walking the talk
Culture made do-able

Culture Counts

To what extent does culture influence the views of investors within the investment community?

Foreword

Contents

Walking the Talk is delighted to share with you the findings of our research into whether culture influences the decisions of the investment community.

I have been working in the field of culture change for 25 years, alongside visionary executives who have shared that belief. My book on this experience, *Walking the Talk: Building a Culture for Success* documents the links between culture and business performance experienced by our clients.

Recently the profile of corporate culture has increased, and more organisations are looking for ways to manage and improve their culture. Phone hacking, financial mis-selling, oil spills and other misdemeanours have stemmed from the explicit or implicit tolerance of questionable behaviours, which have become embedded in the culture.

How an organisation, or an individual, spends time and money is a good indication of what is *really* valued. Should we be shocked at the growth in reputation issues when investment in culture still lags far behind investments in other key enablers of business performance, such as brand and technology?

We strive to convince Executives that culture is truly a direct contributor to performance. Through our work we know it to be true, but we are always looking for opportunities to add to our body of evidence.

One way to contribute to the conversation was to ask professional investors to what extent an organisation's culture influenced their views of company valuations. Stamford Associates a leading independent investment consultant, kindly provided us with access to a population of investment professionals, to explore the relationship between culture and company valuations

The results suggest that Executives will hear more about culture from their investors in the future and that culture really does count.

Carolyn Taylor

CEO

Walking the Talk

Foreword

In January 2012 I read a fascinating financial report from UBS Investment Research Analyst, Nik Modi. Mr Modi had downgraded his rating of Procter & Gamble Co. from 'buy' to 'neutral'. At the heart of this decision was his belief that "P&G's culture has limited the company's ability to meaningfully change how it does business. This has a direct impact on its ability and speed to cut costs or make other meaningful changes."

As someone, who has spent their career in culture and has dealt with the challenge of making culture tangible, it struck me that this was an example of how culture impacts upon the value of an organisation.

During the last few years, I have used this story with many organisations as a powerful insight around how their market value and their culture are linked. It is credible evidence that culture does impact business performance.

Since reading the article I have sought out similar commentary with little success, which led me to question to what extent do professional investors take culture into consideration when developing their view of company valuations?

This research is the start of answering that question and looking at the implications for businesses and HR.

Amanda Fajak

Regional Director, Europe

Walking the Talk

1. Executive Summary

> *"If you ask our CEO, what's the variable that you would want to have the clearest insight into, it would be management quality and the company culture. Everything else you can pick up from the industry analysis."*

Culture counts.

Culture is an important consideration for the majority of the investment professionals who participated in our research. Culture is influencing their views of company valuation.

For most respondents culture sits as one of many factors they take into consideration in their valuations. But it is worth noting that for nearly one third of respondents culture is listed as one of their primary considerations.

Respondents acknowledge that their means of gathering data around culture is not sufficiently systematic. However there is an interest and growing determination to more accurately assess culture.

There are a small number of respondents who have become relatively sophisticated, in our opinion, in their understanding of what culture is and how they should be assessing it.

However, culture is still largely seen as nebulous, ambiguous and intangible, hard to define and assess. Part of the challenge is that there is no clear definition of what culture is.

> *"Culture is tough to define and nearly impossible to measure systematically."*

Culture assessment is often driven by the perceived alignment between published aspects of culture, such as value statements, and the behaviours of Senior Executives and leadership experienced by the respondents. This assessment can be frustrating in its subjectivity.

Despite the challenges, respondents are seeing evidence of dilutions or improvement of investment value as a result of culture. These observations ensure that culture will continue to be of importance in company valuations and motivate investors to improve their cultural assessment capability.

Implications

For CEOs and Directors

Culture is already impacting the way some analysts are evaluating your organisation and is likely to become more commonplace in the future.

Whilst the current means of evaluating culture are, on the whole, unsophisticated, as more changes in company value are linked to culture and as professional investors engage in more debate and discussion around the value of culture, this will change. We believe that more accurate ways to assess culture from a distance will be developed by the investment industry.

Today the focus for professional investors is on the behaviour of your executive and whether they can be trusted to operate consistently with your stated values. It is therefore, no longer sufficient to just talk about your culture. Your ability to demonstrate it in action, 'your walk', is critical.

The opportunity for Executives is to get ahead of the curve on culture, whilst professional investors build their cultural assessment sophistication. An investment in culture capability now may pay dividends, quite literally, for your shareholders.

