

the voice of the investor relations profession

THE
**SHAREHOLDER
 VALUE MYTH**

HOW PUTTING
 SHAREHOLDERS FIRST
 HARMS INVESTORS,
 CORPORATIONS,
 AND THE PUBLIC

LYNN STOUT

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INSIDE**



22 Rational Investors Vs. the System

69%

Percentage of the global buy-side that believes activist investors are a positive force in the equity markets.



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About NIRI

Founded in 1969, the National Investor Relations Institute (www.niri.org) is the professional association of corporate officers and investor relations consultants responsible for communication among corporate management, shareholders, securities analysts and other financial community constituents. NIRI is the largest professional investor relations association in the world, with more than 3,300 members representing over 1,600 publicly held companies and \$9 trillion in stock market capitalization. NIRI is dedicated to advancing the practice of investor relations and the professional competency and stature of its members.

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Time to Start Reconnecting

The New Year has only recently gotten under way, but after going through an earnings cycle ... and for many of you going through the troughs of fiscal year-end reporting ... it feels like 2014 started a very long time ago.

Regardless how the market and your analysts are treating you, this is the season to start reconnecting with your NIRI colleagues, attending chapter meetings, comparing best practices, and polishing your IR program plans for the year.

IR Update is another great source of new ideas and best practices you can incorporate into your program. In this issue, you will learn what some IROs are doing to influence the number of sell-side analysts covering their companies (I have a few I'd be happy to donate to those looking for more coverage!).

This issue also features an in-depth interview with Lynn Stout, who believes that shareholder value is a myth and has written a provocative book about that issue.

You'll also find a timely article on investor relations in the insurance industry. Health care insurance has, and will continue to be, a hot topic in the U.S. media, but with the number

Regardless how the market and your analysts are treating you, this is the season to start reconnecting with your NIRI colleagues, attending chapter meetings, comparing best practices, and polishing your IR program plans for the year.

of natural disasters and unfortunate accidents that affect so many of us each year, I think you'll be able to relate to this article in both a personal and professional way.

This is also the time of year to make your plans to attend the NIRI Annual Conference in June. The Annual Conference Committee is hard at work preparing an exciting and informative educational program to match the excitement of holding the event in Las Vegas. Block the time on your calendar and register now (www.niri.org/conference).

Please feel free to call or e-mail me with any questions or thoughts you have about NIRI. Also, please know that your board of directors and staff are working hard to further NIRI's mission of "advancing the practice of investor relations and the professional competency and stature of its members."



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SHAREHOLDER VALUE: A MYTH?

Corporate governance expert **Lynn Stout** discusses why the shareholder value movement is an alarming mistake.

By Matt Brusch





Professor Lynn Stout



“Shareholder value is the dumbest idea in the world.”

This quote from former shareholder value proponent and former GE CEO Jack Welch is the title of the introduction to **The Shareholder Value Myth**, a provocative book by Lynn Stout, distinguished professor of corporate and business law, Clarke Business Law Institute, Cornell Law School.

Attendees at the 2013 NIRI Senior Roundtable were fortunate to hear Professor Stout's arguments for debunking “the shareholder value myth” in her session on that topic. *IR Update* chatted with Professor Stout following her session to learn more.

IRU: Why did you write this book?

Stout: I wrote the book because I've come to the conclusion that running a company strictly to maximize shareholder value as measured by share price is harmful to shareholders. There is alarming evidence to support this, and we've all seen it.

American companies are disappearing. There are 50 percent fewer publicly held companies than 15 years ago. The life expectancy of large corporations has declined – from 75 years in the 1920s (for Fortune 500 companies), to 15 years today, and falling. ROI, by many measures, has seriously declined over the past 20 years. So this says to me that embracing shareholder value has not led to better results for shareholders as a class over time.

I believe that shareholder value thinking leads management teams to focus primarily on quarterly results, and discourages the type of research and development and capital investments necessary for long-term corporate health. I contend that the shareholder value doctrine jeopardizes employees, consumers, and our communities as well.

This is all critical in understanding that the notion is false that corporations ought to be run to maximize shareholder value.

IRU: It is quite a leap from suggesting that shareholder value isn't necessarily the best business strategy, to declaring that it is false. Aren't boards required by law to maximize share price?

Stout: This is a hard pill for many of us to swallow because shareholder value is a

cherished myth, as you've just reiterated, but it is false.

U.S. corporate law does not, and never has, required corporations to maximize either share price or shareholder wealth. As such, boards are not required to maximize share price or profits.

Proponents typically cite *Dodge v. Ford Motor Company* as the case law supporting shareholder value. This nearly 100-year old case – from a state that is relatively unimportant in corporate law (Michigan) – is actually not even about corporate purpose. In fact, the state that *does* matter in corporate law – Delaware – has never cited *Dodge v. Ford* with the proposition that boards must maximize profits and share price.

In more recent cases, Delaware courts have held that, under normal circumstances,

the “business judgment rule” applies to board decisions, and the business judgment rule gives directors wide latitude in their decision making. Shareholder value maximization is a choice, not a legal requirement.

The argument that this is the best way to run companies from an economic perspective is also wrong. To grasp this, you must understand that shareholders don’t own corporations. I know that based on what we’ve all been taught it sounds like heresy, but U.S. law states that, in fact, corporations are legal entities that own themselves.

The Supreme Court’s 2010 *Citizens United* decision correctly reminded us of this. Corporations own themselves, and the profits earned belong to the corporate entity, not the shareholders. Shareholders simply own a contract between themselves and the corporation.

Many also believe that shareholders are the corporate principals and directors are their agents. This is legally incorrect. Shareholders do not get to control directors, and such control is one of the hallmarks of a principal-agent relationship. Corporate law is very clear that shareholders cannot tell directors how to run the firm.

Another mistaken assumption is that shareholders are the residual claimants in corporations, meaning they are entitled to all profits after the business has met its basic legal obligations. The bottom line here is that the corporation (rather than the shareholder) is its own residual claimant, and the board may exercise its discretion in determining what to do with the corporation’s residual.

This is an *extremely* abridged version, and I encourage anyone interested to read the book for a more comprehensive discussion.

IRU: What led to this movement?

Stout: It hasn’t always been this way. To be sure, since the birth of U.S. public companies in the early 1900s, there has been a debate over the proper purpose of

Another mistaken assumption is that shareholders are the residual claimants in corporations, meaning they are entitled to all profits after the business has met its basic legal obligations.

these corporations. On one side are “shareholder primacy” proponents who hold that publicly held corporations should serve only the shareholders’ interests, and directors and executives should focus solely on maximizing shareholders’ wealth through dividends and higher stock prices.

