

Annual Reports: Inside the corporate

June 2013



Background

- ◆ Five companies and sectors in 15 years
 - Engineering: TI Group PLC
 - Transport: Exel plc
 - Chemicals: ICI
 - Consumer goods: Cadbury
 - Utilities: National Grid
- ◆ Five very different process and audience considerations
 - Driven by legacy – TI Group, ICI and National Grid
 - Driven by change - ICI in later years, Cadbury and Exel
- ◆ Chairman, Investor Relations Society
 - Chaired the Best Practice committee and judging panel for 4 years

What you want to know...

1. Who are the narratives mainly aimed at (financial analysts, institutional investors, retail investors, other)?
2. What sort of information are they looking for? How do you know that this is the case?
3. How soon during the financial year does thinking about the content of the annual report narratives begin? Does this vary much across firms? Could the timing be brought forward in the light of unexpected good or bad news?
4. Who are the main players involved in putting the annual report narratives together? Roughly what percentage contribution do they make to the content? How closely involved are the CEO and CFO?
5. What is the typical time line in terms of intensity of activity, and when the various parties are involved?
6. To what extent is the Chairman's statement really his/personal view, and to what extent is it the view of the Company?
7. How do firms decide what topics to cover in the narratives?
8. How does the firm decide what forward looking statements to include? Would you say this is a particularly sensitive part of the process?
9. How is the commentary on financial performance for the year put together?
10. How is the discussion of the firm's strategy and business model put together?
11. To what extent are this year's narratives determined by the previous years? Would you say that normally the process involves updating the previous years report, or would you say that you more or less start from scratch? Does this vary across firms or according to events occurring during the year?
12. How does the process change when the financial year has gone worse than expected?
13. How does the process change when the financial year has gone better than expected?
14. How does the process change if management have reasons to expect trading conditions to be much better in the next financial year/s?
15. How does the process change if management have reasons to expect trading conditions to be much worse in the next financial year/s?
16. Is there close co-ordination between the formal financial reporting process, leading to the audited financial statements, and the production of annual report narratives?

Who are the narratives mainly aimed at?

(financial analysts, institutional investors, retail investors, other)

Unclear

Considerations

- ◆ Compliance document drives certain content
- ◆ Avoid risk - maximise disclosure as required
- ◆ Professional investors and analysts only look at specific sections
- ◆ Retail investors drive simplified language, narratives and style

**What sort of information are they looking for?
How do you know that this is the case?**

Not relevant

Considerations

- ◆ We're told what to provide even if its of little value or not timely
- ◆ Other documents published during the year provide much more focused and relevant content

When does thinking about the annual report begin?

Does this vary much across firms? Could the timing be brought forward in the light of unexpected good or bad news?

Too soon

Considerations

- ◆ Processes can start 7-8 months before the end of the year and 8-9 months before publication
- ◆ Can be as short as 4-5 months
- ◆ Many companies make this a complicate process
- ◆ Many items written or started preparation before events and outcomes decided
- ◆ Longer the process the more resources consumed, too many opinions sought and generally less effective the product

Who are the main players involved in putting the annual report narratives together?

Roughly what percentage contribution do they make to the content? How closely involved are the CEO and CFO?

Some bits are always clear...

- ◆ Remuneration report : Compensation and benefits
- ◆ Technical aspects of financial review: Financial Control, Treasury, etc
- ◆ Directors report : Company Secretarial

Others vary considerably...

- ◆ Finance, Investor Relations, Corporate Affairs, Company Secretarial, divisional leadership
- ◆ Rarely 'originated' by CEO, CFO or Chairman, but occasionally edited

What is the typical time line in terms of intensity of activity, and when the various parties are involved?

Depends...

- ◆ On whether or not the design and content is reinvented every year
- ◆ On who wants to be involved
- ◆ On the number of people involved

Typical milestones...

- ◆ Christmas vacation for senior management to read some content
- ◆ Linkages to year end results reporting processes
- ◆ Consistent strategy in the business against which KPIs, in year priorities and narratives are developed

