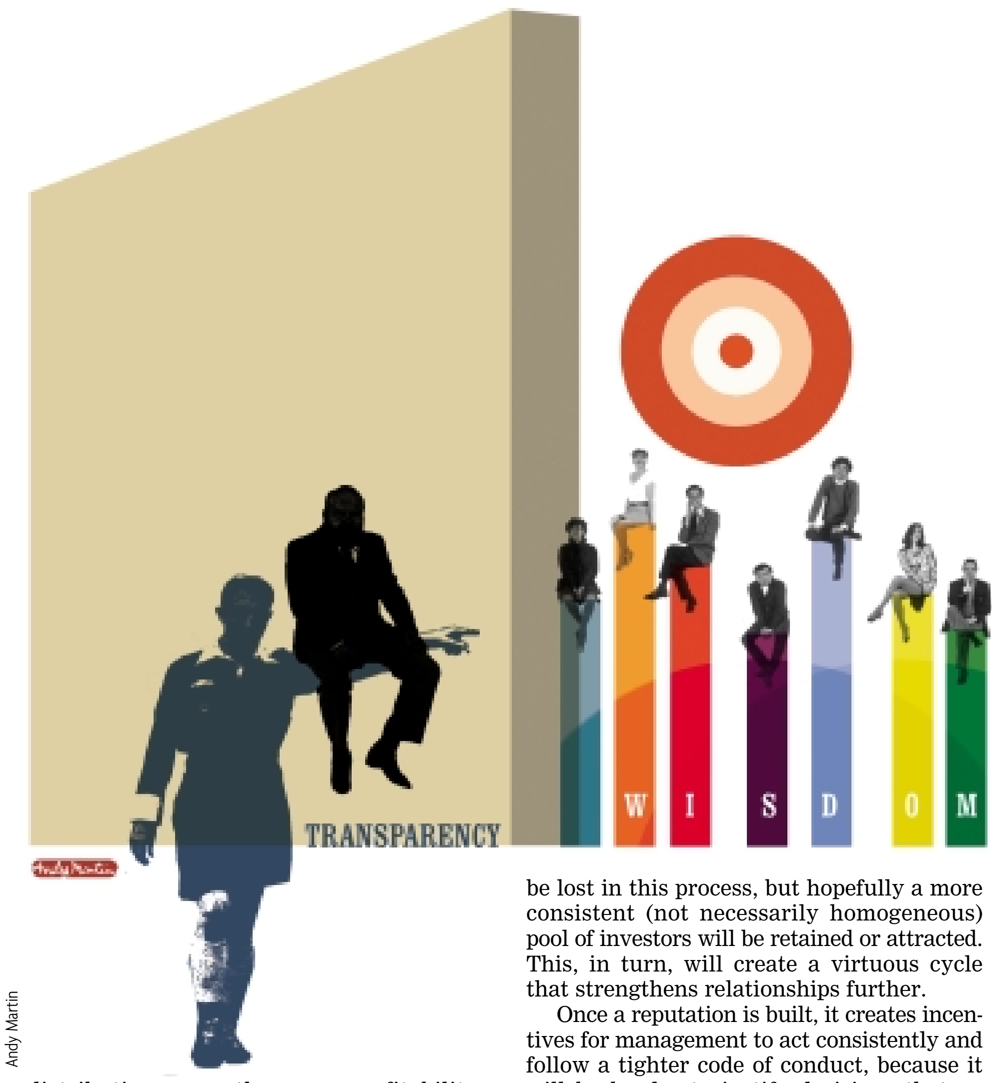
An open channel of communication

Today's investor relations officer must be a good communicator and skilled in the art of negotiation



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By HORACIO FALCÃO

Traditionally, the role of the investor relations officer (IRO) has been to help a company achieve a fair valuation of its share price. This has always required working with a range of departments from finance and communications to marketing. More recently, in the wake of recent corporate scandals, it has had to embrace securities law compliance, too. This article will focus on the role and obligations of the IRO in business today.

The new IRO

As the person who manages the flow of information with a number of corporate relationships, the IRO could be redefined as the "information and relationships orchestrator". Since the IRO has no formal power, this definition would better reflect the new key skill: negotiation. The IRO should not just communicate, but educate and be educated via a constant negotiation to persuade, link and build internal and external relationships in order to improve company value. Of course, this is not always easy, so below are a series of qualities that the IRO should embody.

