In addition to activist-oriented hedge funds, there are four other general categories that together represent the bulk of capital managed by hedge funds: Global Macro, Event-Driven, Relative Value, and Directional. The latter is the type of hedge fund that is generally suitable for meetings, with either the IRO or a member of the senior management team. These firms have different investment styles (e.g. growth or value) and holding periods. And some have a particular sector or geographic focus. A thorough targeting analysis helps pinpoint which of them merit a meeting.

Another reason hedge funds can be good targets is they are often more knowledgeable about a company than other investors. That is because hedge funds typically manage portfolios with fewer holdings than traditional money managers. A mutual fund, for instance, may have holdings in as many as fifty or even a hundred companies. A higher level of knowledge means that hedge funds are often well prepared to meet with senior management and, more importantly, can value your company appropriately as well. It also means they can make faster investment decisions. In other words, a meeting can quickly result in an investment in your company, something every IRO hopes to achieve. Hedge funds are particularly adept at understanding complex equity stories that tend to cause a valuation discount.

The analysts and portfolio managers at hedge funds can also be an excellent source of sector intelligence for management, providing valuable information that can be incorporated into their decision making. Hedge funds also have a relatively greater appetite for risk and can therefore provide price support during periods of distress, when other investors are selling or unwilling to invest. Finally, given their relatively smaller size, hedge funds are better able to invest in shares and ADRs that are illiquid.
Hedge funds continue to attract more capital

In the aggregate, hedge funds manage approximately 3 trillion in capital, or 3.6 percent of equity assets globally. (among active investment managers, the percentage is higher at 5 percent). The level in 2005 was 2.8 percent, indicating that this class of investor is growing at a fairly steady rate. Ninety percent of hedge funds are U.S.-based, and 60 percent of the capital managed by all hedge funds is from the U.S.

According to Hedge Fund Research, Inc., investors allocated $3.6 billion of new capital to hedge funds in the fourth quarter of 2014, which brought full-year global inflows to $76.4 billion, the highest level of annual inflows since 2007. These inflows and performance gains increased total capital managed by hedge funds to a historic record $2.85 trillion.

Hedge funds also continue to grow in terms of size. While hedge funds used to be relatively small—most managing under a billion dollars in capital - today there are many sizable firms managing tens of billions of dollars. They include Bridgewater Associates, J.P. Morgan Asset Management, Och-Ziff Capital Management, Brevan Howard Asset Management, and BlueCrest Capital Management. In addition their ability to attract capital with their consistent investment returns, large hedge funds increasingly appeal to investors who seek to lessen risk by working with larger and more established firms. Exemplifying the scale that hedge funds have achieved is Pershing Square Capital Management’s recent $2.7 billion initial public offering. IPOs of this size were once the reserve of corporations or large private equity firms. As hedge funds continue to attract more capital, this category of investor will become more attractive to issuers who want to drive incremental demand for their shares and ADRs and who wish to further diversify their shareholder base. As noted earlier, a sound targeting analysis can help you determine which hedge funds are worth meeting. An equity sales team that covers investors at a local level, has established relationships with them, and therefore has detailed knowledge of them, can advise on which hedge funds would be interested in your company and which would make good shareholders. This highly effective combination of targeting analysis and market intelligence is available to J.P. Morgan’s depositary receipt issuers.
APAC EAUM is projected, by some estimates, to grow at approximately double the rates of assets managed in North America and Europe.

APAC institutions are expected to invest more capital outside their region in the coming years.

Asia’s rapidly growing pools of capital

In 2015, Asia-Pacific investors (APAC), excluding those domiciled in Japan, accounted for approximately 7% of all equity assets managed by institutions around the world. While this figure is small compared to equity assets under management (EAUM) in North America (67%) and Europe (22%), APAC EAUM is projected, by some estimates, to grow at approximately double the rates of assets managed in North America and Europe.

Also noteworthy is that APAC institutions are expected to invest more capital outside their region in the coming years. Currently, they allocate only 14% of equity assets abroad, as compared to overseas allocations of 18%, 43% and 47% by North American, European and Japanese investors, respectively. This implies that future investment in companies located outside APAC could increase substantially.

In Asia there are 50 funds with exposure to global equities, which is double the number of just 5 years ago. It should be noted that investors include not just institutions headquartered in Asia, such as Daiwa Asset Management, CIC of China and Temasek in Singapore, but also the Asian offices of Western firms such as Capital Research, Fidelity, MFS, Templeton and Wellington that manage the assets of their Asian clients. However, not all of the Asian offices of western asset managers allocate a significant portion of capital outside Asia, Aberdeen Asset Management being one example.

Attracting investment from APAC investors

In order to be best positioned to capture future growth in APAC’s EAUM, it is important to begin building relationships there now. Only 2% of the time that North American and European companies spent on roadshows in 2012 was in Asia, according to a recent survey by IR Magazine. This suggests that your company could have something of a first-mover advantage if it were to begin targeting investors in APAC today. It is also why some of our depositary receipts clients, such as Rio Tinto, Sanofi and Volkswagen, have based Investor Relations Officers in China. Other J.P. Morgan clients have listed in Hong Kong, such as Vale of Brazil.

In order to be best positioned to capture future growth in APAC’s EAUM, it is important to begin building relationships there now.

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1 As of September 30, 2014
Organizing successful APAC roadshows

Four to five days are needed to conduct an effective roadshow in the APAC region. The optimal cities to visit in the region are Hong Kong, Singapore, Kuala Lumpur and Sydney. Japan should also be part of the itinerary, given the size of this equity market and its investors’ longstanding appetite for foreign equities. Depending on how a roadshow is structured logistically, flights between these cities can be under four hours. Another capital market to consider is Seoul. Companies with a longer term view might also consider Beijing or Shanghai, but these cities should not be a priority, particularly with regard to management roadshows.

For initial investor meetings, we recommend using a senior Investor Relations Officer. Subsequent visits should be made by a member of your company’s senior management team. It should be noted that Asian investors are most interested in companies with market capitalizations greater than $5 billion.

An equity market that should not be overlooked

Given the rapid growth in APAC’s equity-dedicated capital and the emerging trend of allocating more capital abroad, the region should not be ignored by investor relations teams in Europe and Latin America. J.P. Morgan has operated in APAC for over 100 years. And in the past three years our firm has invested heavily in its Corporate & Investment Bank in the region, giving us an on-the-ground presence in its most important capital markets, unlike most other brokers. Our long-standing relationships and daily conversations with Asia’s largest equity and fixed income investors mean we understand their investment philosophies and are therefore well-positioned to introduce your company to them.

The optimal cities to visit in the region are Hong Kong, Singapore, Kuala Lumpur and Sydney. Japan should also be part of the itinerary, given the size of this equity market and its investors’ longstanding appetite for foreign equities.

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Source: Ipreo
Corporate sustainability
For decades, investors have used Socially Responsible Investment (SRI) as a broadly defined investment discipline. ‘Socially responsible’ is a label frequently used by publicly-listed companies in their annual reports and press releases. It stems from the belief that responsibility is a hallmark of quality. Initially, SRI centered on values and attributes of Corporate Social Responsibility (CSR): a form of corporate self-regulation that serves to uphold ethical standards and allay harm to society. There remains a notion that while SRI is ‘a good thing’, it can be sidelined during times of economic uncertainty. This is largely based on the misperception that the application of ethical principles to investing sacrifices return.

From SRI to ESG — Environmental, social and governance criteria
The global financial crisis and the economic downturn that it precipitated resulted in a call for ‘responsible capitalism’, accelerating the discussion around responsible and sustainable investment. As a result, the scope of SRI has significantly expanded to look beyond purely ethical motivations, encompassing ‘best-in-class’ companies with both sustainable and competitive advantages. This shift is reflected in a relatively new term that has entered the business lexicon: ‘Environmental, Social & Governance’ (ESG). ESG-focused investing is motivated by long-term financial performance. It is a framework aimed at capturing the effects of environmental, social and corporate governance factors on the risk-adjusted return of portfolios.

The approach of ‘integrating’ ESG criteria into investment decisions has gained popularity, as investors have started to appreciate that a company’s ESG record is not just important to investors concerned about the impact of its activities on society and the environment, but takes into consideration key factors that can have a significant bearing on a company’s bottom line, now and in the future. The core principle is that these companies are run by quality management teams whose operating perspective is wider, enabling them to more effectively mitigate business risk—such as litigation related to environmental damage or workplace hazards—as well as identify unique business opportunities.

The ESG movement can be traced to initiatives such as the U.N.—backed Principles for Responsible Investment Initiative (the Principles). Its goal is to help investors better understand the implications of sustainability. The Principles provide a voluntary framework by which investors worldwide can incorporate ESG issues into their decision-making and ownership practices. They reflect the view that ESG issues can affect the performance of investment portfolios and must be given appropriate consideration by investors if they are to fulfill their fiduciary duty—deploying shareholder capital effectively. Among investment managers and asset owners there are currently more than 1,200 signatories to the Principles.

Sustainability practices and reporting
An obvious fit for SRI portfolios are renewable energy companies. But what about other sectors, such as financial services, that may seek to limit waste and whose operations inherently have relatively limited environmental impact? In practice, each industry has its own set of sustainability challenges relevant to the businesses and communities through which it operates. Companies with proactive strategies in place to manage ESG risks and opportunities have the potential to be industry leaders with sustainable competitive advantages.

Sustainability and resilience are attractive traits for longer-term investors, including many pension and mutual funds. Investing in businesses that effectively manage ESG issues may help a pension fund protect against downside risk, while also benefiting in terms of stable—namely, sustainable—dividend flows and less volatile market values. A company’s cost of financing can also be affected by ESG-related factors. Firms with, for example, environmental concerns, have a significantly higher cost of borrowing and in some cases have difficulty attracting capital. This is due to the risk of litigation, clean-up costs, reputational risk and related revenue shocks. Correlations have been found between the effective management of ESG issues within high risk industries and lower-cost debt financing.

