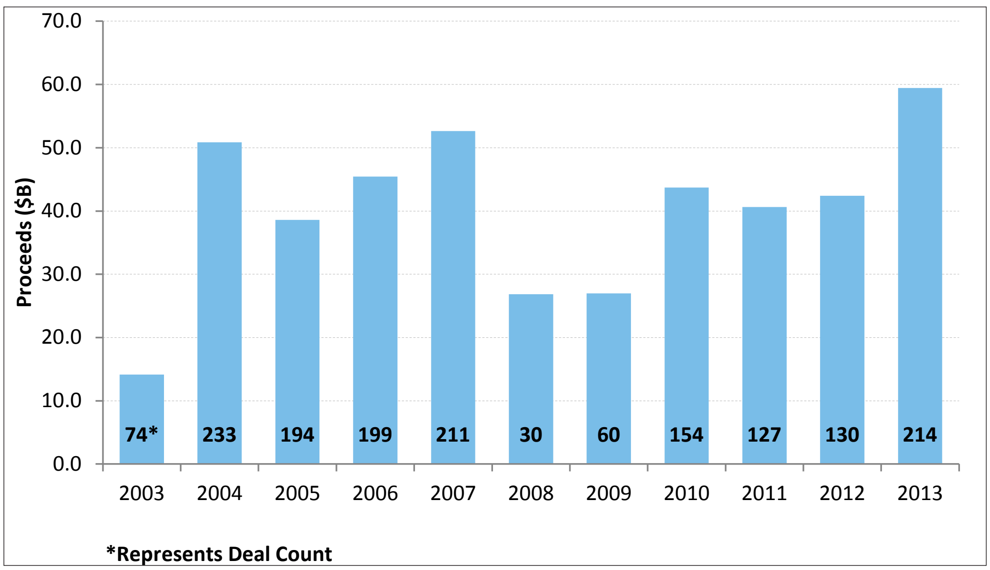
NAVIGATING THE IPO PROCESS FROM THE IR SUITE

IPREO SPECIAL REPORT
Better IR SERIES

As a result of the bull market in equities seen over the last several years, the IPO market has been extremely active. According to Robert Lurie of Ipreo's Capital Markets team, "2013 saw 214 IPOs come to the market raising $59.4B in capital, marking the best year for IPOs since 2004, when 233 companies debuted and took in $50.8B." (Figure 1 Below). With all the new public companies coming to market, corporations have been in need of quality investor relations, and many of our readers and clients have filled those IR roles. In order to research best practices for investor relations for an IPO, Ipreo interviewed several investor relations professionals with recent IPO experience along with an experienced member of the underwriting community. While the investor relations process leading up to an IPO is similar to that of a public company with a longer history, there are certainly some nuances and tips that may prove to be useful.

Figure 1: IPO Proceeds and Deal Count (2003-2013)



Key Takeaways:

- IROs should seek to participate in as much of the IPO process as early as possible in order to better serve investors and management post-IPO.
- Issuers are well served to target long-term quality investors for the initial share allocation, but must be prepared to deal with hedge funds with short term horizons that will almost certainly be a part of the initial shareholder base.
- During the roadshow, distilling the company's story down to digestible points for investors, and breaking down different business lines separately, has proven to be a winning strategy.
- Providing conservative and achievable guidance during the IPO process can help a company avoid disappointing the markets post-IPO, which can irreparably damage a company's credibility and future valuation.
- Providing consistent performance metrics and data points pre- and post-IPO helps build credibility and create transparency. Inconsistencies in this regard tend to raise suspicion.
- An issuer cannot over prepare for the first earnings call.

