MORROW SODALI

INVESTOR RELATIONS - A COMMUNICATIONS CLEARINGHOUSE

A TALK WITH FORMER NATIONAL INVESTOR RELATIONS INSTITUTE CHAIR, VALERIE HAERTEL

BY JOHN C. WILCOX, CHAIRMAN, MORROW SODALI

INTRODUCTION

Companies in today's market face growing pressure from institutional investors to provide more substantive explanations of business strategy and more detailed information relating to environmental, social and governance (ESG) factors that materially affect the business. At the same time, shareholders are complaining about excess disclosure – reports with too much standardized information and too many details that obscure meaning. Instead of more disclosure, investors want better communication in the form of a narrative that "tells the company's story" and paints a coherent picture of the company's operations, governance, financial and non-financial risk factors, culture, competitive position and long-term strategic goals as well as its financial performance. Behind this demand is the conviction shared by many investors that a company's ability to tell its story convincingly is a reliable indicator that management and the board know what they are doing and are running the enterprise effectively.

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The demand for this type of narrative is becoming widespread. It is the official goal of the International Integrated Reporting Council (IIRC), which leads a global movement to reform how companies think and communicate. It is also a goal of the European Commission, which has been pressuring issuers to improve the quality of their explanations and provide more substantive information in support of their ESG policies. The emphasis in the EU's voluntary, "comply-or-explain" governance system now falls heavily on "explain."

In the U.S., with its rules-based governance system and detailed disclosure rules, the concept of an individualized narrative gives rise to legal uncertainties. This is particularly the case when the narrative contemplates the type of forward-looking information that institutional investors want but that disclosure rules discourage. Even in the U.S., however, customized communication has made significant progress, much of it outside the framework of regulated disclosure documents. "Engagement" has become an alternative communication path that is endorsed by both companies and institutional investors.

U.S. issuers are dealing with these expanded informational demands in different ways. One of the most successful solutions has been developed by Valerie Haertel, a former NIRI chairman, who during her career has created a role for the IR department as a "communications clearinghouse." Working directly with her peer executives in different departments, she has taken an approach to investor relators that is more strategic and that addresses the full scope of informational needs of investors, including those on the governance side of the house.

I met recently with Valerie to discuss how her communications clearinghouse worked in practice.

JW: Valerie, for many years people have been predicting the convergence of investor relations and corporate governance. Is that finally happening?

VH: Yes. I would describe it as an informal evolution rather than a deliberate effort to converge. The trend started primarily at larger, more progressive companies, although I see that there is increasing interest at companies of all sizes. In fact, this has become an important trend that the National Investor Relations Institute (NIRI) has recognized and is addressing through educational programs. The demand from institutional investors for information about ESG practices has been a big stimulus. If you were to attend the annual conferences of both NIRI and the Society for Corporate Governance you would find that the topics on their agendas are similar – ESG, shareholder activism, engagement, stewardship, director accountability, short-termism, and so forth. Since IR and governance professionals are dealing with this common set of challenges, there is more collaboration and the corporate roles are naturally converging.

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But IR and governance are separate disciplines and are assigned to different executives or departments at most corporations. Doesn't that create a problem?

It should not be a problem if IR officers are able to collaborate effectively with their business partners. That is the approach I have taken.

OK. You describe your Investor Relations role as a "clearinghouse function." What do you mean by that?

Well, my primary role leading Investor Relations has always been the traditional one of financial communications. Once an IR strategy is put into place, I work with the CFO and CEO organizing communications with the buy- and sell-side, preparing quarterly earnings releases, conducting IR road shows and fielding calls from investors. In addition to that traditional role, I have made a point of working directly with other departments across the company to collect and communicate information about issues of concern to shareholders that are not purely financial. I use the term "clearinghouse" to emphasize the way that internal collaboration works across departmental boundaries, thereby enabling the company to present a more comprehensive, accurate and unified picture.

How did the clearinghouse work in practice?

I collaborated directly with a number of corporate business partners and line of business leaders in most of the companies where I worked. One was the Corporate Secretary. I provided data and analytics about ownership, including the feedback I received from my daily contacts with shareholders and analysts. In my role leading IR at several financial services companies, I worked directly with the governance professionals who oversaw investment stewardship and proxy voting for the asset management groups, as well as the individuals responsible for Corporate Social Responsibility who oversaw activities related to sustainability and reporting. Those relationships and input really helped me to understand how investment professionals think and react to various ESG issues. Additionally, the business unit leaders helped me to better understand the nuances and complexities of the various operating businesses. These interdepartmental relationships enabled me to bring together diverse perspectives in shaping the content of the investor relations and engagement programs. This is what I mean by a clearinghouse role.

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Are Investor Relations road shows being expanded to reach stewardship teams as well as portfolio managers and analysts?

