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Financial Profiles

Investor Relations & Financial Communications

2009 IPO Workshop

November 17, 2009

Managing a Successful IPO – Been There, Done That

The workshop featured three senior corporate executives who recently completed successful initial public offerings: Michael Burke, Chief Financial Officer of AECOM Technology Corporation, James Jackson, Chief Financial Officer of BrietBurn Energy Partners, and Ira Kerker, Chief Executive Officer of Vitacost.com. Rob Carlson of the law firm Paul, Hastings, Janofsky & Walker LLP moderated the panel. The discussion entailed both the IPO process itself, as well as the conduct of a business as a public company following completion of an offering.

Reasons to Go (and Not to Go) Public

The panelists discussed the various pros and cons of becoming a public company. They panelists gave the following advantages:

- Greater access to capital, at a lower cost of capital, permitting the company to grow even in more difficult economic environments;
- The ability to grant equity incentives to employees, to provide an ownership stake in the business and capital appreciation to those employees while providing greater liquidity;
- Liquidity for the company's shareholders, who have taken risks by investing in a privately held company; and
- Greater discipline applied to a company's business operations that tends to come with being subjected to greater public investor scrutiny.

Conversely, the panel provided the following as disadvantages of being a publicly traded company:

- Increased costs of being public, as opposed to being privately held;
- Significant costs, time and effort involved with the IPO process itself;
- Substantial time and effort required for dealing properly with investors and analysts; and
- Pressure of satisfying shorter-term performance metrics, at the potential expense of longer-term performance.

The IPO Process

Selection of Outside Advisors

The panelists discussed the process of going public, from selection of underwriters and other professionals, to the investor "road shows" and the importance of a strong management team who can effectively communicate the company's message. With respect to underwriters, the panelists talked about the tendency to focus on an investment bank's name, the looks of its "pitch books" or its promises of potential valuations. While these can be pertinent drivers to some companies, the panelists emphasized the importance of management looking beyond those factors and focusing on selecting the investment banking team that brings real value to the process. Given the turbulent nature of the initial public offering process, the investment banker often functions as a coach as much as a banker, and it is important for the management team to have real trust and chemistry with the investment banking team. Investment bankers tend to be salespeople by nature (and by the dictates of their profession), so it is pertinent to have honest dialogues with them throughout the process.

Each panelist emphasized that selecting the right external advisors –including accountants, attorneys and investor relations counsel -- is as important as assembling a seasoned internal management team - for a successful IPO process. All of the major national and international accounting firms are strong; the key is

to make sure that the firm is - providing the company the “A” team as opposed to the “C” team. Management should not be shy in demanding the best partner possible for them from their retained accounting firm. The legal team is critical through the process of becoming public, as well as following the IPO. The lawyer must provide guidance to management, as well as challenge the advice from other advisors (such as the investment bankers) when necessary, to the extent that advice raises legal issues and there are alternative ways of achieving the same goals. Interactions with the Securities and Exchange Commission during the registration process require quality attorneys and accountants, who can address the SEC’s comments while also arguing their client’s case persuasively where necessary. The investor relations team is ideally an extension of the company’s senior management in its ability to articulate a narrative of the company’s story to ensure that investors and analysts properly comprehend it. These professionals also provide an integral point of communication for Wall Street so that management can focus on the business operations.

Selection of Management Team

As with private companies, selecting the right management team for the company is critical. However, the required skill sets can differ from private companies; specifically the ability to interact with investors and the analysts covering the company’s stock. During the road show presentation that is integral to the offering process, management must be able to address investors’ questions and concerns. As one panelist explained, “Reframe the questions so [investors and analysts] can see the way you view the business. If you can align the way the Street looks at the business with the way you look at the business, you’ll be much more productive.” This requires management team members that not only have a strong grasp of the company’s business fundamentals, but also the capability to communicate those to the investor community.