On the other side are those with a “managerialist” view who believe that corporations have a broader social purpose beyond simply maximizing shareholder wealth, a purpose that includes serving the interests of other stakeholders such as customers, employees, and society as a whole. The managerialists had the upper hand in the first half of the 20th century.

But in the 1970s, prominent members of the so-called Chicago School of free-market economists began again arguing loudly for shareholder primacy. As others began piling on, the movement took hold across academia, business schools, government regulators, and ultimately, corporate boardrooms.

This thinking has been very influential over the last 20 years. Everyone’s been taught shareholder value maximization, and we’ve changed the law and business practice to move in that direction. For example, Congress changed the tax code to require executive pay to be tied to an objective metric, and everyone picked stock price as that metric. The U.S. Securities and Exchange Commission (SEC) has implemented a number of changes designed to give shareholders more power over boards and make it

easier for them to cooperate with each other to vote. We’ve also seen corporate boards and management teams embrace shareholder value ideology over this period.

So, as a result, we should be seeing more corporations that are more profitable, people flocking to the United States to form companies, and investors experiencing higher returns, right? The reality is that we are, unfortunately, left with the very disturbing real-world results that I’ve already described.

IRU: How do you recommend we fix this situation?

Stout: Corporate boards and management teams must move beyond a single-minded focus on share price. The assumption that raising the stock price will please all shareholders is a fallacy because it assumes that all shareholders have the same objective. Investor relations professionals know, possibly better than anyone else, that this is not true. Just as there is no single investment style or investment objective, there is no single metric (i.e., stock price) by which management teams should be measured.

The award-winning documentary, *The Corporation*, argued that because corporate managers believe they must maximize shareholder wealth, a corporation is a “psychopathic creature” that can “neither recognize nor act upon moral reasons to refrain from harming others.” Now, some investors may be psychopaths who aren’t concerned if corporations engage in behavior that

exploits child labor, deceives consumers, harms employees, pollutes, and so forth, in order to generate a superior stock price, but scientific data actually indicates that the vast majority of us would tolerate slightly lower returns in order to avoid these intolerable social outcomes.

So boards should recognize and rely on the discretion that corporate law grants them in running corporations. Use this discretion to focus on the long term as well as the short term, and make decisions that factor in all of the firm's stakeholders. *All* stakeholders ultimately contribute to the corporation's success, and its enduring value.

IRU: You made an interesting observation regarding Congress, the SEC, and a variety of "private policy entrepreneurs," that their governance reform efforts have failed to make improvements for all shareholders.

Stout: These groups are part of the problem and must, therefore, be part of the solution. I believe it is a mistake to react to every corporate scandal with another layer of regulation intended to "improve" corporate governance by making directors and managements more "accountable" to certain shareholder demands.

As your readers know, over the last 20 years, these groups have enacted changes that, in totality, have pushed corporations to focus on shareholders and shareholder wealth maximization. The result of this "shareholder democracy" movement has been broadly lower shareholder returns.

Many of these "reforms" certainly seem to benefit specific investor types (especially undiversified activist hedge funds), but ultimately do not benefit all shareholders as a class. I would also note that the U.K. is further down the "shareholder democracy" road than we are, and investment returns there are worse than in the United States.

IRU: Who are these private policy entrepreneurs? ISS? They certainly exert a strong influence. What would you counsel companies to do in the face of their pressure? Corporate boards dismiss them at their peril.

Stout: ISS has influence because many mutual fund managers vote their shares based on ISS policies, which are biased toward the short term.

If executives, and especially boards of directors, want to truly promote "shareholder value," they need to embrace the discretion that corporate law grants them to use their power and authority to mediate among the various (and often conflicting) views of shareholders. This is preferable to a board slavishly responding only to the concerns of the most short-sighted, opportunistic, and undiversified subset of shareholders.

IRU: What is the investing community's responsibility in this?

Stout: Investors need to move beyond the mindset that anything that raises stock price is necessarily good for all investors. The new scholarship on the nature and purpose of the corporation severs this supposed linkage. Short term, temporary stock price increases do not necessarily help all investors, and there is reason to believe that such strategies ultimately hurt the investing class as a whole.

I also believe investors' stock holding periods are too short, so a change to the tax code to increase capital gains from one year to maybe seven years would be helpful.

IRU: What else can be done to address the issues you've raised?

Stout: I would also advocate for more academicians to take up this cause because business leaders can't fix this by themselves.

IRU: It feels like your book refutes most of what business schools have taught over the past 20 or 30 years about ownership of

publicly traded companies. If it is all wrong, why haven't we heard more about it?

Stout: It's more pervasive than just business schools. I learned in law school in the early 1980s that the purpose of corporations is to maximize shareholder value. And schools continue to teach it. But there are other academics supporting my position, and there are more articles in the press questioning this dogma.

I think that a rising generation of business and legal scholars don't buy shareholder value thinking. However, the concept is still fairly ingrained in business and law schools, and there is a saying in academia that 'academic change comes one funeral at a time.' So significant change will probably take some time.

IRU: What do you see as the implications for investor relations professionals?

Stout: IR has an opportunity to help evangelize this message throughout its sphere of influence. IROs can also help shareholders understand that there is more to the company than tomorrow's share price.

But the biggest obstacle I see is ISS, whose out-of-date corporate governance ideas lead mutual funds and other investors to focus on short-term stock price performance. For instance, ISS routinely recommends that corporations de-stagger their boards to make hostile takeovers easier, and has historically supported pay-for-performance schemes linking executive compensation to share price.

Executive compensation is also a real problem. As long as 80 percent of executive comp is tied to stock price, it will be hard to fix. We've basically aligned management incentives with activists' interests. **IRU**

