GUEST ARTICLE

IPO: So, You Think You Are Ready?!

By Elena Lytkina Botelho and C. Rodgers Palmer, ghSMART & Company, Inc.

"The IPO is not the end game—it's the beginning of a very different new game."
—Public company CEO

If you are a CEO or investor preparing your company for an IPO, you are laser-focused on Sarbanes-Oxley compliance, SEC filings and the other requirements of going public. If you've done this before, you also know that as challenging as it is to get ready to go public, the marathon of successfully running a public company post-IPO is tougher than the pre-IPO sprint. In the words of a successful public company CEO: "Everyone is focused on the brass ring but the IPO is just 'the wedding.' It's the marriage you need to worry about and that takes a lot more work and a lot more can go wrong." Leadership consulting firm ghSMART reviewed its client experience and interviewed 30 CEOs, investors and directors responsible for more than 100 IPOs to share what it takes to prepare an organization to succeed as a public company.

Elena Lytkina Botelho

Life As a Public Company

Many CEOs intellectually understand the increased demands on a public company, but few are prepared for the emotional shock and wholly different pressures that hit "the day after." Here's what it feels like to run a public company:

- The Street is unforgiving and lives by different rules: "The company is like your child—you are growing and nurturing it. But for investors it's just a trade and 25-year-old analysts have no trouble telling you your child is ugly. You have to be able to communicate with analysts who'll beat you up about your quarter but never lose sight of managing the business for the long term," said **Tom Erickson**, a board member and senior adviser to leading private equity firms. Another shift newly public companies often struggle with is that while private investors are focused on EBITDA and total cash generation, public markets are focused on predictable growth in net income. Early days as a public company are the most challenging. You're just working the kinks out, and the Street is demanding a rock solid pattern of consistently delivering on expectations.
- You are under a microscope 24/7: If the demands of the Street weren't enough, a public company is always in the spotlight and often makes for an attractive target. If a scathing blog in the old days bruised mainly egos, now it can move valuation, impacting your ability to make strategic moves and directly hitting management team's pockets. Bad press about Wal-Mart's labor practices cost the company $16 billion in market valuation, according to *Business Week*.
- Your team needs help adjusting to the new world: Most CEOs leading up to IPO are busy selling their story to the analysts and often under-invest in educating the organization about what life as a public company will mean to everyone at the company down to the last employee. Why do we keep spinning our wheels on the forecasts instead of just running our business? What is gun jumping and why is it a big deal? Why are these hedge fund guys and consultants calling me to ask about deliveries last month and why is it such a big deal if I talk with them? Why are my options under water if we are hitting our numbers? These and other questions can become a distraction at best or a liability at worst if not proactively addressed early.
- You lose 20-30 percent of your time on the demands of running a public company, just as the bar on your performance is raised! The new game of leading a public company puts new demands on a CEO. With many new constituencies to manage, CEOs consistently report spending 20-30 percent of their time on managing requirements of a public company, especially early on. As you read this, look at your calendar and try to free up one day weekly for the next six months. How difficult does that look? How would you reprioritize your agenda? How would you need to reallocate responsibilities on your team? What help will you need to make sure the company hits targets despite the distraction of preparing for an IPO? Missing targets out of the gate is both common and incredibly damaging for a newly public company. It can take years and management changes to repair your team's reputation once tarnished.

Six Steps to Success

Given the fundamental changes ahead, the road to success as a public company starts at least 18-24 months before the IPO and continues long after. The following six steps will help ensure success and avoid predictable crises:

1. **Strengthen your board.** Sophisticated investors know that a well constructed board is a source of competitive advantage and begin to strengthen the board soon after acquiring a company and long in advance of IPO. In addition to meeting regulatory requirements for the number of independent directors, typically the following board roles get early attention: audit committee chair with strong public company experience, industry insider with an extensive rolodex, and a seasoned executive (often a former CEO) who can mentor the CEO. **Steve Key**, director on 10 boards and former CFO of ConAgra and Textron, noted: "An effective board is the best tutorial for a CEO in taking a company public. Trust between CEO and board is paramount—if it's not there, it's deadly in a public company."
2. **Rehire yourself into the new CEO role.** Given the degree and pace of change required to succeed as a public company, it can be fatal for a CEO who is slow to adapt. To avoid the infamous "boiling frog syndrome," a CEO must take an objective look in the mirror:

a. What are the business outcomes and leadership competencies required from the CEO and top team to deliver on the IPO story and maximize value creation as a public company (i.e. "organizational scorecard");

b. What are his/her own strengths and gaps against these new requirements.