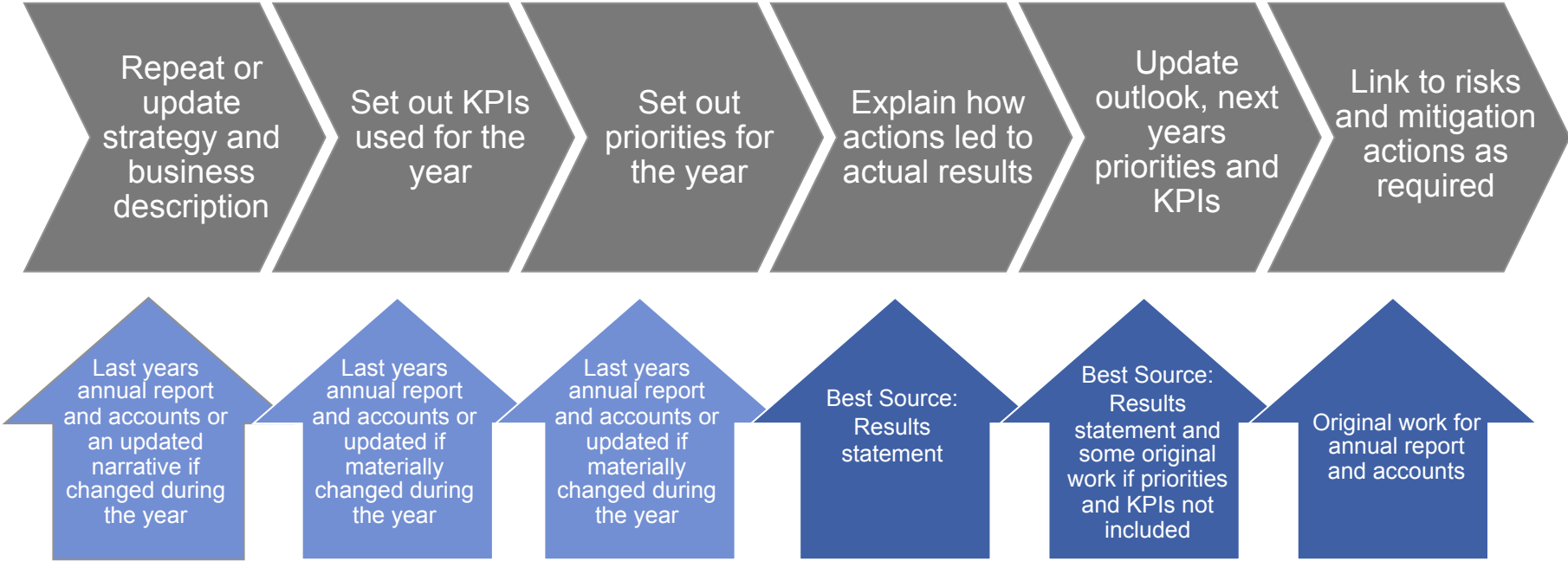
Where should the content of an annual report come from?

Content led

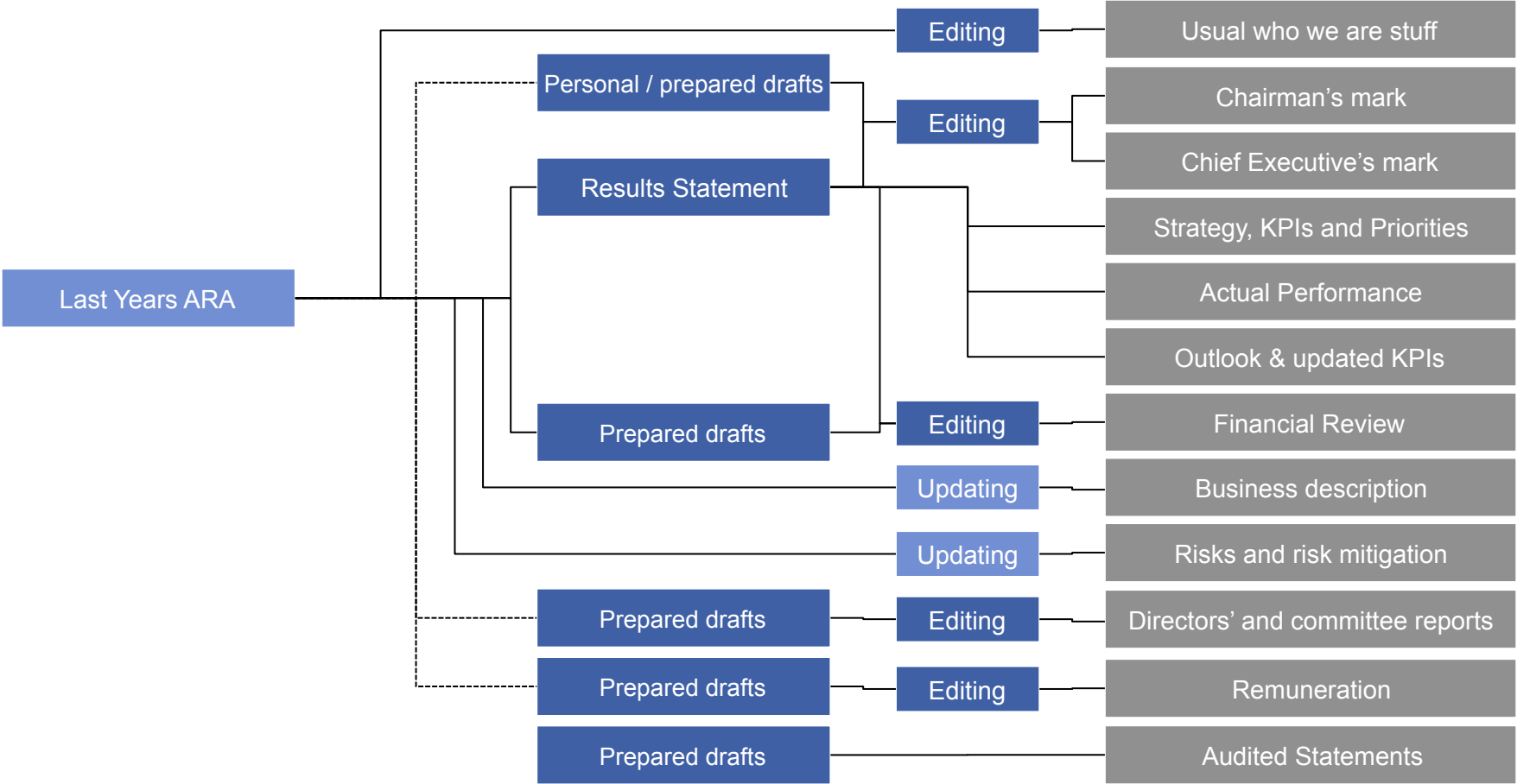


- ◆ Most of the framework would have been dictated the year before when priorities, KPIs and outlook were first discussed

How would this content integrate with other sources?