In response to ever-increasing shareholder scrutiny, companies are escalating their sustainability practices and related disclosures. A sustainability report enables companies to account for sustainable practices and evidence progress in this area in a way that is similar to financial reporting. Establishing
a sustainability reporting process helps management teams set goals, measure performance, and orchestrate change. The Investor Relations Officer (IRO) may be asked to contribute to this process, which includes setting up a reporting cycle and collecting information and performance records from across the entire organization. It is important that these efforts receive the support and commitment of management and the board, as senior-level endorsement is essential in order to make progress.

The Global Reporting Initiative (GRI), an independent institution, has established a reporting framework that helps companies effectively report on the economic, as well as the ESG dimensions, of their activities. GRI’s Sustainability Reporting Guidelines explain what companies should disclose, as well as how to disclose and manage the underlying process. Although GRI offers to check the extent to which Guidelines have been applied by a company, it does not police or guarantee the quality of all reports. The fourth generation of GRI’s Guidelines was launched in May 2013 to try to enhance the relevance and quality of standalone sustainability reports.

Integrated Reporting

In the past couple of years, there has been a sharpened focus on ‘integrated reporting’. It is defined by the International Integrated Reporting Council (IIRC) as “the language evidencing sustainable business”. Adopting this type of reporting is a means of linking business strategy with sustainable development by fusing content typically communicated in the annual report with that of the sustainability report. Good reporting, in this interpretation, is about providing a long-term perspective on how value is created. The IIRC has published a list of content elements that an integrated report should contain, including an organizational overview and business model, operating context, risks and opportunities, governance and remuneration information and future outlook.

Integrated reporting requires collaboration between the finance and sustainability teams, and if this does not exist in the company, the report can never achieve integration. Some question whether integrated reporting represents a revolution in reporting or if it is just the next phase in best practice—companies that have published an integrated report remain in a small minority. However, it is noted that the 2012 ICSA Hermes Transparency in Governance Award for ‘Best Annual Report’ by a FTSE100 company went to one such company, Johnson Matthey.

ESG Ratings, Rankings and Indices

There are a large number and variety of external ratings, rankings, indices and awards that claim to measure corporate sustainability performance. Stakeholders of all kinds increasingly rely on these ratings to help inform their decisions. But who are these raters and how do they go about their research?

There are more than 30 leading sustainability ratings agencies. They rely on companies for the inputs for their work, and thus need reported information to be robust in their analysis. For investors as well as other stakeholders, making comparisons between companies can be difficult, owing to a lack of consistency in performance measures, methodologies employed and ratings. To get more value from the process and results of ratings, it is critical for companies to understand how and why they are being evaluated and if the outputs are of high quality. Knowing who specifically is using the ratings can enable more useful responses and inform on the benefits of participation for the company. Ultimately, sustainability professionals within companies should be using ratings to identify strengths and weaknesses in order to drive change and engage their business colleagues; hence the actual engagement process (with challenging questions on the most material issues) will often be more valuable than the final scores.

Global indices, which have set standards for corporate performance and which become benchmarks for investors, include the Dow Jones Sustainability Indexes, the CIPS Sustainability Index (CSI) and the FTSE4Good Index Series. These indices are often used as a basis for creating index-tracking investments or fund products focusing on responsible investment, and are a helpful reference by which companies can assess their progress and achievement. In-house or affiliated research units undertake engagement programs with index constituents and contenders. In the most recent semi-annual review of the FTSE4Good index review, companies were removed for not meeting criteria on human and labor rights,
environmental management and climate change. Because these indices largely rely on data provided by companies, they may favor companies with the greatest capacity to respond to questionnaires and information requests. Also, companies with larger market capitalization values tend to be better rated in sustainability indices (such as Dow Jones’s) and thus are included to a higher degree.

**Responsible Investment**

Institutional investors are increasingly integrating ESG assessments into their investment process. Following the recommendation of a stock by the in-house sector analyst and prior to investing, the investor may conduct ESG quality reviews to understand how services, products and policies impact business opportunities and risks. These reviews often require the institution to contact a company’s executive management or board member in order to gain a better understanding of its approach to certain ESG matters. For institutional shareholders, dissatisfaction with a company’s policies may result in AGM and EGM votes against the company on ESG issues.

Research by the market intelligence firm Ipreo has identified over 500 funds globally that are specifically dedicated to SRI investment strategies. True to ESG principles, few of these funds are limited to pursuing ‘green’ investments only (such as solar power companies), and instead use a variety of screens to identify companies meeting their requirements.

Norges, the Norwegian sovereign wealth fund, heads the list of SRI investors by some margin. Over 90% of its portfolio is in SRI investments, valued at a total of £340 billion. A U.S. leader in socially responsible investing is TIAA-CREF, which manages the retirement funds of employees of non-profit organizations, such as educational and cultural institutions. Three of this investor’s value-oriented funds feature in the top 50 dedicated SRI funds by the number of holdings in companies. Its CREF Social Choice Account has assets under management of close to $7 billion and growing. TIAA-CREF partners with an independent investment research firm to determine which companies are eligible for investment. Constituents of the MSCI USA IMI ESG or MSCI World ex-US ESG Index are considered to meet the Fund’s ESG criteria. Companies are also evaluated on “the most relevant ESG issues for their industry group”.

New York-based Neuberger Berman Management was one of the world’s first institutions to offer socially responsible mutual funds among mainstream investment managers. It integrates social criteria into the investment process without outsourcing the analysis. Its Socially Responsive Portfolio, which invests in mid- to large-cap domestic stocks, as well as foreign companies, is one of the larger SRI funds by value ($1.7 billion). F&C Asset Management, which boasts the largest specialist Governance and Social Responsibility team in Europe, manages the CAF Socially Responsible Portfolio (SRP). The SRP, which holds U.K. and international stocks, does not invest in organizations that, for example, manufacture (or sell) arms, alcohol or tobacco or are involved in casinos and gaming. F&C holds close to $2 billion in SRI funds.

SRI strategies are also being adopted by firms that have not historically identified themselves as SRI. Signatories to the UN’s PRI Initiative, for example, are estimated to hold over $30 trillion of assets, representing 20% of the total value of global capital markets. They include not only the pioneers of sustainable and responsible investing but also more conventional investment firms that are beginning to develop SRI divisions or to analyze how portfolio companies’ ESG policies affect their financial returns. According to the U.S. Forum for Sustainable and Responsible Investing, more than one out of every nine dollars under professional management in the U.S. is invested according to strategies of sustainable and responsible investment.

Portfolio managers are evaluated on their ESG investment strategies in the same way that companies are rated on ESG practices and disclosures. As indicated by the investment consultant Mercer, which evaluates efforts to integrate ESG factors into core investment processes, Emerging Markets and Asia-Pacific portfolios had the highest proportion of top-rated strategies in 2012. It appears to speak to greater demand for broad sustainability considerations in these regions, perhaps given population growth and demands on resources. The lack of consistent and comparable data in some of these markets makes reliance on company governance and reputation, both linked to ESG, more important for investors. Among investment styles, hedge funds had the fewest number of top-rated strategies.
Through annual Responsible or Sustainable Investment Reports, institutions are reporting on how they put responsible investment into practice. Communication of this type is driven by new regulatory guidelines, such as the U.K.’s Stewardship Code, and by clients and pension fund beneficiaries, who demand to know whether their money is being managed responsibly. As of 2013 it is compulsory for all PRI signatories to complete and publish their responses to the PRI reporting framework. For companies, these reports provide useful insight into the priority interests, values and concerns of individual institutions. Since company engagement is often a vital area of investor research, the reports also inform on how the investor conducts analysis and discussion with boards and senior management.

A quick study of some recent Responsible or Sustainable Investment Reports reveals that remuneration features prominently among investors’ planning and board appointments are the other governance practices routinely under scrutiny, reflecting the broader scope of ESG relative to SRI. In terms of social issues, risks relating to supply chain management (particularly for the retail sector), labor standards and human rights have prompted investors to seek more information or actively engage with companies. The reports also indicate that investors continue to monitor companies’ progress on their greenhouse gas emissions, waste generation, and use of water, forest resources and chemicals. Investors who participated in a 2013 survey by J.P. Morgan’s Depositary Receipts Group cited efforts to address environmental issues as one of the main reasons they have a positive outlook on the Chinese government’s new economic policy agenda.

Summary

In the new era of ‘shareholder stewardship’, companies and investors face an increased responsibility to focus on sustainability issues. ESG factors are now a familiar part of the investment decision-making process, as portfolio managers query how risk and returns are affected by business attitudes and behavior toward the environment, community, workplace and shareholders. One of the biggest challenges of sustainability reporting has been the degree to which voluntary disclosures are accurate. Companies are encouraged to engage stakeholders in the development of their reports; stakeholders are persuaded to challenge reporting issuers on their sustainability goals and their reported performance. Those companies furthest along the sustainability reporting journey are effectively integrating stakeholder engagement into the reporting process.

The IRO has an integral role to play by providing reassurance to investors with regard to specific aspects of company behavior. This necessitates strong understanding of the key material risks that surround the business and the company’s approach to managing them. In response to shareholder campaigns for better practices, companies should be prepared to discuss concerns and, if need be, establish more stringent standards. Companies that recognize ESG issues in the world and exert a good-faith effort to address those issues in how they conduct business will be more sustainable than others and could be prioritized for investment capital allocation.
One of the most important investor relations activities for any public company is nondeal roadshows, during which senior management and the Investor Relations Officer (IRO) travel to meet with shareholders and prospective institutional investors. Over the course of several days or more, management and the IRO seek to strengthen relationships with shareholders and to convince other investment managers to take a stake in the company. Meetings take the form of one-on-one discussions in each investor’s office or group forums such as luncheons.