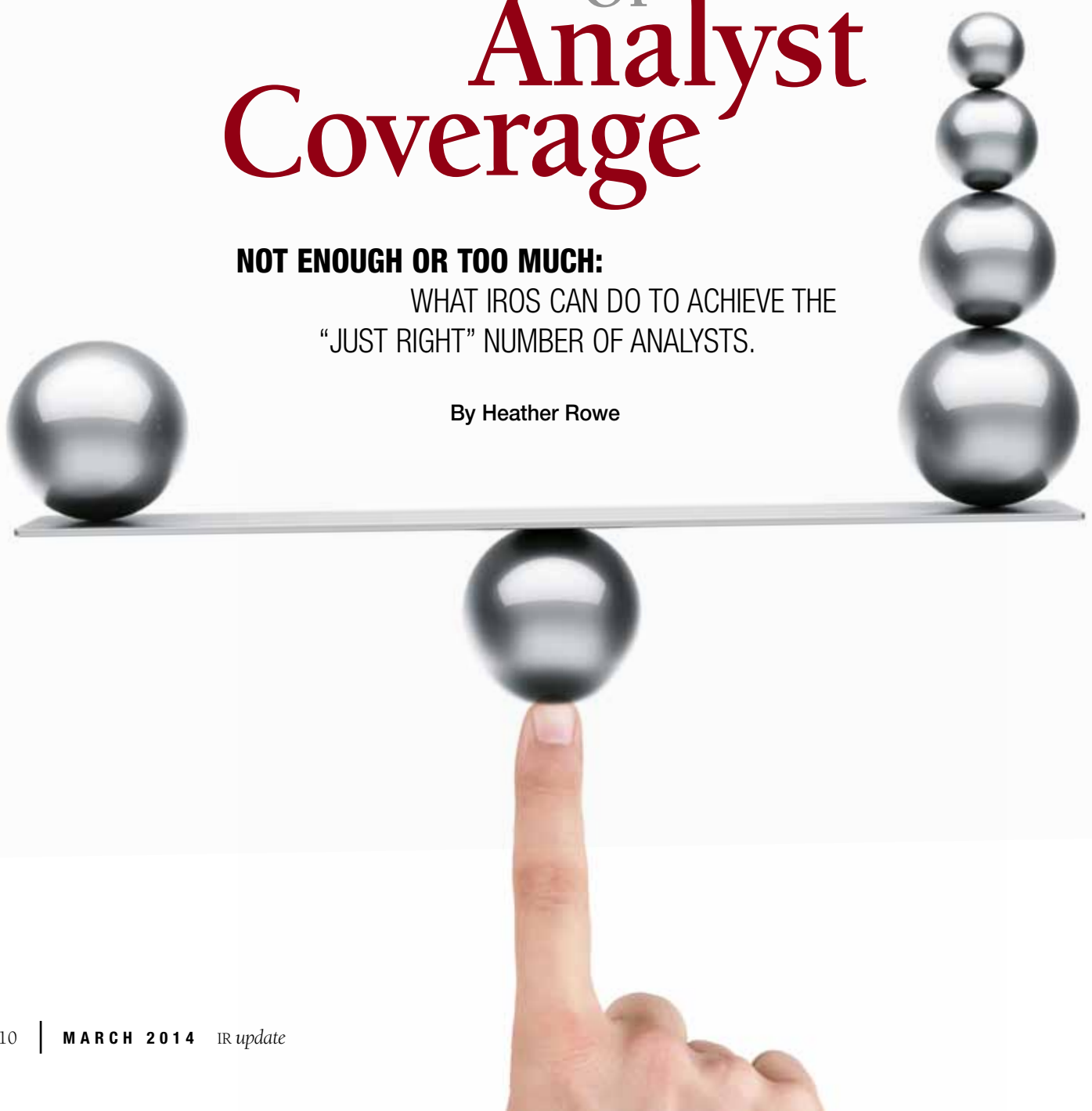
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GETTING THE **Right** **Balance** OF **Analyst** **Coverage**

NOT ENOUGH OR TOO MUCH:

WHAT IROS CAN DO TO ACHIEVE THE
“JUST RIGHT” NUMBER OF ANALYSTS.

By Heather Rowe



When it comes to analyst coverage, IROs offer varied opinions about the level their company receives. These opinions often teeter between not enough and too much.

Small companies often seek additional analyst coverage to elevate their company profile.

“It’s the amplification and expanded distribution of message to your primary target audience of institutional investors – that’s what the analysts achieve for you,” says Derek Cole, president, Investor Relations Advisory Solutions.

According to the NIRI-Korn/Ferry International Corporate IR Profession and Compensation Study (2008, 2012):

- From 2008 to 2012, the percentage of small- and micro-cap companies reporting between zero to four analysts increased from 23 percent to 38 percent.
- From 2008 to 2012, the percentage of mid-, large-, and mega-cap companies reporting 10 or more analysts increased from 76 percent to 88 percent.

Regardless of where your company’s analyst coverage falls on the spectrum, you can turn to strategies and tactics to achieve the “just right” number of analysts.

The Changing Landscape

First, be aware that the sell-side landscape has changed. Kathleen Heaney, principal, K2 Corporate Communications, alludes to the effect of the 2003 global research settlement, which stipulated that analysts could no longer be compensated directly from investing banking deals. As a result, Heaney says, non-deal road shows have taken on a greater importance in determining com-

REGARDLESS OF WHERE YOUR COMPANY’S ANALYST COVERAGE FALLS ON THE SPECTRUM, YOU CAN TURN TO STRATEGIES AND TACTICS TO ACHIEVE THE “JUST RIGHT” NUMBER OF ANALYSTS.

On the flip side, IROs at large-cap companies sometimes complain of too much coverage, citing diminishing returns when there are more analysts than additive viewpoints.

“I prefer quality over quantity,” says Greg Secord, vice president, investor relations, Open Text Corp. “If they are not bringing quality research or if they don’t have a specific view or angle, then there is not a huge value in the relationship.”

While there is no official “just right” number of analysts, research demonstrates that analyst coverage has increased across all market caps since 2008.

Consolidation and lowered commissions from the buy side also have an impact.

“The industry had consolidated – there are fewer firms and fewer analysts,” Heaney says. “Also, there is a push for more non-deal road shows since that’s a key component of how analysts get compensated these days.”

In addition, as Secord points out, the buy side increasingly relies on in-house research. As a result, he says the role of the sell-side analyst has transitioned from being a stock picker to being more of an advisor and idea generator for the buy side.

“Gone are the days when an analyst would set a target price and then watch the stock rise to meet it. Modeling and target price setting are still a big part of the analyst role, but now the role is more about advising the clients and generating ideas,” Secord observes. “It’s a different perspective than trying to influence market reaction with an entry and exit point into the stock.”

Understand Who and Why

So what can IROs do?

First, construct a peer group matrix of peer coverage. Next, create an individual analyst coverage list, including size of market cap.

James D. Fraser, CFA, vice president, investor relations, BOURBON, stresses the importance of understanding why an analyst

“I try to see which analysts are located in different regions if I am trying to gain additional geographic coverage in one region to eventually do a road show or otherwise gain exposure to that market,” Fraser explains.

Define Objectives

Cole emphasizes the importance of defining company objectives that extend beyond the mere quantitative goal of adding analysts.

“Just adding additional coverage isn’t the real goal – that’s the activity,” Cole points out. “Know why you want to add and know who you want to add.”

Similarly, he recommends matching company priorities with likely analyst coverage. He suggests achieving up-front agreement with management on potential trade-offs.

last but not least, you want differing analyst investment theses.

“For example, you don’t want 10 analysts who love to only talk about how your company sees sales opportunity from a regulatory change. You want to see new ideas and variance in their investment theses.”