Bringing this together, what are the best sources and timelines for an ARA?



Various questions 6-11

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Varies but it's likely to be drafted for him/her and consistent with company disclosure style

Varies – typically follows materiality & disclosure considerations

Reputation & relevance : need to ensure adequate guidance is provided – significantly sensitive

Investor Relations typically write this based on knowledge / management reports, with input from others

Investor Relations updates or writes new disclosures – sometimes done by Strategy or Finance

Varies - in the best Annual Reports, where there is a well communicated strategy, priorities and performance, core parts should only be updated as required by major changes - as a result using last years report is very sensible and consistent from others

Overall Editorial Owner

- ◆ Corporate Affairs

Budget

- ◆ High

Number of people involved: 30

Process

Level of Chairman supervision	8/10
Level of Board supervision	6/10
Written/edited by IR	2/10
Written/edited by Corporate Affairs	7/10
Written/edited by Legal/Secretarial	5/10
Written/edited by Finance	7/10
Written/edited by Businesses	5/10

Results

Consistency with Preliminary Results	3/10
Consistency with Investor messaging	5/10
Strategic integration	2/10
Risk aversion in content	6/10

Other considerations

Print run: 45,000

Review: none

Web-site: Early HTML and PDF

Overall Editorial Owner

- ◆ Investor Relations

Budget

- ◆ Medium

Number of people involved: 16

Process

Level of Chairman supervision	1/10
Level of Board supervision	6/10
Written/edited by IR	9/10
Written/edited by Corporate Affairs	4/10
Written/edited by Legal/Secretarial	1/10
Written/edited by Finance	5/10
Written/edited by Businesses	1/10

Results

Consistency with Preliminary Results	9/10
Consistency with Investor messaging	9/10
Strategic integration	9/10
Risk aversion in content	6/10

Other considerations

Print run: 20,000

Review: Yes but focused on broader stakeholders

Web-site: Early HTML and PDF

Overall Editorial Owner

- ◆ Investor Relations

Budget

- ◆ Low

Number of people involved: 20

Process

Level of Chairman supervision	2/10
Level of Board supervision	8/10
Written/edited by IR	7/10
Written/edited by Corporate Affairs	4/10
Written/edited by Legal/Secretarial	1/10
Written/edited by Finance	7/10
Written/edited by Businesses	2/10

Results

Consistency with Preliminary Results	9/10
Consistency with Investor messaging	9/10
Strategic integration	8/10
Risk aversion in content	8/10

Other considerations

Print run: 10,000

Review: Yes in final year approx. 100,000

Web-site: PDF

Overall Editorial Owner

- ◆ Investor Relations

Budget

- ◆ Medium

Number of people involved: 14

Process

Level of Chairman supervision	3/10
Level of Board supervision	7/10
Written/edited by IR	9/10
Written/edited by Corporate Affairs	1/10
Written/edited by Legal/Secretarial	2/10
Written/edited by Finance	4/10
Written/edited by Businesses	3/10

Results

Consistency with Preliminary Results	10/10
Consistency with Investor messaging	10/10
Strategic integration	10/10
Risk aversion in content	8/10

Other considerations

Print run: 20,000
Review: Yes aka “Treat”
Web-site: HTML microsite

National Grid

Overall Editorial Owner

- ◆ Company Secretarial

Budget

- ◆ High (very)

Number of people involved: 40

Process

Level of Chairman supervision	4/10
Level of Board supervision	8/10
Written/edited by IR	1/10
Written/edited by Corporate Affairs	3/10
Written/edited by Legal/Secretarial	7/10
Written/edited by Finance	6/10
Written/edited by Businesses	5/10

Results

Consistency with Preliminary Results	6/10
Consistency with Investor messaging	2/10
Strategic integration	3/10
Risk aversion in content	9/10

Other considerations

Print run: 20,000

Review: Yes – over 1.3m shareholders

Web-site: full HTML

Final Question: Is there close co-ordination between the formal financial reporting process, leading to the audited financial statements, and the production of annual report narratives?

There should be...

...but sometimes there isn't

Considerations

- ◆ If the company uses its results statement consistently as a source for all materials and nuances then there should be, after all the results statement are very heavily scrutinised
- ◆ But some drafting gets well ahead of itself and becomes locked down and limits willingness to properly edit
- ◆ In many cases this does not matter, as no material errors will creep in, but it can reduce the value of the ARA as a proper document of record

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Thank You