Yes. During the course of my career, I have gotten to know the stewardship teams at the major institutional investors and I have made a practice of including them in investor outreach programs. I found that interest in governance and ESG issues has been increasing in the U.S. and tends to be greater on the buy-side than the sell-side, unless there is activist activity and governance is being questioned. At several firms, I participated with management and board members in engagements with shareholders. Typically, the Corporate Secretary's office and I would reach out together to the governance decision-makers on the buy-side outside of and during the proxy season. This practice is becoming an increasingly important part of the investor relations practice generally as buy-side analysts and PMs are also better coordinated on these issues. Depending on the circumstances, engagement accomplishes two goals. First, it is a great way to get candid feedback from shareholders. That is the listening part. Second, it's a great way for shareholders to get to know the management team and in some cases, board members personally. Conference calls are useful and efficient, but face-to-face meetings are the most effective way to build trust over the long term. I should mention that in my roles leading IR programs, I was directly involved in the preparations and mechanics of the annual meeting, including being a contributor to the proxy statement, which gave me another opportunity to build personal relationships. I think that the annual meeting is a meaningful inves-

tor relations event because governance is on the agenda and the board of directors is in the spotlight. IR can add a lot of value in the preparation process leading up to the annual meeting.

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Do you treat indexed investors differently from active managers?

Yes and no. Active managers and the sell-side are still the primary audience for financial communications, quarterly earnings announcements and the like. But outreach to index investors and their stewardship teams is not just limited to ESG topics and proxy votes. Index investors have made it clear that they want to understand business strategy and financial performance as well as ESG policies. From their perspective as long-term "permanent" investors, there's no separation between financial and non-financial factors affecting the business. Both active and indexed investors want to know about both. That being said, active managers generally require more frequent and detailed information on the strategy, financial performance and outlook.

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What is your view about the debate over short-term versus long-term business goals?

That is an easy question for me to answer. It is imperative that companies build and run their business for the long-term. NIRI has recently issued some updated guidance related to quarterly earnings guidance, focusing companies on the importance of managing for the long term. In my view, companies shouldn't manage to meet short term street expectations, or run the business based on how they think the stock market will respond in the short-term. It is important to understand investor perceptions and to communicate strategy and priorities clearly in order to ensure a realistic assessment of future performance by investors. The market has changed during the past decade – trading activity and stock prices are now influenced by technical factors that often have nothing to do with a company's intrinsic value. So I agree with the statement that the Wall Street tail shouldn't wag the business dog. Luckily, in today's market many investors also agree and explicitly support a long-term focus. Sustainability is also an increasingly important and shared goal for companies and for the stable, long-term shareholders they want to attract.

Many commentators recommend the elimination of quarterly earnings reporting as a means to combat short termism. Some high-profile companies have done so. What is your view?

I've heard the argument that bi-annual reporting would keep investors more focused on the long term. But my experience is that both buy and sell side investors prefer quarterly earnings reports. From the corporate perspective, quarterly reporting keeps the leadership team and employees focused on strategic direction and results, creating discipline and enabling course corrections if necessary. However, to keep investors more focused on the long-term, I think the consensus estimates which push companies to provide guidance and shorter-term investors to continue to demand it, should be abolished. This may be a somewhat radical view, but the consensus

estimates being generated by sell side analysts – some of whom are knowledgeable and others who may not be paying close attention – create expectations not necessarily set by the company. This causes volatility in shares when companies miss the analysts' estimates.

Investor relations at the board level is a perennial topic. Is it starting to happen?

Board-level investor relations is actually not new. It was always a factor in proxy contests. It became more common with director involvement in say-on-pay campaigns. In recent years, shareholder activism has elevated the board's role in investor relations to the point where it is no longer controversial for directors to meet and speak with investors. Many attorneys see the merit of it and recommend it. Board-level IR still isn't typically organized systematically like the rest of the IR program unless it is supported and included as part of the outreach program. It often occurs when there is a special reason such as a request from a shareholder, rather than on a fixed schedule, although this is still evolving. Regular, periodic interactions are becoming more common. Board involvement has affected my role leading investor relations programs in several ways. First, one of my responsibilities has been to keep the board of directors informed about who the owners are and what issues are of concern to them. Depending on the issues raised by shareholders, I would get the internal clearinghouse up and running to provide the information that management and the board need to formulate a response and determine how to respond. I would help create the message content and engagement materials, set up and attend the investor meetings with management and board members and then follow up to get feedback afterwards.

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What role does IR play when a company is targeted by an activist?

