IR
INVESTOR RELATIONS

THE FINANCIAL COMMUNICATIONS JOURNAL

The Investor Relations Firm AG
www.irfirm.biz

9th Issue June 2004
2,000 copies

Timing issues in IR

Stock exchanges around the world have regulatory frameworks in place which aim to ensure the transparency of capital markets and the equal treatment of shareholders. Heinrich Henckel, CEO of SWX Swiss Stock Exchange, clarifies why these requirements are important and what mechanisms are in place to enable companies to make timely announcements.

Illustration: Paolo Friz, Illux

The stock exchange: establishing a marketplace and monitoring its participants

MORE HASTE – LESS SPEED

Timing issues in communication can be pivotal in a number of situations of a "communicator's" life. Unfortunately, very often it will be only noticed by the audience once the implicit and explicit guidelines of handling critical information have not been observed.

The most relevant explicit rule in timing refers to the "Ad hoc Publicity" guideline, which is used in different variations throughout the various stock exchanges. However, the core of all the "proprietary" rules and obligations is the same principle: All investors are supposed to be informed at the same time, in the same fashion and at the same time as the issuer gains knowledge about price-sensitive information. Furthermore, investors and analysts are supposed to be given sufficient time to analyse and interpret the information release. Hence, in the regulatory environment, the time issue pops up in three different guises: 1) immediate information, 2) equal treatment, i.e. informing everybody at the same time, and 3) releasing material information sufficiently before or after trading.

However, for the Investor Relations professional, there are other relevant – rather strategic – time issues. When considering how to communicate corporate actions or changes in outlook, timing and extent of information become hotly discussed. The question arises whether priority should be given to quick information and taking the risk of not being in the position to give full information and having to continuously change the facts, or to wait until complete information can be given to the interested public. Some might think that the Ad hoc Publicity guidelines would offer some guidance. Yet, on the contrary, the guidelines offer loopholes in these special cases and ask for priorities and sound personal judgement.

News and its fast distribution is a critical commodity in today's financial world. Newswires play a central role in this drama. Their capability to collect, put into context and distribute information in virtually no time is vital to the investment community. Being able to cope with reams of information, to screen and handle them under heavy time pressure – very often early in the morning –, and still not lose the gut feel for what is the market-moving story, seems to be the key profile of the newswire journalist.

Hence, the Investor Relations professional will very often have to take timing issues into account. He will almost always apply his personal judgement and experience, whether when asked to hurry – because the regulator requires him to do so – or to slow down – because the management expects him to do so. Yet, very much to the professional's relief, latest-stage information technology will very often offer new tools to support him in the execution of this task.

Jan Gregor, Partner
The Investor Relations Firm AG

What can you do as a stock exchange in enacting regulations to bring improvements to transparency and to conform to the international established accounting regulations which will be required from 2005?

Heinrich Henckel: The Stock Exchange Act binds us, in the framework of self-regulation, to take into account internationally established standards. The SWX Swiss Exchange therefore follows international developments closely. However, changes to the regulatory framework must balance benefits against costs. In the given context we are fully compatible with developments in the EU: International Financial Reporting Standards (IFRS), formerly called International Accounting Standards (IAS), have already been accepted as standard by SWX for many years now.

The ever-increasing requirements in communication also lead to an increasing complexity; and a simple task – that of the communication of a company's activities – hence becomes more and more complex. In the future, people will hesitate to communicate substantial information without first having legal advice, which is not really in the interests of shareholders.

Heinrich Henckel: The company's obligation to communicate has never been an easy one. The rules of the SWX Swiss Exchange, which have been in existence for several years, are well established and correlate to the standards of other stock exchanges. The professionalism of the issuers when dealing with questions regarding Ad hoc Publicity rules is today at a very high level – in fact, nowadays we are barely encountering major breaches of these rules.

Article 72 of the Listing Rules formulates an obligation for issuers to communicate – it is clear that in doing so, the relevant rules must be adhered to and that if the case may be, expert help is available by the SWX.

The SWX and you postulate self-regulation as a sustainable principle of stock exchange surveillance. Where do you see the limits to this self-regulation?

Heinrich Henckel: The idea of self-regulation is subject to misconceptions. It leads one to think that the SWX regulates itself. That is clearly untrue. The stock exchange is regulated by the legislator and by the Federal Banking Commission. The stock exchange's regulations need to be

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Communication's legal framework

As companies' obligations increase and the timing of communication acquires paramount importance, the regulator has had to adopt the appropriate framework for capital markets communications.

Dr Dieter Gericke, LL.M. Partner,
Homburger attorneys-at-law, Zurich

From a legal point of view, corporate communication can be divided into four categories:

- periodic information (mainly financial reports),
- event-related ongoing disclosure regarding price-sensitive facts (so-called Ad hoc Publicity),
- transaction-related information (prospectuses, proxy statements, shareholder information), and
- informal "other" information (reputational publications, product advertisements, information on non-material events, etc.).

Historically, only the formal prospectuses in connection with capital market transactions (public issuance, sale or purchase of shares, bonds and other securities) have been subject to capital market regulation. Today, however, most types of corporate communications are regarded as relevant to guaranteeing transparency of capital markets and, therefore, have become subject to increased regulation.

Market transparency and efficiency
All corporate communication serves the purpose of furthering a company's image as being reliable and trustworthy: however, such communication also informs capital markets on the value and prospects of shares and other securities, thus increasing transparency of the market.

What is efficiency of capital markets, and what is its purpose? The theory is that, in an ideal world, the price of a security reflects all information available on the security, both good and bad. Prices would, therefore, be "right", and the funds of investors would thus be allocated to their most productive use. This, in turn, leads to the growth of businesses and economies, while "punishing" and minimising inefficient use of funds. Therefore, prospectus requirements and other information requirements do not (only) serve the goal of informing or protecting individual investors but, rather, the efficiency of the market as a whole. From such perspective, most categories of corporate communication are deemed relevant in achieving the goal of market efficiency: it does not matter on which occasion, and for what purpose, a company is informing the public, i.e. the capital market. In lockstep with this development, rules on periodic information by financial reports, ad hoc disclosure of the fact that a company's CEO has resigned, or the information of existing shareholders on the goals and impact of an upcoming merger with another company, etc. are reaching beyond their traditional underpinnings (rules of bookkeeping, avoidance of fraud, equal treatment of investors, corporate law and shareholder rights, etc.) and are now seen as part of the framework that provides for market transparency.

