



Compass Points: SOME ADDITIONS TO THE IR EVALUATION TOOLKIT

“The opinions that are held with passion are always those for which no good ground exists; indeed the passion is the measure of the holder’s lack of rational conviction.”

- Bertrand Russell

*Reviewing the efficiency and effectiveness of the messaging role in Investor Relations (IR) can be aided by several measurements discussed here. These evaluation tools attempt to measure the 4Cs of messaging: **clarity, consistency, compliance and credibility** and at the same time, effective messaging delivery. With these metrics companies can get closer to setting next year’s IR goals, expected outcomes and the resources necessary to make them happen.*

When it comes to the annual or semi-annual review of the IR function, the contribution of IR’s role to annual or long-term planning or the annual bid for funding, those responsible face a familiar set of challenges. IR must direct the communication of the company’s performance and prospects in ways that are clear, consistent, compliant and credible. The IR activities must result in the highest sustainable stock price deserved by the company’s performance and prospects. While that much is agreed, it is also important to ask whether IR activity has been efficient and effective. In what ways did the IR function get the company closer to those communications goals than would have occurred without any IR function? What are next year’s IR goals, what are the expected outcomes and what resources are necessary for success?

What follows describes five measurement devices that can assist IROs CFOs, CEOs and Board members when assessing the IR function. There are many excellent metrics in most company IR evaluations, but adding these measures may prove a useful addition to the evaluation toolkit.

AN INVESTMENT THESIS MAP

An investment thesis is a set of reasons for investing in the company. The first objective is to find the investment highlights in the company’s communications. Whether this proves easy or difficult will be a check on clarity. Make a table with each column headed by one investment thesis point. If there are more than ten points, a busy portfolio manager will not recall them. Ideally, there should be four to seven investment points. Next, make rows of communication channels and events at which you would disclose and discuss these thesis points. Examples would be in the 10-K, at the annual shareholders’ meeting, at an analyst day, in your investor presentation for conferences or non-deal roadshows, on your quarterly conference calls and on your website. Now, you will have a series of boxes in the table. For the column titled, “Dominant Market Share in Asia Widget Market,” for example, you will have a row for “Non-deal Roadshow Presentation.” In that box, apply a score from 1- 5 for clarity and profile. Is the point made clearly and forcefully in the presentation deck?

Once your table is complete, consistency of delivery will be readily apparent. If you show consistency of message across channels then you have reason to expect awareness of the point to show up in your annual or bi-annual study of investor perception. If there are weaknesses, then expenditure of resources to improve consistency is vital for next year’s IR plan.

This is a useful device because it is easy to create and it directly measures (albeit somewhat judgmentally) IR’s function as a clear, consistent communicator of the company’s performance and prospects. The IRO has plenty of tools at his or her command to improve performance (a re-vamped roadshow presentation, better liaison with marketing for future press releases, and so on).

Once you’ve applied scores for all fields, if the investment thesis map was full of “5s” in every box, then the job is being done well, operationally. If the company’s most recent perception study still reveals weak unaided recall of key thesis points, then maybe it is credibility that is the problem. Resources devoted to finding out why investors do not recall or, perhaps, believe you hold the “Dominant Asian Widget Market Share” may be in order.

AN ANALYST ESTIMATE DISPERSION ANALYSIS

This very simple analytical device can facilitate IR’s job of communicating the company’s performance, the reasons for it and the prospects. Sell-side analysts will publish their earnings models out one to two years, usually on a quarterly basis. The set of estimates from the Company’s analysts for any given period can be analyzed for dispersion by dividing the standard deviation of those estimates by the mean.

For example, for the year ending December 31, 2012, IBM has an analyst estimate dispersion of its earnings per share (EPS) of just 1%, suggesting a very tight dispersion. Hewlett Packard’s dispersion, in contrast, is 8%. When benchmarking, you may find comparison