Understand the Business Models

Multiple factors, including size of the firm, influence an analyst’s ability to cover a company. Bulge bracket firms may have more stringent stipulations while smaller firms may be willing to follow small- or mid-cap companies. Other variables may include an analyst’s ability to champion individual pet projects.

“You need to understand the analysts’ and the firm’s business model. It’s understanding why they do research coverage and what that does for them,” Cole says. “Do the research to understand what their side of the table will want from you. Also understand where your story fits and where their business model fits.”

Fraser agrees. “Ultimately, it is either potential deal flow or trading commissions that will have the greatest influence on them deciding,” Fraser says. “Unless of course you are a top-tier player in your sector, in which case you can simply illustrate how it would be a significant gap in their coverage if they do not cover you.”

Similarly, Cole recommends that IROs determine if they “need” to be covered, citing an example of a small-cap company with cutting-edge or disruptive technology.

“There is an industry core that analysts need to cover. For smaller and mid-cap companies, having cutting-edge or disruptive technology may be something that drives more coverage than a company would otherwise get,” Cole says.

He also recommends targeting what he calls smaller, more boutique-oriented banks

“THERE IS AN INDUSTRY CORE THAT ANALYSTS NEED TO COVER. FOR SMALLER AND MID-CAP COMPANIES, HAVING CUTTING-EDGE OR DISRUPTIVE TECHNOLOGY MAY BE SOMETHING THAT DRIVES MORE COVERAGE THAN A COMPANY WOULD OTHERWISE GET.”

– Derek Cole, president, Investor Relations Advisory Solutions

may not be covering the company. He cites common reasons such as lack of trading volume, analyst geographic focus, and relative size compared to peers.

Next, target accordingly.

“I target based on our geographic IR strategy, quality of analyst, and peer analysis,” Fraser says. “I strongly believe you can influence the coverage by making your case. You cannot, obviously, influence the rating with which the analyst initiates coverage, but that is okay.”

Geography plays into Fraser’s objective to diversify his shareholder base.

“Agree beforehand if you are willing to take coverage that is not as broadly known but that can still provide amplification of the message,” Cole says, adding that if IROs hold out for only the top analysts, then they could miss out on other opportunities to amplify the story within the financial community.

Similarly, Secord recommends analyst style diversification, which he likens to an analyst portfolio mix.

“You want a mix of different analyst skill sets as well as different ways of addressing the market or audience,” Secord says. “And,

that are more tied to new idea generation than pure trading. This is where he says companies will likely find success sooner.

“Understand their business model. They want to get credit for discovering great new ideas that they can pass on to their investors and generate good returns,” Cole says.

Understand the Analyst’s Angle

Beyond understanding the business model, Heaney says it is paramount to understand the analyst’s individual angle. Prior to her current role of providing investor relations services to companies, Heaney spent 20 years on the sell side. During that time, she was assigned an industry and would look at all the companies within that industry. She’d next determine which companies she needed to cover to be credible. She then looked for areas in which she could differentiate.

Secord, too, highlights the importance of knowing and supporting an analyst’s investment thesis.

“The IR professional looks to not just be aware but to also think of ways to build that relationship and to give insights to support [his or her] investment thesis,” Secord says. “It’s knowing, recognizing, and supporting the thesis within the arena of publicly available information.”

Fraser adds: “Once you feel the analyst could still reasonably have you in their universe, it is up to you to make the case as to why you should be covered – show how their clients could benefit from an investment in your company.”

Target Associates

In addition to looking beyond tier-one firms, IROs should also look beyond the lead analyst to target associates or those whose names appear lower on the research report.

“Not only is it good to communicate with a primary analyst’s associate in general, but

they also may grow into the primary role and may be able to take on names of their own or they may move to another firm as a primary authoring analyst,” Cole says. “And so, it’s a great opportunity. Targeting the number-two person is a very good route to go.”

Secord, too, recommends targeting associates, including times when the lead analyst appears less engaged with the company.

“When the lead analyst is no longer personally invested and feels the company is over-covered, then he or she will often hand coverage over to the associate,” Secord notes. “One of the best strategies is to know and engage the associate ahead of the handoff.”

Secord, who currently supports 17 analysts, estimates that he forged strong relationships with more than 50 percent of them before they became lead analysts and were still associates.

“I’ve watched some rise from being the number-three on their team to being top-ranked analysts,” Secord recalls.

Touch Points

Next, after targeting and research, it is important to maintain touch points.

For example, Heaney recommends adding target analysts to the news distribution list to build awareness and as a simple reminder. She says this approach worked when companies tried to get on her radar screen when she was in research.

“If I wasn’t covering the company or 100 percent sure that I was going to pick up coverage, then I wouldn’t always make the effort to keep track of their earnings calls,” Heaney says, adding that a simple e-mail announcement would remind her.

“I had a better chance of listening to the call or eventually picking up coverage thanks to the reminders,” she notes.

Conferences are another important touch point. Fraser recommends reaching out to target analysts before a conference, which he says has

worked well for him. In one instance, several months in advance of a sell-side conference, he reached out to the managing director of research. It worked.

“Two months before the conference, they initiated coverage,” Fraser says.

Dealing With Too Much Coverage

On the flip side, there are times when companies have too much analyst coverage. Secord recalls analysts who didn’t seem to engage the company.

“When an analyst indicates that he has to cover you because he was ‘told to,’ it should be a red flag – generally, [such analysts] don’t add value,” Secord observes.

“I’ve had analysts tell me they had to cover us because we were big fish in the pond. Others have said that they had to cover us to be able to have a dialogue with some on the buy side even though they knew these clients would never trade our stock with them. They saw it as an opportunity to build a dialogue with the buy side where they could then sell them on new ideas in which to invest.”

Secord says he tries to educate analysts when possible, but if that didn’t work, he would initiate frank conversation. If an analyst dropped coverage, he would often reach out and re-engage the associate.

