

REPUTATION
DIVIDEND What's your reputation worth?

The 2016 US Reputation Dividend Report



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...studies like this should focus the minds of
all those in positions of corporate power

Questor, The Daily Telegraph

Corporate Reputations - Beacons of Dependability in an Uncertain World

- ▶ Corporate reputations accounted for \$3,977bn of market capitalization across the S&P in March 2016; 20.7% of all shareholder value and 2.5% points more than a year before.
- ▶ Value of corporate reputations in 2016 up for the first time in four years as they increasingly signaled safe-havens in markets characterized by uncertainty.
- ▶ Rising investor caution increased store placed in perceptions of *long term potential, core product quality and global competitiveness* at the expense of more natural recovery characteristics such as *people management*. A sign that expectations for recovery are, for now, on hold.

Introduction

Reputation has long been recognized as a cornerstone of corporate value. The thoughts, feeling and impressions of companies residing in the minds of professional observers form the basis of the confidence that underpins their decisions and the lens through which the investment community consider their positions. Warren Buffet's much repeated mantra '*We can afford to lose money - even a lot of money. But we can't afford to lose reputation - even a shred of reputation*' has long been asserting the case, but just how much those precious assets actually contribute, has only become clear in recent years.

The 2016 US Reputation Dividend Report summarizes the health of corporate reputation in the United States and its impact on shareholder value. It offers the latest perspectives on how well, or not, reputations are working for the companies and the people who invest in them. It uncovers the key drivers of reputation value and points to opportunities for more effective messaging.

Reputation Value Analysis is critical intelligence for both the C-suite and the managers of reputation assets. It helps to create a better understanding and appreciation of how to most effectively deploy reputation management for risk mitigation and lasting material impact. Insight into the mechanics of the value generating capacity provide the means to ensure that corporate communications work as hard as they can, not least in times like the present, when uncertainty and volatility can all too easily distract attention and derail progress.

Overview

Reputations Taking the Strain in the Face of Economic Headwinds

As well as keeping a close eye on company performance and prospects, investors have had to deal with an unusually toxic cocktail of macro-economic events through 2015 and the first half of 2016. The engine for global growth that was until then, China, stalled as concerns for the ability of the government to manage the economy increased and currency pressures grew.

Overall, Eurozone woes showed little sign of being resolved and indeed, were exacerbated by the refugee crisis and the UK's Brexit vote. The post-crash oil-price 'rally' in early 2015 proved to be short-lived and was compounded by a wider slide in commodity prices and growing realization that low prices were set to stay for some time. The strength of the US dollar continued to create problems for many companies and on the political front, the rise of populist, protectionist and anti-elite sentiment around the developed world, not least in the US with elections in November, have raised a host of difficult questions for the established orders.

As a result, investors showed a marked tendency towards caution and exhibited distinctly less optimism for companies' underlying commercial prospects. Sentiment became characterized as 'watchful' rather than 'nervous' with the effect that there was an increasing nod to the 'safety' inferred from strong corporate reputations.

The main effect of the change in sentiment was an increase in investor 'reliance' on corporate reputation to guide and secure their confidence. Whereas in March 2015, reputations accounted for an average of 18.2% of market capitalization across the S&P 500, a year later, in March 2016, they were delivering 20.7%, \$3,977bn worth of shareholder value. Reputation Contribution – the proportion of corporate value accounted for by reputation – was up by an average of 2.5%-points reversing a trend evident since 2011 thus mitigating the downward pressure on stock prices and leaving shareholders across the index \$584bn better off.



Fig 1: Reputation Contribution Development

The Ten Most Powerful Corporate Reputations in the US

The impact of reputation varies considerably from company to company. In the majority of cases (almost nine out of every ten companies in the S&P 500), it drives real 'tangible' benefits and create positive shareholder value but in the remainder, they are so poor as to be damaging confidence and in that, destroying value. Individual Reputation Contributions across the index in March 2016 ranged from highs over 50% (four companies) to lows below -20% (five companies), where the underlying reputation assets are damaging confidence and limiting the share price by more than \$1 in every \$5.

Apple and Walt Disney continued to be the reputational stars holding on to the number one and two positions with the most economically powerful corporate reputations in the index. Apple's Reputation Contribution consolidated by more than 6%-points to 55.9% as company watchers appreciated wide-ranging commercial success regardless of the absence of any new blockbuster product performance. iPhone sales achieved the rare feat of growing share while commanding a substantial price premium and the company's efforts in China began to pay off big time. The only cloud to dampen investor enthusiasm was concern in some quarters that the company might be challenged to top its success again in 2016.