Dr Dieter Gericke

While capital market information takes on a variety of forms, the standards to be observed with respect to the content and the quality of such information all reflect the goal of market efficiency. International deal practice has enabled the convergence of views as to such quality standards. Irrespective of the applicable set of rules and regulations, generally, a

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Continued from page 1

submitted for approval to the FBC and the latter also acts as supervisory authority. This time-proven regulatory model comes across as an efficient, flexible system which benefits from expert knowledge. Another example for this sharing of responsibilities are the modern accounting standards (IFRS, US GAAP, Swiss GAAP) which today no longer come from the legislator but rather from non-governmental organisations.

Self-regulation no doubt has its limits where the stock exchange is itself being listed. In such a situation, conflicts of interests may arise, so that the stock exchange might have to be relieved of regulatory tasks.

What influence has the increase in technical developments allowing the availability and fast dissemination of information, especially the internet, had on the SWX?

Heinrich Henckel: We are eager users of new technologies as long as we consider them to be safe and reliable. In the last few years, we have continued to expand our internet site. Publications of the disclosure department, which is entrusted with the monitoring and enforcement of issuers' duties following listing, appear frequently only as Web documents.

Has this medium also been subject to guidelines, for example in the context of information archives, alternatives to traditional business reports or invitations to AGMs, which all could be done via internet?

Heinrich Henckel: There are interesting options in this area which are subject to discussion. One issue is, for instance, the internet AGM. At present numerous legal obstacles and legal uncertainties still exist, which first must be eliminated by the legislator. It is clear that the Article 72 of the Listing Rules does not truly take into account the possibilities of the internet. On the other hand it must be noted that even today not all listed companies at the SWX have a website.

The Ad hoc Publicity rules regarding disclosure regularly provide subjects for discussion. Individual entrepreneurs and managers have criticised the SWX for their unrealistic attitude, which promotes reserved communication. Do you see a need for action in this field?

Heinrich Henckel: First of all, it is misleading to say that the concept of Ad hoc Publicity is something unique to the SWX. Comparable rules exist in all developed capital markets and thousands of enterprises have learned to deal with them. We therefore do not experience overall criticism on this issue; and we would not see such criticism as justified. Article 72 of the Listing Rules provides an obligation for issuers to communicate openly, however, with an eye on the appropriate rules to consider – prohibition of selective information, requirement of the true, clear and complete information, requirement of rapid information, regulation of delays in publication.

We see action needed particularly in the appropriate training of individual managers – amongst other reasons because the Swiss regulations admittedly give a comparatively large scope for discretion and therefore responsibility to the companies.

In the event that a company needs to put out information on an ad hoc basis, the official criteria are not really helpful and, in cases of crisis, allow for large room to manoeuvre. Shouldn't there be more committed rules governing this?

Heinrich Henckel: It would be conceivable to have a model, where it is not the issuer, but the stock exchange or a government authority that is responsible for taking the appropriate decisions. It appears to us that this concept would be unrealistic and entirely wrong given that it would be based on the assumption that those authorities know how to judge the potential price relevance better than the issuer.

We support a more liberal approach leaving decisions to the issuer. However, we can see that this freedom can be cumbersome as it comes along with a share of responsibility.

Enterprises with dual listings have various obstacles when communicating; amongst other things, different guidelines and different time zones. What is your view on the coordination of publication guidelines across different stock exchanges?

Heinrich Henckel: I think that it would be extremely difficult to achieve international coordination of publication guidelines in strict detail. In any case, with regards to Ad hoc Publicity, we are basically in line with New York, London, Frankfurt and other major stock exchanges.

The SWX does not know of a "Regulatory News Service" like in the UK, but requires the dissemination of relevant information through at least one newswire. How did you come to this solution?

Heinrich Henckel: The SWX actually specifies in Article 72 of the Listing Rules that the circulation of information is to be made in such a way so as to ensure equal treatment of all market participants. With the available electronic media, at least one electronic information provider widely used by the professional market participants is mandatory.

Besides publication in the aforementioned media, we recommend to inform the public as comprehensively as possible, for example through the internet.

Today's technical possibilities will probably lead to an increased use of internet-supported media, whereby push concepts (unsolicited mailing) and pull concepts (subscription services) might be used. Issuers are today free to publish their communications themselves or purchase these services. The SWX hopes that an intensive competition between providers leads to a good, fairly priced service for issuers as well as for market participants. We do not feel that the SWX should intervene in this competition by making a central system mandatory.

Many small and mid caps at the stock market are often overlooked. They complain about high listing costs, about low liquidity and about lack of interest from institutional investors. Do you consider this to be a problem?

Heinrich Henckel: The stock exchange only provides a marketplace and a basic framework enhancing liquidity. It cannot, however, guarantee that liquidity. The fact that the shares of small capitalised enterprises are less liquid than those of the large companies lies in the nature of things – the phenomenon belongs to the stock exchange world like the ups and downs of exchange rates. There are models making a market-maker mandatory for example for smaller listed shares. The costs and risks of such models can be substantial and is hardly worthwhile for the market-makers concerned. We never introduced such models – with the exception of certain obligations in the SWX's New Market. In the long run, each company must decide for itself whether it wants to enter the capital market and list its shares at the stock exchange or not.

How do you judge the value of shareholder communication within the Listing Rules?

Heinrich Henckel: We put great emphasis on the importance of shareholder communication. Good communication conducted in accordance with the rules lies in the interest not only of investors, but also of listed companies and of the stock exchange.

Interview: Jan Gregor,
The Investor Relations Firm AG

company has to make sure that it communicates all facts of material significance in a timely, accurate and fair manner and does not omit any facts that could render the information provided misleading, or lead to distorted market conditions.

Timing issues

In this general context, timing issues, in contrast, are often unclear and disputed. As regards *periodic disclosure*, arguably, the more frequently a company is required to publish financial statements, the more efficient the markets are. In line with this rationale, the general trend for listed companies is quarterly publication of financial statements. In continental Europe (including Switzerland), where semi-annual financial reporting is still the norm (about to change – see Outlook), quarterly financial statements have been criticised as furthering a short-term view of a company: the more frequently a company has to publish financial figures, the more the management is prone to maximise short-term instead of sustainable success. Also, a management that is constantly preoccupied with preparing financial statements is diverted from its main job, which is to lead the enterprise's operations to success.