Retaining long-term oriented shareholders can reduce price volatility, while continually cultivating new investors helps generate incremental demand for shares as well as diversify a shareholder base.

**Preparing for a roadshow**

Whether conducting a nondeal roadshow independently or utilizing a broker or IR firm to arrange investor meetings, an IRO can maximize the chance for success by managing the roadshow process from beginning to end.

- **Have a plan:** As part of your annual planning cycle, develop an IR calendar that sets forth the various activities required to achieve the objectives of your company’s IR strategy. In the calendar, set aside time for management and IRO roadshows that reach different tiers of investors in different markets throughout the year. Using the results of comprehensive investor targeting is the best guide for planning roadshows, according to Kolby, who conducts targeting analyses on behalf of J.P. Morgan’s DR clients.

- **Mind the details:** Make sure flight arrivals leave sufficient time to reach each investor’s office. Also, ensure that hotel meeting rooms are properly equipped with audio-visual equipment and can accommodate all of the investors who will attend group breakfast and luncheon presentations. The more hands-on you are with planning and organizing roadshows, the better experience your management team and investors will have—ultimately benefiting everyone involved. Being involved in the organization process sends a strong signal to your brokers, who will then be more focused on ensuring the roadshow’s success. Also, give the brokers or IR firms enough time (more than two weeks) to arrange appointments with investors. That will get you in front of the right investors, not just those who are available at the last minute.

- **Be informed:** Prior to roadshows, give management investor profiles: briefing sheets that contain information about each institution’s size, investment strategy and style, peer holdings, etc. Ideally, management should also understand the disposition of each investor toward the company as well as potential questions they might receive (see ‘Obtain substantive feedback’).

- **Practice:** For management teams that are new to nondeal roadshows, rehearse presentations and investor questions as if for an annual shareholders meeting or earnings call. Investors are generally well prepared for meetings with management. So they want to go beyond your last earnings report to understand the nuances of your business and management’s priorities and plans.
Focus on the “right” investors and messages

Systematic investor targeting helps maximize the effectiveness of roadshows. Identifying investors that would have the strongest interest in your company’s investment proposition will make the best use of the time that senior management and the IRO devote to roadshows. If an issuer does not have targeting expertise in-house, the analysis can be performed by some IR firms. Your depositary can also be used as a resource.

Equally important is understanding what is most relevant to each investor on the roadshow schedule and focusing management’s discussion accordingly (see ‘Obtain substantive feedback’).

• ** Employ targeting:** Effective targeting identifies potential new investors outside the client bases of brokers that companies typically use to arrange most roadshows. Adding some of these investors to a broker sponsored roadshow expands the universe of prospective investors and could help expand the broker’s client base. Comprehensive targeting analysis will also seek to identify underweight shareholders (those that have the potential to buy more shares), which can help prioritize meetings with existing investors.

• ** Learn from past conversations:** If you know that a particular investor is concerned about certain issues, be sure to proactively address this subject during a meeting. Listening to investors and addressing their concerns helps build trust and sows the seeds for long-term relationships and holdings.

• ** Be straightforward:** Don’t be afraid to tell an investor “I don’t know,” if you are unable to provide accurate information in response to a question raised during an investor meeting. As long as the question concerns an obscure detail about the company and you supply an answer shortly after the meeting, an investor won’t hold this response against you. In fact, being forthright about not being knowledgeable about one or two small details indirectly conveys that your other answers can be relied upon.

Leverage all partnerships

Brokers are the most common and effective channel to reach investors and drive demand for a company’s shares. Beyond the roadshows they organize, the institutional salespeople at each brokerage firm covering a company’s shares regularly call their clients when there is a “buy” rating in place. There are other partners in the capital markets arena to help organize roadshows that will place management in front of as many of the right investors as possible. Each partner will likely have relationships with investors to whom your company could be introduced.

• ** IR firms:** As they don’t rely on trading commissions, IR firms can suggest investors to meet with beyond those who are existing clients of the brokers.

• ** Your depositary:** A depositary bank that has an experienced IR advisory team can provide important guidance about which institutions to meet.

Travel frequently and widely

For companies that are not global giants, retaining quality shareholders, maintaining a diversified shareholder base and sustaining a share price equivalent to intrinsic value requires being visible in the equity markets. This is particularly true when the capital markets are turbulent and investors are risk averse. IROs are similar to airline pilots in some ways—always there, but most critical during turbulence.

Staying connected to investors, keeping them informed, and remaining present and calm during volatility are the hallmarks of a strong management team and IRO.

• ** Divide and conquer:** While your senior management is meeting with current shareholders or large potential investors, an IRO can be meeting with smaller Tier II and III institutions and seeding the ground for future investment. Following broker conferences, IROs spend several days holding one-on-one meetings with investors.
• **Expand your horizons**: Go beyond the traditional names in each city to meet investors who hold DRs. A local broker is often your best guide to investors in any region of the world. Consider visiting smaller cities and different regions to augment your efforts in large investment centers. Investors located outside major capital markets give due consideration to companies that make an effort to meet with them.

• **Travel frequently**: Senior management should meet with key shareholders and prospects at least twice a year so senior management is demonstrating interest in the company’s owners and driving investor demand for the shares and DRs. Outside of roadshows and broker conferences, investor meetings can also be arranged around global business trips made by management. Often the IRO travels more frequently, acting as a missionary to broadly disseminate the company’s investment story well beyond current holders and prospective Tier I investors to smaller prospects located in places that are inconvenient to reach.

**Obtain substantive feedback**

As a best practice, IROs should gather investor feedback before/after roadshows. Gauging how well investors understand a company’s investment thesis and soliciting their opinions of it provides invaluable insight for future investor meetings and for other areas of an investor relations program.

• **Jointly develop questions**: Go beyond the broker's standard set of questions by working together to create a post-meeting questionnaire. A well-developed questionnaire will help glean from investors the information you need to refine the investor presentation and prepare for future meetings.

• **Follow up**: As soon as possible after each meeting, be sure the broker calls the investors for their feedback—positive or negative—regarding the company's investment proposition, such as the corporate strategy, strategic initiatives underway, management team, etc. As Paterson notes, this critical step is often overlooked and suggests confirming with the broker that feedback will be obtained.

• **Continuously improve**: In addition to assessing an investor’s likelihood to buy, sell or hold your shares, use investor feedback to determine if your company's investment thesis was successfully communicated and how its delivery could be improved in future meetings.

• **Track results**: Using available public filings and shareholder IDs, track buying and selling activity to measure the impact of past roadshows. However, an IRO shouldn’t always expect to see immediate results. Institutional investors can take months, and even years, before they become comfortable with your company and start building a position.

**KEY TAKEAWAYS**

- Utilize investor targeting to identity potential institutional buyers to complement a broker’s client base and to optimize management’s time devoted to nondeal roadshows
- Closely monitor and manage the planning and organization of roadshows, paying careful attention to details such as the timing of investor meetings and the particulars of hotel meeting facilities
- Leverage the investor relationships of all partners in the capital markets
- Meet with investors as frequently as possible to build relationships and maintain an appropriate level of visibility in the equity markets
- Gather investor feedback before and after roadshows, in order to prepare for investor meetings and improve future interactions
CHOOSING BROKERS THAT CAN OPTIMIZE NONDEAL ROADSHOWS

Bringing companies and investors together

A broker with a strong distribution platform can put your company's senior management and Investor Relations Officer in front of prospective institutional investors that can help optimize the company's market valuation, reduce price volatility, and maintain ready access to capital over time. Additionally, brokers offer varying ancillary services that can benefit an issuer. Like any good matchmaker, determining which investors a company should meet with requires knowledge of the institutional landscape, an understanding of broader market and sector themes, and insight into the company’s objectives. Accordingly, even companies with fully-resourced IR departments often utilize brokers to reach and attract investors. At J.P. Morgan, a rigorous approach to targeting is the foundation for organizing non-deal roadshows and other investor events. A number of factors are considered in the process, chief among them key underweight and non-holding institutions, those invested in the company's sector and geographic market, and the mix of long-only investors and hedge funds. The research analyst, institutional sales team, and regional corporate finance teams are also consulted to ensure that a comprehensive effort is made on the company's behalf.

Selecting the right brokers

Issuers regularly receive requests from numerous brokers seeking the opportunity to offer management meetings to their institutional clients. With limitations on management time, not all brokers can be accommodated, of course. This presents a challenge with regard to maintaining research coverage by brokers, as management meetings are an integral part of the value proposition that brokers offer institutional investors. Hence, over time many issuers alternate brokers to organize investor meetings for them.

TIPS

One of an IRO’s essential responsibilities is marketing the company to investors. Consider the following when selecting a broker to arrange non-deal roadshows:

- **Reputation**: IR peers at other companies are often willing to share the experiences they have had with individual brokers. Key attributes to consider are the number and quality of investor meetings and the smooth handling of logistics
- **Local distribution platform**: Brokers with a presence in local geographies may have deeper relationships with local investors
- **Analyst influence**: Generally, priority should be given to a broker whose relevant sector analyst is most influential among investors and have the highest independent ratings
- **Briefing information given management and the IRO**: Information such as an investor’s meeting style, investment holdings and opinion of the company help company representatives prepare for investor meetings and can increase the likelihood of success
- **Market intelligence**: Some brokers will let you know what market and sector activity their traders are seeing
- **Investor feedback**: This feedback can be valuable and is delivered as an unattributed report and reviewed by management to understand investor sentiment toward the company and its sector, and is sometimes presented at the company’s Board of Directors meetings. Some brokers offer this service, and the quality of feedback can vary. So ask a broker to provide examples of the feedback (with names redacted) it has obtained in the past
- **Trading market share**: This can indicate the strength of a broker's relationships with the buy-side community and hence its ability to successfully market your company to the greatest number of investors

1 To learn more about this subject, please refer to the chapter entitled: Investor Targeting Forms Solid Foundation for IR Strategy
2 To learn more about this subject, please refer to the chapter entitled: Perspectives: An Interview with a J.P. Morgan Equity Salesperson
3 To learn more about this subject, please refer to the chapter entitled: The Value of Perception Studies
To attend or not attend

A recent National Investor Relations Institute (NIRI) survey explored a range of practices that companies’ employ with regard to equity conferences, which are organized and hosted by brokerage firms. These conferences are typically thematic—companies that are showcased to institutional investors are from the same industry (e.g. healthcare or consumer products), country or region, or have similar market capitalizations or growth profiles. The former grouping is the most common.

