REPUTATION DIVIDEND What’s your reputation worth?

The 2018 UK Reputation Dividend Report
The sheer size of these numbers is beginning to shape communications and investment strategies.

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Reputations continue to be major drivers of corporate value in the UK. As of January 2018, they were responsible for £1,062 billion of market capitalisation across the FTSE 350, up 8% over the year.

Brexit uncertainty and a difficult economic environment saw investors increasingly respond to the reassurance provided by reputations. The confidence they inspire now accounts for 38% of market cap., close to the all-time high seen at the start of 2017.

Unilever regained the top spot recording the UK’s most economically impactful corporate reputation.

Investor interest is turning back towards defensive characteristics as volatility un-nerves sentiment creating opportunities for both the relatively more Brexit-immune FTSE 100s and the more at Brexit-risk FTSE250’s.

Introduction

Commercial performance sets the foundation for corporate success but it’s companies’ reputations that keep the heart beating. Profitable revenue generation, effective operation and strong governance creates the possibility of earnings momentum but it is the thoughts, feelings and impressions in the minds of company watchers that underpin investor confidence in the financial returns expected and ultimately what determines share price.

The 2018 UK Reputation Dividend Report summarises the health of corporate reputation and its capacity to drive shareholder value in the UK’s largest listed companies. It provides the latest perspectives on how well, or not, reputations are working for the companies they surround and the people who invest in them. It spells out the drivers of the value they deliver and reveals the opportunities for more effective messaging.

Reputation value analysis is critical intelligence. It presents company leaders, boards and reputation managers with unique understanding and in that, the means to deploy their companies’ reputations for both risk mitigation and value growth. The insight it brings provides the foundation needed to ensure that corporate communications and investor relations can prioritise the operational, performance and messaging strategies that underpin market confidence.
Overview

After all the drama of the Brexit vote, Trump’s election and world markets buoyed by the ‘wall of cash’, investors might be forgiven for thinking that 2017 would be less eventful. Any optimism however, would have been misplaced as political and economic forces combined, if anything, to up the pressure on corporates to manage the assets at their disposal.

The UK economy, arguably, performed better than expected over the last twelve months but all the signs are that the markets have stored up even greater risk. On the surface many FTSE 100s appear to make progress in 2017, but much of it can be attributed to a weak sterling (increasing the value of foreign earnings) and their greater alignment to a world economy which is, by many measures, looking healthier than at home. Compared to this time last year, while average reported pre-tax earnings were up more than 20% across the index, declared results were 9% below the forecasts at the time.

By contrast, FTSE 250s are looking at more fundamental challenges. The consumer base is increasingly reluctant to spend, imported raw-material costs are rising and, regardless of potentially more attractive pricing, export markets continue to be uncertain. In response, the average reported pre-tax earnings across the index was 15 percentage points lower than in the FTSE 100 at 7% and a full 6% below the levels forecast at the start of the year.

With all those factors at play the average Reputation Contribution – the extent to which they guide and secure investor confidence in the economic returns expected – was only marginally changed by 2018 and despite higher corporate earnings. The total market capitalisation across the index was up 10% over the preceding twelve months while the average Reputation Contribution was down, albeit less than a single percentage point, to 38%. Movement was showing signs of ‘reverting to norm’ (the long-run average is close to 32%) but the absence of compelling evidence from the fundamentals wrapped up in growing uncertainty, especially among those FTSE 250s at high Brexit risk, ensured that corporate reputations continue to be major drivers of individual company valuations.
Put simply, corporate reputations continued to underpin shareholder value as the fundamentals did not improve to the extent expected, uncertainty persisted but equities still offered some hope for investors chasing returns in an otherwise lacklustre market.

A Tale of Two Indexes

Within the FTSE 350 as a whole, companies in the lead index, the FTSE 100, were experiencing different pressure to many of those in the mid-cap FTSE 250 which is creating differences in their respective reputational needs. Reputation impact across the FTSE 100 remained higher than the lesser mid-cap index (averaging 41.2% vs 23.5%) and slipped less (-0.6 vs -1.6 percentage points). The two indexes delivered similar levels of market cap. growth (+10.0% and +8.5% respectively) but while reputation value was up (+8.5%) in the lead index the rise was far less (+1.7%) in the mid-caps.

Managers across the FTSE 100 need to have an eye to maintaining the impact of their reputation assets while others in the FTSE 250 would do well to ensure they’re doing everything they can to build success into the impressions they’re creating.