Client - Analyst Estimates										
EPS (\$) FY 2012										
Analyst	Q1		Q2		Q3		Q4		Full Yr	
	New	Prior	New	Prior	New	Prior	New	Prior	New	Prior
B. RILEY	0.89	0.95	0.88	0.88	0.84	0.87	0.88	0.85	3.46	3.49
BOFA	0.89	0.84	0.80	0.80	0.87	0.90	0.85	--	3.50	3.45
DEUTSCHE BANK	0.88	0.88	0.88	0.92	0.91	0.95	0.94	0.97	3.61	3.72
EVERCORE	0.92	0.92	0.92	0.94	0.93	0.97	0.92	0.96	3.70	3.90
FBR	0.97	1.02	1.11	1.11	1.03	1.10	1.03	1.07	4.05	4.39
GUGGENHEIM	0.84	0.81	0.81	0.82	0.78	0.80	0.76	0.80	3.19	3.29
JEFFERIES	0.93	0.95	0.91	0.92	0.91	0.92	0.95	0.94	3.70	3.73
JMP	0.91	0.92	0.92	0.95	0.91	0.95	0.91	0.93	3.65	3.78
KEEFE, BRUYETTE	0.90	--	0.93	0.95	0.96	1.00	0.96	1.00	3.75	3.85
LADENBURG	0.90	1.00	0.92	1.00	0.93	1.00	0.95	1.00	3.70	4.00
MACQUARIE	0.81	0.80	0.77	0.72	0.74	0.72	0.73	0.71	3.04	3.00
RBC	0.98	1.03	0.99	1.04	0.98	1.03	1.00	1.03	3.95	4.13
STERNE, AGEE	0.94	1.00	0.93	1.00	0.95	1.00	0.93	1.00	3.75	4.00
STIFEL NICOLAUS	0.93	0.98	0.94	0.98	0.93	0.96	0.92	0.97	3.72	3.90
WELLS FARGO	0.91	1.00	0.92	0.98	0.92	1.02	0.92	1.00	3.67	4.00
WUNDERLICH	0.89	0.92	0.94	0.93	0.97	0.96	0.98	0.97	3.78	4.00
Mean	0.91	0.93	0.91	0.93	0.91	0.95	0.91	0.95	3.64	3.79
Dispersion	4.8%	8.0%	8.7%	10.2%	8.1%	9.7%	8.7%	10.0%	6.9%	9.1%

across industries is not as valuable as benchmarking against your peers or against your own historical track record, even so a number like 8% is likely to be quite high.

This device will lead the IRO to search for reasons for the dispersion. Is there perhaps one analyst who is way out of line? If there are several analysts in the high camp and several in the low area, perhaps this is an indication of poor clarity of messaging. Could this indicate that key buy-side analysts are similarly confused? Again, the IRO has many tools at their disposal to fix the problem – better scripting for quarterly conference calls, better responses during Q&A sessions, improved guidance, and so on. Or, is an analyst day required where performance and prospects can be re-messaged with all sell- and buy-side analysts in attendance? These are all important available channels to enhance future investor communications.

AN INCIDENT REPORT

A simple listing of failings in disclosure can be created to form an incident report. This is a very useful test for compliance. Like an accident report in a manufacturing operation, an incident report can measure any increase in the number of incidents and then call for investigation into the state of operations. Did the company receive complaints from investors that guidance was changed well after the company knew conditions had improved or deteriorated? Did any press releases have to be re-issued due to errors? Did the IR website malfunction or fail to be updated during the quarter? An honest assessment of the incidents' causes may lead to well-supported requests for increased IR resources or improved protocols (for information flow to and through the disclosure committee for example).

AN INSTITUTIONAL INVESTOR PROPENSITY CHART

Having checked for consistent, clear and credible messaging, it is important to deliver that messaging where it will make the most positive impact. This device can prove useful, again, because it is simple to calculate and easy to understand. There are many targeting services available some with a “black box” element that can be used instead of or in addition to this device. The objective is to see if a given institution is “underweight” your stock. The simple idea is that if an institution owns fewer shares of stock in proportion to its ownership of your entire peer group, then they are worth targeting with some extra effort.

For each of the major institutional shareholders of your peer group, including you, create a column of those names. Now create successive columns, each headed by the name of a member of your peer group, including a column for your own company. In each cell of that table make a calculation, as follows. Assume the first cell is the relationship between your company and Fidelity.

Take the dollar value of shares Fidelity owns in your company and divide that by the dollar value

Fidelity owns in all the companies in your peer group, including you. Let's say that produces a number like 0.3. In other words, 30% of Fidelity's holding in your industry is accounted for by its holding in your company. Then take your market capitalization and divide by the total market capitalizations of you and the rest of your peer group. Let's say the answer is 0.4. In other words, your company makes up 40% of the equity value of your industry. Now, divide the first number by the second and multiply by 100. In this case the answer is 75. This means Fidelity is "underweight" your company in comparison to its holdings in the industry.