Picking an Underwriter

Choosing underwriters is typically the first important decision that follows the decision to become a public company in the first place. The underwriter's decision will likely be driven by factors outside of the IR suite, as many different constituencies typically have input on which banks should be involved in running the deal. According to our interviewees, having previous relationships with bankers is an important factor, with an emphasis on honesty and trust. Items to consider include the underwriter's ability and willingness to reach a broad swath of the investment community, including both deal-oriented hedge funds as well as long-term investors that may be attracted to the story. It's also worth evaluating the underwriter's track record in successfully executing offerings of similar size, as well as the bank's willingness to provide credible sell-side coverage on the issue following the offering. Peter J. Nelson, CPA, Chief Financial Officer of American Homes 4 Rent, commented:

“The depth of their relationships in the financial community is paramount; who else they can bring to the underwriting team? I also think honesty and having a level of trust with your bankers is very critical these days.”

Peter J. Nelson, CPA, Chief Financial Officer
American Homes 4 Rent

Prior banking relationships are also important to consider, as they may offer management a comfort level built on previous experiences. It’s worth nothing that in some instances, previous working relationships between a bank and the company may not be entirely relevant during the IPO process, as new players unfamiliar with the company’s story may be introduced to bring the company public. An IRO from a recent IPO noted, “There are banks that I was very comfortable with, but that really didn’t mean a whole lot in the grand scheme of things because the folks that you would be talking to on the underwriting side are completely different from the ones that are on the lending side and the Treasury side. Just because the teams that have been following your company for years know you very well, doesn’t mean that the people that are going to be selling the stock are as knowledgeable as the people that you have been dealing with.”

Pre-IPO Targeting

As marketing efforts get underway, the constituencies involved in the IPO must balance near-term priorities associated with generating the substantial market demand needed to facilitate a successful offering with the longer-term goals of establishing an appropriate institutional ownership base of buy-and-hold investors. In many instances, the initial targeting efforts will be driven by the underwriters, who will likely introduce the investment story to their client base. The issuing company should also look to attract interest for the offering by identifying long-term investors with investment portfolios suited to the company’s story and fundamental profile. Any prior relationships that the company or management team has had with the buy side can be revisited, while stakeholders in the private entity that also have equity ownership complexes should also be evaluated. The IR executive should look to work with the underwriters to make sure management’s time is effectively and efficiently used to market to both constituencies. Darin Arita, Senior VP of IR for Voya Financial commented that it’s important to influence the roadshow and he,

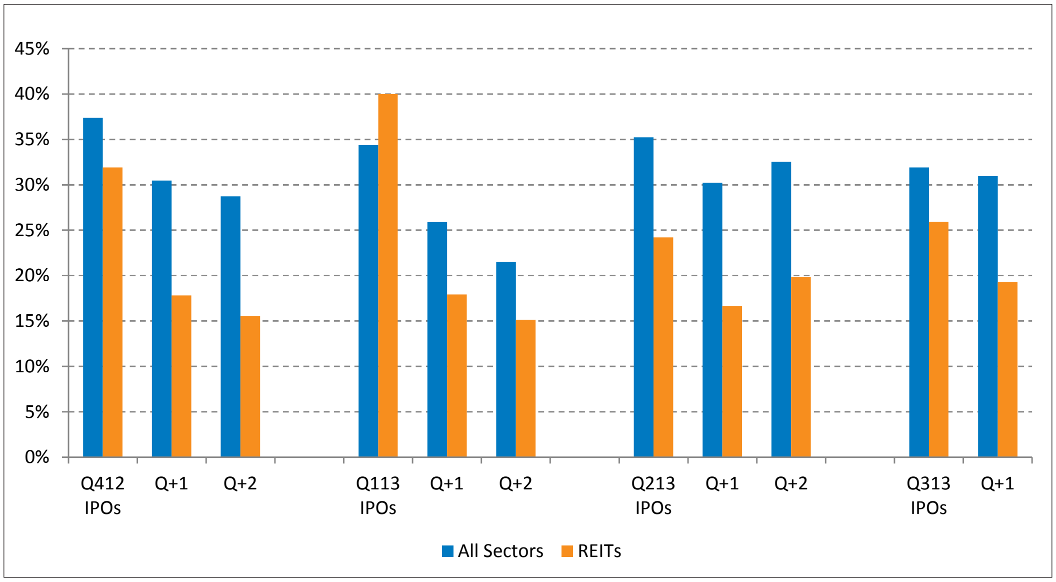
“made sure we were meeting with the right investors in the right cities”

