Financial Profiles
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New Rules for the Road — Communicating with Wall Street in 2009

For many companies, 2008 was a "perfect storm" from many perspectives, including investor relations. The S&P 500 Index declined by over 38%, the worst performance since the Great Depression. As a result, most companies experienced significant declines in valuation - large cap stocks became mid cap stocks and mid cap stocks became small cap stocks. The following is an overview of some of the factors behind the decline along with our recommendations for re-engaging Wall Street in 2009.

- Mutual fund outflows topped $195 billion during 2008. This compares to outflows of $28 billion in 2002, the only other year since 1990 that experienced net outflows. Investable dollars sitting on the sidelines are substantial with over $4 trillion currently invested in money market funds.

- Hedge fund assets declined from a high of $2 trillion in early 2008 to $1.5 trillion at year-end as investor redemptions forced many hedge funds to quickly liquidate assets. Nearly 700 funds shut down in the first three quarters of 2008. Some experts predict that hedge fund assets could decline to less than $1 trillion by the end of 2009 as thousands of still struggling hedge funds face continued redemptions and the Madoff scandal takes its toll. Barclays Capital strategist Robert McAdie forecasts that as many as 70% to 80% of hedge funds could disappear in 2009. Hedge funds played a critical role in creating liquidity for small and micro cap stocks in recent years and companies who relied on them will have to identify new sources of support.

- Unprecedented consolidation of top tier investment banks drove continued declines in the quantity and quality of sell-side research in 2008. Institutional Investor magazine's recently published 2008 All-America Research Team, notes, "The upheaval on Wall Street is reflected in our results, with 19 of the No. 1-ranked analysts new to the spot since last year – and 13 of those appearing on top for the first time." Looking ahead, we expect resource-constrained investment banks to decrease the research, roadshow and conference opportunities they offer corporate clients. More so then ever, companies will have to take their stories direct to the buy-side.

Is now the right time to re-engage Wall Street?
While many fund managers are currently sorting out what strategies they will put in place for 2009 and beyond, many have already formulated their plans and some have already begun placing bets. Investors will likely take a more measured approach toward committing capital than in the past. However, we believe that companies with sound fundamentals should begin the process of re-engaging the Street.

Our market intelligence tells us that:

- Fund managers will put money back to work this year but they will choose stocks slowly and selectively. The risk aversion barometer remains high but even some of the most skeptical fund managers believe this market has created some of the best ever buying opportunities. That being said, fund managers, like consumers, are bargain hunting. The good news is many fund managers have assumed a longer term investment horizon than we have seen in recent years.

- Investors realize that lots of investments that looked like home runs last year are worthless in the changed environment. Companies that have fine-tuned their strategic plans and positioned themselves to not only weather the storm but to more effectively compete in the future will be best positioned to attract new capital. Near term, we expect that fund managers will be looking at recession-resistant industries and those that will benefit as the Obama administration allocates stimulus funds to its top priorities

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– healthcare, infrastructure and clean technology. They'll also be searching for companies with healthy balance sheets and liquidity, proven business models, high barriers to entry, and strong market share.

Who should you talk to?
Given the year-end volatility, many companies are awaiting December 31, 2008 13F data which is due on February 15. An analysis of this data should be helpful in getting a handle on what your shareholder base looked like at year-end and in formulating shareholder targeting plans for 2009.

- Shoring up relationships with existing institutional holders should be a top IR priority for companies this year. We'd suggest reaching out to existing institutional investors to encourage the continued support of your large holders and to capitalize on opportunities to convert smaller holders into larger holders.

- If your company has transitioned from a midcap momentum play to a small cap value play, you'll need to target a new set of investors with a revised set of investment messages. As you look at comparative 13F data, it's important to compare your company to other companies with similar market capitalizations and fundamentals. Your investment peer group may need to be reevaluated.

- Keep in mind that if your market cap has shifted substantially, you may have an opportunity to transition existing positions to another fund manager at the same institution. Some fund managers have begun to change their market capitalization definitions. Baron Funds, which manages $19 billion in equity assets, for example, recently decreased its minimum market cap requirement for its mid cap growth fund to $1.5 billion from $2.5 billion. At the same time, many micro cap and small cap fund managers have increased their minimum market cap requirements.

What should you say?
We believe now is an ideal time to update your corporate positioning and investment messages to address the current environment. Too much has changed to simply hit the road with last year's story. Outline for investors the changes you have made to your operating plan to deal with the fact that the world has changed. Explain why your company is a relevant investment today and why you'll emerge better positioned coming out of the crisis than you were going into it.

You'll be able to sell your long term opportunity only after investors are satisfied that potential risk is already baked into the current valuation. The credit markets remain essentially frozen and balance sheet strength and liquidity are top of mind concerns for investors. While you should expect continued questions about these factors and your prospects for 2009, we'd suggest continuing to remind investors of your longer term growth plans as well. And, as always, talk about what you know and as part of developing your 2009 story, avoid making statements that you'll be forced to change or retract later. Consider conducting an investor perception study of analysts and current holders to get your arms around current Street sentiment.

If you'll be educating a new group of investors this year, make it easy for them to understand your story. Take a step back and provide basic market opportunity and competitive landscape data. Credible information is in short supply right now; back up estimates with third party data from credible sources whenever possible.

If there's more to the story than what shows up on a quant screen, take the lead in filling in the blanks for investors. For example, if you have a large debt position but have no debt maturing until 2012 and your lead bank and syndicate includes all the top tier banks, you'll need to address such risk factors in conversations and meetings with investors.

We would welcome the opportunity to talk to you about your strategies for Wall Street communications in 2009. Please feel free to call Moira Conlon or Jonathan Destler at 310.277.4711.

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Sources: Seattle Times, Istockanalyst.com, Business Week