Each year hundreds of equity conferences are held around the world, although the bulk of them take place in the U.S. and U.K., where nearly 75% percent of global equity assets are managed. The ability to meet many investors in one place and in a relatively short period of time is the primary benefit of participating in them. But the decision about which conferences to attend can be difficult for an IRO to make, because there can be so many from which to choose.

What other companies are doing

According to NIRI’s study, U.S. companies attend an average of 5.6 domestic equity conferences each year, spending an average of 10.05 hours per conference. At a conference, the CEO, CFO or division head will present their company’s investment proposition to a large or small group of investors, via one-on-one meetings with them, or by some combination of these meeting formats. 89% of the most frequent conference attendees are CFOs, while 78 percent are CEOs. IROs also represent the company, but their participation is usually limited to one-on-one meetings. Like investor roadshows, conferences are a significant time commitment to make, especially for senior management, who must also spend time traveling to these events.

Key factors to consider about attending an equity conference

There are a number of factors to consider when making the decision about which conferences to attend. First, there is the issue of timing. Generally, a company should not attend a conference that is held near the end of its reporting period, in order to avoid the risk of inadvertently disclosing material, non-public information during the conference, where numerous conversations with investors will take place.

Another particularly important consideration is the institutional investors that will be attending the conference. Ask the broker which firms have registered for the conference. Also ask for the previous year’s list of attendees to get a rough idea of the types and quality of investors that usually participate. When examining a list of registrants, you should be checking to see what percentage of institutions have medium- to long-term investment horizons.

Much like roadshows, firms with high portfolio turnover rates should be avoided generally. Any time that management spends with investors should be with those that not only have the potential to invest in your company currently but are likely to continue doing so over the long term. This factor is especially important for companies that are reliant on external sources of funding for growth.

Equity conferences can also be an opportunity to meet with current shareholders. If they are not located in or near the city in which the conference is held, some will invariably travel to the event, especially those located in smaller cities that companies rarely travel to. However, bear in mind that some top shareholders might expect senior management to meet at their offices and not at a conference if it is held in their city. Also, although sector analysts often attend conferences, portfolio managers do so far less frequently.

Whether an investor is a shareholder or a prospective one, it is important to understand why they would like to meet with senior management, in order to gauge their level of interest and thus the importance of the meeting. If you are unfamiliar with an investor with whom the broker would like your senior managers to meet at a conference, ask the broker’s Corporate Access team for this type of information, as well as data such as the size of the institution, peer holdings, portfolio turnover, etc. New York and Boston are home to the largest number of institutional investors and therefore host the lion’s share of conferences. Another benefit of attending conferences held in these cities is their close proximity to one another, which allows investors to easily travel to either one. For example, a Boston-based investor can take a flight to New York City in less than one hour.

The size of a broker’s client base and the reputation of the sector analyst are what often determine the level of attendance. However, be sure to alternate between conferences each year,
in order to gain exposure to different sets of investors. In other words, if you attend the same broker conferences every year, you will only see those brokers’ institutional clients. It is also important to alternate with regard to rewarding brokers for maintaining research coverage of your company. Apropos of research coverage, a company’s participation in a broker’s conference is usually dependent upon this.

The investor presentation

Participating in a conference requires a presentation, which can also be useful for one-on-one meetings with prospective investors. As with any investor meeting, the presentation should focus on your company’s growth opportunities and the strategy to capitalize on them, not its most recent financial results. The presentation should also address the challenges your company is facing.

Like investor roadshows, conferences offer little time to communicate your equity story. Accordingly, the presentation should be concise; supplemental information, such as technical data, can be helpful to explain certain things to investors, but it should be located in the appendix of the presentation or bound separately. When speaking at a conference, your CEO or CFO will only have a half hour to present. However, the one-on-one and small group meetings usually run for about 45 minutes to an hour. Small-format presentations are generally appreciated by investors, as they will invariably travel back to their offices with them. Also, be sure to post the presentation in the IR section of your company’s website, in order to make it available to investors who are unable to attend. For presentations delivered to a large audience, some companies will broadcast it via the website.

Other preparations to make

Most division heads are unfamiliar with investors and how to interact with them. Therefore, it is important to brief them in advance of any conference they will attend. In addition to reviewing with a division head the types of questions that could be expected from investors, it is important to caution them that impromptu conversations can take place during a conference, such as in hallways and elevators. Some investors can be aggressive in their line of questioning, potentially trying to get a manager to divulge material information that has not already been made publicly available. Lastly, be sure to schedule a break for senior management representatives during the lunch hour. They will invariably need the time to check emails and make telephone calls.

KEY TAKEAWAYS

- According to NIRI, on average, U.S. companies attend 5.6 domestic equity conferences each year, spending 10.05 hours at each conference
- Among those who attend equity conferences most frequently, 89% are CEOs and 78% are CFOs
- Generally, a company should avoid attending equity conferences near the end of its reporting period, to avoid inadvertently disclosing material, non-public information
- When deciding whether to attend an equity conference, it is important to know which investors will be at the conference
- For any investor that would like to meet with your company’s CEO or CFO, determine the nature and level of their interest
- Alternate between equity conferences each year
- The investor presentation used at an equity conference should be concise and focus on your company’s major opportunities and challenges, and the strategy to address them
- If a division head will attend an equity conference and is unfamiliar with this type of investor marketing, provide training to help them prepare

1 To learn about how to create an effective investor presentation, please refer to to the chapter entitled: Creating Effective Investor Presentations
Q. What are some of the things an institutional salesperson like you does that are not readily apparent to the companies you take on roadshows?

A. As one can infer from my title, my core responsibility is to sell written research produced by J.P. Morgan’s analysts to institutional investors. Within each research report are great investment ideas. It’s my job to bring those ideas to the attention of the analysts and portfolio managers at investment firms that are J.P. Morgan clients, such as mutual funds, pension funds and hedge funds; my clients are U.S.-based institutions and the research I sell covers Latin American companies. In my conversations with buyside analysts and portfolio managers, I add color to a research report. For example, I highlight for them the additional insights provided by our research, such as the dynamics of a company’s industry—the distribution channels and price points for its products and services, for instance—and the dynamics of the supply chain. Such insights can help them in their investment decisions.

Q. As someone who regularly talks with the people who make investment decisions, what investor relations advice would you give a company that has gone public recently?

A. Within the first six months after the IPO and every six months thereafter, senior management and the Investor Relations Officer (IRO) should meet with their new shareholders and with prospective investors. Without these meetings, shareholders can feel neglected or lose interest and sell their positions. Also, additional research coverage—from brokers that didn’t underwrite the IPO—is often driven by investor demand. So the meetings you have with potential investors can result in increased demand and increase the likelihood of new sellside coverage. More coverage, by the way, means more salespeople like me talking with investors about your company and driving demand for its shares and DRs. It’s a virtual cycle that can benefit a company’s share price over time. My other suggestion is if some of your shareholders are located outside major equity markets like New York, Boston and London, consider talking with investors via a telepresence system. Although most investors prefer in-person meetings with management and the IRO, they would rather hold a telepresence conference than not be able to talk with you at all because their offices are inconveniently located. Some large institutions, such as Principle Financial Group, for instance, are located in remote places like Iowa.

Q. Some IROs feel that a broker’s institutional clients take precedent over them. Presumably you take the company into consideration too when arranging meetings with investors.

A. Absolutely. We are always mindful that a company is spending its own time and money to do an investor roadshow. In fact, we always ask the IR team if there are specific investors they’d prefer to meet with; this is also true for equity conferences that we organize. We endeavor to arrange roadshows that have the right mix of investors and that will have maximum impact, in terms of maintaining sufficient investor demand and diversifying the shareholder base by adding investors to it. Our aim is always to strike a balance between the objectives of a company and those of the investors who are our clients. If the company is pleased with a roadshow, it increases the likelihood we’ll be invited to organize future ones, which we consider a privilege.

Q. What are some of the other broker best practices for roadshows?

A. Beyond providing written profiles of the firms that senior management and the IRO will meet with, a salesperson should be able to give insights into what the investor thinks about their company and its market, and what the investor’s concerns are, if any. Before a meeting, I also tell the company what it’s like to meet with a certain portfolio manager or analyst. For example, I’ll let management and the IRO know if a certain person asks questions in an aggressive manner or will bluntly challenge management’s assumptions. Some PMs and analysts can be the opposite—very quiet—which a CEO, CFO or IRO might interpret as indifference, if they don’t know this in advance. At a minimum, a salesperson should give the different responsibilities and titles of the people who will be in the meeting room.
Q. What sets J.P. Morgan apart from other brokers, with regard to investor meetings?