Darin Arita, Senior VP of Investor Relations
Voya Financial

Mr. Nelson of American Homes 4 Rent said, “Coming out as a REIT, I think we felt more comfortable that we could bring in some of the REIT investors we know. Hedge funds definitely did backstop us on the IPO, but we pushed for the type of investor that we are going to be targeting in the long run and that strategy has worked well. Don’t take anything the underwriters say as gospel truth, always second guess it and if you have a hunch, go with it and check it with a second opinion.” As with any stock, it will be necessary to have certain holders, such as hedge funds, to provide liquidity and build a market for the initial offering. Starting with the roadshow and continuing as a company that is still in its infancy as a public company, it is imperative to begin the process of educating and attracting longer-term shareholders to ease the transition as the company evolves. So while the company may have a hedge fund-heavy shareholder base when it first reaches the secondary market, the focus should be on grooming potential investors and gaining interest to fit the profile of how the company will look as the story matures.

In practice, many event-driven investors that focus on IPOs will likely be a part of the company’s initial investor meetings. This type of investor presents unique challenges since they will likely have a shorter investment horizon than many institutional investors evaluating a more mature public company. Given their shorter investment window, event-driven investors may not familiarize themselves as deeply with the company’s story. Therefore, many of these firms will be headline sensitive, which can both create volatility in the newly issued shares and exhaust more of an IRO’s time. Recalling his own experiences, an IRO from a recent IPO noted, “Hedge funds with high turnovers are there for the big pop and then post IPO they are out of the stock within 3 to 6 months. That added a lot of volatility to the stock. The end of the rope for them is the end of the quarter, so they get very agitated with any little short term perceived negatives to the story and we had to do a lot of hand holding because of that.”

Figure 2: Percentage of Hedge Fund IPO Ownership



* Graph depicts decreasing hedge fund ownership in the quarters following the IPO

Source: Ipreo

To evaluate prospective investors' suitability to the company's pitch, an IRO should evaluate factors including the firm's current portfolio makeup, with particular attention being paid to the portfolio's float-cap/liquidity tolerances and fundamental characteristics. Of note, an IPO roadshow represents an excellent opportunity for the company to speak directly with the portfolio managers at many larger firms, rather than speaking to the analyst level as may be the case in many non-deal roadshow situations. Public ownership information can give you a good idea as to which investors have held recent IPOs in the first reporting period subsequent to the IPO. Finding a set of similar, recent IPO companies can serve as a good empirical peer group to help identify investors likely to hold at, and well after, the IPO.

Educating the Street

Once the underwriters are chosen and the roadshow process is underway, educating the Street becomes an important concern for an IR executive. Many company-specific factors come into play, which need to be considered in concert with one another in order to craft the appropriate strategy and message. Among the pertinent factors to consider is the Street's familiarity with the company's story, industry, and business model. This may vary from industry to industry. If there are peers that are in similar businesses, the buy side may already be up to speed on the broader nature of the business, drivers, and investment themes. Even if the business fits well into a current segment of the equity market, the differentiators and competitive advantages of the company's story will need to be covered at length with potential investors. Conversely, many companies coming to the equity market won't have pure-play competitors in the market. In these instances, industry comparisons may not be readily available for the Street to use as a guide when evaluating a new issuance. A lack of industry experience can steepen the learning curve for both the buy-side and sell-side. A challenge for the IRO in these situations is trying to bridge the knowledge gap between a management team composed of industry veterans and members of the investment community who may be taking their first deep dive into the company's story. Reflecting on his company's recent IPO, one IRO said, "When we look back at our IPO, maybe we could have focused on some of the operational things that produce some optically challenging issues for outsiders that weren't particularly conversant, or didn't have a good understanding of our industry, much less our business."