Similar observations can be made with respect to the time lag between the relevant date of a financial statement and its publication, which shall be shortened effective January 1, 2005, for companies listed on the SWX Swiss Exchange. The shorter the period between those two events, the better the transparency, but the higher the risk of loss in quality.

As regards *ongoing disclosure obligations*, most countries and exchanges impose the general obligation to make immediate disclosure to the general public of price-sensitive information so as to ensure that it will be accounted for in share prices.

Regulations, however, do differ when it comes to the question whether, or at what point, plans and preparations, which, if disclosed, would be price sensitive, should be disclosed. If such price-sensitive information had to be published immediately upon its occurrence, a transaction may have to be made public already in the preparatory stage, which might well disrupt the process of a significant share issuance or a negotiation of a merger or takeover. While this would certainly lead to more transparency, it would also lead to unnecessary volatility of a stock price, as many such transactions are at some point abandoned, often in the preparatory phase, and never come to a signing or closing. Even if they do come to fruition, they often do so upon terms other than those initially contemplated. Furthermore, requiring disclosure at such an early stage could mean that transactions that are in the interest of a company and its investors cannot be completed.

For example, if a company had to disclose the fact that it is planning the public takeover of another company, speculative trading could lead to an increase of the share price of the target company, reflecting the market's expectations as regards the potential premium of the offering. If the market expects a premium of 30 % over the current prices, while an offerer does not want to offer more than 20 %, the stock price of the target, in anticipation of the deal, may rise to a level that causes the offer to be abandoned.

For such reasons, the timing of ad hoc information, as well as the task of drawing the line between relevant price-sensitive information and irrelevant (although potentially price-sensitive) information, is one of the most difficult to be addressed by regulators and by lawyers in advising companies. In most countries, the mere preparation of a potential transaction does not have to be disclosed as long as its confidentiality is maintained. Therefore, a framework of confidentiality agreements, leak contingency plans and pre-approved press releases for certain developments that are prepared in close cooperation with communications and legal experts play a crucial role. Also, the fact that a company can present such a framework if rumours start affecting trade volume and share prices has proven to be a valuable line of defense if a regulator starts inquiries regarding insider trading or violation of ongoing publication rules.

In the case of prospectuses, shareholder information and other *transaction-related standardised information* timing also plays an important role, as the quality of the content of such informations can only be measured with respect to the time at which such documents were released. Price-sensitive information that comes to the attention of a company after the release, of course, is not included. Consequently, the question arises whether – and what – information needs to be updated after the public release of a prospectus, shareholder information and the like. Even if updated, it is not always clear whether such update serves its purpose.

A good example is the manner in which most shareholders exercise their voting rights. As most shareholders do not attend shareholders' meetings in person, but rather vote through proxies, an update of information may not have any impact because instructions have already been given at the time of the release of such information.

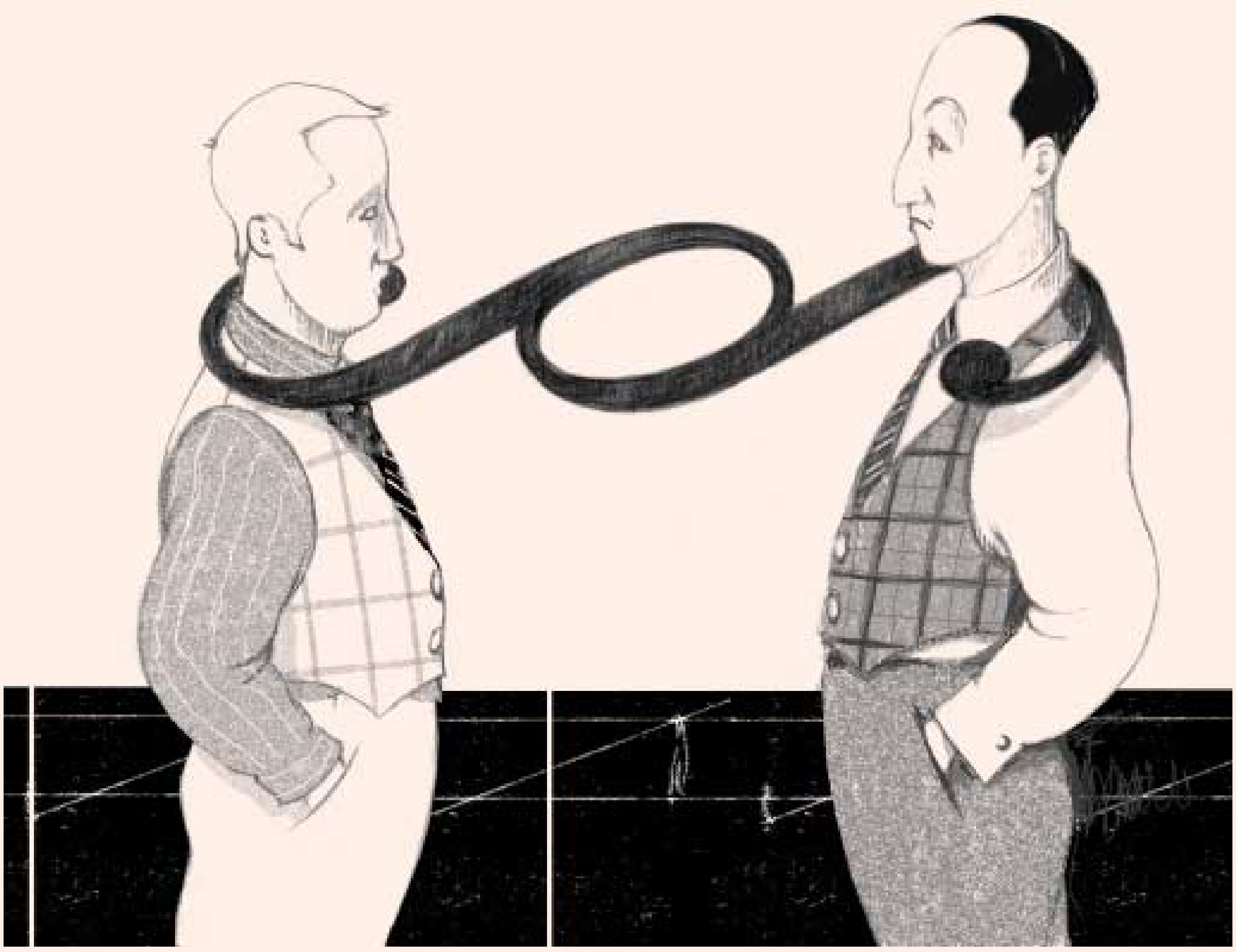
"Other" information has not yet received much attention from regulators of capital markets, although it can have an impact similar to that of the categories of information discussed above. So far, such "other" information is regulated mainly by laws on fair trade, healthcare regulations, etc., which are still dominated by considerations of consumer protection. These standards often leave a company more discretion than capital market regulations to highlight positive information and omit negative aspects. The different set of rules seems justified, however, as investors can (still) distinguish an advertisement ("we build the greatest cars") from relevant market information regarding the value and prospects of an investment ("at [date] our car sales have reached a market share of 30 % in country x") and put it in the right context. Nevertheless, even the truth of such "other" statements is coming under increased scrutiny by regulators and courts. Only the timing and form of such information is left to the discretion of companies and their communication advisers.