A. Besides the high quality of our roadshows, J.P. Morgan has a global distribution platform that enables us to introduce companies to investors located in a wide variety of cities in the U.S. and in other capital markets throughout the world. We can also introduce them to investors that don't have specific sector or geographic mandates for their portfolios. In other words, we have the ability to expose a company to a large universe of new investors across the globe. In addition to our breadth, we have depth, in terms of the number of colleagues whose relationships I can leverage on behalf of a company. If I don’t have a relationship with a specific fund manager or analyst within a large institution, one of my colleagues either does or can identify the right person to contact. We dig right down to the individual fund levels at the big firms.
Saving travel time and money

Meetings with investors are an essential step for a company to secure their investment. However, investor roadshows entail considerable travel, making them costly in terms of money and time; the latter is particularly true with regard to senior management’s participation. Moreover, companies are increasingly traveling farther afield to places like Singapore, Sydney, Brazil and the Middle East, with the aim of better diversifying their shareholder bases and seeking out incremental demand for their equity. In past years, videoconferencing was tried occasionally in lieu of traveling to meet with investors. But the technology had never developed sufficiently to serve as a suitable alternative for face-to-face meetings. With the advent of digital conferencing systems, such as Cisco’s TelePresence and Polycom’s RealPresence, companies are beginning to adopt virtual investor meetings in certain circumstances. The advanced technologies behind these services now provide clear images of people, allowing essential eye contact, and their voices are not delayed, enabling a natural, free-flowing conversation. In other words, it’s as if all of the participants in a virtual meeting are together in the same room.

When to employ virtual meetings

In the U.S., some of the largest investors are located in remote locations, such as Principal Global Investors in Iowa and Thornburg Investment Management in New Mexico. Many companies are surprised to learn that a fairly sizable institution is located in Alaska—McKinley Capital Management, which manages over $7 billion. As part of a roadshow that comprises important investment centers like New York and Boston, a company can set aside time to conduct virtual meetings that encompass remote investors like these, in order to take advantage of being in a closer time zone. However, virtual meetings should never be done at the expense of first-time in-person meetings.

As more institutional investors install digital conferencing systems, this alternative to in-person meetings is gradually becoming feasible.

As more institutional investors install digital conferencing systems, this alternative to in-person meetings is gradually becoming feasible. However, these systems are expensive and few investors have installed them to date, other than the largest institutions. As a result, the systems are far from being ubiquitous. J.P. Morgan has digital conferencing systems in most of its offices and these can be made available for virtual meetings between investors and companies. Besides a limited number of installations among investors, compatibility can be another challenge. That is to say, a company or broker’s system might not be able compatible with an investor’s virtual meeting system.

In addition to extending a company’s geographic reach, virtual meetings can be used to gauge an investor’s level of interest. Following a virtual meeting, senior management and the investor relations department might decide that an in-person meeting would be worthwhile. Virtual meetings can be beneficial in another way too. If the shares and ADRs fall to a certain price level, one or several institutions might wish to meet with management immediately. Using a digital conferencing system means a meeting could take place that would not have otherwise, and any subsequent investment could provide price support. It should be noted that a virtual meeting is far more appreciated than a conference call, especially when it concerns shareholders.
A more virtual future

Cisco and Polycom have introduced desktop versions of their virtual meeting systems. These are somewhat akin to Skype and are far more affordable than the more sophisticated systems found in conference rooms. Other alternatives have emerged recently, such as OpenExchange, which offers a platform that enables investors and companies to use existing devices such as desktops and laptops, as they can be compatible with each other from a technology standpoint. Thus, in the near future, more investors could be available via virtual meetings, small and mid-sized institutions in particular. Regardless of the adoption rate, it can be expected that investors will continue to prefer face-to-face meetings with companies, although those in hard-to-reach places will almost always find a virtual meeting an acceptable alternative.

“...virtual meetings should never be done at the expense of first-time in-person meetings. In addition to extending a company’s geographic reach, virtual meetings can be used to gauge an investor’s level of interest. Following a virtual meeting, senior management and the investor relations department might decide that an in-person meeting would be worthwhile.”
Giving investors a closer look at your company

An integral part of an institutional investor’s due diligence on a company is meeting with senior management, whether the investor is an existing shareholder or one contemplating an investment. Such meetings mostly take place during roadshows or at broker equity conferences.

Another forum is the Investor Day, also known as an Analyst Day. Held annually, these group events usually entail a half or full day of presentations by the CEO and CFO as well as executives just below them, such as division heads. For example, the head of R&D might present at the Investor Day of a pharmaceutical company. One hosted by a consumer products company might include a presentation by the head of marketing. Some companies even feature product, service and production displays, which is why some host Investor Days at their headquarters or operating facilities.

Investor Days also allow more time for senior management to discuss their company’s strategy, operating environment and competitiveness. Additionally, exposing investors and analysts to the next layer of management and giving them a closer look at a company’s products, services and operations all provide deeper and broader insights into a company’s business and, ultimately, its investment proposition.1

Organizing an Investor Day

The first step in organizing an Investor Day is to set a date. Once you have decided who will present at the company, you will need to find out the dates when they would be available to participate. Be careful not to schedule the event near the end of your company’s reporting period, because you do not want senior management to be subjected to questions by investors about pending financial results. Also, Investor Days should not take place soon after the earnings conference call, generally, as there will be some overlap in information other than financial results. Be mindful of major equity conferences for your sector or region too, as investors might prefer to attend these instead.

If the Investor Day won’t be held at a company facility, choose a central location that will be convenient for the greatest number of investors, such as a major capital market like New York City or London. Do not start the event too early in the morning, otherwise investors cannot fly in the same day.

Generally, it is best to use a hotel that has experience with investor events, as their staff members are trained for and familiar with them. Hotels also have the ability to serve meals and refreshments for large groups of people. If a luncheon is part of your Investor Day, it is customary for each presenter to host a table. Should your Investor Day require complex audio/visual equipment, consider hiring a firm that specializes in event production.

Invitations and press release

Endeavor to email invitations to investors and analysts as far in advance of the event as possible, as this will help maximize attendance. Some companies send a save-the-date notification two months before their Investor Day. If getting to the Investor Day will require travel by most investors, send an invitation at least 6 weeks in advance. In addition to the event’s date and location, indicate who from your company will present and at what time during the day. At least four weeks before the Investor Day, send the invitation, which should provide a convenient email- or internet-based mechanism to register or decline the invitation; your company’s marketing department might have software for such purposes. The following week another invitation should be sent to those who did not respond to the first one. Use emails returned as undeliverable as an opportunity to update your investor database, which should include targeted investors, as well as existing ones.

Several days after sending the follow-up invitation, you will have a near-final number of acceptances and thus know how many meals and refreshments will need to be served at your Investor Day.

In addition to creating name badges, use the registration list to calculate the number of information handouts, such as the presentations, agenda and speaker bios, to print for the event. Some companies make this information available on a USB device or the investor relations section of their corporate website. Gifts are considered unnecessary, although low-cost gifts are generally suitable for consumer products and retailing companies.

1 To see an example of an Investor Day agenda and executive presentations, go to: http://www.eastman.com/Company/investors/Pages/InvestorDay.aspx
In addition to the invitation, consider distributing a press release announcing the event (regulations might require such an announcement, so consult your legal counsel about this and all other aspects of your Investor Day). As a best practice for investor relations, your Investor Day should be webcast in order to give access to those unable to attend in person. Podcasts are welcomed by those who cannot participate via either means, due to a schedule conflict.

**Other considerations**

While members of the senior management team are accustomed to presenting to and interacting with investors and analysts, other company presenters, such as those referenced above, usually are not. Accordingly, set aside time with them to create and rehearse presentations. As with any investor event, try to anticipate questions that could be asked and make sure the presenters are prepared to answer them effectively. Legal counsel also needs to train them to help ensure that answers do not include material, non-public information; as a best practice, the Investor Relations Officer should monitor the Q&A periods that follow presentations, so a press release can be issued if such information is divulged (regulations might also require this measure).

Organizing an Investor Day is time consuming and can be complex with respect to scheduling and logistics. If your company has an events department or a marketing group that regularly plans and manages events, they could be a valuable resource. Alternatively, consider using an investor relations consultancy that has expertise in Investor Days. A well organized and executed Investor Day can be a highly effective way to update shareholders and sellside analysts and to communicate your company’s investment thesis to prospective investors.

**KEY TAKEAWAYS**

- Investor Days give senior management more time to present the company’s investment thesis and also expose the investment community to the next layer of management.
- These annual events are held at a company’s headquarters or operating facility or at an offsite location, such as a hotel.
- Investor Days give investors and analysts a deeper and broader view of a company’s investment proposition.
- Be careful not to schedule an Investor Day too close to your company’s earnings announcement and be mindful of broker equity conferences for your sector or region.
- To help maximize attendance, send invitations as far in advance as possible.
- Issue a press release to announce your Investor Day and make it available via webcast.
- Company representatives who do not interact regularly with the investment community will need help creating and rehearsing their presentations and should receive training from legal counsel.
- Review your planned Investor Day with your company’s legal department.
USING RETAIL INVESTOR SHOWS TO REACH RETAIL INVESTORS

A prevailing misperception among Investor Relations Officers is that only high profile or consumer products companies, such as GE, BP and Procter & Gamble, benefit from retail IR programs. However, a fair number of both U.S. and non-U.S. companies know from experience that marketing to retail investors is a sound investment of time and resources, not least because individual investors add relative stability to a shareholder base.

One of the foremost retail investor events in the U.S., one that is steadily gaining the attention of non-U.S. companies, is The Money Show, a trade show whose “buyers” are individual investors and whose “sellers” are public companies whose products are their investment stories. Like any trade show, there is an exhibition hall housing display booths of companies and market intermediaries, and each day there are a series of educational seminars and speakers who talk about market trends and investment strategies. Investors can also attend presentations by public companies.

Every year, four Money Show events are staged across the U.S., with sponsorship and support from major stock exchanges, investment advisers and software providers, to name a few. In February, this year’s Orlando show attracted more than 10,000 individual investors, who could avail themselves of over 340 educational workshops and panel presentations featuring a wide array of corporate speakers and investment professionals.

Attendees, many of whom command sizable investment portfolios, also visit the exhibition booths of numerous public companies within the large exhibition hall that serves as the centerpiece of the event. Other Money Shows are held in Las Vegas, San Francisco and Washington D.C., sequentially.

