CONVENE

WHITE PAPER

WHY MEETINGS ARE SUCH AN IMPORTANT PART OF THE INVESTMENT PROCESS

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It is no secret how fundamental meeting with management is to a Portfolio Manager's (PM) investment process. Industry surveys consistently highlight that access to company management continues to be the most valuable research service provided by the sell side and even as the way meetings are organized and paid for evolves (due to the upcoming MiFID II regulations), it is clear that PMs will continue to view access to management as a necessity.

Smaller asset managers can engage in 1000+ meetings a year, with this scaling up to 200+ meetings a week for some of the largest global firms. We don't believe it is an exaggeration to state that for a value focused PM, attending meetings with corporates, combined with the preparation and writing of notes, consumes the majority of their working hours. Considering how much effort goes into investor meetings on all sides; the Portfolio Managers, IR teams, Sell Side Corporate Access teams and not least the management participants, for this whitepaper we wanted to explore, why PMs place such importance on meeting with management? What type of meeting formats they prefer? And most importantly; the key characteristics they look for when assessing management.

When asking the question "Why do PMs place so much value on meeting with management?", It is often assumed that the purpose is to gain an information advantage about the short-term outlook for a company. Not only is this illegal, it's also often a futile exercise as management are typically very well prepared by their IR teams on what they can and can't divulge. From our canvassing of PMs, the answer is much more straightforward - the most common reason given was to assess management's skill at allocating capital. As many PMs will state, even CEO's that are well intentioned and have a wealth of skills and experience do not always know how to allocate capital effectively. Proper capital allocation builds long-term value, which is then reflected by the stock market in terms of share price. Alternatively, the companies that primarily focus on boosting their short-term share price frequently make decisions that erode shareholder value.

With this in mind, it is no surprise that PMs place such importance on evaluating this skillset when meeting with management.

Assessing the ability of management to make the correct capital allocation decisions is no easy task and definitely more art than science. From our research there appears to be a number of different approaches Portfolio Managers take. However the one consistent theme that emerged was that no one we spoke to had yet distilled their approach into a quantitative process that they considered to be foolproof. Many Portfolio Managers were quite open about the fact that making judgements on an individual's capabilities in just a few, relatively short meetings is challenging and that to compensate for this, often their primary goal is to just try to get a feel for management's mindset and temperament. The belief is, there are a set of common characteristics that give a good indication of how likely it is that management will act in the most appropriate way when faced with the big decisions.

To go a level deeper on this, we asked each of the PMs we canvassed two questions:

1. How important is the meeting format in helping to make an accurate assessment of management?

2. What are the key characteristics they look for in the management of the companies they invest in?

Meeting formats and PMs frustrations

The overwhelming conclusion to the first question was that, the meeting format is very important in helping to make an accurate assessment of management. It was surprising to hear PMs were rather particular with what they regarded as bad formats. Specifically, things that frustrated them in relation to the structure of meetings. As might be expected, the number one frustration for many PMs was related to the volume of attendees (on both sides) in the meeting. The presence of company managers, investor relations, sell side analysts and salespeople, in addition to the investment professionals from various internal teams is widely considered to be an hindrance to building open dialogue. The smaller the number of attendees, the easier it is for management to be more open about how they think and for the PM to build a relationship with management. Building good relationships with management emerged as a central focus and one asset manager we spoke to has even implemented a policy that designates a single PM as the lead contact for specific corporates (irrespective of how many holders of the stock exist in the firm), with the express purpose of ensuring continuity and building familiarity, in the belief that people are more open with those they know.

A further point raised about smaller groups was that it reduces the risk of colleagues trying to display how knowledgeable they are about a certain subject, which often leads the meeting away from the core discussion topics and takes up valuable time on unnecessary detail. With meetings usually lasting only an hour, PMs want to keep the discussion focused and avoid going off on tangents.

The final point raised in relation to meeting format was the role of analysts, which is closely related to the point raised above - not letting the meeting get bogged down in unnecessary detail. A number of PMs highlighted the tendency of some analysts to drive the conversation on behalf of management which can subsequently lead to a heavy focus on near-term issues that impact earnings. For the investor focused on the long-term, topics such as how a short-term spike in the oil price, or specific weather conditions during the quarter impact earnings are nothing more than a distraction and of little interest. They would much prefer to focus on areas such as whether management has a good understanding of the competitive environment they find themselves in and whether they can articulate clearly their long-term strategy for driving growth.