Regardless if a company has too much or too little analyst coverage, the right strategies and tactics can help IROs achieve the “just right” balance. **IRU**

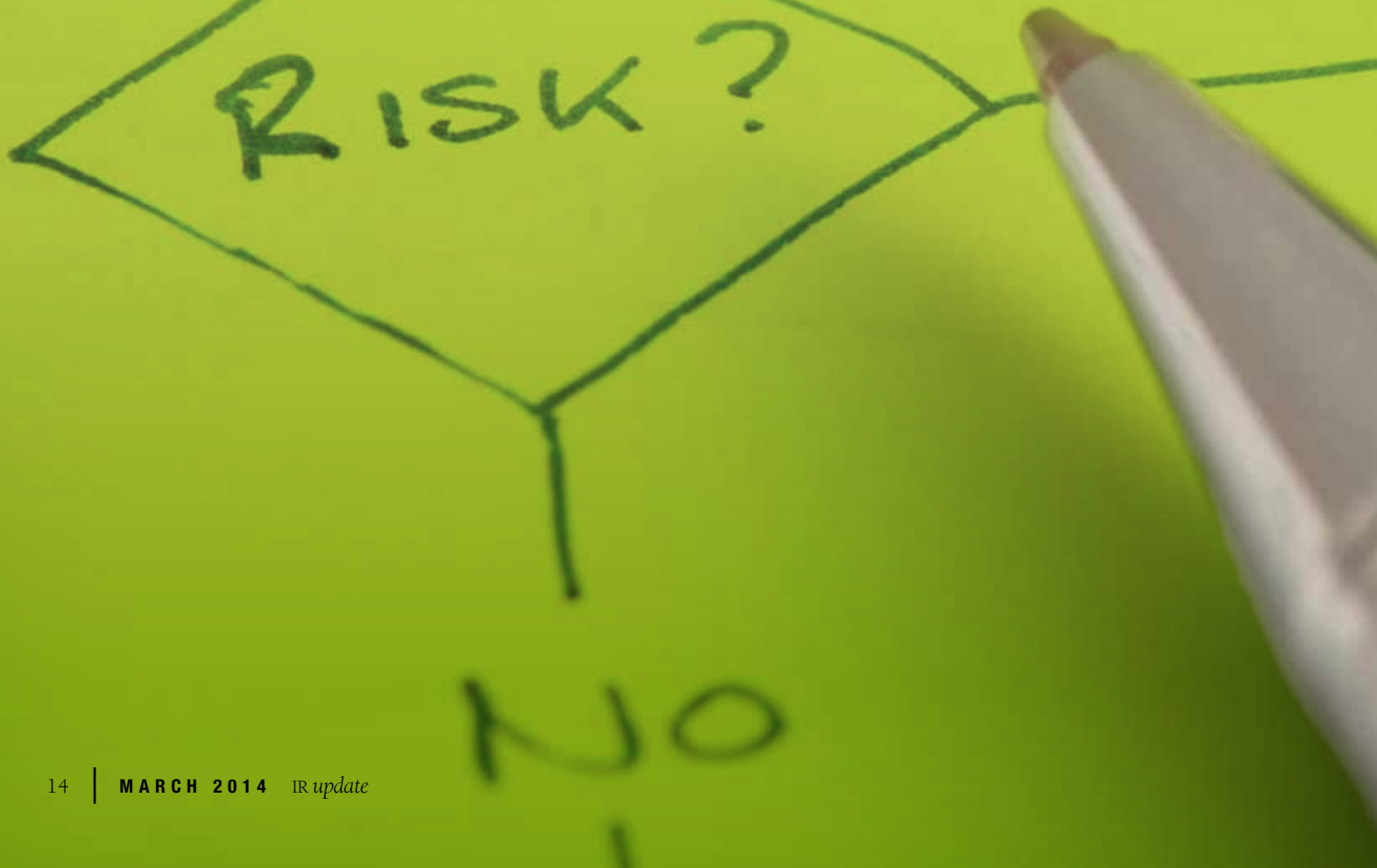
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TOUCHING LIVES AND PROTECTING LIVEL

**Constantly changing
insurance industry keeps
IROs on their toes.**

By Alexandra Walsh



IHOODS

- Yes -

As a result of globalization, regulatory changes, and terrorist attacks, the insurance industry has gone through a tremendous transformation over the past decade.

“Probably one of the biggest trends in the insurance industry is globalization,” confirms Bernie Kilkelly, managing vice president of investor relations at Tower Group International, a Bermuda-based property-casualty insurer with operations mainly in the United States. “Many companies are operating in multiple global markets, many international companies are buying U.S. insurance companies, and if a domestic insurance company gets to a certain size, it has to expand outside U.S. markets to seek growth.” Prior to joining Tower in 2013, Kilkelly was IRO for Delphi Financial Group, a small-cap U.S. specialty insurer that was acquired by large international insurer Tokio Marine Group in 2012.

In the simplest terms, insurance of any type is all about managing risk. For example, in life insurance, the insurance company attempts to manage mortality rates among its clients. The insurance company collects premiums from policyholders, invests the money, and then reimburses this money once the person passes away or the policy matures.

An actuary constantly crunches demographic data to estimate the life of a person. This is why characteristics such as age, sex, and lifestyle choices such as smoking, all affect the premium that a policyholder must pay. The greater the chance that a person will have a shorter life span than the average, the higher the premium that person will have to pay. This risk-assessment process is virtually the same for every other type of insurance, including automobile, health, and property.

**In the simplest terms,
insurance of any type is all
about managing risk.**

In the United States, the Gramm-Leach-Bliley Act of 1999 repealed part of the Glass-Steagall Act of 1933, clearing the way for banks, brokerages, insurance firms, and other types of financial institutions to join together to offer their customers a more complete range of services. In the insurance business, this has led to a flurry of merger and acquisition activity. In fact, a majority of the liability insurance underwritten in the United States has been through big firms, which have also been scooping up other insurance names.

Ownership of insurance companies can come in two forms: shareholder ownership, with shares publicly traded, or mutually owned insurance companies. Here, the company is actually owned by the policyholders, so an account called policyholders' surplus, rather than shareholders' equity, appears on the balance sheet.

Over the past decade, many of the top mutual insurance companies have gone through demutualization to become shareholder-owned. Today, there are fewer policyholder-owned companies than ever before.

There are many factors to examine when consumers and investors look at insurance companies, chief among them, the insurer's financial strength and ability to meet ongoing obligations to policyholders. Poor fundamentals not only indicate a poor investment opportunity, but also hinder growth. Nothing is worse than insurance customers discovering that their insurance company might not have the financial stability to pay out if it is faced with a large proportion of claims.

Over the years, there has been a big shift in the life insurance industry. Instead of offering straight term insurance, the industry now also tends to sell customers

on more investment type products like annuities. As a result, insurance companies have been able to compete more directly with other financial services companies such as mutual funds and investment advisory firms. To capitalize on this, many insurance companies even offer services such as tax and estate planning.

What's Different About Insurance

With the launch of the Affordable Care Act (ACA), almost everything is different about health insurance.

IROs, we live and breathe these changes every day. However, we have investors who cover multiple industries and are unable to do the deep dive. So, we have to craft our story carefully during this period of change."

McCabe says another difference with health insurance is that because health care is so personal, the industry deals with a number of advocacy and consumer groups. In addition, health insurers are subject to the scrutiny of regulators and politicians at both the state and federal levels. "If we were making widgets, there would be a dif-

"Any IRO needs to understand how the financials work in their specific sector. In health insurance, financials can be very complicated."