By contrast, Walt Disney's number two spot was somewhat fortunate with only an index-average increase in Reputation Contribution of 2.6%-points (to 52.0%). The launch of Disney's first Star Wars film and the opening of the Shanghai theme park fueled optimism but there were concerns that The Force might be slipping as subscriber losses continued to mount in the ESPN profit engine and questions were raised about the company's succession planning.

Alphabet, in third place, posted a solid 4%-point increase in Reputation Contribution to close the gap on Disney. Moves to instill greater discipline, get costs under more control and increase transparency coincided with the arrival of the new CEO from Morgan Stanley and a corporate reorganization that separated core business from the 'moonshots' under the new moniker.

Company	Reputation Contribution	Reputation Value	2015 Rank	Change in Rep Cont vs 2015
	55.9%	\$313,971m	1	6.4%
	52.0%	\$81,944m	2	2.6%
	51.6%	\$260,834m	4	4.4%
	51.2%	\$177,216m	3	2.6%
 NIKE, INC.	47.3%	\$48,976m	7	6.6%
	47.1%	\$150,089m	10	7.7%
	47.0%	\$40,711m	16	11.0%
	46.3%	\$81,890m	6	5.2%
	45.0%	\$131,118m	8	4.5%
	44.3%	\$35,145m	14	7.8%

Fig 2: The Most Economically Impactful Reputations in the US in 2016

Outside the leaders, the most notable changes in the top ten was Starbucks and Boeing replacing AT&T and Occidental on sizeable rises.

Starbucks' 11%-points rise in Reputation Contribution to 47% elevated the company from 16th to 7th position. Although attracting criticism for its tax practices in Europe its defense was solid and overall, its reputation asset was strengthened by programs such as the employee online degree support and the 'Race Together' campaign wrapped up in good profit growth around the world. **Boeing**, the only other company to break into the top ten, benefitted from a nearly 8%-point increase to 44.3%. 2015 was a strong year for the company as it capitalized on a relatively benign market to grow profits on high deliveries.

But for every riser there was a faller and, while Starbucks and Boeing moved up, AT&T and Occidental Petroleum dropped out of the leaders. Although their reputation assets remained high performing, both lost some shine. **Occidental** was felt to be suffering disproportionately from the sector issue of the enduringly low oil price while worries over subscriber growth and the merit of the \$49bn tie-in with DirectTV cast shadows at **AT&T**.

As in previous Reputation Dividend reports, the evidence remains clear. Individual success in growing reputation assets can produce considerable gains for shareholders. It cannot be assumed however and the foundations of any value created need constant support if they're to continue to deliver as they can.

The Pillars of Reputation Value

Effective reputation management is about working the elements under the company's control within the constraints of those that are not. Reputation impact is determined by a variety of lagging indicators and leading drivers. Any can have a bearing on a company's reputational capital, however while the implications of the former need to be recognized, it's the latter that offer the opportunities for reputation management.

S&P 500	Average Market Capitalization	Reputation Contribution		
		Mean	Min	Max
Top 20%	\$164,072m	35%	-3%	56%
2nd 20%	\$47,218m	28%	2%	43%
3rd 20%	\$25,587m	20%	-25%	39%
4th 20%	\$14,119m	16%	-25%	35%
Bottom 20%	\$7,027m	10%	-19%	41%

Fig 3: Reputation Impact and Company Size

First and foremost among the lagging indicators is company size. Larger companies not only tend to be better known, but also, applauded and rewarded for 'success'. As at March 2016 the Average Reputation Contribution in the top quintile of the S&P 500 (companies 1 to 100 by market cap.) was 35%. In the second quintile it was 28% and so on down to the fifth and last quintile where it was just 10%.

Size undoubtedly relates to reputation impact, but it clearly isn't everything. Within each band there are companies with high performing reputation assets and companies with low performing ones. In the top quintile, the highest Reputation Contribution was 55.9% (Apple) while the lowest was -3.2% (Kraft Heinz). By contrast, the highest Reputation Contribution in the bottom quintile was 41.4% (Alcoa) while the lowest was -19.2% (Gap). Company size is feeding investor confidence but it is only one part of the story and, given the wide spread within similar size organizations, only a minor one.

A more significant factor is business sector. Corporate performance is judged in part by reference to peers and competitors where points of comparison help the analyst focus on the strengths and weaknesses that indicate potential and qualify promise. As at March 2016, average sector Reputation Contributions varied from as much as 34.3% in Telecommunications to as little as 13.2% in Utilities.