Then "rehire yourself" into this new job: Proactively adapt your role, time allocation, surround yourself with team members who have a complementary skill set, and get other support you need to succeed. For example, a

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highly operational "Mr. Inside" CEO may not enjoy and not perform best in front of analysts and would need others to complement him (e.g., CFO, IR, COO, head of strategy or others on the team). On the other hand, highly charismatic sales-oriented "Mr. Outside" CEO would benefit from detail-oriented CFO and operations leaders vetting the numbers to avoid overpromising and underdelivering—a death knell for a public company. The most common derailers for public company CEOs include inability or unwillingness to hire a strong team and delegate, tendency to hold on to underperformers prizing loyalty over performance, habit for firefighting and lack of process orientation, lack of transparency and thin skin in dealing with inevitable setbacks dealt by the markets.

3. Build the right management team to take you into the future. Companies should ask themselves three questions in evaluating their current organization against future business requirements:

a. What are the areas where CEO will need support and additional leverage? About a third of the companies we surveyed introduced a COO role to drive day-to-day execution while the CEO spends 20-30 percent of his/her time on the activities required to run a public company.

b. How well do my current organizational structure and people map to the IPO story? To be credible with the Street, it is critical that you have the organization to back up your IPO story. If you are telling investors that most of your growth will come from Asia and meanwhile your entire international business consists of one person based in Chicago, it will be a stretch to convince the audience.

c. How will becoming a public company impact expectations and success requirements for each role and do the incumbents in these roles have an 80 percent-plus probability of delivering on these new objectives? The functions most typically upgraded in anticipation of IPO include: CFO (~60 percent of the companies we surveyed) and finance organization (particularly reporting, compliance, and FP&A roles); investor relations (~50 percent), and general counsel (~60 percent). When upgrading these and other areas, it is critical to start by creating forward-looking scorecards and conducting a candid assessment at the top to avoid temptation to add resources before you make sure that you have the right person

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leading the function. Best companies look broadly across the organization beyond the obvious areas most directly impacted by the IPO and proactively reset expectations, upgrade talent, and provide support and development to ensure new requirements are met. For example, human resources must be prepared for intense scrutiny over executive compensation; sales, marketing and operations must improve accuracy of forecasts; and the entire organization must adopt a mindset of process excellence.

It takes three to six months to hire an A player executive and major changes at the top once a company is public can increase share price volatility, so it is critical to evaluate the organization and begin to upgrade talent about two years prior to IPO.

4. Operate as a public company well before IPO. Depending on your starting point, successfully adapting to life as a public company may require deep changes in culture, people, processes, and systems which are impossible to achieve quickly. The best way to ensure success is by operating with public company mindset well before IPO. That includes: no surprises in financial results; accuracy of forecasts; increased financial acumen and analytical sophistication throughout the business; every employee must know the key targets and how their actions impact financial results; insights into competition (analysts will know your competitors and compare you to them); process orientation; flawless compliance record. If you anticipate changes that are risky for the business or make it harder to compare financial results, it's best to undertake them before IPO or hold off for ~18 months after. Undertaking projects like relocation, SAP implementation, change in accounting methodology, or a major reorganization too close to IPO timing increases execution risk and may negatively impact share price. **John Loyack**, Optim Energy CEO said: "If you have to take the pain, it's better to do that before you go public. Post-IPO all your mistakes get magnified. It becomes a time bomb!"

5. Pick your friends carefully—not all investors are created equal. Savvy CEOs (with the help of strong IR and CFO) are increasingly selective in picking potential investors. Capital markets bankers may want to fill your schedule with hedge fund presentations but your ride as a public company would be a lot smoother with longer term investors on board.

6. Communicate, communicate, communicate. Preparing for life as a public company is a change-management task that rises and falls on effective communication. To make sure you are heard internally and externally, tell your story five times more than you think necessary and assume that only 20 percent of your message is getting through. Effective communication can be worth hundreds of millions of dollars: a global growth investor shared that valuation of less known companies frequently increases after management team does a strong round of meetings with investors and analysts.

Conclusion

Many of these steps are common sense, yet most companies don't do them well or at the right time, often because the urgent priorities of preparing for the event of the IPO overshadow the more fundamental steps required to build a solid foundation for success and growth. Now that you know what needs to be done, don't let this go the way of typical New Year's resolutions. If you are an investor, CEO or board member preparing for IPO, launch your organizational readiness initiative today. ❖

Elena Lytkina Botelho is a partner, and C. Rodgers Palmer is a principal, at ghSMART, a firm offering quality-guaranteed services in the areas of management assessment and leadership coaching.