— Angeline McCabe, vice president of investor relations, Health Net

"Any IRO needs to understand how the financials work in their specific sector. In health insurance, financials can be very complicated," explains Angeline McCabe, vice president of investor relations for Health Net, a managed care organization that delivers managed health care services through health plans and government-sponsored managed care plans.

"With the implementation of the ACA, the business is changing and there are many new programs. As an IRO, you have to understand and be able to communicate the implications of these new programs to investors," says McCabe. "As

ferent level of communication and scrutiny. While we're shareholder-owned, and we strive to increase shareholder value, we also have to be sensitive to the needs of our other stakeholders. Because of this, the development and implementation of our communications strategies are more challenging than in other industries."

Diana Hickert-Hill, vice president of investor relations and corporate identity for the Kemper Corp., a multiline property, casualty, life, and health insurer, concurs. "We are a highly regulated industry, as are many, but not only are our IR activities regulated at the federal level, our industry



is regulated at the state level. That presents some challenges.”

Hickert-Hill adds that another unique aspect of the insurance industry is the difficulty of predicting and modeling. “We’re in the business to accomplish our promise to fulfill valid claims – we want to do that well; that’s our value proposition. Then an event like Superstorm Sandy comes along. Accomplishing our promise becomes far more complicated and challenging, yet we did it well. We just always try to be smart about doing the right thing for our customers.”

One of the challenges of the insurance industry today, says Kathleen Till Stange, vice president of corporate and investor relations for FBL Financial Group, a life insurance and annuity provider that markets to the Farm Bureau, is that there is more data than ever.

“Our company and the entire industry is making a huge investment in technology and upgrading legacy systems. The challenge for insurance companies is to utilize all that subsequent data to our advantage and our customers’ advantage.”

What It Takes to Excel

“When I was getting my degree in chemical engineering and slogging through four classes in thermodynamics, I never would have dreamed I’d be doing this,” muses Hickert-Hill. “When I was a teenager I used to babysit for a family that had a parent with a degree in chemical engineering, but the parent worked as a stockbroker, and I remember thinking – couldn’t he have found an easier way to break into stocks? And here I sit!”

Hickert-Hill’s counsel to those interested in pursuing a career in insurance IR is to read, research, and understand everything about their own company as well as the

competition, in addition to participating in NIRI conferences, workshops, and other resources to share best practices.

And, she adds, “A traditional finance background serves you well but so does having tremendous writing and editing capabilities. I appreciate nuanced messaging. That’s a skill that has to be cultivated and nurtured over time and will serve well in any capacity.” She also recommends media training, including practice time in front of a video camera.

“The insurance industry is very data heavy,” adds Till Stange. “Fifteen- to 40-page detailed financial supplements are published each quarter and statutory financial statements need to be reported to the insurance regulators. That, together with the actuarial pricing side and the investment side of the industry, means that a large majority of my peers have much more of a financial rather than a communications background.”

As Till Stange was a CPA auditor working for a variety of industries before her life as an IRO, it’s not surprising that she believes it’s important for those considering a career in insurance IR to keep up their continuing professional education and have a CPA certificate or other professional designation.

“Some of the industry-specific certificates are important to help you learn the business from a technical perspective.” Till Stange recommends the Fellow of the Life Management Institute (FLMI) and the Associate in Insurance, Accounting and Finance (AIFA) among others.

Kilkelly, who started his career as a consultant on the agency side of the IR business, believes that having both a communication/writing and finance background is a great way to start an investor relations career. “It’s good to have strong writing


skills as well as knowledge of finance and accounting,” he says.

Given his exposure to companies in many different industries, including the insurance industry, Kilkelly observes that the insurance industry can be a difficult industry for investor relations unless you specialize in it. “You have to know statutory accounting in addition to GAAP, and understanding how reserves are set is important.”

When McCabe recruits, she says she’s looking for someone who can think strategically as well as dive into the job with minimal training, and who also has strong writing skills. “I don’t want to spend all my time coaching on IR and the business. Most IR programs run with skeleton crews, so I want to hire someone who has a passion for IR, good people skills, and who can write and edit.”

Making a Difference

So what draws IROs to the world of insurance? “When people graduate from college, they often don’t aspire to work in the insurance industry, it’s not exactly the most glamorous,” admits Kilkelly. “But once I got a sense of how large, how important, and how global it is – it really is a fascinating industry that touches the lives of every individual and every business.

“We’re there in people’s times of need and we make a difference, that’s why we do what we do every day. This is a relationship business and our agents sit across kitchen tables with our customers asking how we can meet their needs and protect their livelihoods and futures,” sums up Till Stange. 

Alexandra Walsh is vice president of Association Vision, the company that produces IR Update; awalsh@associationvision.com.

Planning the Annual Meeting

Learn about recent trends and how you can run a smoother meeting.

By Tammy K. Dang

“Annual meetings still have value,” said Carol Merry, senior vice president and director of investor relations at Fahlgren Mortine Investor Relations. Merry moderated a discussion on an October 2013 NIRI-sponsored webinar titled, “Planning the Annual Meeting,” with Gregg Lampf, vice president of investor relations at Ciena Corp., and Marian Briggs, executive vice president at PadillaCRT.

Merry, like many others, would agree that the annual meeting has slimmed down through the years. “The annual meeting is not the only annual chance for shareholders to find out what’s going on, just as the annual report is no longer the only source for information about the company’s performance and strategy,” she said.

According to Briggs, the annual meeting is clearly more useful for a consumer-facing company, particularly in its headquarters market. “I think industrial companies are definitely less likely to want to devote much in the way of time and money to an annual meeting, so if you think about branded consumer companies, you will see them do more robust meetings,” she said. “Another industry category, banks, often move their meetings around to various markets to build community relations in key geographies,” Briggs added.

Taking the Lead

Lampf believes that the annual meeting is a time when investor relations should take the lead since it is a shareholder event. It’s an opportunity to work with executives, legal, and other departments in the company at the highest levels. Directing his comments to IROs who are earlier in their

careers, Lampf said, “It’s a good opportunity to show some leadership as well as to get to know other people within the company with whom you may not always have had a chance to interact.”

In lieu of a physical meeting, Lampf’s company did its first completely virtual meeting in 2013. Some of the benefits included easier logistical management since there was no need for coordination with an outside facility or guests, making it much more efficient and easier for participants to attend. Companies focus a lot of time on institutional investors, but a

“Virtual meetings can be leveraged to broaden your outreach, to be more inclusive to the retail shareholders.”

– Gregg Lampf, vice president of investor relations, Ciena Corp.

virtual meeting can also make it easier for retail investors to participate.