AAII (American Association of Individual Investors) and NAIC (National Association of Investors Corp.), two U.S. not-for-profit organizations made up of individual investors, hold similar events bi-annually and annually, respectively, the locations of which vary.

High attendance levels aside, the Orlando World Money Show is considered the signature event of the year for DR issuers focused on reaching U.S. retail investors, as this particular show has an international theme. Individual investors see some 70 non-U.S. companies exhibit at this event, and international investing was the subject of many of the workshops and panel discussions.

In addition to the scores of educational forums that attract individual investors to Money Shows, the event’s vast exhibit area accommodates booths, large and small, where Investor Relations Officers (IROs) share their companies’ investment stories alongside vendor booths showcasing everything from trading software to investment newsletters. During the four-day event, prominent Wall Street and business speakers also attract retail investors. Notable speakers in the past have included Vanguard’s John Vogle, Steve Forbes, investment newsletter luminary John Dessauer, as well as famous people outside the world of finance, such as former Speaker of the U.S. House of Representatives Newt Gingrich.

A consumer brand is not required for success

For Japanese manufacturer Nidec Corp., attracting individual investors is a challenge, and the Money Show is the optimal place for this issuer to reach and influence them, according to its U.S. IRO. As a supplier to electronics companies, Nidec lacks a consumer brand. Consequently, most retail investors are surprised to learn that Nidec’s motor and drive technologies are an integral part of their everyday lives, running inside numerous electronic products, such as iPods, DVD players, PCs and laptops. At the Money Show, Nagayasu-san spends most of his time pointing this simple fact out to them, which serves to quickly illustrate the company’s investment proposition.

“Our number one reason for participating at the Money Show is to market our ADRs to individual investors,” says Nidec’s U.S. IRO. “But it is also an opportunity for us to understand first hand what individuals think about Nidec, which helps us shape
our retail IR program. Being at the Money Show also helps me better understand the overall retail market, a key focus of our ADR program. Besides talking with individual investors, I can exchange ideas with peers who are also exhibiting.” In addition to interacting with investors at Nidec’s exhibit booth, IRO presents at J.P. Morgan’s panel events, which draws up to 150 investors (other presenters included CVRD, Petrobras, and Volvo).

Interest in international companies is rising in the U.S. among retail as well as institutional investors. With some 80 million citizens directly owning equities valued in excess of $5 trillion in 2008, the U.S. retail market is the single largest pool of equity capital in the world. For that reason non-U.S. companies see the opportunities available to them in broadening their retail exposure. Even a moderate effort can pay off, provided a retail program is sustained over time. There are a lot of high-net-worth individuals who attend the Money Shows—that is the main reason to participate in is these events. They attract a huge pool of capital.

Getting investors to understand a company’s basics, such as how it operates, is something IROs must do a lot more of with respect to the retail audience. Institutional investors are generally far more sophisticated and often possess fundamental knowledge of a company before meeting with its IRO and management. But the average retail investor often needs more basic information when first approached by an issuer.

At the Money Show, the two principle means for educating investors and telling a company’s investment story are handing out investor factsheets, annual reports and other information materials, as well as answering questions in the exhibit hall, either in the company’s own booth or within one of the stock exchanges’ booths. Many companies consider presentation panels as having the highest value, as investors who attend have particular interest in their industry, markets or technologies.

Find customers as well as investors

Besides market intelligence, another of the Money Show’s ancillary benefits is the potential to attract new customers. Many Money Show attendees are wealthy retirees and Baby Boomers, who are prized consumers as well as investors. The event is an opportunity to market its consumer products services, in addition to its shares.

Consistent participation needed

As is the case for other marketing tools employed to deliver a company’s investment story, repetition is required over time. Regular attendance at retail investor shows will make you better known among U.S. retail investors, especially if you do not produce a consumer product or service. With respect to foreign issuers considering the Money Show as part of a retail IR program, it is a good place for retail investors to discover new companies and learn about ADRs.

Retail investor shows are not necessarily for every company. If a company doesn’t have the resources, in terms of time and money, to attend regularly, participating won’t pay off. It requires a concerted effort over time. Like other areas of investor relations, you need to be consistent.

**KEY TAKEAWAYS**

- At over $5 trillion in size, the U.S. retail investor market is the largest pool of equity capital in the world
- The retail market can be a viable target for companies that don’t have brand name recognition
- Regular participation at The Money Show or AAII or NAIC conventions is an effective way to reach and influence individual investors
- Associated benefits of participating in these events include gathering informal market intelligence, sharing best practices, and potentially gaining new customers
RESEARCH
Shareholder IDs can reveal, at a given point in time, a meaningful percentage of the institutions that hold an issuer’s Depositary Receipts (DRs) as well as its ordinary shares. Knowing who your company’s equity holders are is the foundation on which an effective investor relations program is built.

Shareholder IDs are usually conducted on an annual basis. But some companies wish to know on a more frequent basis who their institutional holders are and how their trading activity is affecting their DRs and shares, in terms of price and volume.

A market surveillance firm can be retained to monitor trading activity in your company’s securities. While there are benefits in using a surveillance service, it has limitations.

### The issue of anonymity

Anonymity is the cornerstone of any broker’s relationship with an institutional investor. With respect to trading a security, one of a portfolio manager’s greatest fears is that their intention to buy or sell that security could be revealed prior to their trading order being executed. When this happens, other brokers and investors could use this knowledge to their advantage, potentially resulting in an unfavorable change in the security’s price for the portfolio manager. This concern is especially true for large institutions or those known to be particularly savvy investors, which are increasingly using so-called Dark Pools, among other off-market trading systems, to conceal their trading activity. Whether a portfolio manager wishes to buy or sell a security, their investment return (or potential return) could be eroded if other investors learn of that manager’s intention and subsequently trade ahead of his or her order.

Because of the anonymity afforded institutional investors, issuers do not know the identity of the institutions that are trading in their DRs or shares on any given day. This can be especially frustrating for companies that recently made the transition from being private to publicly-held. After all, a company must publicly disclose virtually every aspect of its business in order to issue stock, so it can seem unfair that the rules of transparency are not fully applied to the institutions that hold their securities.

For a U.S. company or foreign issuer with a Level II or III ADR program, the anonymity that brokers (and bank custodians) afford their clients means that the institutions behind trading activity and the composition of their shareholder base remain unknown until ADR holdings are revealed in quarterly 13F filings with the U.S. Securities and Exchange Commission (SEC). And even then, these filings would not reveal those institutions that bought and sold a company’s securities intra quarter. Furthermore, institutions have until 45 days after the end of each quarter to file a 13F, so the ADR holdings an issuer sees in a filing can be as old as 135 days. For issuers of Global Depositary Receipts, discovering who owns and trades them can be similarly vexing.

### What your depositary bank can and cannot tell you

Some DR issuers mistakenly believe that because a depositary bank issues and cancels DRs the bank can tell them which institutional investors are behind these transactions. This is not the case because nearly all issuances and cancellations are executed through brokers acting on behalf of their institutional clients, whose identity they do not reveal.

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1 U.S. investment managers that manage $100 million or more in securities are required to file with the SEC their equity holdings at the end of each quarter. A 13F filing is not required for Level I ADRs.
Also, depositary banks are not directly involved in the trading of DRs on stock exchanges or over-the-counter (OTC), nor are they told the beneficial owners of securities held at bank and broker custodians\(^2\). Furthermore, at J.P. Morgan, company policy requires that all client business is conducted with strict confidentiality.

A depositary bank can give an issuer client general insights into Issuance and Cancellation (I&C) activity. In addition to alerting a client to large DR transactions, the depositary should be able to help the client understand prevailing trading conditions and trends in their sector and the equity markets. It should also help the issuer distinguishing between fundamental I&C activity and that attributable to arbitrageurs and hedge funds seeking to exploit short-term market inefficiencies.

**Lifting the veil of secrecy**

Market surveillance firms utilize various information sources to advise issuers which institutions are most likely trading in their DRs and/or shares; in certain circumstances these firms can specify the actual investor behind a trade or series of trades. In addition to pronounced changes in price and volume, large block trades can prompt investigations, as these may also indicate significant shifts in the shareholder base. However, because block trades are so conspicuous, institutional investors are increasingly trading in small lots, even though this often entails higher trading costs.

The vigilant nature of market surveillance\(^3\) means that an IRO can be made aware of ownership changes long before institutions make their regulatory filings or the next periodic Shareholder ID is performed. Depending on an IRO’s information and internal reporting requirements, market surveillance reports can be delivered on a daily, weekly and/or monthly basis. Regardless of the frequency of reporting, whenever unusual trading activity occurs, the IRO would receive a phone call or email alerting them to this activity.

**How issuers use market surveillance information**

Beyond satisfying the natural curiosity of knowing which investors could be influencing a security’s price and volume, market surveillance can reveal to an IRO if an institution has bought or sold DRs or shares following a meeting with that investor, such as during a non-deal roadshow or a visit to the company’s headquarters. Convincing investors to buy a company’s securities is one of an IRO’s primary responsibilities, so this information can be particularly valuable to an IR program. Apart from buying associated with investor meetings, some issuers are particularly interested in knowing if an activist investor has taken a position in their company.

For an issuer with a shareholder whose large position represents a price overhang, being alerted to aggressive selling gives an IRO the opportunity to call that shareholder (if identified by the surveillance firm) and potentially convince them to stop (without revealing knowledge of the trading activity), i.e., re-emphasize the merits of the company as an investment.

Surveillance firms also alert an IRO to substantial price and volume changes in the DRs or shares of an issuer’s peers, changes which often follow corporate announcements, analyst ratings changes, and the release of economic data. This market intelligence is relevant, as the performance of a peer’s security could have an impact on an issuer’s DRs and shares. It should be noted that the expiration of options can also result in unusual trading activity.