Any resulting number less than 100, using the above calculation, is an indication of the institution being underweight your stock. There can be many reasons for this. When considering the reasons, the most important thing is to make sure the underweight stock holding is not caused by Fidelity's lack of appreciation of your investment thesis, a lack of the Company's attention to Fidelity, or a lack of your understanding of their investment process. An understanding and explanation of the numbers in this table will provide a very good narrative about the relative attractiveness of your company's stock in the minds of investors. Any numbers under 100 that are proving difficult to explain may well imply additional IR resources should be targeted to those institutions in the future.

Affinity Index						
Firm Name	Cliet	Comp 1	Comp 2	Comp 3	Comp 4	Comp 5
BlackRock	130	92	127	121	130	91
Vanguard Group, Inc.	147	117	155	146	150	72
State Street Global Advisors (US)	126	69	142	127	136	100
Fidelity Management & Research	56	283	71	18	144	28
Thornburg Investment Management	0	0	229	279	559	62
Waddell & Reed Investment Ngmt	0	434	0	0	0	0
Bank of America Merrill Lynch (US)	131	95	19	8	10	124
Wellington Management Company, LLP	53	14	170	139	894	8
Anchor Capital Advisors LLC	0	195	6	0	0	102
Jennison Associates LLC	0	0	0	326	550	72
TIAA-CREF	77	79	75	84	82	117
NFJ Investment Group LLC	0	0	0	0	0	185
Newton Investment Management Ltd.	0	0	0	0	0	185
Artisan Partners Limited Partnership	695	0	153	0	0	82
Morgan Stanley Smith Barney LLC	109	101	40	87	43	112
Legg Mason Capital Management, LLC	8	77	0	7	20	147
Goldman Sachs Asset Management (US)	2	2	2	0	1054	13
Credit Suisse Securities (USA) LLC	68	219	87	149	115	48
Morgan Stanley (US)	2	0	28	2	710	68

AN ANALYST OR SELL-SIDE MAP

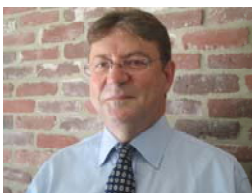
A good sell-side analyst can be very valuable in endorsing your company's investment thesis and putting you in front of investors with a high propensity to listen to your story. A simple way to determine whether you have the full complement of sell-side coverage is to arrange a table of successive columns headed by the names of the companies in your peer group. On the "y axis," or first left-hand column, list the names of all the analysts covering any member of the group. In each cell, place a check mark if there is coverage. When the table is complete, it is easy to tell if you have "gaps." If, for example, the analyst at UBS covers all of your peers but not you, then an understanding of the situation is required. Again, there could be many

reasons for the absence of coverage, but we want to make sure that it is not due to lack of marketing by IR, or lack of understanding by the analyst of the attractiveness of your story with investors. Again, any unexplained gaps may well demand more IR resources and attention in the upcoming year.

SAMPLE ANALYST MAP								
BROKER	ANALYST	CLIENT	CO 1	CO 2	CO 3	CO 4	CO 5	Total
BARCLAYS	B. Harting							1
BGB	M. Ross							6
B of A-MERRILL	K. Bruce							3
CITI	D. Fandetti							2
CREDIT SUISSE	D. Harter							3
DEUTSCHE BANK	S. Laws							6
FBR CAPITAL	G. Poggi							5
FLAGSTONE	C. Faems							4
J.P.MORGAN	A. Wessel							2
JEFFERIES	D. Furtado							3
JMP	S. Delaney							6
KEEFE, BRUYETTE	B. George							6
MACQUARIE	M. Howlett							6
PIPER JAFFRAY	R. Napoli							1
RBC	J. Arnold							5
SANDLER O'NEILL	M. Taiano							6
STERNE, AGEE	H. Coffey							6
STIFEL NICOLAUS	M. Widner							6
WELLS FARGO	J. Shanahan							1
			12	12	11	11	14	18
PRIMARY TARGET								
SECONDARY TARGET								

In summary, it is not always easy for those responsible for the success of something as important as investor relations to communicate their need for additional resources or management attention. These very simple devices have the merit that they are easy to create, easy to understand and can be very helpful to IROs, executives and Boards in discussions about the effectiveness of the IR function from quarter to quarter.

A version of this article was published in Financial Executive, April 2012.



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