“Virtual meetings can be leveraged to broaden your outreach, to be more inclusive to the retail shareholders,” he said, adding that he expects more companies to do virtual meetings in the coming years. However, Lampf cautioned that if a company has a larger shareholder base that expects a physical presence or a special situation arises that needs to be dealt with, an all-virtual meeting may not be adequate.

Sometimes a special situation involves an activist in a stock. Briggs suggested it’s best to assume the activist will attend the annual meeting. This person or persons will have had dialogue with management, so you will know their issues. Prepare to calmly and effectively address them.

“Whether it’s a board member with whom people have an issue, a comp ratio, some governance practice, a poison pill, a staggered board – whatever it is – your answer needs to be well-thought-out and vetted,” Briggs said.

Controlling the Process

The company can also control the process by limiting questions and answers as well as who gets into the room through shareholder identification. In this instance, and assuming that nothing new will be disclosed, webcasting the meeting would

not be advised as it would give any activists a larger audience for their views.

Lampf advises IR to stay on top of the latest corporate governance trends. In

situations that involve issues such as an activist, or a controversial proposal or board member, engaging a proxy solicitor can be helpful. “You want to make sure you have a proxy solicitor and set a strategy,” he pointed out.

Proxy solicitors can also help to ensure proper mailing, logistics, and effective solicitation practices. Assuming that IR has good relationships with its transfer agent and shareholder base as well as knows how the majority will vote with nothing controversial on the table, IR can run the meeting without a solicitor.

For more information about future webinars, please visit www.niri.org/webinars.

Tammy K. Dang is manager, professional development, NIRI; tdang@niri.org.

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“IR TODAY” IS A SERIES of short online videos covering topics affecting the practice of investor relations. Hosted by NIRI CEO Jeff Morgan, each video features insights from IR experts. Recent “IR Today” videos include:

- “2014: Investor Relations and NIRI” with John Chevalier, 2014 NIRI Board Chairman, and director, investor relations, The Procter & Gamble Co., on the state of investor relations and of NIRI.
- “Annual Reports – Trends & Innovations” with Maureen Wolff, president and partner, Sharon Merrill Associates, on the latest trends and innovations in corporate annual reports.
- “Communicating With Your Board” with David Dragics, senior vice president of investor relations, CACI International, on investor relations communication with corporate boards of directors.
- “Reforming 13F Reporting” with Scott Cutler, executive vice president of listings at the New York Stock Exchange, on the need for rulemaking by the Securities and Exchange Commission to improve shareholder communication.
- “CEO Pay Ratio Disclosure” with Dennis Zeleny, co-CEO of the Center on Executive Compensation, on the SEC’s recent proposed rule that would require most issuers to disclose the ratio between their CEO’s total compensation and the median compensation of their employees.

Access all the videos in the media section of www.niri.org under “videos” or by visiting the NIRI YouTube channel: <http://www.youtube.com/NIRINational>.

On the Move



Michael A. Steele, CFA, was named vice president, investor relations, for

Office Depot. He was previously vice president, investor relations for OfficeMax, which merged with Office Depot. **Rich Leland**, who led both treasury and investor relations for Office Depot, will continue as vice president, finance and treasurer, assuming additional responsibilities in an expanded role.

Quick Takes

Three veteran CEOs spoke at the NIRI Senior Roundtable in December 2013, where they offered insights on corporate turnarounds, effective management, and the importance of investor relations. Some of their comments on investor relations are featured here.



Lewis B. Campbell

Former President and CEO
Textron and Navistar

“As a CEO, the main bridge between me and the investor community was the IRO. That person will make or break me. Two people’s reputations are at stake – mine and the IRO’s. We have to have a close inner-circle relationship. They even needed to know if something personal was happening in my life because it would affect my professional life.

“There is no more important personal relationship in the company than between the CEO and the IRO. The further up the ladder you go, the less you know about what is going on further down in the company. The IRO is a tremendous sounding board if you let [him or her] be honest. They could even be CEOs if they wanted to – they know the finances, they think strategically, and they have to have guts.”



Jay Grinney

President and CEO
HealthSouth

“During the turnaround process, it was critical to have someone in the investor relations position who had knowledge of the financial markets and the company, and who could cultivate long-term shareholders. Our IRO was instrumental in building credibility in the financial markets.”



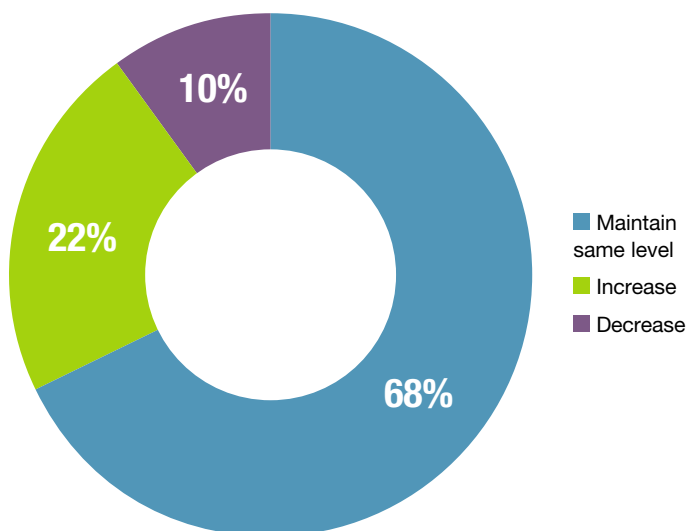
Paul Reilly

CEO
Raymond James Financial

“Most investors are simply looking for the truth. In my opinion, the more open and honest a company is, the more trust and value it can earn with investors. That often translates into investors giving you the benefit of the doubt when issues do arise. Investor relations officers are key to building trust with investors. What they do is important and those who do their jobs well bring significant value to the companies they serve.”

IR Research at a Glance

In 2014, are you looking to increase, decrease, or maintain the same level of participation in analyst-sponsored investor conferences?



Source: NIRI Analyst-Sponsored Investor Conferences Survey – 2013.
Compiled by NIRI, December, 2013. 382 Respondents.

Professional Development Calendar

March 2014

- 11** 2014 Institutional Investor Awards webinar
- 24-26** Finance Essentials Intensive seminar, New York, NY

April 2014

- 1** Think Outside the IR Box webinar
- 8** 2014 IR Magazine Awards webinar
- 29** Distinguish Yourself as an IRO in an Extreme Environment webinar

May 2014

- 6** Investors Part I: Sell-Side Coverage webinar
- 20** Investors Part II: Targeting the Buy-Side webinar

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Rational Investors Vs. The System

The Alternative Trading System has created complex market dynamics that complicate IROs' jobs. Here's how to cope.