Outlook

The *USA* know a long tradition of centralised regulation of capital market communication by federal securities laws, while the situation in Europe and other markets remains fragmented. Recently, however, the *European Union* enacted the Prospectus Directive, which will lead to convergence of the content of prospectuses in connection with capital market transactions. Furthermore, the European Union is expected to enact a Transparency Directive shortly, which aims to coordinate periodic financial reporting and the distribution of sensitive information by companies throughout the common market. For example, the Directive will require issuers of listed shares to publish financial information on a quarterly basis. By October 2004, the member states will also have to implement the Market Abuse Directive, which regulates ad hoc disclosure of price-sensitive information in detail.

In *Switzerland*, takeover law and the practice of the takeover board are probably among the most developed in this field, and transparency in public-takeover situations is guaranteed. On the other hand, shareholder information included in proxy statements and shareholder invitations has hardly been regulated in the past. In that regard, the new act on mergers and restructurings, effective as from July 1, 2004, will provide a regulatory framework for the form and content of such information in connection with mergers, demergers and transformations.

As most countries are closing the gaps of unregulated fields of market-sensitive information, this will create opportunities for collaboration among communications experts and lawyers. Generally speaking, communications advisers may need to develop some understanding of the legal framework affecting the timing, form and content of information. Lawyers, on the other hand, may need to learn how to explain complicated issues in plain terms (and regulators have developed rules on how to write in plain language). While this may affect the freedom and "fun" previously enjoyed by these professionals, who now are forced to learn from one another, it also suggests a huge potential for growth and quality enhancement in both areas.



The stock exchanges rules bind market participants

Newswires – quality reporting in 2 minutes?

Getting important company information out to the public in a timely and accurate fashion, is at the centre of every media relations or Investor Relations professional's job. The effectiveness of the release of this information and its guarantee of reaching a wide, worldwide investor audience, is facilitated by newswires which channel this communication instantaneously. In an interview with Anita Greil, Bureau Chief of Dow Jones Newswires in Zurich, I got an insight into how newswires really work.

Ana Nogales, The Investor Relations Firm AG

I have often wondered, from a public relations professional's point of view, how it is that as soon as my client's announcement has been formally released to the public, at least four newswires have managed to write the story up, and all this in the astonishing space of two minutes. The sceptic in me would say that in fact, all they do is copy and paste that document on which so many hours, late nights and last-minute discussions with CEOs and CFOs have been spent, but it seems, that indeed, the art of this magical instant reporting by newswires is more complicated than two clicks of a mouse.

In an interview with Anita Greil, Bureau Chief of Dow Jones Newswires in Zurich, Ms Greil dispelled the myth of "press release editing" and explained how, in fact, information is processed, stories are written and how all companies' news in the nearly one hundred stock exchanges and in different time zones worldwide gets covered.

Newswires play a crucial role in the dissemination of information, specifically in the context of price-sensitive information. The delivery of accurate, timely information about a company's financial welfare will help the investing community to form an opinion about a company's valuation and therefore influence the performance of the stock.

Newswires aim to exist as an objective source of factual and background information to be used by all members of the financial community, from the newspaper print journalist to the fund manager making decisions about his portfolio. They effectively tap information from decision makers and exist as the channel to reach other decision makers. In the financial community therefore, the scope of this decision maker audience is huge.

When working in such an environment with such strict delivery times, the newswire journalist is expected to deliver quality information, which is to be understandable by a wide audience, while at the same time being professional.

In order to achieve this, the preparation behind that story which pops up on screen in those two minutes after the official release of a company's financial information, is rather elaborate. When the early-riser newswire journalist knows a company's figures are going to be announced, a prewritten headline and the main outline of a story is written, reflecting the journalist's speculation of the results based on research previously done, including analyst forecasts and general market expectations, leaving gaps for the unknown figures.

As soon as faxes start beeping and e-mails arrive in in-boxes with the official figures from companies, the figures get filled in to the previously blank gaps and the headline is sent out. Objectivity, at this point, Ms Greil tells us, is essential. The headline should always try to avoid words which have negative connotations or which may contain some sort of prejudgement of the news. The first headline put out is thus always edited by two people to ensure accuracy and will create the base for further stories throughout the day, which, in turn, will be also be constantly edited.

Very soon after, the initial headline is accompanied by a short story, which, in fact, is an "edited" press release, taking the key facts as supplied by the company. In cases when the news is unexpected, such as a profits warning, the newswire journalist still aims to get the information out on the screen in little time, this time, "edited press releases" playing a bigger role.

Objectivity is to be complemented by adding value to the story, therefore, depending on a company's size and the importance of the information put out by the company, the information will get updated throughout the day to include interviews conducted with the management and the market's reaction to the information, noting specifically any movements in the stock and analyst opinions.

The aim of the story is not to influence the stock price, but rather to help the investor form an opinion after reading the concise, well-written facts, supported by market information.

The emphasis on getting the headline and story out as soon as humanly possible, is ominous. This is what will differentiate the newswire from its competitors: other newswires. It comes down to time in delivering the story. In fact, quality controls

Newswires and the art of fast quality reporting exist at each newswire to measure how long it is taking for the headlines to be sent out and these are compared with their competitors.