To summarize, PMs want a meeting format that is intimate thus providing them with an opportunity to build a relationship with management and most of all, allowing for a focused discussion on the long-term outlook for the company.

Taking a look beyond the meeting format, when asked "What are the key characteristics they look for in the management of the companies they invest in?", there was a general consensus in the responses we received. We have selected five of the most common characteristics provided by PM's in their answers:

1. Management are honest
2. Displays humility
3. The CEO/CFO trust each other
4. Able to clearly articulate company strategy
5. Understanding of potential disruption in their industry

Honesty and Humility

The challenge PMs face is that it is very difficult to accurately judge whether someone is honest in the relatively short amount of time that meetings allow. Again, this results in PMs looking for certain behavioral clues that can help them gauge the trustworthiness of management. The answer to an innocuous question at the start of the meeting about how management would assess the previous 3-6 months, can be quite telling with respect to the intellectual honesty that management display. Does management only focus on the positive? How do they communicate the mistakes that have been made? The ability to be honest about where management have made the wrong decisions or even mentioning areas of the business that are weak and in need focus, especially when unprompted, is highly valued by PMs.

It shouldn't be underestimated the level to which PMs will analyze even the smallest of behavioral patterns in order to get a 'read' on management. This goes beyond how management conduct themselves in meetings and extends to any piece of information that the PMs can extract. Where are management staying during their trip? Is the management team that is staying at the most expensive hotel in the city really one that is concerned with company money? Is the CEO that is overly focused on the cultural activities available in the city they are visiting properly focused on investor meetings? Even something as simple as travelling with a large delegation can be interpreted as self-important behavior on the part of the CEO. Travelling with assistants and various company managers who are not provided with a platform to speak in meetings is often seen as a vanity exercise. Also, do not be surprised if even the clothes management wear are scrutinized. One PM highlighted that if the management of an industrials company are wearing designer suits and shoes, this could be a sign that they are more comfortable in the boardroom with management consultants than on the factory floor with their employees. Although this may be getting firmly into the realms of conjecture, a consistent theme emerged in PM's answers that signs of vanity were universally interpreted as negative. To return to a point we made at the beginning of this paper, displays of vanity raise concerns that management may be more interested in making decisions that boost the short-term share price and in turn their own reputations rather than taking the actions that build long-term value even if they are less likely to make the business pages.

Trust between the CEO and CFO

To anyone with only a basic understanding of how large organizations work, it is obvious that the CEO and CFO need to be aligned on company strategy and more generally have the ability to work together as a cohesive team. The best companies operate with a CEO and CFO who trust each other to not only have the company's best interest at heart but also their own. In addition to this, PMs want to see that there is regular, ongoing dialogue and that the CFO is involved in strategy setting. As CFO's are typically more involved in the granular running of the company and the quantitative day-to-day activities, if they are not regularly consulting with the CEO, the CEO could be missing the key details that impact their ability to meet strategic objectives. To put it bluntly, if CFO's are not at the table when strategic decisions are being made then they are not doing their job properly and neither is the CEO.

To this end, PMs will look closely at how the CEO and CFO interact in meetings. Are their answers aligned and are they delivering a consistent message? Does their body language indicate two people who are comfortable spending time with each other and more importantly, demonstrate mutual respect? Simple behavior such as the CEO cutting off a CFO's answer can be a sign that the CEO doesn't fully trust their CFO and will be marked down as such by an astute PM. Not for the first time in this article, we will reiterate that PMs will take every piece of information available to them in order to build up a picture of the how management operate and will constantly be looking for visual clues as to the strength of the relationship between the CEO and CFO.