If the business is unique, complicated, or new, more time and care needs to be taken during the roadshow process. The IRO continued, "We put together a road show package and we tried to educate the buy side as much as possible, but there were still some nuances to the business that really weren't obvious to us during that initial pre-IPO process that immediately became obvious later in the process. You have to be able to talk to that junior analyst and get him or her to understand your company and get them up to speed so they don't get tripped up later on." Breaking down a business into smaller parts is one tactic that pre-IPO companies have employed on roadshows. Mr. Nelson of American Homes 4 Rent said, "We had a very basic presentation that broke down our business to the most elemental level, from buying, renovating, leasing and then managing the properties. We just broke it way down into user friendly pieces." Mr. Arita of Voya Financial recommends "working hard with the underwriters to distill the investment story down to 3 main investment points in order to make the presentation more digestible." Mr. Arita was able to leverage his experience on the sell side covering insurance companies in order to appropriately lay out the nature of a complicated investment story.

Early in the process, the company's underwriters should be engaged to add their perspective to the company's message. As a recommendation to aide this process Brad Miller, Managing Director, Equity Capital Markets with Deutsche Bank recommends:

> "Coming in while they're in registration and meeting with a select group of sales people or testing the waters helps organizations get their arms around the story, understand what the main points are and what investor pushbacks potentially could be and how you sell through them."
>
> Brad Miller, Managing Director, Equity Capital Markets
> Deutsche Bank

He added that the benefit of having the underwriter's sales force up to speed is crucial. "Getting a sales force up to speed the morning you're launching your IPO can be somewhat difficult if the story is complex. Can they make that initial sales call? Absolutely, but if there are any pushbacks, it's hard for them because they haven't had an opportunity to really dig deeper into the story."

While helping to develop her company's message to the Street, Kathryn Kieser, Sr. Vice President of Investor Relations with Primerica, explained some of the resources her team utilized. She commented,

> "We did go back and look at all the recent financial IPOs that we thought were received very well and looked at the points that they made, how they approached the market, and their presentations."
>
> Kathryn Kieser, Sr. Vice President of Investor Relations
> Primerica

Ms. Kieser continued, "We also reviewed peers' recent investor presentations to better understand key themes in the sector and to develop differentiating points for a strong investment thesis."

Roadshow

The importance of setting appropriate expectations with the investment community was also highlighted by our interviewees. In order to do this, the best practice is to set achievable, measurable goals and to set guidance where it can be met or exceeded. The results of the first few quarters in which a company is public will be scrutinized by investors as they gauge how much credence they can put into what the management team communicates, projects, and promises. If promises and guidance are not kept, valuation can suffer on that basis alone. Additionally, expectations from the Street will be that management will provide at least the same types of guidance and disclosures post-roadshow as was included in the roadshow. More is acceptable, but less is viewed as less transparent and may cause suspicion. When asked about the company's relationship with the investment community pre- versus post-IPO, Mr. Nelson of American Homes 4 Rent noted, "It has expanded dramatically. I think we gain more respect every day that goes by. Pay attention to what you say and make sure you hit your numbers. So, again, if you are careful and measured about what you say in the IPO, the reaction of the investment community post-IPO will be more positive than if you promise the world and started not delivering results, not hitting targets, not meeting your goals and objectives when you were selling the stock at the IPO." Speaking of his experiences with companies moving through the process, Mr. Miller with Deutsche Bank commented, "The biggest issue that we see companies get wrong is when bankers try to maximize valuation and therefore press a management team's financial model so they're absolutely stretched 100% as far as making their first quarter. Not leaving any cushion for the first or second quarter as a public company is the number one mistake. Those companies that fall in to this trap often have management teams that are stretched and have a higher probability of missing their first or second quarter. If this happens they become fallen angels very quickly and lose their institutional sponsorship. Those companies that get premium valuations to their comp group are those with management teams that build credibility with the Street for being conservative, and having the ability to meet or exceed the Wall Street research community's consensus estimates, quarter after quarter after quarter."