Each newswire therefore aims to be the first in putting out the news following initial announcement and the first in speaking to the CEO and in getting the first quote. The quality of reporting will have much to do with previous research carried out and having a feel for what constitutes a good story.

To contradict my initial scepticism and talking from the point of view of someone in the public relations industry, where we aim to influence people with what is often known as "spin", I asked Ms Greil how the newswire journalist avoids too much "press release editing" and being taken in by this spin, especially when they have such little time to write the article. Her answer, of course, was that most newswire journalists are experienced enough to get straight to the facts, as, after all, that is what they are there to report on.

At the height of reporting season, this is the focus of the work of newswires. When it is over, newswire journalists have more of an opportunity to write more opinionated articles or conduct more investigative journalism, without being constrained to writing just facts. At Dow Jones, where there is a special relationship with the Wall Street Journal (WSJ), journalists will often be asked to cover stories for the newspapers, to ensure that each story going on in the world will be covered by the local journalist.

To complement factual reporting, newswires tend to also have room for more opinionated information in special columns focused more on market gossip and in making clear for instance, what their opinion on a particular stock is. Dow Jones for example, has columns such as The Sceptic and Market Talk.

And so, here is an overview of how the world of newswires works. To finish my chat with Ms Greil, I wondered what kind of person you needed to be to be a newswire journalist. An early riser and fast reader and typist for sure, but I was told you have to really be a team player as all newswire journalists work in teams to ensure accuracy, speed and maximum market coverage. Flexible too, as your working hours can be altered depending on what last-minute news is out. And last but not least, a news junkie.

To illustrate the point, Ms Greil, when asked how many publications she would buy while holidaying in the Côte d'Azur, gave us a wide, impressive range of international publications that she would read daily, to keep abreast of the latest news in the world.

I came away from my meeting with Ms Greil, much wiser and feeling less sceptical about the world of newswires. It seems that, behind newswires are not supernatural humans obeying different time laws, but experienced journalists, who, working under much stress created from the endless information around them and ever-present time pressure, are capable of delivering good-quality, well-researched information on which plenty of time has been spent, but which just happens to appear on our screens within two minutes of release. Impressive, I would say.

New technologies speed up Investor Relations

Time to market is crucial in Investor Relations. For the sake of good practice and transparency, companies are expected to assure that information should reach all its investors worldwide at the same time. As new technologies develop, new horizons appear for Investor Relations to make this possible.

Markus M. Müller, The Investor Relations Firm AG

Some ten years ago, the smallest time frame at a stock exchange for a trade was one day. Many investors were reading the corporate news and the stories in newspapers the next morning after they were issued. Thereafter they made their investment decision. Releasing intra-day company news was not having a huge effect because stocks were only traded at a specific period of time. Events taking place somewhere around the world would have not been taken into consideration that quickly. Intra-day trading was almost useless because neither up-to-date information nor trading platforms were available to everybody. In addition, market liquidity was significantly lower than in today's electronic environment and orders from retail investors were not often seen at the trading desk, the costs were just too high. This all changed with the introduction of electronic exchanges and the wide use of the internet.

The revolution in speed

By increasing the time frame for trading stocks, new possibilities arose such as a market for corporate information and its distribution and interpretation (e.g. newswires) or intra-day trading. New companies offering information distribution and online trading were set up. Consequently, prices for trading fell and an increasing number of retail investors entered the market. Everybody tried to make their fortune with stocks, derivatives and other usually unknown products. Indices climbed to new highs and the media started to report on the easy way to make money. Time became money and profits and losses were now just seconds away.

An increasing amount of information about the economy and rumours about companies sneaked into the market. The flip side of course, was the necessity to tighten regulation. This led to the new problem of information overflow. Accessing information is – at least for professionals – not a big issue anymore; the problem boils down to quickly finding the relevant information. To know with certainty what information will affect the expectations of the market participants and thus the stock price, has become key to any investment decision. The question remains, whether people can process the information as fast as needed.

To mistake the timing will affect your portfolio even more than picking the "wrong" stock. The pressure on decision making is therefore rising. That might be one of the reasons why markets have become more volatile and sometimes overshoot information input – which is quite lucrative for some short-term traders. The investment horizon, therefore, seems to have become shorter on average.

In any case, markets have become a lot more efficient. Every piece of information is processed into the price at all times. You might judge this development positively or negatively. The fact is that information flow has to cope with the faster way of trading and Investor Relations has to fulfil investors' needs for fast and accurate information while still closely obeying the regulations.

Time and information became so closely linked together that new rules had to be applied to guarantee equal treatment of market participants. Thus, the SWX Swiss Exchange's Ad hoc Publicity rules are one of the most important guidelines for IR departments to follow today. They provide that companies should ensure that information is made available at the same time to every market participant. This poses a challenge for Investor Relations in being able to reach all its shareholders, living in different time zones worldwide. How should this requirement be handled today and what can technology do to improve the process?

Removing the retail investors' disadvantage

Nowadays, media releases are the most common tool to publish corporate news. They are usually distributed by e-mail, either as a PDF attachment, as plain text or HTML, published on the website or sent out by fax. Although the labelling might lead to the assumption for a "media-only" release, it is also sent to institutional investors, analysts and sometimes even – if a subscription to the news is available – to retail investors. Nevertheless, the range of people being on the distribution list is up to the company's own consideration. If retail investors want to stay informed, the website is generally the only place to go. But how will they come to know of the release of new information? Currently, investors are highly dependend on information providers such as Reuters, SDA or media websites such as NZZ or FT. However, this information will be delayed and

FOUR IDEAS TO IMPROVE YOUR INFORMATION EFFICIENCY

Raising awareness for all investors

10 to 60 minutes – the exact time is customisable – before the release, an SMS alarms the investor and informs him on how to access the information. The information can then be ordered via SMS and accessed by several different types of media such as website, MMS (Multimedia Messaging Service) or fax.

Reducing information overflow

An independent distributor of information – such as Bloomberg, SDA, Swissquote, Argus – installs an SMS service for headlines. The top 5 headlines of a press release will then be sent to subscribers. This can also include summaries of interviews and main newspaper articles.