I have had direct experience with activist campaigns twice during my career. What I have learned is that activism is the ultimate test of effective investor relations because it galvanizes internal resources to respond to the issues raised by the activist. Each situation is unique and requires a thoughtful assessment and response that will produce the most effective course of action for the leadership team, the board of directors and the shareholders. The role IR plays in an activist campaign is to evaluate the situation, analyze the issues, gather the facts and work with the leadership team and the board to formulate appropriate responses that clearly and effectively communicate the company's position to investors. I believe that at firms that have dealt with activism much of the internal adaptability and progressive elements of their IR programs grew out of management's deeper understanding of the strategic role IR can play when responding to complex activist challenges. The collaborative IR programs that I have run include many of these features – they are proactive, transparent and responsive. The best defense is a good offense. I think it would be fair to say that the Investor Relations information clearinghouse can be a model for companies that want to proactively take steps to strengthen both internal and external stakeholder relationships and avoid being targeted by activists. Companies should know their vulnerabilities, address them and be prepared with a plan to address activism if it arises. That being said, a clear strategy and solid financial performance must be combined with an effective investor communications program to avoid being placed in a defensive position.

CONCLUSION

The "them versus us" mentality that characterized relations between shareholders and public companies for decades is giving way to much more complex, individualized relationships. Globalization, governance standards, indexing, strategic activism, board accountability, stewardship codes, ESG and technology are among the factors that have changed the way companies and shareholders interact and relate to each other.

These developments substantially increase the challenges faced by public companies, but there is a positive impact as well: in today's environment individual companies have a better chance of being evaluated by investors on the merits rather than exclusively in terms of their compliance with external standards. This depends, of course, on two conditions – (1) companies must be willing to build sustained relationships with shareholders and improve the quality of the information they provide; and (2) institutional investors must reconfigure their investment models to include ESG and non-financial metrics and they must focus on the long term.

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Valerie Haertel's response to this changing environment has been to designate the Investor Relations Department as an "information clearinghouse." This approach worked well for the companies where she worked. Other solutions are also possible. Many companies have appointed dedicated corporate governance officers who work collaboratively with other corporate departments and with boards of directors. Proxy statements have morphed beyond traditional formats to include livelier and more informative presentations. Directors are emerging from the boardroom to meet, listen and talk to shareholders. The corporate secretary's role is expanding to strengthen relations with institutional investors and guide director engagement campaigns. Companies have created new departments to deal with their environmental and social responsibilities.

Our experience at Morrow Sodali is that issuers increasingly recognize that managing their relations with shareholders and institutional investors is central to risk oversight and annual corporate planning. They are dedicating additional resources and time to the various tasks associated with the annual corporate governance cycle and taking steps to prevent activism from occurring rather than waiting until it happens and reacting defensively. Well-established disciplines such as market research and customer relationship management are serving as models for companies to deal effectively with these challenges through research, ownership profiling, market surveillance, board-level engagement and enhanced communications that "tell the company's story."

In the end, relations between issuers and institutional investors are a two-way street. Both sides must cooperate. The most important question still remains to be answered: Will institutional investors follow through on their commitment to: (1) evaluate companies individually, (2) focus on long-term performance and (3) consider corporate purpose, ESG and non-financial factors when they make their investment and proxy voting decisions?

VALERIE HAERTEL

Valerie Haertel has been a leading investor relations professional for more than 25 years. She is on the Board of the National Investor Relations Institute (NIRI) and when she served as chair in 2017, she co-led the search and seated a new CEO, encouraged the development of its certification program and became an Inaugural Investor Relations Charter holder. Most recently, Valerie was the Global Head of Investor Relations at BNY Mellon, and State Street Corporation where she partnered with leadership during shareholder activist activities and managed comprehensive engagement programs that included competitive analysis and positioning. In addition to her work in banking, she also led strategic IR programs at both Medco Health Solutions and Alliance Bernstein which enabled her to expand her leadership responsibilities. At Alliance Bernstein, she led the corporate rebranding from Alliance Capital to Alliance Bernstein and initiated plain English SEC disclosures. She also worked through the restructuring of C-TEC Corporation which spun out RCN Corporation where she created an integrated IR and Corporate Communications program from the ground up. She was also a director of Nasdaq Company Services, counseling clients on capital market activity and investor relations issues. She has been recognized and honored by IR Magazine and Institutional Investor Magazine for her work as one of the nation's top IR professionals.

ABOUT MORROW SODALI

Morrow Sodali is the leading global consulting firm specializing in shareholder services, activism and contested situations, corporate governance, strategic stock surveillance and proxy solicitation. The firm provides corporate clients and shareholders with strategic advice and services relating to a broad range of activities, including: mergers and acquisitions, contested director campaigns, shareholder activist initiatives, shareholder meetings and multinational cross-border equity and debt transactions.

From headquarters in New York and London and seven offices in major capital markets, Morrow Sodali serves more than 700 corporate clients in 40 countries, including many of the world's largest multinational corporations. In addition to listed and private companies, its clients include mutual funds, stock exchanges, membership associations and activist investors.

CONTACT US

US: +1 212 300 2470

Europe: +44 (0) 2071006451

APAC: +61280227910

info@morrowsodali.com