Effective Story Telling: The Key to Investor Confidence

How is it that certain executives and companies are able to emerge from difficult announcements or even crisis looking clear-headed and in control?

The financial news of the day is filled with examples of the destruction of executive reputation. We have all seen the extremes of malfeasance sensationalized in the press, but the reality is that the reputations of executive management teams are constantly under attack from one direction or another. In some highly public instances, a major misstep in strategy – or worse, ethics – results in an irreparable loss in reputation and confidence. But much more frequently, executive reputation erodes over time (or simply never elevates to a strong market-shaping position) as a result of an accumulation of small errors or the lack of a clearly articulated strategy – a position that leads investors and other stakeholders with the sense that a company is directionless, disconnected with its industry, unclear in its strategy, and vague about its prospects.

In companies that lack an ongoing thread that binds together their communications, hard questions are often not answered soon enough or, if answered, seem to message an unforeseen shift in strategy that investors take as a signal management has lost its way. A “death by a thousand cuts” drains investor confidence, pressures valuation, and leads to ill-timed strategic announcements that would not have been necessary had the company’s capital markets communications had been more consistent, effective and compelling. Paradoxically, while important as support points, some of the elements that are the hallmarks of investor communications – operational issues like Lean implementation, financial processes and employee realignments, for example – can contribute to the sense that a company’s (and executive’s) approach is tactical versus strategic if overly focused upon.

By contrast, successful executives build up credibility during good times – and use that credibility to help manage bad times – by creating a compelling investment narrative. This narrative defines a company’s long-term objectives and outlines how management will execute in a variety of environments to achieve those objectives, and includes qualitative elements like company culture, customer interaction processes, key individuals, R&D processes and other factors that round out the public’s perception of a company’s ability to sustain performance and compete effectively. Doing so lays the groundwork for future communications when performance seems to diverge from financial expectations. A tough announcement can be explained in the context of a long-term story about a company’s strategic direction – one their management has communicated and reported against consistently over quarters, if not years. While a negative event will still lead to investor questions, those questions can be more effectively addressed through consistent, honest dialogue – one that gives investors the confidence to stick with their investment and support executives during difficult times, and that gives new investors a compelling sense that bad news can represent, if anything, an opportunity to buy into a company they believe in.

As a roadmap to establishing or maintaining that trust, consider the following guidelines.

Communications with investors needs to be viewed as a continuum, not as "spot" communications in isolation.

Every story needs to flow logically and build on what has already been said. Articulate the strategy and goals at the beginning and, over time, develop the narrative of how the business is evolving, how the strategy is being executed and how the scenario is progressing. Each discrete communication needs to be positioned within the context of and flow from what has been said previously.

Operational and financial plans and achievements are the proof points to the value of the story – not the story itself.

Investor communications are, by their very nature, filled with some of the smaller and larger elements of a company's successes, struggles and failures. But for these elements to have stronger value, they need to be the proof points to the story of how a company is progressing towards its stated goal. And that goal needs to be expressed not in terms of operating margins, cash flow or EBITDA, but in terms of where the company is and wants to be within its industry segment.

Investors always want more information – and not necessarily just more financial guidance. They also want to understand the qualitative dashboard key executives use to run the business, as well as the mosaic of factors that are driving performance across all dimensions of the business and their interrelationships. Many fundamental investors try to assemble this mosaic themselves by calling vendors, customers and other industry experts. In a market with a thirst for context, companies with the steadiest followings are those that tell a compelling story rather than simply issuing financial reports or resorting to corporate taglines.

Articulating and believing a corporate narrative frees executives to go off-script, making them more responsive and believable in challenging times.

Executives who grasp and own the corporate narrative put themselves in a strong position to respond to crisis, or to drive perception in instances when it becomes apparent their explanation of an issue is not cutting it with investors. Going off-script may make communications professionals in the room cringe, but candid, direct responses give investors confidence in ways that are not measurable by consensus estimates – provided they support rather than depart from or undermine the ongoing narrative. And that confidence translates into stronger credibility when communicating bad news or managing crisis.