Choosing the right tool for everyone

A complete annual report will probably not be read by the shareholder who only holds a few shares. His interest will be in a few key figures like in the profits, the dividend, the performance of the share, and the outlook of the business. He will skim through the financial statements and the corporate governance report. A short summary of at most four pages would be enough. The complete text of the annual report can be published online. Institutional investors and analysts will, in any case, access the full reports online.

Not excluding anyone

Today's telephone conferences are often only available to invited analysts and investors. To bring the live audio stream to the website is not a problem. A sole shift of expression from a "press" to a "public" conference could open the way to ensuring this equal treatment of shareholders by making all information available to everyone. Using MMS and soon also UMTS – which enables fast data transmission to mobile devices – can even bring the moving picture to an investor's mobile phone. *(mmm)*

Listen and communicate to behavioural investors!

When talking about Investor Relations, finance theory is hardly ever taken into account. Quite surprisingly, because analysing the underlying assumption and effects of finance theories results in deviating actions. Standard finance theory and Modern Portfolio Theory should result in very simple and fact-based communication, while behavioural finance, includes many psychological aspects of human behaviour which should be actively addressed for communication purposes.

Jan Gregor, The Investor Relations Firm AG

Communication, more precisely Investor Relations, is not worth the trouble! This at least should be taken as a key insight if standard finance is taken as granted. Because in economic theory there is no differentiation in the decision-making process depending on market phases. Rather, "economic" individuals will always seek their personal advantage and will always behave rationally. Following this theory market prices are efficient and information is always immediately incorporated into share prices. This property is known as capital market efficiency, or information efficiency. No investor will be in the position to outperform the market thanks to superior information and therefore communication strategy or personal contacts to a firm's management become redundant.

IR and Modern Portfolio Theory

Furthermore, the widely accepted and applied Modern Portfolio Theory (MPT) is based on a number of assumptions, which should have potential implications on how company-specific information is processed. Central to MPT is the assumption that investors make rational buy and sell decisions; i.e. meaning that they incorporate information correctly, and consequently act rationally based on the information gathered. Rational investors are supposed not to make systematic errors. Investors are presumed to assess the risk and return of assets within a portfolio context, not each investment individually. In addition, rational investors are presumed to be risk-averse, which denotes that they require a higher return as compensation for higher risk, and vice versa.

Investor Relations would be a rather straightforward task, should these limiting assumptions be accepted without any reconsideration. The only data which analysts and investors would be interested in are the company's raw numbers. Then all market participants would form the same – rational – expectations based on this information, and would buy or sell the stock according to their individual risk aversion and utility irrespective of the actual phase of the stock market.

Yet, any financial markets observer will notice that people often behave irrationally – some extreme swings of stock prices can only be explained by irrationality – and sometimes make systematic errors. Some behavioural tendencies can even cause investors to act risk seeking rather than risk averse. And, very often investment decisions are made on a case-by-case basis rather than in a portfolio framework. This, of course, first and foremost applies to the analyst's ratings, yet portfolio managers will also very often make individual buy or sell decisions on a case-by-case basis. It is the need to take decisions under uncertainty or risk which will always be influenced by behavioural tendencies and which will allow for irrational and inefficient actions.

Changing assumptions due to behavioural finance

Hence, accepting that many behavioural tendencies affect investment decisions, the communications professional may ask himself to what extent these peculiarities may also influence how information should be provided to the investment community.

Anyones who has ever taken right or wrong investment decisions knows the feeling: regret or pride. The fear of regret refers to the pain felt after making a bad decision, whereas the seeking of pride refers to the joy felt from making a wise decision. This effect is particularly important in relation to company-specific news releases relating directly and uniquely to stocks held in the investor's portfolio. Economy-wide news, on the other hand, is considered out of control and does not produce strong feelings of regret or pride related to individual stock purchases. Fear of regret causes the investor to hold on too long to a stock that has dropped in price, whereas the proud investor sells the winner often too soon.

A relevant effect from a communication perspective is the endowment effect. It refers to the tendency by people to place higher value on what they own rather than on identical items that they do not own. The endowment effect can also be seen as the "do nothing" effect; investors will have a tendency to keep their original investment and to pay little attention to changing risk and return characteristics.

When analysing human information processing, the communications professional will find that the actual processing strongly depends on the context of the information provided and will cause some relevant consequences. One of the best-known effects – especially relating to quantitative information – is anchoring. When asking for estimates of numbers, people will always be influenced by a given value. Furthermore, investors must rely on available information, which is usually provided by the companies themselves, competitors or trade organisations. The problem, however, is that information is rarely complete or precise; it arrives randomly and with noise. Nevertheless, investors must make decisions based on this information and they will assume that the information is correct and precise. The behavioural issue is that investors overestimate the precision and importance of the information they gather. Also, the IR officer will not be surprised to learn that people do not weigh all information in the same way. Individuals overrate directly

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Continued from page 5

retail investors are once again informed at a disadvantage. What can be done to remedy this? The answer is most definitely: use up-to-date technologies and redesigning processes.

To find an appropriate solution, we should think back in time to medieval ages when messengers rang a bell in the middle of a crowded marketplace. After everybody was aware that the messenger had something to say, he began to read out the news. Today, it should be quite the same: the new release could be divided into two steps, 1) a pre-announcement and 2) the publication itself. The pre-announcement would reach the person almost wherever he/she is. The best way to accomplish this task is by using mobile services like SMS (see box). After the pre-announcement, the investor accesses the website where the news is published.

Alternatively, the investor can receive the information by MMS, which is the next step for mobile information and offers improved interactivity. It can be used to issue the most important information as a table of content. The reader will then decide which parts he would like to focus on. Even small videos with corporate information, such as for example part of the webcast of a company's annual results presentation, can be accessed together with the formal announcement.

Fast data exchange

The use of such tools can not only decrease the time to information but also reduce the time needed to evaluate and process the data. The use of smart interfaces allows analysts to easily import the latest numbers into their Excel spreadsheets or even import the data instantly from the website into the spreadsheet. The company's important announcement dates can be downloaded straight on to the investor's PDA.

Thinking about huge amounts of numbers sets the focus on the annual report. In order to analyse the balance sheet and the income statement, today, an investor has to either copy the numbers from the print version into his spreadsheet, to transfer the numbers out of the PDF file into the Excel table or to download a separate Excel file with the numbers. The next step will be an import of the numbers directly from the website into the spreadsheet. This feature will be available as soon as new data exchange standards such as XML and XBRL (eXtensible Business Reporting Language) are implemented in today's software. This will open the way to a report that is published totally on the internet therefore providing for a faster publication.