"Information about organisational culture (good or bad) is reflected in a security's price."

For Human Resources

Culture is already impacting the value of your organisation in the eyes of many of our respondents, perhaps more so than your Board and Executive realise.

To what extent are you, as HR, consciously influencing your organisational culture in terms of what it is and how it can be evaluated by the investment community?

"Access and discussions with company leadership teams, ideally on a 1:1 basis are of most value."

It is not often that HR can play a role in the investor relations space but this research provides you with a legitimate platform to raise culture capability and culture communication as a strategic focus and influencer of market perceptions of your organisation.

This research reinforces and enhances the strategic role HR can play as a contributor to shareholder value.

"We're very hands-on with management, we visit with every management team, we like to visit plants and meet with middle level management as well as senior level management."

2. Research results

Methodology

To what extent does culture impact upon an analyst's investment predictions and recommendations?

To answer this question Walking the Talk partnered with Stamford Associates to conduct both a quantitative on-line survey and a series of in-depth qualitative interviews during April 2015.

Questions were targeted around whether culture factored in their investment decisions, how the community defined culture and what evidence they were using to support any cultural assessment.

The online survey went out to 1000 contacts, with the results based on responses from 10% of this group, a market average sample size.

All opt-in questionnaires tend to suffer from self-selection bias, it tends to be those most in favour, or most against that invest the time to respond. Survey results gathered reflect a range of views about the importance of culture, including those which believe culture to have no value.

We recognise that the results may be biased towards those in the investment community that are already using and valuing culture as a business assessment criteria, however there are interesting trends and comments revealed which we feel are indicative of the wider community.

Figure 1: Role profile of respondents

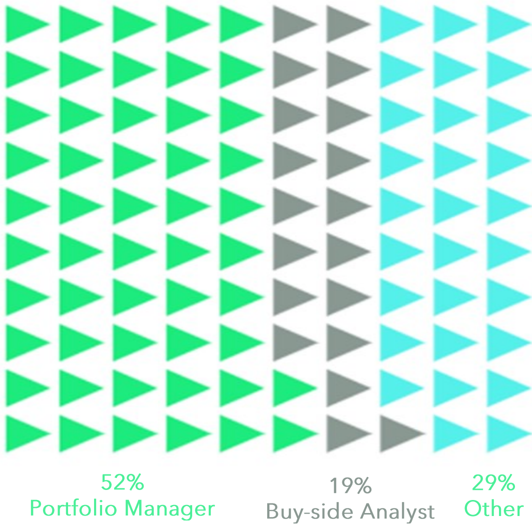


Figure 2: Asset class managed

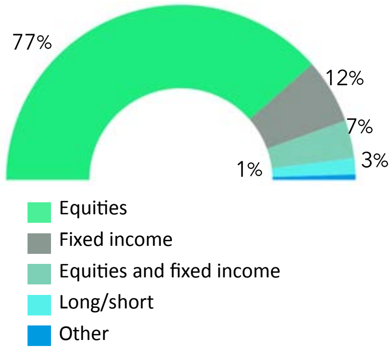
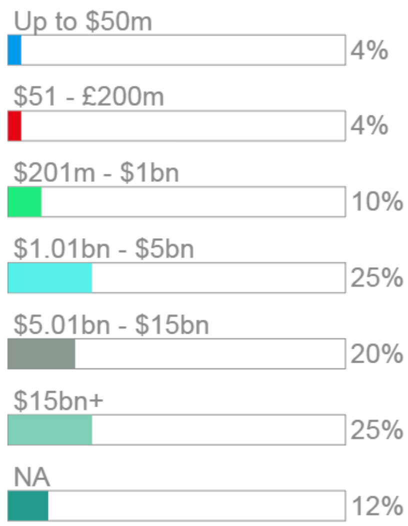
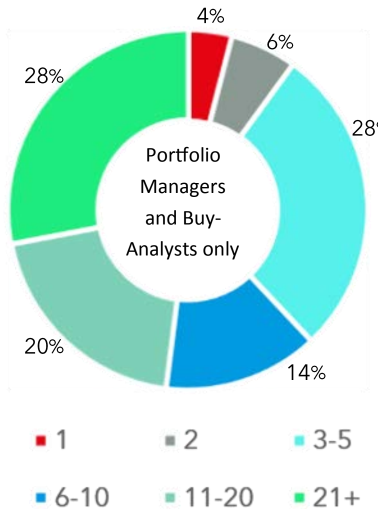