Ability to articulate strategy and the competitive landscape

The last area of focus is the ability of management to communicate their strategic vision and understanding of the competitive landscape. PMs want to see not only the existence of a clearly thought out strategy (rather than simply a list of short-term share price targets), but also an honest appraisal of the situation the company is in versus their peers, the competitive threats they face and how they plan to respond to these threats. It is always worth remembering that PMs are often looking in detail at the whole sector and are almost certainly analyzing what competing companies are saying. Many PMs will want to test management by asking questions such as "Your competitor x, stated that prices in Asia were under pressure due to oversupply. Is this also your experience?". Being fully prepared to talk about the activities of peer companies shows a detailed understanding of the market which goes a long way towards impressing PMs.

Although a charismatic CEO who has the ability to paint a picture of a future that both excites and inspires commitment to their vision is still something that a number of PMs value, they increasingly want to see that the management team can display a good understanding of any incoming threats to their business and aren't showing any signs of complacency with regard to competitors or industry and regulatory change.

Takeaway for IR teams

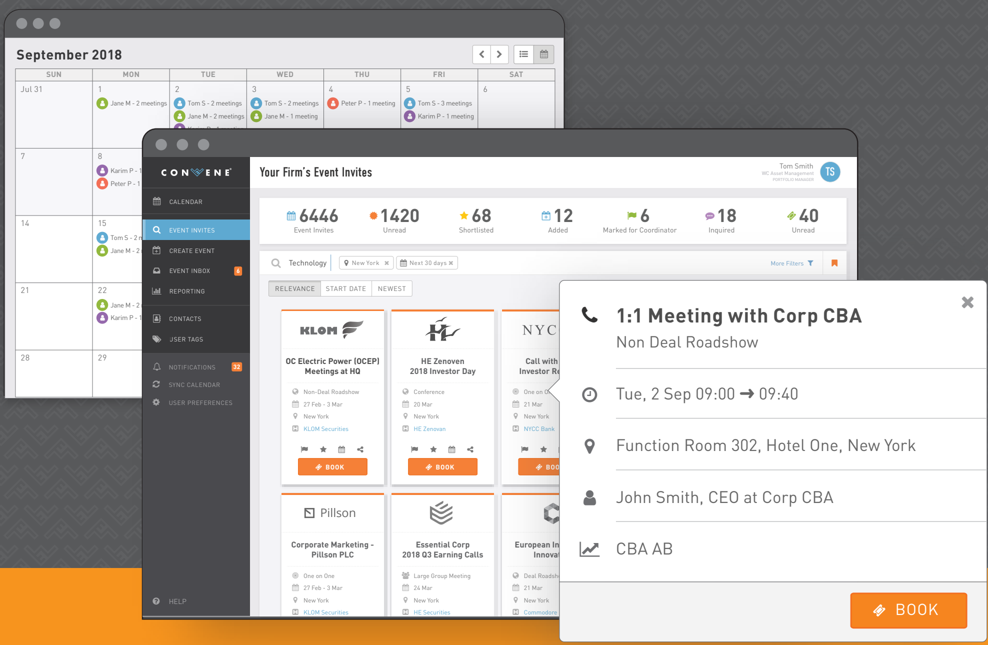
Throughout this paper, we have highlighted the key focus and frustrations that many PMs often face and hope that these insights into the mind of PMs can help IR teams prepare their management teams for future investor meetings. The challenge as we see it, is that a large part of how PMs assess management is based on personality and for obvious reasons, it is unlikely to be within the power of the IR team to fundamentally change the personality traits of their senior management.

That said, with the knowledge that PMs are constantly trying to glean any informational edge wherever they can, IR teams should focus their efforts on controlling the areas where perception is key. Limiting the people in a meeting to only those who strictly need to attend; perhaps thinking twice about staying at that expensive hotel (no matter how good the broker secured corporate rate is) and most importantly ensuring that management are well prepared with a consistent message and can speak intelligently about the company strategy and competitive landscape.

And if the above proves too much of a challenge, one fail safe way to impress PMs is for the management team to demonstrate a genuine interest in hearing the PM's opinions and commit to taking them on-board. Nearly everyone we spoke to highlighted that they appreciate when management asks their opinion - something that is simple, takes no time and absolutely anyone can do.

ABOUT WECONVENE

WeConvene is a global, independently owned web-based platform that automates corporate access consumption and evaluation for the investment community. Events large and small directly impact investment strategies and WeConvene provides value to buy-side, sell-side and corporate organizations by enabling efficient discovery, booking and tracking of meetings.



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