Significant changes in your company’s DRs or shares could cause shareholders, as well as senior management, to be concerned. It is therefore advisable for an IRO to be prepared to answer any questions that could arise. When unusual trading activity occurs in a security, some shareholders will invariably call to make sure they have not missed a corporate announcement. If it is the CFO or CEO who inquires, a market surveillance firm can arm the IRO with information such as the likely buyers and sellers and the possible reasons for their trading. With respect to the latter, surveillance analysts periodically call institutional investors to obtain their views on a company and its sector.

\(^2\) The exception is non-objecting holders, who have granted the custodian permission to reveal their identity

\(^3\) Also known as stock surveillance
What to expect from market surveillance

Because market surveillance requires speed and generally utilizes fewer information sources, accuracy is inherently less reliable as compared to Shareholder IDs. Relatively speaking, market surveillance involves more guesswork as clues are analyzed to identify the most likely buyers and sellers of an issuer's DRs and shares. Bear in mind that surveillance firms rely on information such as DTC settlement and custodian bank lists, which take time to procure. Also, settlement of U.S. securities takes three business days. Accordingly, the more time that a surveillance firm has to conduct its work the more reliable its investigations are likely to be.

Much of surveillance's value is in being alerted to unusual trading activity as well as in knowing what could account for this activity other than trading related to changes in a company's fundamentals. Without it, an IRO may be uninformed until either regulatory holdings become public or a Shareholder ID has been performed. Also, because market surveillance entails continual monitoring of trading and settlement activity, it can improve Shareholder IDs in terms of the percentage of holders identified and the accuracy of the overall work. Accordingly, some issuers forgo these studies in favor of market surveillance, which could be considered a continuous Shareholder ID.

Recently, stock exchanges have begun offering market surveillance services. But an IRO does not need to rely exclusively on the exchanges, surveillance firms or DRX for market intelligence. An IRO should not hesitate to ask an institution to reveal its position (although it has no obligation to), particularly when an investor requests a meeting with management. And always remember that any trading information that a surveillance firm or investor provides should not be shared with anyone other than senior management.

Finally, it should be noted that the frequency of surveillance reporting can lead an IRO and senior management to become too focused on their company's ADR or share price and short-term trading activity—be mindful that it can become distracting.

EXAMPLES OF INFORMATION CONTAINED IN MARKET SURVEILLANCE REPORTS

- Price and volume data for issuer, peers and key market indices
- Most likely buyers and sellers
- Investor feedback
- Market and sector commentary
- Short interest
- Valuation comparisons with peers
- Analyst ratings
- Market maker activity

KEY TAKEAWAYS

- Knowing which institutions make up your company's shareholder base is crucial to maintaining an effective investor relations program
- Market surveillance alerts an IRO to unusual trading activity and can identify the likely institutional buyers and sellers
- Information gleaned from market surveillance can help an IRO be more proactive
- A depositary bank should be able to give an issuer client general insights into I&C activity as well as ADR trading
- Do not hesitate to ask an institution to reveal its holdings in your company
Shareholder Identification (ID) studies, which reveal institutional investors who hold a company’s shares, can play an important role in formulating or refining an investor relations strategy and program.

**The role of the Shareholder ID**

Every successful company knows that in order to win and retain customers it needs to understand them thoroughly. Public companies with effective IR programs apply the same approach to investors, with an emphasis on building relationships with them. But before a company can understand its shareholders, it must first understand who its shareholders are. While some countries, such as the U.S. and U.K., generally require institutional investors to disclose their shareholdings, the often limited scope and timing of this information can reduce its usefulness. In other countries, public disclosure of holdings is not legally required, leaving companies almost completely in the dark as to who owns their shares.

Shareholder ID studies can reveal a telling portion of the institutions that comprise a company’s shareholder base. The studies are periodically performed by firms specializing in this area of investor relations. Acting like police detectives, these firms draw upon various public and proprietary information resources to perform the often complex task of identifying shareholders to provide a reasonable snapshot of a company’s ownership mix at a given point in time. A final report would also include an analysis of the types of investors the company has been attracting and how this ownership has affected—and could affect—the share price and trading activity, in addition to providing other insight.

Beyond compulsory financial reporting, IR is a marketing activity. Ideally, a company should market its shares with the same vigor and discipline it applies to marketing its products and services. Effective marketing necessitates understanding your customers, and for an IRO this process begins with identifying which investment managers hold your company’s shares.

Shareholder IDs can be a key source of information when formulating or refining an IR strategy and plan. The studies can give insight into how ownership impacts a company’s market valuation. From a strategic perspective, the ultimate aim is to assess the quality of your company’s shareholder base and then endeavor to align ownership with your company’s fundamentals as much as possible. On a tactical level, an IRO and management need to identify shareholders so they can reach out to them and build relationships where appropriate. Some companies even contact shareholders who have been identified as selling, with the aim of stemming their price pressure.

With regard to attracting investors, the market intelligence gleaned from Shareholder IDs can also serve as an important starting point for targeting investors. Investor targeting can be an effective way to improve a shareholder base that has concentrated ownership levels or that lacks sufficient geographic dispersion among shareholders, as targeting can identify new investors as well as underweight shareholders.

Other ways in which Shareholder IDs are commonly used include flagging potential price overhang from concentrated ownership by one or several investors; detecting shareholder activists, as well as knowing which investors are likely to support a corporate action; and measuring the effectiveness of a company’s IR program.

**What to look for in a Shareholder ID**

The basic information that can be found in a Shareholder Identification report is a list of shareholders at the beneficial and fund levels (as opposed to share positions held by brokers, who are not the ultimate owners), although the percentage of institutions that can be uncovered, and what they actually hold, varies depending on a number of factors. Also, bear in
mind that some institutions, such as pension funds, employ sub-advisors, so investment discretion might not lay with the institution that has been identified as a shareholder.

The report should also give the distribution (usually depicted in pie charts) of investment styles (growth, GARP, value, core value, index) and trading turnover rates (high, medium, low, very low) within the shareholder base, as well as the contact information and location of the portfolio managers and analysts at the identified investment firms.

Equally important, the Shareholder ID report should give context to the ownership mix that has been revealed. In other words, the shareholder identification firm that performed the study should help the client understand how changes in the composition of its shareholder base have likely affected the stock price and trading volume during the specified time period and what the future implications of the current ownership mix are likely to be with regard to the company’s market valuation.

Regarding the latter, holdings by one or several institutions could, for example, result in significant price pressure if any of these firms were to sell large portions of their positions in a short period of time.

Some ID firms go so far as to contact institutions that have altered their positions substantially, in order to discreetly gather feedback that can help a company understand the reasons for an investment manager’s decision to buy or sell the shares. For example: Was a trading decision made because the shares reached a certain valuation level? Was it due to changing fundamentals at the company? Or was the firm rotating into or out of the company’s sector?

Data about trading activity in peers, broader market activity, derivatives trading, short interest and ratings changes can also give context to changes in a company’s shareholder base.

An ID firm should also alert its client to activist shareholders that it has detected, those who have a history of challenging company management and boards regarding financial performance or corporate governance practices. A significant position held by such investors, or by traditional corporate raiders, can be a precursor to a proxy fight or hostile bid—forewarned is forearmed. Identifying troublesome shareholders before they build a significant position or make their intentions known can buy a company invaluable time to locate advisors and prepare a communications strategy to effectively defend management’s corporate strategy. Conversely, some institutions are known to be consistently supportive of management, and it can be helpful to identify these investors as well.

Other ways Shareholder IDs can be useful

Monitoring the shareholder base can also help a company measure the effectiveness of its IR program. For an IRO, the findings of Shareholder IDs can answer questions such as: Are the investors that we have been courting buying our shares? Is the geographic distribution of our ownership sufficiently diversified, or are we relying on a limited number of equity markets for capital? Is the balance of DR investors at a level we planned? Are we attracting enough medium to long-term investors to help reduce price volatility?

Knowing if your company is attracting sufficient numbers of the right investors can be a key benefit of Shareholder IDs. For example, a fast-growing technology company should, in theory, have a preponderance of growth and aggressive growth investors in its shareholder base, as these institutions typically pay relatively higher price multiples for high earnings growth. If this company were attracting a disproportionate number of GARP (growth at a reasonable price) investors, its market valuation could be adversely impacted; it might also indicate that the company’s investment story is not fully understood. Such a situation could necessitate recalibrating the company’s investor targeting and the focus of its roadshows or investor communications.

With regard to investor targeting, companies often overlook their existing shareholders as a source of demand, a fair number of which could have the capacity to buy more shares. After identifying its shareholders, a company can then start determining which among them are underweight, using an analysis of relative peer holdings. Existing shareholders are frequently your best prospects, as they are already familiar with your company, management and its strategy, unlike other investors who would require time to get comfortable with your company as an investment. He therefore recommends redirecting some of the IRO’s and management’s time to meet with underweight shareholders.
When Shareholder IDs are performed

Typically, Shareholder IDs are conducted once a year. However, the shareholder bases of some companies shift more frequently, necessitating half-year or quarterly updates. Some companies utilize market surveillance services offered by a number of IR firms, in order to understand trading activity on a monthly basis, with some focused on daily and weekly trading activity. However, the accuracy and value of this short-term information is frequently debated by IR professionals.

Other sources of market intelligence

IROs do not have to rely on Shareholder IDs and regulatory filings alone to understand the composition of a company’s shareholder base. The picture improves the longer an IRO is at a company. Shareholders who are active investment managers will seek you out to request information or meetings with management, which can be one of your best sources of market intelligence. Occasionally these institutions will divulge their positions when requesting a one-on-one meeting with the management team. However, such disclosures are made under an honor system. Check the position you’re given against the Shareholder ID or other sources.