Figure 4: Value of total assets under



Figures in USD

Figure 3: Investment team size



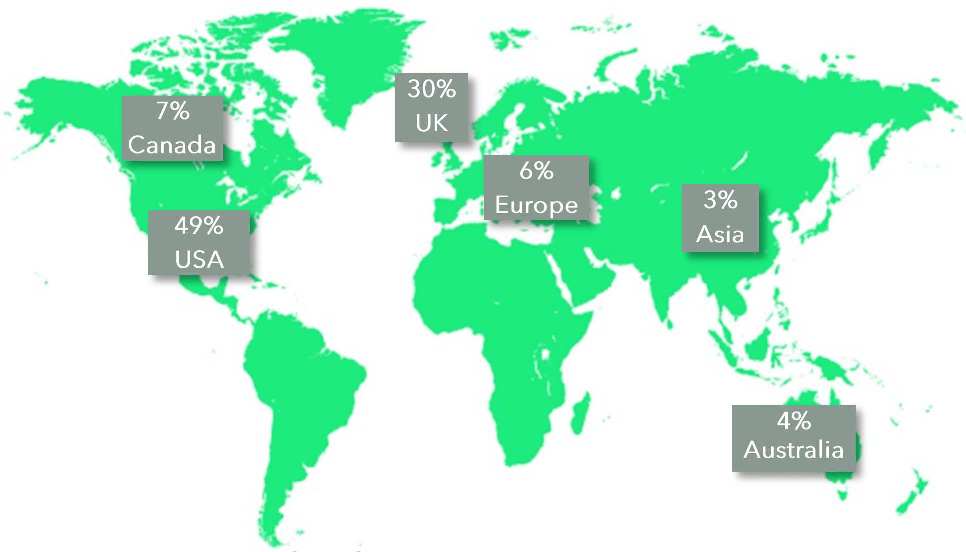


Figure 5: Regional profile of respondents

Figure 6: Familiarity with the concept of culture

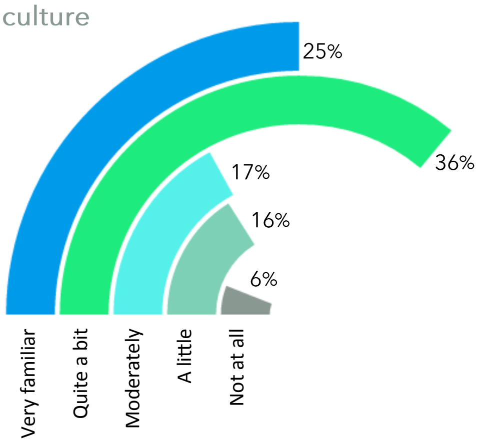


Figure 7: Importance of culture in investment decisions

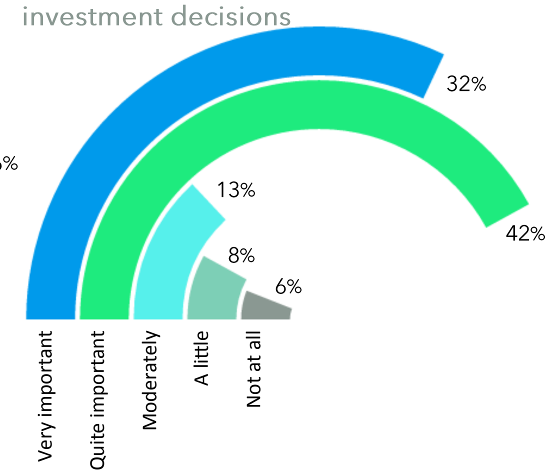


Figure 8: % extent to which culture impacts the buy-sell decision

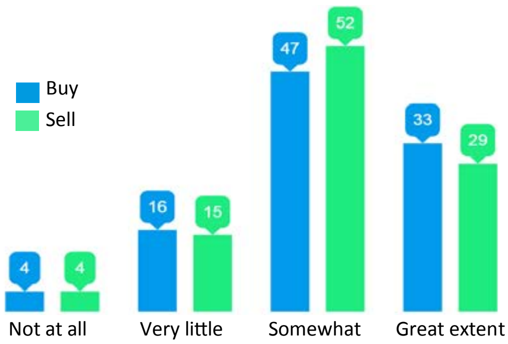


Figure 9: % respondents with experience of an investment value dilution due to culture

