A TALE of two stories

Value creation needs a new narrative, say IAN ROE and HANNAH GRIFFITHS of MerchantCantos

FORTY YEARS AGO, INVESTOR ANALYSIS RARELY needed to go beyond the financials. Over four-fifths of a business's market value was its tangible assets.

Today, the reverse is true. Tangible assets now represent less than one-fifth of the value of S&P 500 companies, according to research by Ocean Tomo, an intellectual property merchant bank. Companies must tell a more complete story or risk short-changing their investors and undermining their own reputations.

Integrated reporting – weaving together both financial and non-financial considerations in long-term value creation – helps to tell that story. But beyond one or two jurisdictions that mandate it, the practice remains outside the mainstream. In the UK, for instance, Deloitte found that just 7 percent of FTSE 100 businesses make an explicit reference to the framework established by the International Integrated Reporting Council (IIRC).

Companies and their bosses are increasingly expected to explain not just what they do but also how they do it – and why. Two-thirds of investors and three-quarters of CEOs surveyed by PwC in 2016 said they defined business success by more than financial profit. So why is integrated reporting not ubiquitous?

The answer involves a reality check: corporate reporting is already tortuous. The bigger the company – global businesses operating across multiple jurisdictions for instance – the harder it becomes. As it is, companies must run the gauntlet of legislative requirements, regulatory codes, voluntary frameworks and best practice guidelines just to meet minimum expectations.

In addition, many businesses tell us that investors are simply not demanding integrated reporting. Worse, many investors mistrust alternative (non-GAAP) performance measurements – as many as 40 percent according to Deloitte research.

Despite these obstacles, it seems equally clear that integrated reporting isn't going away. Far from it. Although relatively few businesses formally recognize IIRC's framework, Deloitte's research found that over half of businesses reviewed were explicitly using aspects of it. Nearly two-thirds used both financial and non-financial key performance indicators.

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PERCENT OF COMPANIES REPORT NON-FINANCIAL KPIs
Source: Deloitte

KNOW YOUR AUDIENCE

BUSINESSES THAT EXPECT TO BE SUCCESSFUL IN reporting non-financial results need to focus as hard on the communication as they do on the integration. Too many of the early integrated reporting adopters had over-engineered, spaghetti-junction business models and inch-thick reports. Essential points about your business are less likely to be noticed if your presentation is padded out with immaterial metrics or tangential narrative elements.

Companies that tell compelling, integrated stories of their operations do not all get it right in the same way. But they have one thing in common: they understand what their audiences need and give it to them in a way that is easy to digest.

INTEGRATED REPORT Some companies go for the full integrated report. Novo Nordisk, for example, has a central integrated report that refers to IIRC's framework. It still manages to be a simple, jargon-free and compelling articulation of Novo Nordisk's work.

TAILOR TO FIT Material can be framed differently for specific audiences. Lloyds Banking Group structures its annual report around essential issues and supplements that with data sheets for analysts, issue-led summaries for different stakeholder groups and, for those who need even more detail, online indices that cross-reference their reporting.

MULTIMEDIA Multiple channels may be used to communicate a broader message of non-financial value outside of the context of quarterly or annual reporting. That includes infographics for key messages, animation explaining complex concepts, and CEO interviews to authoritatively establish company priorities.

Ultimately any approach needs to answer the question increasingly being asked of every business: what do you do, how do you do it, and why does it matter to the world? Each company must find its own way to answer, in line with its business model and the long-term vision of its leadership.

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