Other considerations for an IRO to address are related to internal preparations. Company executives must be prepared to interact with the Street, as their comments will now be governed by Reg. FD. Both the company's IR and Legal teams will need to mindful that C-suite executives only talk about publicly disclosed information.

Kathryn Kieser with Primerica commented on her experiences preparing with management, saying, "A broad group of officers went through Regulation FD training to sensitize everyone to risks related to the disclosure of non-public material information. As a new public company, we reviewed all information previously disclosed to our varying constituents and developed new policies about which information could be shared piecemeal and which could only be shared through public disclosure. We also educated all company spokespersons on key message points and certain internal metrics that were redefined for ease of understanding by the investment community."

During this transition period, it is important that the management team's strengths and the weaknesses are identified and addressed. Management's aggregate experiences with the business will be called upon, so depending on each member's tenure and career path, varying degrees of preparation time may be necessary to ensure the team can speak knowledgably and on-message about any disclosures made through the company's S-1.

First Earnings Call

Following the IPO, the IR team's attention must shift toward the reporting requirements of a publicly traded company. In most instances, the first major event on the company's calendar will be its quarterly earnings release and the related investor call. Decisions about the format, content, and timing of the press releases and calls should be made with care and rigor, so planning should begin well in advance. Considerations should be given to industry norms and the disclosures made during the IPO process.

In terms of executing the earnings call, considerable preparations should be made with the presenting members of the managament team, including dry runs at the earnings call and the fielding of mock questions from the analyst community. Ms. Kieser with Primerica recalled, "Preparation for the first earnings call was difficult because we were starting with a blank sheet of paper and no one had ever done it before. We began by asking a lot of questions like: What are we trying to accomplish? What pieces of information must be communicated and in what format? What should be in the release, the call or saved for Q&A?" She continued, "The first release was really a ground up process and it has been refined over time. Now we start every earnings cycle by developing an outline of the points to be communicated in each document and then internally discuss which points may need more or less prominence in the materials. Achieving consensus on content prior to drafting the documents has really streamlined the earnings process." Mr. Arita of Voya Financial remarked his team ran "6 mock calls in order to build a level of confidence" heading into the call.

An IRO can greatly add to this process by having a good understanding of what's at the forefront of the investment community's minds. Maintaining an ongoing dialogue with existing stakeholders and other buy- and sell-side analysts following the company's story is paramount. Management should be prepared to answer queries from constituencies with varying interests in the company, which may differ from management's internal views or those expressed by the Street during the IPO process. By working to anticipate questions from outsiders and trying to thoughtfully frame responses to those inquiries, an IRO can help the company set the appropriate tone of consistency with stakeholders.

Underwriting and banking relationships from the IPO process can also be leveraged for guidance during this period. Thinking of common missteps made by newly public companies, Mr. Miller of Deutsche Bank said, "Having management strike the right tone and being fully prepared to respond to investor questions on quarterly updates is critical. All too often, we see a company's stock prices decline during an update call because questions were not answered appropriately, which can raise doubts with investors. Typically, we see this in companies that do not have a head of IR who prepares management for potential questions and investor concerns."

Parting Advice

From an IRO's perspective, tackling the challenges associated with bringing a company public can be an exciting period of career growth. The process is time intensive, but provides a great opportunity to take deep dives into both your company's operations and strategy, while gaining further insights into the functioning of the capital markets.