Let the agent do the work for you

In the future, we will see a shift from push to pull. Smart agents – intelligent, self-learning programs – will be programmed to look up news on different websites and put the information together to a customised site or hardcopy newsletter. In a so-called online investor cockpit, the software will put all information together into one platform and present it to the investor. Together with an interface to an online trading system, this open architecture system could be the standard tool for almost any information device – whatever it may look like.

To-do list for IR departments

What should IR departments do to plough the path to new interactive and more timely information for their shareholders? The IRO should engage to facilitate the information flow from one platform to the next and simplify the access of devices to his information platform. This, of course, can only be achieved through an electronic platform. Printed versions (e.g. annual report, corporate brochures) will still be used, but only for specific content and target groups.

To conclude, therefore, here is the IRO's to-do list:

- Shift the focus of IR publications from paper to electronic platforms
- Redesign your production process for publications and set the priority on electronic publishing
- Store all information on a publicly available server in an open format (as XML) and link it to the website
- Reduce information overflow by smart public releases that make use of Hyperlinks

received, easily available or salient information. Background information in contrast, is perceived to be less relevant. Most investors are even subject to a confirmation bias. Very often, people search selectively for confirmation of their existing opinions.

When seeking for information, the investor is often subject to an information source effect. Identical information derived from a choice of sources is being taken as more relevant and thus confidence in making decisions based on this information is augmented. On the other hand, very few investors go deeply into researching causalities. According to the credulity effect, hints to patterns and explanations of causal connectivity are too readily accepted.

Given standard finance theory, investors should never look back. The only relevant basis for the investment decision should be the outlook. However, in financial markets, the primacy effect can be observed: people weigh recent events high and personal experiences are a lot more in people's minds than hypothetical alternatives. Even the stance that the investor's risk aversion remains constant should be questioned. Many observations prove that investors tend to become more risk averse in falling markets while they are more risk seeking in rising markets.

Including behavioural tendencies in communication

Some of the listed effects and observations may find their way into the communications professional's tool box. The anchoring effect, for example, gives an intuitive explanation for the reasoning for a precise guidance and an elaborate outlook. It will ensure that analysts' estimates will not spread too wide. However, it should be taken into account that the guidance is to be put into a context. This frame may include assumptions about the economy and strategic or operational actions being taken by the company. Anchoring underlines the effectiveness for investors, but also for the company in order to manage expectations.

According to behavioural tendencies, when proving a point, a company should consider which data to use. It ideally puts forward information that is easily available and used by its peers as well. Data that is not available to the investment community or is not used by any competitors would – according to behavioural finance – not be relied on as much. The company can even actively use the information source effect. It can highlight its key message by using information that is derived from various sources. As a result, investors will refer to this data and base their decision on data and causalities provided by the company.

Probably the strongest driver, mainly for analysts, is the pride of making right decisions while not being able to constantly change their opinions. Being able to list the key arguments behind buy and sell decisions becomes important. The communications professional should actively address the reasons given by opinion leaders. He can then actively influence the opinion leaders' feeling of pride and regret and would then also be in the position to actively influence potential changes of mind.

Independent Research – a new growth industry

As small and mid-cap companies around the world have dropped off the radar screen when it comes to quality institutional research, a huge new research industry, independent of the traditional investment banks and broking houses, has developed to fill the gap.

Tony Cooper, Research Director, City Insights

The Holy Grail of investment research is the pursuit of shareholder value, and research plays a key role in investor decisions. The information provided by research moulds the stock market's expectations. If research is distributed evenly and simultaneously, the market can function efficiently.

RESEARCH HAS A MAJOR IMPACT ON SECURITY PRICES

Investment research → *Investment decisions* → *Share prices* → *Increase/decrease in value*

In reality, market efficiency is reduced because both the provision and timeliness of information is uneven, and some research may contain hidden biases. Research is mainly produced by four distinct groups:

1) Sell-side security brokers and investment banks;
2) Buy-side asset and fund management institutions;
3) Independent research houses;
4) Investor Relations organisations.

Traditionally, sell-side brokers and investment banks have produced most company-specific research, and have served their own interests by directing it to institutional clients (mainly pension funds and life assurance companies) who are generally well informed and knowledgeable, usually having their own analysts and researchers. The focus of much of this research is on the top tier of companies by capitalisation. On the main London Stock Exchange, the shares of nearly 2,000 UK and International companies, with a total market value of over £3.3 trillion were traded at the end of 2003, while the New York Stock Exchange listed the securities of 2,750 companies with a global market capitalisation of over US$17 trillion. The costs of this research are not met directly but covered by what the USA calls "soft commission", related not just to the volume of trades executed but for an overall level of service.

Independently funded research, as distinct from the above, has grown in scale in response to demand from individuals and organisations, unsatisfied, or dissatisfied, by the quantum or quality of research provision. The providers have proliferated especially since the investment boom of the late 1990s and 2000 with the technology and dot.com boom. In the USA, where independent firms receive only US$500m of the US$10bn spent each year on research, independent research houses form a still relatively small and fragmented industry, the longer-term survival of many such firms depending ultimately on their quality and consistency.

Retail investment markets, on the other hand, are less well served by research while access to information is generally patchy. Private client stockbrokers manage clients' funds, and some 80 per cent is held on an advisory or discretionary basis in the UK. True, many broking houses have both institutional and private client business, but a free flow of information across departments rarely occurs. Regular in-house surveys conducted by the author's own firm, City Insights, on the research available to private client advisers have revealed a paucity of regular information, limited access to brokers' research and much reliance on secondary sources – newspaper comment, investment magazines and the wire services such as Bloomberg and Reuters. Even corporate websites are not regularly accessed for company information.

Differential research access, especially between institutional and retail investors, is one though not the main factor behind the outpouring of research from independent organisations. In fact, in the USA, independent research houses have mostly catered to large, institutional investors – hedge funds, university endowments, and trusts – paying hefty annual subscription fees of up to US$100,000. The retail investors are still largely left out.