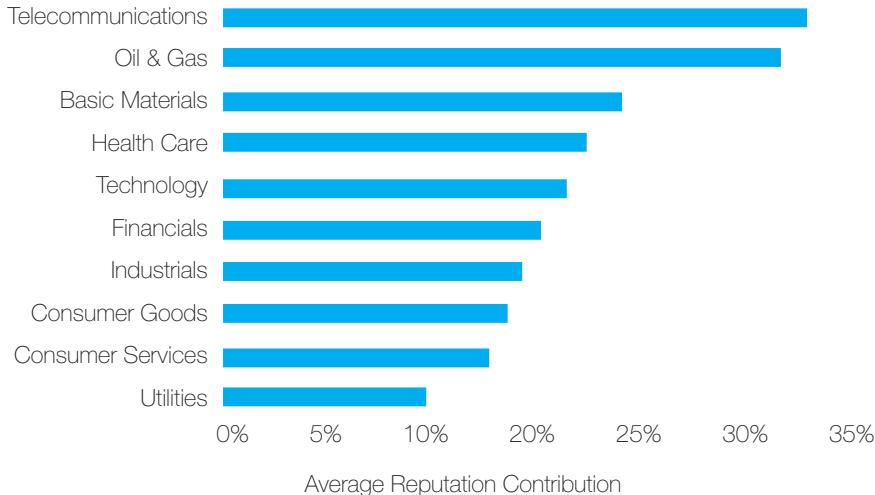


Fig 4: Reputation Impact by Sector

Telecommunication companies, characterized by the likes of AT&T and Verizon, operate in a mature and closely examined sector. A large degree of the 'faith' in stock performance is dependent on companies' reputations which are, therefore, disproportionately influential. Oil & Gas company reputations are similarly high performing albeit less so than they were in 2015 (-3.5%-points) because of stubbornly low oil prices which has challenged the confidence in some companies' ability to succeed. Corporate reputations have helped to carry the promise thus far but they are in need of support if this is to continue.

By contrast, the average Reputation Contribution in the utility company sector was only 10.8% in March 2016. Reputations are important in that they have a material impact but, given the more stable nature of the underlying businesses and the lower potential for significant margin building initiatives, predictability there requires less of an article of faith.

Lagging factors such as company size and industry sector are important determinants of reputation impact however, the single greatest influence and indeed, the leading driver, is what the company is known for, its reputation and how well, or not, it is regarded on each dimension. And that, filtered through the lens of what matters to investors most, provides the key to maximizing the effectiveness of the asset and optimizing its economic value.

Crucially for reputation managers in 2016, there have been a number of changes in investor priorities. The widespread ‘failure’ of companies to deliver on what turned out to be over-optimistic commercial promises being made at the start of 2015 combined with the worsening macro-economic headwinds engendered marked shifts in their interests.

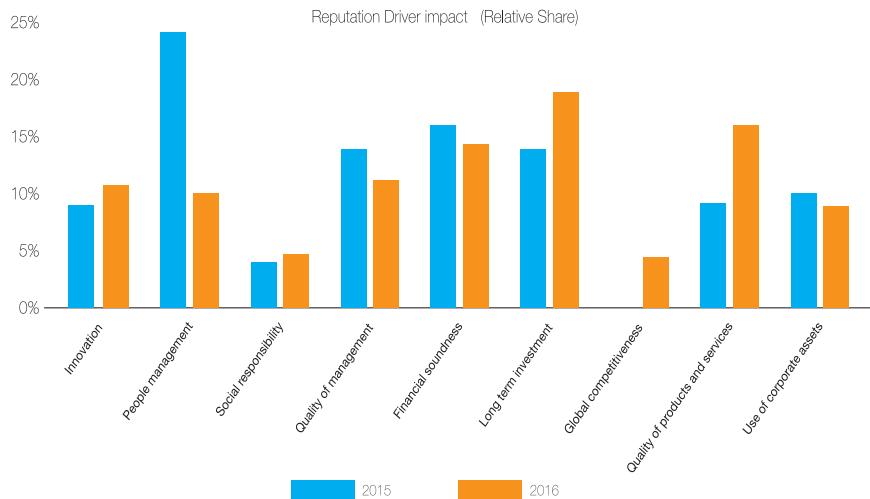


Fig 5: The Reputation Value Drivers

Currently, the reputational factors resonating most with investors relate to views on the *long term potential* and underlying *financial soundness*. Given the disappointments of 2015 the former has grown in importance while the latter though marginally down, remains a key driver.