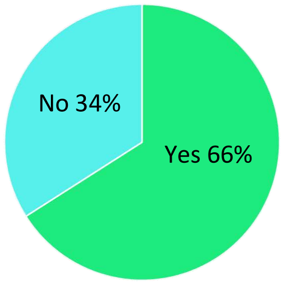


Figure 10: Key culture themes

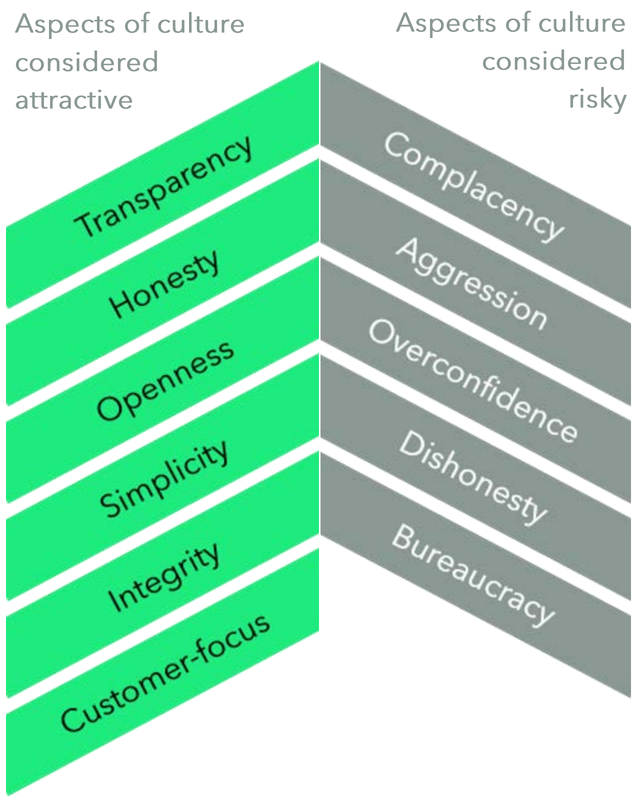


Figure 11: No common definition of culture

Figure 12: Main sources of culture information

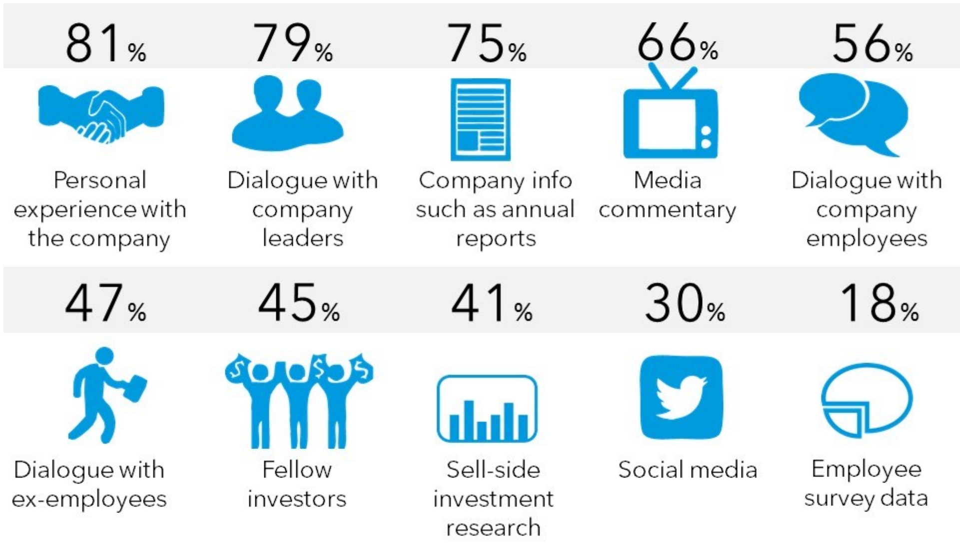
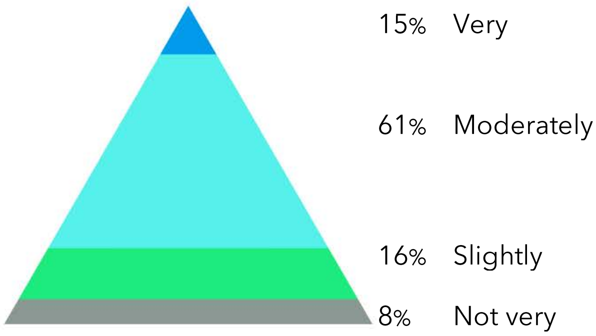