Many skills will be called upon during the process, as was pointed out by Mr. Nelson with American Homes 4 Rent. "An investor relations executive needs to be conversant at multiple levels. They need to understand the motives and investment profiles of investors. They need to be conversant in the business that they are a part of as well as the financial aspects of the business. They have to touch all of those buttons to be successful, so I would encourage anyone to participate in the way the business is run as well as preparing their earnings release and the

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administrative aspects of the job," noted Mr. Nelson. Offering similar sentiments, an IRO from a recent IPO recommended that IROs try to insert themselves purposefully into the IPO process whenever possible. He further mentioned, "It is very easy to lean on the underwriters, and if you are owned by private equity, to lean on the sponsors to run the show for you and then you just clean up after the IPO is done. There are decisions that are being made that you are going to have to live with and if you are not part of the process going into it, you are surely going to be part of the process of cleaning up those issues when the show's over and everybody has gone home."

Additionally, Ms. Kieser offered some thoughts on starting the process, saying, "You should start preparing your investment thesis, roadshow presentation and Q&As as well as outlining earning material formats well in advance of becoming a public company. The biggest challenge is having enough time to get everything done within the IPO timeline. Beginning the process early allows you to be more thoughtful and effective in your messaging."

Regarding the importance of having quality IR throughout the process, Mr. Miller of Deutsche Bank commented, "Sometimes management teams exclude their head of IR during the roadshow, and I think that is a mistake. The more that IR interfaces with the buy side through the IPO process, the more credibility they will have in understanding the positives and negatives of every mutual fund and hedge fund complex that they interface with, and then therefore the more responsibility they can have post-IPO as far as interfacing directly the buy side. Some people neuter the head of IR by not including them in the IPO process, and then therefore they're only establishing rapport and dialogue after the company is already public, and I think that's a huge mistake."

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Guest Contributors:

Pete Nelson:
Mr. Nelson has served as the Chief Financial Officer of American Homes 4 Rent since October 2012. From 2004 to 2012, Mr. Nelson was the managing partner of Morecambe Partners, LLC, an advisory and consultancy firm focused on early stage companies, workout situations and real estate businesses and transactions. From 1997 until 2004, Mr. Nelson served in several executive positions with Alexandria Real Estate Equities, Inc. including Chief Financial Officer, Senior Vice President—Operations and Treasurer. From 1995 until 1997, Mr. Nelson served as Chief Financial Officer of Lennar Partners, Inc., where he oversaw all financial and operational aspects of the company's investment in and operation of commercial properties. Mr. Nelson graduated from California State University, Northridge with a B.S. in Accounting. He is an inactive Certified Public Accountant in the state of California.

Darin Arita:
Darin Arita is head of Investor Relations for Voya Financial. Prior to joining Voya, Mr. Arita was Deutsche Bank's senior equity research analyst following the life insurance and financial guaranty sectors. In 2011, The Wall Street Journal ranked Arita as the #1 life insurance analyst in the "Best on the Street" survey. Darin graduated from Johns Hopkins University with a BA in Economics. He is also a CFA Charterholder.

Brad Miller:
Brad Miller is a Managing Director in Equity Capital Markets and Global Co-Head of the Equity Syndicate Desk. Mr. Miller is responsible for pricing and execution of the firm's lead-managed equity business across all industry sectors. Prior to joining Deutsche Bank, Mr. Miller was employed as an Executive Director in Equity Capital Markets at UBS Investment Bank, the co-head of Syndicate at CIBC World Markets and a Vice President at Prudential Securities in Equity Syndicate. Over the past five years, Mr. Miller has priced over 200 lead-managed deals helping raise over $250 billion including IPOs, follow-on offerings, block trades, pipes and convertible issues. He sits on Deutsche Bank's US Equity Commitment Committee, is a member of the Global ECM Executive Committee, and is a member of the Syndicate Industry Association.

Kathryn Kieser:
Kathryn Kieser has served as Senior Vice President of Investor Relations at Primerica since the company's initial public offering in 2010. She started with Primerica in 1995 and has served in various capacities since that time, including as the Chief Marketing Officer of Primerica Life Insurance Company. Kathryn graduated from Auburn University and holds a Master's degree from Georgia State University.