The most notable change was in the role of *people management*. Whereas in early 2015 it was a signal of companies’ capacity to capitalize on a putative up-swing, it became less important as optimism gave way to uncertainty.

Equally, *global competitiveness* returned to the more active driver fold, albeit in a minor capacity, as the merit of risk spreading grew and investor belief in a growing domestic economy largely insulated from global troubles faltered. Similarly, the importance of strong perceptions of the quality of good and services went up as investors reasserted their belief in the role of fundamentals ... in the short term at least.

Reputation managers have to ensure that their messaging delivers against these precise investor 'needs'. Amid growing economic headwinds, market volatility and game changing transformations such as digital, understanding role of reputation as a beacon of reliability, dependability and delivery is more relevant than ever. Only then can they be sure that their activities will have maximum effect and the critical assets in their care work as hard as they can, and indeed, must.

Looking ahead

The challenges for reputation managers are clear and demanding answers if the assets are to be managed to best effect. Reputation value analysis helps companies deal with uncertainty and:

- ▶ Get back to the business of proactively managing corporate reputation: By spelling out how much shareholder value is dependent on reputation and how much is at risk?
- ▶ Pay attention to how stakeholders view your competitors and peers: Show exactly how are they perceived and point to your relative strengths, vulnerabilities and how they can be addressed through improved operational performance and messaging?
- ▶ Understand what matters most to your stakeholders: Identify the drivers that have the greatest impact on reputation value...and the messaging that will move the needle?

Reputation Value Analysis, Explained

Reputation value analysis explains the economic impact of corporate reputations with a view to helping companies manage their reputation assets more effectively. It quantifies the financial worth of corporate reputation - making the direct link to market cap and share price performance. Trending data on more than 700 Fortune and FTSE listed companies go back nine years.

Analysis is a two-stage process. To start with, the main factors that influence the investment community, and thus the market capitalizations, of individual listed companies as a whole are identified. This is achieved by means of statistical regression analysis of hard financial metrics, including, for example, shareholder equity, return on assets, forecast and reported dividend, earnings, liquidity and company betas as derived from Bloomberg or Factset, and reputation measures, in this instance, taken 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 are deriving from the reputation asset, the location of value across the individual components of the company's reputation, the extent to which investment in reputation building will produce returns in value growth, and the relative value potential of individual messaging opportunities.

In addition to determining the financial value of a company's reputation relative to its peers and competitors over time, the contribution of the individual drivers of reputation value such as perceptions of companies' ability to innovate, the quality of its management, its credential with regard to corporate and social responsibility and so on are also calculated, as is their trajectory.

Given that the values of individual company reputations can often be significant, Reputation Dividend's work can be particularly useful to help both unite and align the focus of senior management. Corporate clients span all sectors, many tabling their Reputation Dividend report annually to their Boards by way of high-level reputation asset benchmarking

How Reputation Dividend Can Help

Analytics are applied on two levels.

Level 1: Dedicated Company Reports

A study will explain:

- ▶ Reputation Contribution – the value of your company's corporate reputation (including trend data).
- ▶ Comparisons to competitors and peers.
- ▶ An explanation of the sources of your company's reputation value and its contribution to market capitalization - your company's 'Reputation Risk Profile'.
- ▶ The incremental value potential of each reputational driver and potential for ROI – 'what if' analysis exploring 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 meeting with key team members to discuss the implications.

Level 2: Customized Research and Consulting

For any company needing to make a deeper dive investigation, we offer a second level of research and analysis. This provides a more comprehensive and bespoke examination of the drivers of a company's reputation and its capacity to drive shareholder value.

This service is for organizations that wish to assess the impact of corporate reputation in more detail and against company-specific reputational drivers or against a particular timeframe (for example in the run up to financial results).

Level 2 reports take account of reputational and financial data from a mix of your own internal and external sources. We can also undertake additional custom research as required. We use our own research resources and can complement these with any additional sources of your choice.

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 will provide:

- ▶ 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 program.

Level 2 engagements provide regular client liaison and findings review throughout the process and culminate in a presentation to and discussion with the senior leadership team.

Reputation Dividend is proud to have worked with the following companies



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

Simon Cole – Director & Founding Partner

Simon@reputationdividend.com

Sandra Macleod – Director

Sandra@reputationdividend.com

Robert Takacs – Senior Vice President

Robert@reputationdividend.com

Or visit our website : www.reputationdividend.com

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