Figure 13: Confidence that info source is an accurate reflection of culture



An average **5.9** information sources used by those rating **culture as quite or very important**, just **4.4** by those who **consider it less important**

Figure 14: Confidence in information grows with perceived importance of culture

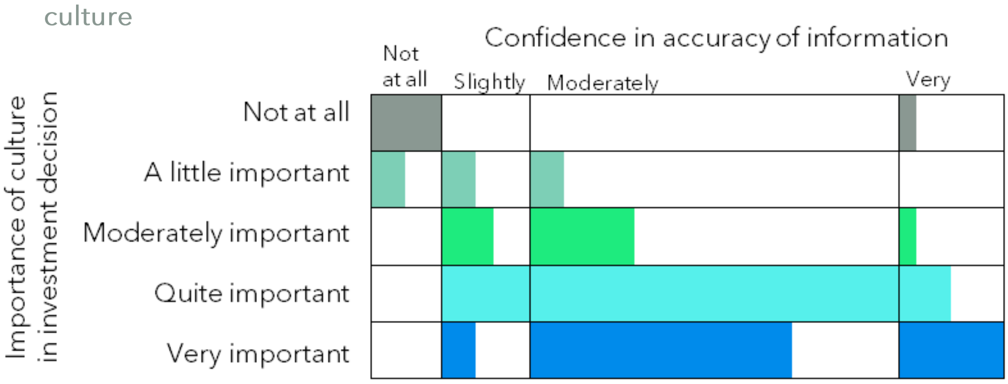
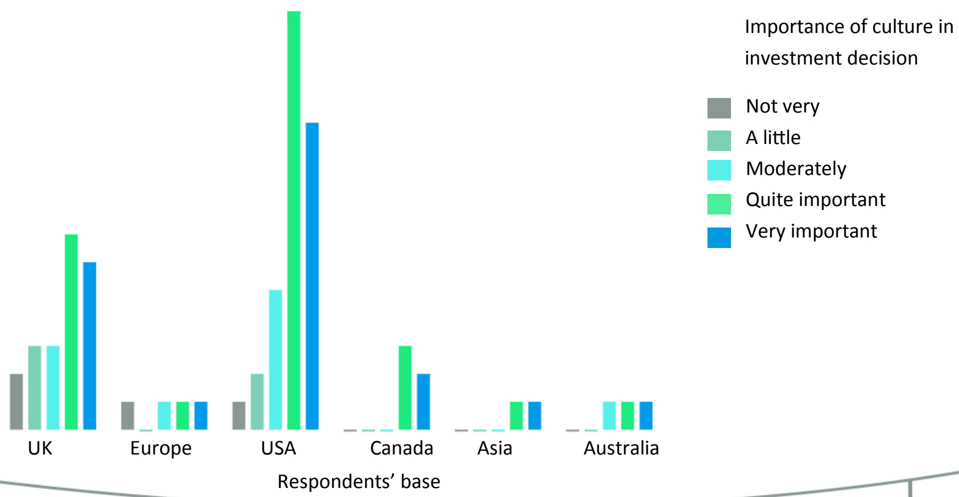


Figure 15: Importance of culture by regional profile of respondent



3. Research Insights

Culture is impacting the way some respondents value organisations.

Culture is firmly on our respondents' agenda, with most believing that culture will impact future performance and are factoring this into their views of company valuation.

94% of respondents reported that culture plays an important part in their investment decisions, with over 70% indicating that it is either quite or very important in their investment process. Only 6% of respondents indicated that culture played no part in their investment decisions.

Of those respondents who considered culture as being important, 66% recalled at least one case where culture had significantly affected a company's valuation, either positively or negatively.

We can conclude therefore, that there is a link between personal experience of the impact of culture, and future investment decisions.

"There's a scale to it… but do we ever place zero weight on culture? The answer to that is no."

There is a high level of agreement around the cultural attributes that increase the risk of poor performance.

Despite little evidence of debate around cultural attributes within the investment industry there was a high degree of consistency amongst respondents as to the cultural factors which can increase the risk profile of an organisation and impact a company's long-term prospects and performance. These included:

- High levels of bureaucracy
- An unexpected change of leadership
- Evidence of bribery and fraud
- Discouragement of internal discourse and upward feedback
- High levels of staff turnover
- A focus on results 'at any cost'
- Arrogance
- Aggressiveness
- An overbearing/ forceful CEO
- Short termism

Through Walking the Talk's consultancy and research work on culture we see these factors parallel many of the common cultural challenges executives know exist and are seeking to overcome.