■ **The IRO must be a neutral party who works for intermittent value creation and share price appreciation.** The IRO can only achieve this by being perceived as a trustworthy and unbiased agent. As soon as someone believes the IRO is creating value for one party only, trust falls apart and so does the IRO's ability to persuade and build relationships.

■ **The new IRO must proactively build relationships.** He needs to help executives build and maintain the highest standards of corporate reputation, based on solid corporate governance and ethical practices. Of course, no relationship works in isolation. The new IRO has to enable consistent, clear and credible two-way communication so that both management and investors can make better decisions.

According to Leonardo Horta, vice-president of the Brazilian Investor Relations Institute, the IRO is most effective when he is able to reduce investor concerns about management. This does not mean being bullish at all times; an IRO must also be strong enough to correct analysts when they offer overly positive valuations of the company. Without this, trust and reputation are difficult to maintain.

Consider Investor AB, a Swedish investment group. It has invested in ABB, the Swiss-Swedish engineering and technology company, for 60 years. Despite ABB's recent run of poor results, Investor AB remains a committed long-term shareholder. The reason is that it trusts ABB's management team and has faith in its overall strategy.

■ **The IRO has to co-ordinate the messages of corporate communications and public relations.** Ensuring the quality and consistency of the corporate message given to all stakeholders is vital. Considering the complex relationships co-ordinated by the IRO, he risks inconsistent messages and reactions if he cannot develop closely co-ordinated channels of communication with each department.

■ **The new IRO should engage in direct conversations with investors.** The IRO should ask investors key questions. What is important for you? What is your decision making process? How can I make this relationship more valuable for you? What are your perceptions of the other relationships? What information do you have that may be interesting for our business? How do you perceive our competitors?

Such questions enable key information to be gathered and shared more easily to improve decision making. In the light of increased investor activism, shareholders will appreciate that management is asking for input on how to create value and manage risk when dealing with their investments.

Moreover, the IRO will learn more about investors based on their interests instead of on their investment position. In the past, investment positions, such as registered, retail, institutional or insider, revealed overarching interests. Increasingly, however, this has become a less effective tool because there are conflicting interests within each position: long-term value creation versus short-term gains; share buybacks versus dividend distributions; growth versus profitability; maximised financial return versus corporate social performance.

For example, consider the last annual meeting of Australian wheat exporter the AWB. During the meeting, many shareholders criticised the company and demanded answers over allegations of bribes to Saddam Hussein as part of the UN's oil-for-food scandal. At the same time, others supported the company and admitted that the AWB has paid out well for several years.

The new IRO should look to relationships with aligned interests that create a favourable environment for value creation. Segmentation by investment interests allows the IRO to better understand the investor base and avoid being overly influenced by more vocal investors who may represent a minority interest or stake. When making strategic decisions, a company should mainly cater for the investment interests of the majority. If managed correctly, these are usually aligned with the company's strategic advantages and corporate reputation.

Building on reputation

A company can build a specific investment reputation – for example, as a long-term value creator or for strong corporate social responsibility – and attract investors aligned with company interests. Some investors may be lost in this process, but hopefully a more consistent (not necessarily homogeneous) pool of investors will be retained or attracted. This, in turn, will create a virtuous cycle that strengthens relationships further.

Once a reputation is built, it creates incentives for management to act consistently and follow a tighter code of conduct, because it will be harder to justify decisions that go against their strategy, reputation and the interests of all stakeholders. A strong reputation helps reduce volatility and, thus, facilitates a fair or even higher share price.

The benefits of such proactive reputation building were on display at the last annual meeting of pharmaceuticals company Pfizer. Despite presiding over a 40 per cent slide in share price, CEO Hank McKinnell received the endorsement of 90 per cent of shareholders. Mr McKinnell successfully argued that Pfizer has extremely long business cycles and, thus, is not a company for day traders or short-term investors.

Conclusion

The IRO must be a diplomat of the capital markets who is prepared to face the challenges of a more demanding investment environment. By improving the flow of information, he will strengthen relationships and create more value for the company.

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