Fig 1: Reputation Asset Value in the FTSE 350
High Performers – The Top Ten

The Reputation Contribution index averages discussed above are driven by the performances of individual companies and how well, or not, their reputation assets happen to be working. The average across the FTSE 100 in January may have been a healthy 41.2% but that comprises high and low performing assets with individual contributions ranging from as little as 0.5% to as much as 56.7% with five companies rating over 50%.
The start of 2018 saw Unilever recover its leading position as the company with the most economically impactful reputation in the UK. It consolidated the already high regard in which professional observers view it and shook off many of the concerns raised by Kraft Heinz's failed bid as Paul Polman, the ‘capitalist with a moral compass’, revealed that sales growth improvements and pipeline innovation was progressing ahead of schedule.
Unilever’s step up to the top spot came at the expense of Royal Dutch Shell. Although aided by a recovery in oil prices higher tax payments, asset disposals and the financial stresses of recent years all combined to dull the company’s light (albeit only slightly).

Third place in the Top Ten is now occupied by the drinks giant Diageo which, on a 1 percentage point rise in its Reputation Contribution edged ahead of GSK with the highest rating seen since the appointment of CEO Ivan Menezes in 2013. The US performed well with the prospect for tax cuts countering the impact of the strong USD, growing revenues from China were beginning to reward the strategic focus and all-around success, illustrated by, for example, the CQI and Cass Business School’s Best Governance award, is being recognised.

High performing reputations are, inevitably, driven by the attention that comes with size, but that’s only part of the story. Attention fosters examination that in turn becomes the familiarity that helps to fashion reputation. Size matters but as a facilitator to and indeed accelerator of the impressions created rather than a basis in and of itself.

Elsewhere in the Top Ten the likes of Berkeley Group Holdings and RELX are showing how companies can punch above their weight.

RELX is ranked around 18th in terms of market capitalisation but its Reputation Contribution of nearly 46% secured its place in the Top Ten. More dramatically, while Berkeley Group Holdings’ market cap. places it towards the bottom of the index the high performance of its corporate reputation ranked it 5th overall. Good figures undoubtedly helped to foster support and, while the company was not immune to criticism, it mollified it by, for example, introducing new caps on executive payments, a positive attitude to a post-Brexit world and broader stakeholder sensitivity.

Corporate reputations, by definition, encapsulate how professional observers and company watchers such as investors see the business as an operating entity. They are complex collections of thoughts, feelings and impressions which, when filtered through the lens of what matters most at the time, fuel trust and confidence in companies’ ability to deliver on expectations and promises made. This is subject to changes in both intrinsic and extrinsic pressures and leads ultimately, to determine not only the overall impact of a company’s reputation, but also the influence of each component part.
Over the course of 2017 investor interest was consolidating a growing attention to the more defensive aspects of company performance. Continued uncertainty was fostering volatility in the markets and the attention of company watchers was looking to ‘evidence’ of companies’ ability to weather the squall if not storm.

Increasing attention on, for example, ‘considerations’ of the quality of management led to it becoming the single most valuable component of reputation across the FTSE 350 by the start of 2018. Together with perceptions of financial soundness and use of corporate assets it accounted for 41% of all reputation value on average in the index, £428 billion market cap.

Separately, lower awareness and lesser appreciation of characteristics related to the quality of marketing, innovation, typically more growth related characteristics and community & environmental responsibility accounted for only around 21% of reputation value on average or £220 billion of the combined market cap.
Building a Value Based Communication Programme

Value delivered can only be a part of the understanding needed to manage a reputation asset effectively. It provides an objective basis to direct communications for value security i.e. to protect ‘money in the bank’, but companies must balance it with messaging designed to play to the possibilities for value growth. It needs to be designed to shore up strengths, address the deficiencies and tap into the opportunities presented in order to serve the ultimate strategic aims of reputation management namely, value optimisation.

Reputation value analysis provides managers with the means to prioritise messaging needs and budgets based on their company’s unique reputation profile. This varies from company to company depending on the standing and status of how it’s perceived by the investment community and company watchers at the time and the nature of their interests more generally.

Fig 5: Reputation Priorities for Value Security and Growth

While every company’s position differs, they will be variations on the ‘average’ situation illustrated above. Value at present i.e. as at January 2018, is indicated on the horizontal scale which shows quality of management, financial soundness and use of corporate assets as the
most valuable components and *quality of marketing, innovation and community & environmental responsibility* as the least.