The panelists talked about the importance of acting like a public company before actually becoming publicly traded. One panelist believed that companies seeking to go public should hold regular board meetings, form committees of boards of directors including audit, compensation, corporate governance and other committees and practice holding an analyst meeting. Our panelists also suggested that management focus significant time on crafting the prospectus that is part of the registration statement, describing the business and its growth strategies. Companies should also determine if the management team in place is properly prepared to lead the company through the IPO process and to operate it as an ongoing publicly traded entity. One panelist talked about how he met with the leaders of each major department at his company to evaluate their skills, and ultimately needed to replace many of them with people who could appropriately satisfy the requirements of operating a public company.

The IPO is Only the Beginning; What to Do Once the Company is Public

The panel closed with a discussion of operating the company after it has become public. Many of the same communication skills required to interact with investors during the IPO process are also relevant after an IPO. The panelists discussed the continuing importance of the investor relations function, and noted that that many companies ultimately supplement agency resources with an internal IR person once they are public. The same rigorous analysis that the board and management should be applying to the company’s performance (revenues, costs, profitability, relative position in the market) will continue, and now will all be monitored by Wall Street and other stakeholders as well. Executive compensation will be more closely monitored, particularly in companies that are not meeting performance expectations.

In short, the IPO is not an exit for company management; it is the beginning of operating as a public company. Being public can be a rewarding success story for many companies, but it requires discipline in management, operations and communications with Wall Street.

IPO Market Update

The IPO market is as strong as it has been in over a year. In 2009, there were 59 IPOs (not including SPACs), an improvement from 31 in 2008, but far from the historical norm. Looking at 2010, Jefferies & Co. expects to see a continued strong IPO market based on a number of factors, including the recent uptick in IPO filings. While the filing of a registration statement for a potential IPO does not guarantee that the IPO will launch, a greater backlog typically leads to a higher number of offerings. At years end 2009 there were 73 filed IPO's on the 180 day backlog with another 20 to 30 confidentially on file with the SEC. This is the largest backlog in almost 18 months.

The 2009 IPO market was well-diversified by industry. Technology companies led the market, accounting for 29% of all IPOs in 2009, followed by consumer at 22%, finance at 18%, real estate at 15%, health care at 11%, and industrials at 5%. In early 2009 profitability was more important to investors than growth, however, that trend reversed throughout the year. By the fourth quarter of 2009, investors were mostly looking for companies with reasonably high growth rates and some level of profitability. The majority of the 2009 IPOs were greater than \$75 million in size, typically resulting in post-IPO valuations of \$200 million or more.

Alex Lehmann, Managing Director of Equity Capital Markets at Jefferies & Co. commented that companies that are considering an IPO in today's market should have:

- High predictability and visibility of revenue and earnings
- Long term revenue growth of 10-15% and earnings growth prospects of 15%+, if a growth company
- Solid industry fundamentals
- Strong track record and secular story
- Defensible market position
- Management team experience, depth, continuity and incentives
- Sound internal systems and financial controls

In recent years it has become apparent that new issue windows can open and shut more quickly than ever and many companies are getting ready to access what appears to be a currently open window.

Jefferies & Co. believes that the IPO market will likely build in 2010 as many PE and VC backers look to capitalize on what appears to be an open financing window. Private equity firms specifically are looking to access the public markets by taking public some of their take-privates that occurred during the period of 2003 to 2006.

Fund flows to both hedge and mutual funds suggest that investors still have a good deal of cash sitting on the sidelines that will need to be put to work in the first quarter of 2010. Hedge funds, most of which were "short" the equity markets in the first two months of 2009 and earned large returns, are holding large sums of cash. Mutual fund outflows of the first two quarters of 2009 have reversed, and they have funds to commit.

With unemployment reaching 10% - and likely to stay there for the near-term - a weak economic outlook and concerns around growing US debt and subsequent long-term inflationary impacts, there remains a heavy overhang on both the US and global markets. This overhang creates some uncertainty for equities in 2010. Even given that uncertainty, however, Alex Lehmann commented that looking to the opening of the new decade his firm is more optimistic than a year ago but still cautious. There is significant capital remaining "on the sidelines" for IPOs and once investors gain more confidence in economic conditions, the IPO market will gain even greater strength. It is therefore important for management of privately held companies who are considering the public markets to take the necessary steps now to be ready to take advantage of market opportunities.

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