Over time, an IRO will naturally build up his or her own databank of the institutions that have held the company’s shares, visited headquarters, or met management during roadshows and broker conferences, all of which can give some indication of what your investor profile is most likely to be. Although a company can never identify all of its shareholders, even a partial picture of institutional ownership can be valuable to an IRO, and a variety of information sources can be used to gain such insight.
THE VALUE OF PERCEPTION STUDIES

Perception studies, which examine how investors view and value your company, as well as how well they understand its investment proposition are, in essence, market research, the findings of which should serve as the basis for setting IR strategy and measuring the effectiveness of a company’s IR program.

Perception studies defined

A perception study is a comprehensive analytical tool used by publicly traded companies to better understand how they are viewed and valued by the investment community. A study is typically based on phone interviews of a representative sample group of investors. These interviews are performed by an IR firm to gain insight on key issues affecting market valuation, such as the company’s strategy, its management team, the quality of communication with investors, competitive positioning, and valuation relative to peers.

Perception studies can employ a qualitative and/or quantitative approach. The former is more effective in terms of understanding what is behind investor views and valuation of a company, while the latter methodology lends itself better to benchmarking.

How perception studies are used

One of the responsibilities of the IR officer is to effectively communicate the company’s investment thesis, or story, to the Street and to ensure that it is clearly understood. However, if the strategy is not clearly articulated or the senior management team is conveying inconsistent messages, this may negatively impact your company’s stock. A perception study can help uncover these messaging problems and any misperceptions or information gaps that might arise from them. This insight enables an IR officer to proactively address these problems and make changes to improve overall communications.

Perception studies are important because they help you understand how investors perceive your company’s overall strengths and weaknesses.

Other forms of investor feedback

It is important to maintain a good dialogue with your shareholders, so that you receive feedback on a consistent basis throughout the year. Accordingly, you should also leverage sellside brokers that are able to provide constructive feedback following one-on-one meetings during roadshows.

This type of ongoing feedback is very valuable, but it is usually directly related to conversations that took place in the one-on-one meetings and may vary from broker to broker in terms of the quantity and quality of information provided. Also, investors tend to withhold information when speaking directly to the company, fearing they might offend and potentially lose access to management if they make critical remarks about the company.

An independent IR firm is often able to solicit critical views and, accordingly, obtain deeper insight that an investor would typically hesitate to share directly with the company. In most cases investors wish to remain anonymous, so they are free to be completely candid in their critique of a company, which is when you are likely to receive the most valuable feedback. So, a perception study differs from other feedback in that it will dig much deeper on many issues and will offer a comprehensive look at various elements—good and bad—of the company’s value proposition.
How deep should a perception study probe?
To be fully comprehensive, a study needs to cover most of the subjects that may influence an investor’s buy and sell decisions. These range from overall business strategy, valuation relative to peers, investor communications, level of disclosure, and exposure to management. On average, most IR firms that perform these studies will ask between 10 and 25 questions, sometimes more. However, the questioning will depend on what the IR firm is trying to uncover for its client. The questions need to be very strategic and should be tailored specifically to the company. It is the IR officer’s job to work closely with the selected vendor to make sure the questions will elicit valuable feedback.

Investors who should be contacted
Contact those shareholders holding the largest positions, among other investors, because they have the greatest influence on your stock price and are often most familiar with the company. You must be selective, though, considering that the number of interviews largely determines the price of a study. In addition to such holders, you will want input from investors who do not currently own your stock, but own the securities of peer companies. This can help you understand what’s driving their decisions and what may trigger them to buy your stock; bear in mind, though, that their level of knowledge of your company will often be relatively limited. In addition to investors, be sure to obtain sellside views of your company, as they are an important communications channel for your equity story.

How often should a perception study be performed?
I would recommend commissioning a study at least once a year. The first one will establish a benchmark, in terms of knowing how well investors understand your company and, ultimately, the effectiveness of your investor relations program at that point in time. Then, every year thereafter, you can measure progress on all relevant factors. In some instances, it may make sense to conduct studies more frequently, but it really depends on what is transpiring at the company. Most companies choose to conduct studies after the release of their annual results or around a major shareholder outreach event such as an Investor Day.

The IR officer should help the vendor develop the target list of shareholders and prospective investors to interview. Prior to conducting the study, sending an e-mail to target constituents can help secure their cooperation and will make it easier for the interviewer to solicit meaningful feedback. Lastly, you should make sure you are personally involved in developing and reviewing the questions to be used in the study. An incisive questionnaire is crucial to obtaining useful feedback.

How the study’s findings are reported
On average, these studies take between six and eight weeks to complete. You should receive, at a minimum, an executive summary highlighting key findings, recommendations on areas where you can improve based on best practices and full verbatim transcripts of each interview. It should be a robust document. Most IR vendors will present the findings to the IR team, and will even give an executive presentation to senior management and the Board of Directors, if requested.
OTHER
IR Officers (IROs) spend a good part of their time interacting with sellside analysts. So it is important for an IRO to understand the basic mechanics of financial modeling, to be familiar with the different types of valuation methodologies employed by analysts, and to know the primary objectives of sellside models. Understanding how analysts estimate target stock prices and arrive at investment recommendations can lead to more effective communication between a company and these highly influential market intermediaries.

**Building the model**

The top-down approach to financial modeling and valuation: from the economy down to the stock. Understanding a sector’s relative attractiveness in the current stage of a macroeconomic cycle and assessing a company’s competitive position within that sector are key to analyzing the attractiveness of its shares. This analysis is what ultimately leads to a Buy, Sell or Hold (on the absolute scale) rating, the end game of sellside models; alternatively, an analyst assigns the stock an Overweight, Neutral or Underweight (on the relative scale) rating. Sellside ratings and the equity research behind them influence the investment decisions of the buyside (institutional investors). The top-down approach to stock valuation, which combines elements of both macro- and microeconomic analysis, is thus frequently used by sellside analysts. The main steps for valuing a company using the top-down framework are as follows:

1. The starting point is a macroeconomic forecast (in the majority of cases on the country level), with the major inputs being GDP growth, inflation, currency exchange rates and government spending budgets. At most investment banks, macroeconomic analysis is conducted by dedicated analyst teams whose forecasts are used as assumptions in the financial models of equity analysts, who specialize in a specific sector of the economy, such as automobiles, software or consumer products.

2. The next step in the forecasting process is the industry (aggregate) model, which is constructed by the equity analyst. This model contains performance assumptions for the sector in which a company operates. Industry forecasts, such as aggregate revenue, are for at least the next three years. Assessing a company’s progression and potential within the sector reveals a gain or loss of the market share over time. This assessment helps the analyst understand its competitive strengths and ultimately forecast its financials.

3. The final stage in the modeling process is the company model, which the analyst uses to estimate a company’s future operating performance, such as revenue, earnings and cash flow. In its final form, a sellside model consists of pro forma income and cash flow statements and a balance sheet, which are based on the analyst’s long-term assumptions to project revenue and expenses as well as associated balance sheet measures.

4. The results of the company model, such as cash flow, are then used to derive a price (see valuation section below) for the company’s stock and, comparing it with the current stock price, assign a recommendation on the stock.

**Estimating a company’s valuation**

The final step in the valuation process for the analyst is to use the results of his or her financial model to estimate a company’s equity valuation (e.g., price per share), which is then compared to its market valuation (e.g., current price per share) to make an investment recommendation. Each valuation method has certain advantages and disadvantages. The most common equity valuation techniques are the following:
UNDERSTANDING FINANCIAL MODELS AND VALUATION

• **Valuation methods based on the present value of expected future cash flows:** These valuation techniques include widely-used DCF (Discounted Cash Flow) and DDM (Dividend Discount Models).

These methods take estimated cash flows (derived from financial models) and discount them to arrive at a present value for a company. They are considered the most comprehensive compared with other valuation techniques but are relatively complex. IROs should pay close attention to a number of inputs, including:

- Operating cash flows and other estimated financials, such as debt
- WACC (Weighted Average Cost of Capital)
- Terminal growth rate
- Target discount of preference shares (if any) to common shares
- Assumed currency exchange rate

If any of the above estimates depart significantly from the company’s internal model and valuation estimates, it could indicate that the analyst has not used (either inadvertently or intentionally) guidance published by the company or has mistakenly entered the wrong numbers into his or her model and valuation calculations.

• **Relative valuation techniques** (price multiples of key financial measures, such as P/E, P/B, P/S, etc.). The advantages of this technique include relative simplicity in terms of valuation and application, as well as the fact that these techniques allow for “market anchoring”—comparing a company’s valuation with peer or market valuations. These methods are not without limitations, however. For example, P/E or EV/EBITDA valuation approaches cannot be used to value companies with negative earnings. In other words, multiples of earnings can be of limited use during economic downturns or when analyzing “young” companies which have not yet reached the breakeven point. For IROs, examining an analyst’s relative valuation analysis can be insightful.

• **The hybrid approach** combines the above techniques in order to take advantage of the strengths of each, namely the methodological superiority of discounted cash flow methods and the proximity to the market and simplicity of relative valuation methods. When looking at hybrid models an IRO should pay attention to the weights assigned for each method used. The weightings will reveal whether the analysis is skewed toward a present value method or a market-oriented approach.

• **Alternative methods:** During the 2008-2009 market downturn, analysts were challenged to choose among valuation techniques. At one point, the cost of equity had quadrupled from normalized levels. Under such conditions, neither cash flow discounting or relative valuation techniques can be used to value companies. Alternative methods of analysis must be employed, such as price-to-branches or price-to-deposits (e.g., banks). However, under normal market conditions these valuation methods yield to the superior conventional techniques.

**KEY TAKEAWAYS**

• Understanding financial models and valuation methodologies can enhance an IRO’s communications with sellside analysts

• The top-down approach is one of the most common methods of financial modeling. This method begins with forecasting the economy and sector to which a company belongs, and then uses this analysis to model the company’s revenue, earnings and cash flow

• Valuation methods are employed next, the most common of which are DCF and DDM, relative valuation, or a combination of the two techniques

• The investment recommendations that evolve from financial modeling and valuation methods can have a significant influence on the decisions of institutional investors
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