The growing role of the Investor Relations organisation

Another source of research is via Investor Relations advisers. The managements of many SMEs (small and medium-size enterprises), whose market capitalisations are too small to attract investor interest, have woken up to the need to utilise part of their Investor Relations budgets to gain the market's attention. Some have commissioned their IR organisations to produce research on them targeted at the investment market. Use of the IR/PR adviser research route is more proactive than relying on corporate material displayed on the investor pages of their own websites.

Tony Cooper

Where an Investor Relations adviser is involved in producing research on its client, it is mainly targeted at those parts of the market not served by the research departments of brokers and banks, typically private client advisers. Since the number of private investors is large, (85 million supposedly in the USA), they cannot be reached directly. Commissioned research is more efficiently targeted at their brokers and discretionary investment managers whose responsibility is to keep their own clients informed. It may be distributed more or less widely, to potential investors on both the institutional as well as the private client side or to the latter only. In any event, the twin objectives of increased awareness and increased marketability of the company's shares are achieved.

SMEs use other self-promotional methods to attract the private investor, with or without research, such as independently sponsored investor exhibitions – where managements display and demonstrate their companies' products while meeting private investors face to face. Individuals with short memories cannot be directly contacted by companies afterwards. Hence such events tend to have a short-lived impact without a follow-up mechanism. Even with potentially limited shelf life commissioned research, supplementing other information flows such as the interim and annual reports is more effective if it galvanises the discretionary investment advisers to take an interest in a company.

To claim that research, paid for out of a company's Investor Relations budget, cannot be "real" if it is not independent is to misunderstand its purpose. "Research" focusing not on the latest financial results but setting out to "educate and inform" the market about a company's products, markets, management and strategy, is of major importance to those SMEs below the major brokers' and banks' radar screens. Such research can underpin a company's valuation even without a profit forecast. In practice, this research will use the market consensus forecast or else that of the relationship broker, since anything else could be misconstrued as a company's own budget-based estimates.

The unhelpful economics of research provision

An increasing neglect of the small caps stems from another factor. In all the major stock markets, sell-side brokers and banks have faced cost pressures and declining commission rates. Up-to-date information on the latter is not easy to come by but an overall rate as low as 0.17 per cent on UK equity was reported by a London Stock Exchange 2000 publication, and the overall rate has declined since. Unsurprisingly, brokers and banks have downsized their research departments and concentrated their top research teams' efforts on the top tier of companies by market capitalisation where the potential rewards bear a more realistic relation to the costs involved. The corollary of this is that the small caps receive little or no attention and little if any in-depth research. In the USA, four out of five listed companies are allegedly not now researched by the brokers and major banks. There is no corresponding figure for London but as the FTSE 100 accounts for 80 per cent of the market by value, it would not be surprising to find a similar figure.

Given that the aim is the pursuit of shareholder value, the neglect of smaller companies that constitute the numerically much larger part of the market, has led paradoxically to an underbroked situation for them while the large caps are overbroked measured by research volume.

Independent research less biased?

Users of independently originated research should have fewer qualms about hidden agendas. In all markets, the regulatory authorities such as the Financial Services Authority (FSA) in London, and the Securities and Exchange Commission (SEC) in New York have strict rules governing market conduct, but had not until recently addressed problems arising from conflicts of interest, notably between the research and corporate sides of the investment banks. Analysts are accused of reluctance to criticise a company for fear that it might cost the broking house a client, or else for acting like pumped up cheerleaders in their reports to curry favour with a potential client.

In the USA, charges arising from alleged "biased" research by analysts supporting in-house corporate interests were brought in 2001 against ten leading investment houses, including Salomon and Merrill Lynch, by the New York Attorney General and SEC. As part of an agreed settlement, ten brokers were required to ensure the objectivity of their own research and to spend collectively US$432m to fund independent research for five years. This would be distributed, along with their own research, to their clients. The high-profile settlement (not replicated elsewhere) was designed to restore integrity to the market and has given the independent research houses, such as S&P's Research Services, Value Line and Morningstar, a strong boost to expand their output and coverage. Thomson Financial's new USA directory lists 200 independent investment research firms and 1,200 equity and fixed-interest analysts.

This stimulus to the independent sector in the USA is a reaction to a perceived abuse. Elsewhere other factors are working to expand the industry. Everywhere, a desire for genuine, objective, innovative and user-friendly product means that expansion will continue outside the investment bank circle.

ABOUT CITY INSIGHTS

City Insights is the City of London's leading integrated Investor Relations specialist. It originates and distributes research on client companies to its extensive database of private and institutional investors and arranges presentations to the same audience. Perception audits are undertaken as well as offering state-of-the-art internet expertise.

IR FIRM – MANAGING EXPECTATIONS

Financial Public Relations have acquired increasing significance in the past few years with the requirements for companies growing exponentially. An increase in the professionalism and in the internationality is to be noted. Shareholders have gained more influence on companies' management teams. Due to these developments, management teams face greater challenges. Strategy, goals, expectations and financial results must be actively formulated and communicated. IR Firm knows the main players in the financial community – institutional and private investors, financial journalists, financial analysts – and their needs. IR Firm knows which tools are needed to reach these people and the institutions they represent. IR Firm's knowledge is based on ample practical experience: advising listed companies in good and difficult times, capital market transactions such as IPOs, mergers, spin-offs, capital increases or going-private transactions as well as supporting financial institutions in specific communications issues.

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You can find further information on The Investor Relations Firm AG on our website www.irfirm.biz. We would be delighted to hold a personal discussion on your needs.

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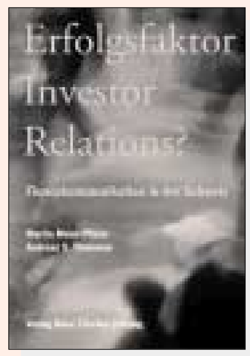

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IR INVESTOR RELATIONS

Print run: 2,000 copies once a year

Publisher:
The Investor Relations Firm AG
Rämistrasse 4
P.O. Box
8024 Zurich

Telephone: +41 43 244 81 44
Fax: +41 43 244 81 45
info@irfirm.biz
www.irfirm.biz

Editorial:
Ana Nogales (ana), Jan Gregor (jgr)

Contributor:
Markus M. Müller (mmm)

Illustrations: David Atkinson and Paolo Friz (both at Illux)

Layout: Atelier Frei, www.atelierfrei.ch
Printer: Rohner Druck AG