How strong these factors are, and how determined management is to deal with them varies considerably from organisation to organisation and it's these distinctions that respondents are seeking to identify.

Respondents recognise that culture must be fit for purpose.

Respondents do not believe that there is a universally 'good' or 'bad' 'type' of culture. Rather, they are interested in the appropriateness and suitability of the organisation's

"If you look at a mission statement and see words like, 'creative' or 'fostering entrepreneurship', and then you walk into that organisation and you see no-one talking to each other and big offices for the senior level management and small offices and down to cubicles… that's not a shared culture."

Culture is not engagement

Imagine two teams about to play a match, both are motivated and happy to be playing. On the pitch, one plays a defensive game, the other offensive, yet both are equally engaged in the moment. With culture we are concerned with what they did and why they did it – the behaviours, not how they felt whilst they were playing, that's engagement. Understanding how to affect culture allows you to adapt your game to win.

Culture is the pattern of behaviours that are encouraged, discouraged or tolerated, by people and systems over time.

"When we meet companies … our job, is to try to decipher if what we've been told is realistically what's happening as opposed to just this story."

culture relative to its strategy.

For example, a culture that is highly tolerant (and perhaps even encouraging) of mistakes and risk-taking may be considered a strength in a high-tech firm that relies on cutting-edge products to maintain profitability, but may be detrimental to more conservative organisations like banks or insurance providers.

Whilst there is no universally good or bad culture, the most common positive attributes that emerged from the research were:

- Transparency
- Honesty
- Openness
- Simplicity
- Integrity
- Customer-focus

Walking the Talk's experience suggests that organisations who are investing in culture are investing in these areas, in particular we observe customer focus and simplicity emerging as global trends.

We find most organisations have words similar to these in their value statements. So there is alignment, at least on paper, on what is important. The questions remain, however, how to tell whether these organisations are walking their talk, and importantly, whether they will do so in the future?

Respondents are looking at a range of cultural factors to make valuation decisions.

The more familiar a respondent is with the concept of culture the more likely they are to use it as an influencing factor in their investment decisions.

But familiarity with what?

Whilst over 60% of our respondents reported to be quite or very familiar with culture, a diverse range of definitions of culture emerged. 'Values', 'behaviours' and 'beliefs' were the three most common words used to define culture.

Amongst those we interviewed, some did confuse engagement with culture, a mistake we find in organisations.

Imagine if professional investors had such a wide range of definitions of the term 'profit'?

In the investment industry, the lack of a clear definition means that effort to assess culture is dispersed and the industry will be less effective at acting collectively to put pressure on organisations to improve their culture and the ways by which they report on culture.

No common systematic method for assessing culture exists in the investment community.

Respondents find culture difficult to assess. Compared to other investment criteria they see it as "…the hardest thing to ascertain." Many investors assess culture via "gut instinct" or "intuition", with one interviewee stating "I do it with my grey hairs!"

Some respondents are devising approaches to culture assessment which may provide a more accurate measure of culture. Some are using a triangulation approach to counteract bias. Here they use two or more sources of information to confirm a particular opinion or idea on an organisation's culture.

The more important a respondent deems culture, the more sources of information, on average, they use to assess it. Respondents who rated culture as quite or very important used 5.9 sources on average to assess it, while those who considered it less important used 4.4 sources for the same purpose.

Some respondents seek former employees to talk to, others walk around the organisation observing what actually goes on. The physical office space was described by several people we interviewed as reflective of culture and some utilised organisational surveys.

The range of factors a respondent may choose to include in building their view of company valuation is broad, with all possible public displays of culture utilised.

Professional investors are looking for consistency.

Some respondents are interested in assessing the consistency of an organisation's culture across its levels of hierarchy (both vertically and laterally). They seek consistency of alignment between management and employees and flowing from vision to application.

This alignment in an organisation implies to respondents better communication, greater buy-in, greater cohesion and probably better performance.

When organisations walk their talk they build trust with professional investors as well as inside their organisation.

Leader behaviour impacts upon the view of company valuation.

The CEO and Executive style of leadership heavily influences respondents' perceptions of an organisation's culture. Leadership behaviours are seen as a proxy for culture.

