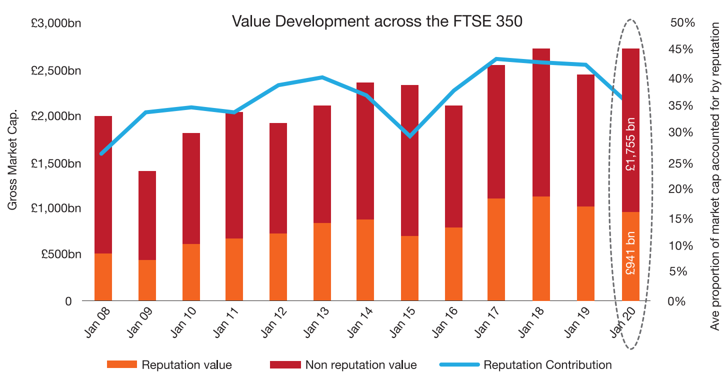
The UK 2020 Report

REPUTATION DIVIDEND What's your reputation worth?

- With a combined worth of £941 billion, corporate reputations in the FTSE 350 represent major assets…but their impact is under pressure as company watchers look harder at performance'
- Uncertainty in the macro environment is nudging investor attention towards the 'harder' evidence of operational performance leaving less weight carried by the 'confidence drivers' embedded in reputation
- While leading company reputations have held up, others have shown some deterioration
- Reputation managers would do well to prioritise messages that secure value extant and build on the most profitable opportunities

Investors Upping the Pressure on Reputations to Deliver

Corporate reputations continue to make major contributions to the value of the UK's largest public companies. As of January 2020, they were creating enough confidence to underpin the share prices of the majority of companies in the FTSE 350 and in that, support close to £941 billion of shareholder value; 35% of the gross market capitalisation.



While this reflects a high level of reputation performance on-going and intrinsic belief in the prospects for UK Plcs, impact is markedly down on recent years. Moreover, it runs counter to earlier trends when the influence of reputation has grown to cushion values in an otherwise weaker environment.

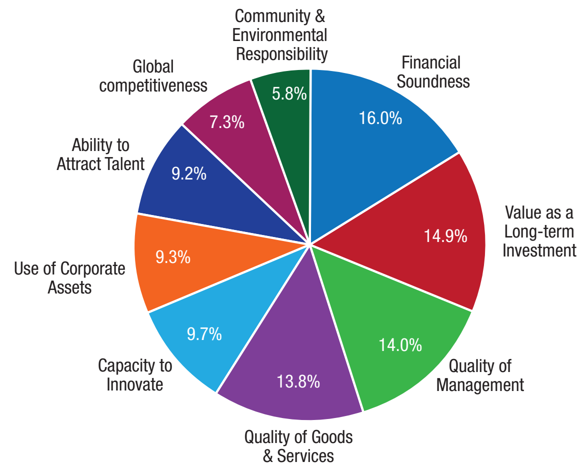
Investors are showing all the signs of having been bruised by the uncertainty of post-Brexit Britain, the prospects for global trade, a rancorous election upcoming in the USA and now the emergence of Covid-19 and they're less ready to place as much trust in anticipated returns on the collected thoughts feelings and impressions that comprise corporate reputations as previously. The double-whammy of a notable reduction in the 'admirability' of many companies across the index and increased circumspection more generally has resulted in an emphasis nudge in the direction of the harder evidence of the performance metrics. Something one commentator recently summarised with the warning that 'we're entering the uncharted territory of a 'risk-off' bull market driven not by optimism, but by a chronic fear'.

The declines in Reputation Contribution – the proportion of a company's market cap. attributable to the confidence inspired by reputation – over the last twelve months have not, thus far, been uniformly spread, with the greatest hits registering among the less influential properties. Whereas the average decline seen in companies in the bottom 20% of reputational performers was c23 percentage points (to -7.0%), it was broadly unchanged (+0.5 ppts) for the top 20%. Moreover, although there were some individual movements among the top five properties, Reputation Contribution ratings in the leading group continued to register at between c49 and 56%.

UK TOP 5	Reputation Contribution	Reputation Value
	55.8%	£92,335m
bp	51.8%	£51,082m
Unilever	50.8%	£58,472m
DIAGEO	49.1%	£36,744m
bhpbilliton	48.5%	£43,577m

Looking ahead to 2020, companies need to organise messaging to reflect the changes in investor sentiment by utilising the fact that different components of their reputations drive very different value opportunities (see fig. overleaf). Rising uncertainty has focussed attention on factors like *financial soundness* and *long-term value potential* with the result that the value contributions of those elements have gone up (to 16.0% and 14.9% of the total respectively). Conversely, interest in factors like *global competitiveness* and *community & environmental responsibility* has slipped so reducing their value contributions (to just 7.3% and 5.8%).

The implications are clear. The learnings from studies like this can offer critical guidance to prioritising messaging strategies and communications. Companies with high performing assets need to consider messaging designed to secure sources of value extant, while those with lower performing assets need to address the parts of their reputations that offer the greatest opportunity for value growth. In the face of market volatility such as we're seeing right now it can lead to game-changing transformations, bring greater objectivity to risk-reduction and, ultimately, support the all-important value creating role of the reputation asset.



Reputation Value - Relative Factor Contribution

Reputation Value Analysis - How it's Done

It is well known that while there are many widely recognised methods of valuing companies, none explain market capitalisation with any degree of accuracy. Moreover, few, if any, provide actionable insight into the influence of intangible assets such as companies' reputations. Equally, survey research measures of reputation are inevitably hamstrung and limited because they offer little means of contextualising their outputs and answers to the question 'so what?'.

Reputation Dividend addresses this head on through the application of its proprietary *Reputation Value Analysis* to both explain and quantify the influence of the main non-financial component of corporate value namely the accumulated thoughts, feelings and impressions that make up its corporate reputation.

The unique approach to reputation measurement which lies at the heart of the process uses a range of financial inputs and drivers that both contribute to a company's value and shape the 'standard practice' valuation methodologies of the accountancy and the capital markets worlds. A combination of 'hard' financial data sourced from the likes of Bloomberg and Morningstar and 'softer' survey research based measures of corporate reputation such as reported in the *Most Admired Companies* studies published by Management Today and Fortune magazine are analysed using statistical regression techniques designed to identify the principal drivers of company value as indicated by the markets.

Analysis involves a systematic examination of if, and then how, each of 40+ candidate 'explanatory' factors work both individually and as a whole to explain the differences between companies' values. By looking at more than 200 of the country's largest listed companies at the same time it distinguishes between those factors that are having a bearing on shareholder value and those that are not. From there, it prorates a proportion of each company's market cap to the main contributing factors according to their relative influence – including corporate reputation if it is found to be having an impact. Finally, with further drilling down, the value impact of each of the different headline reputation drivers is identified individually and assessed. Ultimately, this explains close to 95% of companies market capitalisation and constitutes the 'General Model' of investor behaviour.

Armed with that the specific circumstances of individual companies can be examined in order to calculate the strength of their unique reputation assets and value risk profiles. This reveals the degree to which investors are paying a premium or discounting compared to the value implied by the financials alone. So, where a greater proportion of market cap is attributed to reputation the asset is by definition working harder with the premium denoting the contribution to shareholder value. Conversely, where the proportion is negative (in a minority of cases) it indicates that the reputation is in fact destroying value and at a discount relative to the financial drivers.

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