By John Hastings

Buyer, meet seller. Seller, meet buyer. Get together and set a price.

According to Tim Quast, an expert on financial market dynamics, that scenario is as quaint as calling a sycamore tree a buttonwood. Today's financial markets are ruled by a tsunami of data that is overwhelming the market's infrastructure with frightening frequency and effect.

Quast is the founder of ModernIR, a pioneer in the application of data analytics to market intelligence for IROs. He recently provided the NIRI St. Louis chapter with a high-energy look into how and why financial markets behave.

How It All Began

Nasdaq trading halt. The "Flash Crash." Knight Securities' collapse. Facebook's IPO.

Quast traced these market malfunctions to 1997 with the introduction of the Alternative Trading System. The ATS allowed buyers and sellers to bypass the traditional exchanges and greatly increased the role of intermediaries in market behavior.

The combination of less restrictive trading channels and advances in trading technology has upended the structure of financial markets, Quast observed. While IROs would like to believe that markets are driven by news and fundamentals, the 3,600 public companies in the United States are now components of more than 2 million global indexes, he pointed out.

The explosion of volume is driven by these indexes as well as the introduction of Exchange Traded Funds, high-frequency traders, and alternative investment vehicles.

Together, they dwarf the impact of rational investors who make trading decisions based on bottom-up analysis.

Quast estimated that 50 percent of all trading volume is attributable to indexes and model-driven hedge funds. Another 35 percent of trading volume is what he referred to as "fast money" – arbitrage funds and high-frequency traders. The remaining 15 percent of volume is the

Know the marketplace and how each piece connects to drive price and volume.

IRO's target – longer-term, rational investors who want to understand a company's unique investment thesis.

Four Key Insights

So where does that leave the harried IRO who needs to explain stock price fluctuations to a management or board whose understanding of market dynamics is limited to a few quick peeks at closing prices? Quast offered four guidelines for the IRO:

1. Know the marketplace and how each piece connects to drive price and volume. Quast stressed the importance of becoming the company's expert in the trading environment and not just the compliance manager. IROs should use that knowledge to educate the management and board on the impact of high-frequency trading and index rebalancing.

2. Face the reality of today's financial markets. Market participants have different purposes and time horizons and there are many different trading strategies using your stock. Rational investors, that 15 percent of the trading volume seeking to understand your story, only set the price on average *one day per month*.

3. Continue to engage the investment community. While rational investors represent a small sliver of total volume, there is evidence to suggest that their behavior can have a disproportionate impact on the pricing.

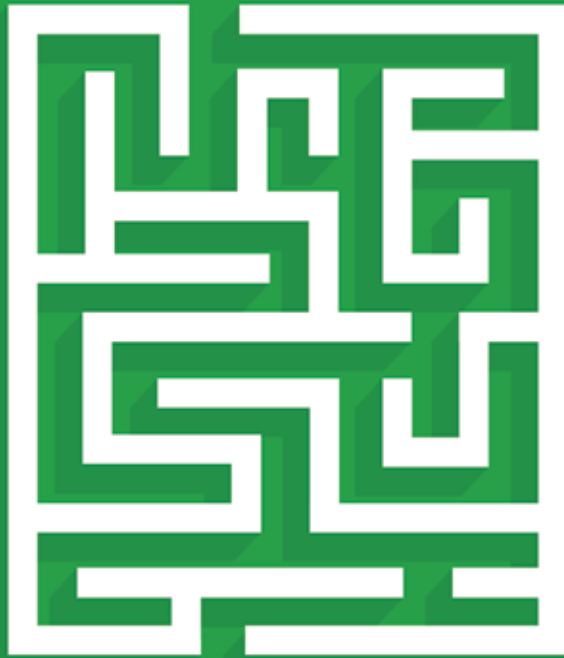
4. A better understanding of market behavior makes it possible to make a simple change: Compare reporting dates for financial results to options expirations dates. Options calendars can be found at the Options Clearing Corp.: www.optionsclearing.com/about/publications/expiration-calendar.jsp.

Quast maintains that by reporting in the middle of expirations, companies enhance speculative opportunity and introduce heightened risk-management activity, both of which distort price and get in the way of the message – which is meant to go to bottom-up investors, who focus on fundamentals.

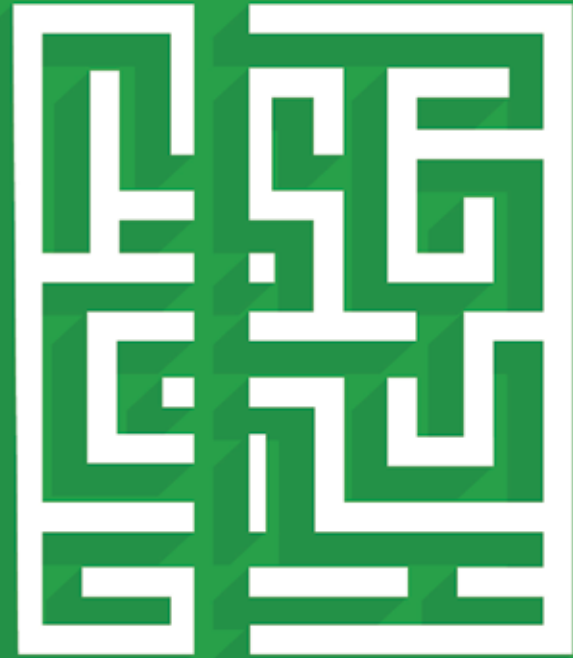
He recommended that by simply moving the reporting date two to four days beyond the expirations window, a company can improve the likelihood that rational investors will play a greater role in setting price. What a quaint concept.

John Hastings is founder and chief pencil sharpener of Sharp Point Communications; john@sharp-point.net.

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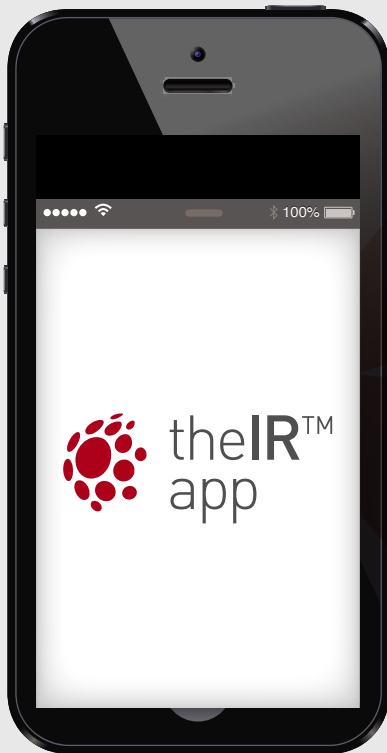
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