The vertical axis indicates the impact or return on investment that can be expected from improvements to perceptions of each factor. That shows the greatest returns coming from improving perceptions of *long-term value* and the least from gains in perceptions of *community & environmental responsibility*. These reflect the average standing of companies and, critically, the changing focus of investor interest as it evolves. Here, Brexit worries, volatility and concerns for consumer spending, or rather, a lack of it, are increasing the influence of factors such as *quality of management, capacity to innovate and long-term value potential* while reducing interest in *attractiveness to talent, quality of marketing and quality of goods and services*.

Crucially, understanding how changes in investor interest play out provides the framework necessary to make decisions about communications strategy. It offers reputation managers a means to prioritise and balance messaging and, amid the headwinds of market volatility and game changing transformations such as digital, a more objective approach value delivery and risk reduction. Only then can managers be sure that their activities will have greatest effect and those assets in their care, i.e. their companies’ reputations, work as hard as they can.

**Looking Ahead**

The questions for reputation managers are clear and demand well constructed answers if the assets in their charge are to be managed to best effect. Reputation value analysis helps companies manage uncertainty and create the framework to:

- Proactively manage corporate reputation - by spelling out how much shareholder value is dependent on it and how much is at risk
- Point to companies’ relative strengths and vulnerabilities - by demonstrating how they can be addressed through improved operational performance and messaging
- Understand what matters most to investors – by identifying the drivers that have the greatest impact on value … and the messaging will move the needle furthest
Reputation Value Analysis – Explained

Reputation value analysis reveals the economic impact of corporate reputation as a means to help companies manage the assets more effectively. It quantifies the tangible financial impact of corporate reputation by making the direct link to market capitalisation and share price performance.

Analysis is a two-stage process. First, the factors that most influence the investment community, and thus the market capitalisations, of individual companies are prioritised using statistical regression analysis of hard financial metrics, including shareholder equity, return on assets, forecast and reported dividend, earnings, liquidity and company betas and reputation measures from Management Today’s Britain’s Most Admired Companies and Fortune’s World’s Most Admired Companies reports.

From there, a combination of metrics are calculated, including the gross economic benefit shareholders derive from reputation assets, the location of value across the individual components of companies’ reputations, the extent to which investment in reputation building is likely to produce returns in value growth, and the relative value potential of individual messaging opportunities.

The financial value of each company’s reputation is explained in isolation, over time (with trends going back up to eleven years), relative to its peers and competitors and in terms of the contribution of the individual drivers of reputation value such as perceptions of companies’ ability to innovate, the quality of its management, its credentials with regard to corporate and social responsibility and so on.

The values of individual company reputations are often substantial and Reputation Dividend’s work has contributed significantly to the direction of reputation management and uniting and aligning the focus of senior executives. Clients span all sectors, many tabling the results of a study annually to their Boards by way of high-level reputation benchmarking.
How Reputation Dividend Can Help

Analytics are offered on two levels

Level 1: Dedicated Company Reports

Individual company studies to show:

- Reputation Contribution – the value of a company’s corporate reputation
- Comparisons with competitors and peers
- Trend data and the direction of travel
- The sources of a company’s reputation value and its contribution to market capitalisation - a company’s ‘Reputation Risk Profile’
- The incremental value potential of each reputational driver and potential for ROI – ‘what if’ analysis exploring different messaging possibilities
- Guidance on reputational messaging priorities as they relate to securing and growing shareholder value

Individual company reports also include an executive level briefing and meetings with key team members to discuss the implications

Level 2: Customised Research and Consulting

For any company wishing to make a more comprehensive investigation, Reputation Dividend offers a deeper level of research and analysis. This provides a more detailed examination of the drivers of a company’s reputation and its capacity to drive shareholder value.

This service is for organisations that wish to assess the impact of their corporate reputation against company specific drivers, at times of major change (e.g. in a merger or acquisition) or against a particular timeframe (e.g. in the run up to financial results).
Level 2 reports take account of reputational and financial data from a combination of internal
and external sources. We can also undertake bespoke research as required. We use our own
research resources and can complement these with any additional inputs.

These engagements often involve interviews with senior management, investment and industry
analysts to ensure that existing strategies are factored into our analysis.

In addition to everything in a Level 1 report, a Level 2 report provides:

► The insights necessary to inform executive management teams how to allocate
resources and budget more effectively

► A framework to align and adjust communications, messaging channels and budgets

► Guidelines for revising the internal strategies to support the reputation opportunities

► A basis to improve the coordination of communications and operational strategies

► The insight and knowledge to better align corporate, internal and customer brand
management

► The basis of a fully integrated and on-going reputation value management programme

For further information and how reputation value analytics can help
your company, contact:

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Reputation Dividend is proud to have worked with the following companies:

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Valuing Corporate Reputation to Secure and Build Shareholder Value