More widely, many of the top sources of information used to assess culture, such as the company report or media commentary, are also those which are likely to be the most influenced or controlled by Senior Executives.

As succinctly put by one of our respondents, "culture emanates from the top."

Respondents who want to understand a company's culture place great emphasis on meeting the senior leadership of the companies they want to invest in. They listen to what is being said, try to determine whether they can trust it and look wherever possible for indicators of whether executives' behaviour aligns to their words.

"If the CEO is taking economy flights everywhere, then presumably everybody else is taking economy and you tell me that the company has a cost-cutting culture, I go, 'yep, I believe it'."

"Everybody's focused on that same end and they all kind of eat and breathe the same story and that's important to us, that it filters down through the organisation, that it's not just a management vision but it's a corporate vision."

4. Recommendations

"If it's an autocratic system, you will get the sense in the meeting where the CEO is giving all the answers and the others just sit there and are deferential to him. So those are kind of the subtle things that you can pick up."

For CEOs & Executives

This research provides an opportunity for those who consider their culture an asset and a warning to those that do not. Those who do not know what their culture is and how it either enhances or detracts from their strategy should start to pay attention, because the people that are valuing your company are, and their expectations in this space will only grow.

Be evidence-based. Professional investors are assessing culture and if you have strong evidence that your culture should be a factor which encourages investment, objectively showcasing this evidence will be key. Those organisations who are skilled at measuring and managing their culture have an opportunity to lead and influence the investment community around how they assess culture from a distance and to champion more rigorous evaluation processes.

If, on the other hand, you know that a deep dive analysis of your culture would result in an unfavourable reading, take heed. In our opinion, it is only a matter of time before investors improve their ability to assess culture. The more experiences they accumulate of culture negatively or positively impacting an organisation they are invested in, the more they will improve their evaluation techniques. This should act as a trigger for you to increase your determination to improve your culture.

Walk your talk. Professional investor assessment of your culture is often centred around the experience with a few key people, namely the leadership, in your organisation. The alignment between their walk and their talk is key. Respondents are looking for consistency so the more that the experience they have of your organisation matches the rhetoric, the more comfortable they are that the espoused culture occurs in reality.

"What culture provides that other sources of information do not is confidence... if I know that a company is going to behave ethically all the time and is going to make the right decisions then I am a little bit more confident in placing my investment."

For example, if empowerment is key, does the CEO let others talk and contribute; if learning is key, do the team discuss how the organisation has recently learnt from a mistake or has tried something new?

For Human Resources

You need to strive for consistency at all levels. Remember, professional investors are getting more sophisticated. They are finding ways to access your broader employee base and test the consistency of your organisation's rhetoric.

Your focus on culture therefore must extend beyond the leadership into the broader business and must be focussed at a behavioural level for culture to be a positive value adding asset.

Final thought

It was Peter Drucker who said "Culture eats strategy for breakfast" and ***Walking** the **Talk*** firmly believe that the future performance of an organisation is rooted deeply in the culture of that organisation and that culture is, therefore, directly associated with business value. This research has shown that a significant percentage of the investment community share this view.

We hope that this report sparks debate in the investment community and motivates increased focus in organisations.

If this occurs, the business community will move closer to Walking the Talk's vision that every organisation has a thriving culture – an outcome which will benefit every stakeholder.

"We have a person who their only task is to contact ex-employees. Conducting an interview with them helps us understand the culture. What were the things they liked about the firm they left and what are the things they did not like."

"Hearing a simple, clear message from many different folks in an organisation can indicate a shared vision or dream for a business which makes it easier for folks to focus on doing their best work."

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Thanks

STAMFORD ASSOCIATES

Stamford Associates is a leading independent investment consultant, providing investment advice to institutional investors and wealth management firms.

Walking the Talk are culture transformation experts. We deliver better business performance by aligning your cultural priorities with your strategic priorities.

We make culture do-able.

Our approach is designed to be:

- **Do-able**, with proven and understandable methodology and easy to use tools that make culture design, transformation and management do-able, giving you an aligned business.
- **Do-able by you**, we work with you to build culture management competency within your business, leaving your organisation stronger and giving you a powerful business management tool.
- **Self-perpetuating** the process is empowering, inspirational and brings confidence, enabling consistent business results. This means the process can weather the changes brought by changes to senior people or strategy

Our vision is for every organisation in the world to have a thriving culture and we can only achieve that by building culture capability across the globe.