Many will point to Regulation Fair Disclosure (Reg FD) as a deterrent to more detailed investment narratives; but in the end, executives have a fair amount of discretion over what information they decide to make widely available. Providing elements of the mosaic is not a violation of Reg FD if they are not material, non-public information. A good approach to creating an effective investment narrative is to forget for a moment about the question of what has to be disclosed in filings and instead to consider the characteristics that make your company unique, your story more credible, and your competitive position more defensible. This more qualitative approach is fully aligned with the SEC's bias towards the issuance of more information, more continuously updated. The fact is that the SEC has never initiated an enforcement action related to qualitative discussions or sent a comment letter questioning management's issuance of additional investor-facing content.

Test the narrative with objective, unbiased, and less-informed audiences, and make sure it answers investors' questions and addresses their concerns.

Products and services are tested with representative target audiences at every turn. A company's investment narrative should get the same treatment. It is critical that the narrative resonate with the audience you are trying hardest to reach and answers the concerns of those who perceive it as falling short. It is important not to not fall into the trap of asking only your largest, most dedicated investors whether they think the investment narrative is effective because they already buy into what you are selling. Instead, consult with investors who are not intimately familiar with your business and investment proposition and do not own the stock. They have less bias and no vested interest in the validity of what you are saying. If you can enhance their perspective and swing their sentiment by providing better answers to their questions, you will know that your message is resonating. You will also likely have attracted some new investors who are willing to pay a premium valuation.

Share the narrative directly with the investors who are most interested in hearing it and are most likely to consider it as a basis for long-term decision-making.

Different types of investors have different holding periods (and attention spans), and targeting and management time should be managed accordingly. The investor relations team should be managing investor interactions closely, rationing your time appropriately to ensure that investors with whom the narrative might resonate, who can initiate solid positions or have the capacity to add to their positions, get their fair share of your time. Also, set aside some time – maybe just one phone call per week – for conversing with a new investor about your company's investment narrative: someone who commands the dollars or influence to make a difference in your stock. And integrate feedback and learnings from those new, fresh interactions into the finer points of the narrative as it evolves.

Make sure the narrative can resist the hiccups or crises that will inevitably occur.

If the past year tells us anything, it is that all companies hit rough patches from time to time. There are plenty of examples of companies that managed effectively through adversity, and others that did not. Investors tend not to forgive executives they believe should have foreseen issues and managed around them, or have failed to position their companies for especially turbulent periods. The quarterly impact of currency volatility, major swings in commodity costs, or the loss of a key customer contract can all chip away at company and executive credibility. Conversely, many such issues can be defused, and executive reputation actually strengthened, by building the potential for performance hiccups into the investment narrative. If your management team struggles with the notion of discussing potential problems before they occur, draft a straw man release of a piece of bad news. This can be a stark "reality check" on how well your investment narrative has prepared investors for difficult news.

Help your board of directors understand how investors and sell-side analysts feel about your current investment narrative.

Company executives are likely to have a solid handle on Street sentiment. And while they do not always use this knowledge as the basis for strategic decisions, they do rely on it to figure out how to best communicate in good times and in bad. Oftentimes, boards do not have access to that same market intelligence and they can, as a consequence, be tone-deaf in their advice on how to manage through tough business news.

Board members need information that will give them an advance look at how investors will react to an investment narrative that has been damaged by short-term business problems. While sharing the most recent sell-side headlines can be helpful as a snapshot of current investor sentiment, it is not often as valuable in predicting longer-term investor reaction. What is likely to be more useful is providing board members with continuous feedback from a wide swath of investors, covering such issues as current valuation and management credibility; missing factors related to corporate strategy and performance – vis-à-vis competitive and investment peers; and concerns on macro-industry or corporate-specific issues and their impact on valuation. Armed with this information, the board can more effectively consider the impact of corporate announcements on stock price valuation. Additionally, it may make them less likely to muzzle management when the news is negative.

Buying the time and trust needed to take effective action

Credibility is, by definition, the sense among stakeholders that you are telling them the truth. Which means that crisis, when the truth is hardest to tell, is when credibility can be strengthened the most. A strong narrative can give an executive the time to put him- or herself in position to address issues with credibility. The most powerful words in a crisis are, “We already have a plan in place and are executing on it to solve the problem, and it does not change our long-term plan.” Yet these words resonate only when trust has already been established through consistent communications. Most negative issues are ultimately rectified by smart management decisions and time. A tested investment narrative is critical to buying a company and its executive team the time to allow executives to do what they are hired to do – manage the business.

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