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A foot in the past and an eye to the future

The importance of forward-looking information in company reporting

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"Annual shareholder letters and other communications to shareholders are too often backwards-looking and don't do enough to articulate management's vision and plans for the future. This perspective on the future, however, is what investors and all stakeholders truly need, including, for example, how the company is navigating the competitive landscape, how it is innovating, how it is adapting to technological disruption or geopolitical events, where it is investing and how it is developing its talent. As part of this effort, companies should work to develop financial metrics, suitable for each company and industry, that support a framework for long-term growth. Components of long-term compensation should be linked to these metrics."

Larry Fink, Chairman and CEO, BlackRock

Introduction

The past decade has seen companies make positive strides in the provision of forward-looking information in their reporting. The large majority of UK companies now include some form of forward-looking information in their annual reports and preliminary presentations.

Yet there is clearly more that needs to be done. Investors' calls for greater and more meaningful forward-looking information are getting louder, short-termism is being criticised by wider stakeholder groups, and guidance from regulators is more pronounced. The calls for longer-term investment now come from many quarters and companies need to respond. Company reporting, whilst not the only solution, will play a pivotal role in addressing these criticisms and confronting the challenges today's companies face.

We first examined forward-looking information in company reporting 10 years ago. The picture then was mixed; while companies were moving in the right direction, the information they provided often left more questions than answers.

Today, the picture is encouraging with for example more companies providing forward-looking market data, but some of the old concerns remain.

This report is intended to be a practical and hands-on guide to what we consider good practice. In it we highlight some of the recent findings from our 2016 survey, *Redefining business success in a changing world: Global survey of investor and CEO views*, draw upon a review of 52 FTSE 350 annual reports, offer our own recommendations for good practice – what we call the eight principles of forward-looking information, and include some good examples from UK annual reports.

The future and how it is reported really does matter.

Contents

Executive summary

Companies are under scrutiny like never before over what is perceived to be an undue focus on short-term profits at the expense of longer-term societal benefit and value creation. This is manifesting itself in pressure from governments, investors and other stakeholders on companies and the way they behave, where they invest and how they report.

Increasing stakeholder demands

In the last few weeks the UK government's Business, Innovation, and Skills (BIS) Committee launched an inquiry on corporate governance that focuses, amongst other things, on whether the duty of directors to promote the long-term success of their company is clear and enforceable, and how executive pay takes account of long-term performance.

In 2015, BlackRock Chairman and CEO, Larry Fink, wrote to the CEOs at all S&P 500 companies and large European organisations to challenge the short-termism seen in corporate reporting. In that letter he implored companies to "lay out for shareholders each year a strategic framework for long-term value creation". He said that communications to shareholders are "all too often backwards-looking" and "don't do enough to articulate management's vision and plans for the future".

His views are echoed elsewhere. The Investment Association, whose members manage more that £5.5 trillion, published its Productivity Action Plan in 2016 – a framework for considering the barriers to long-term investment. In it, the Investment Association called for a raft of measures, including enhanced company reporting and the need to focus on long-term value creation and productivity. It argues that quarterly reporting encourages a short-term view and lacks a focus on productivity. It was warmly received.

Strategic reporting requirements (the clue is in the title) in the UK and the introduction in 2014 of viability statements provide a foundation for companies to present a more forward-looking perspective. The Financial Reporting Council's *Guidance on the Strategic Report* may only mention forward-looking information twice, but its message is unequivocal; reporting should "be fair, balanced and understandable; be concise; have forward-looking orientation".

A mixed picture

Our research highlights that companies are responding and providing more forward-looking information – in the way they discuss market trends, outline strategic plans or define a longer-term purpose that takes into account a wider societal impact – than ever before. But, it also shows there are still a significant number of companies who don't look beyond the next year in their reporting. Or, when they do, there is often a lack of consistency in how the future is described and a lack of balance and meaningful information to provide investors and other stakeholders with a real perspective on the future for the company. The result? In most case, it raises more questions than answers.

Underlying conservatism

Companies, in short, could do a better job of explaining why their prospects are good and why their strategy makes sense. However, management reluctance is perhaps understandable. It is typically rooted in the belief that investors are only interested in short-term returns and that any forward-looking information would be seen as a prediction or target that, if not met, will have a negative impact on the market's confidence in the management team.

This perception is echoed in a 2013 McKinsey Quarterly survey which spoke to c.1000 board members and C-suite executives globally to assess progress in taking a longer-term approach to running their companies. McKinsey found that 44% used a time horizon of less than three years when setting strategy. More telling though was that 73% said that they should be focusing on a time horizon of more than three years – the difference blamed on the sole focus of short-term results undermining the ability of companies to invest (and grow). The safer and more cautious option, hiding behind the competitive sensitivity excuse, is all too often the compromise.

> *"Lay out for shareholders each year a strategic framework for long-term value creation."*
>
> **Larry Fink**, BlackRock Chairman and CEO

Future looks rosy

The debate between company management and investors over greater levels of forward-looking information will become more pronounced as our world becomes ever more complex and the demands for a long-term perspective intensify. There will be many obstacles to overcome, from the quality of information to the way preparers and users behave towards forward-looking information. But our work with investors and corporates means we remain encouraged that the future as it's represented in reporting looks rosy.

In 2016, we published our annual survey of global CEOs and investment professionals. The report, *Redefining business success in a changing world,* highlights that:

- investment professionals often talk about company purpose with a long-term perspective, highlighting the importance of companies finding a way to demonstrate both short-term profitability and their ability to create long-term, sustainable value.
- 70% of CEOs and 60% of investment professionals believe that in the 21st century business success will be redefined by more than just financial profit.

The future matters more today than ever before. The foundations of a company's strategic reporting rest not just on where the company has come from and how it is performing, but on where it is heading. We would argue that by having a clear, transparent, and balanced discussion along a company's entire strategic journey, users will gain a more detailed understanding of the desired destination and appreciate the obstacles and successes along the way.

Practical recommendations

This report is intended for practical use – providing senior management teams with a hands-on guide to what we see as the current/emerging trends in reporting and to consider good practice. Our recommendations are based on the premise that strong reporting with a clear view of the future demonstrates leadership, confidence and commitment, and are represented in our eight principles of forward-looking information:

1 *Explore future markets*

2 *Set out strategic direction*

3 *Keep the business model dynamic*

4 *Articulate resources and relationships*

5 *Identify lead indicators of performance*

6 *Explain future risks and opportunities*

7 *Be clear on financial prospects*

8 *Be consistent*

You can find more information on our eight principles on page 11.

Back to the future

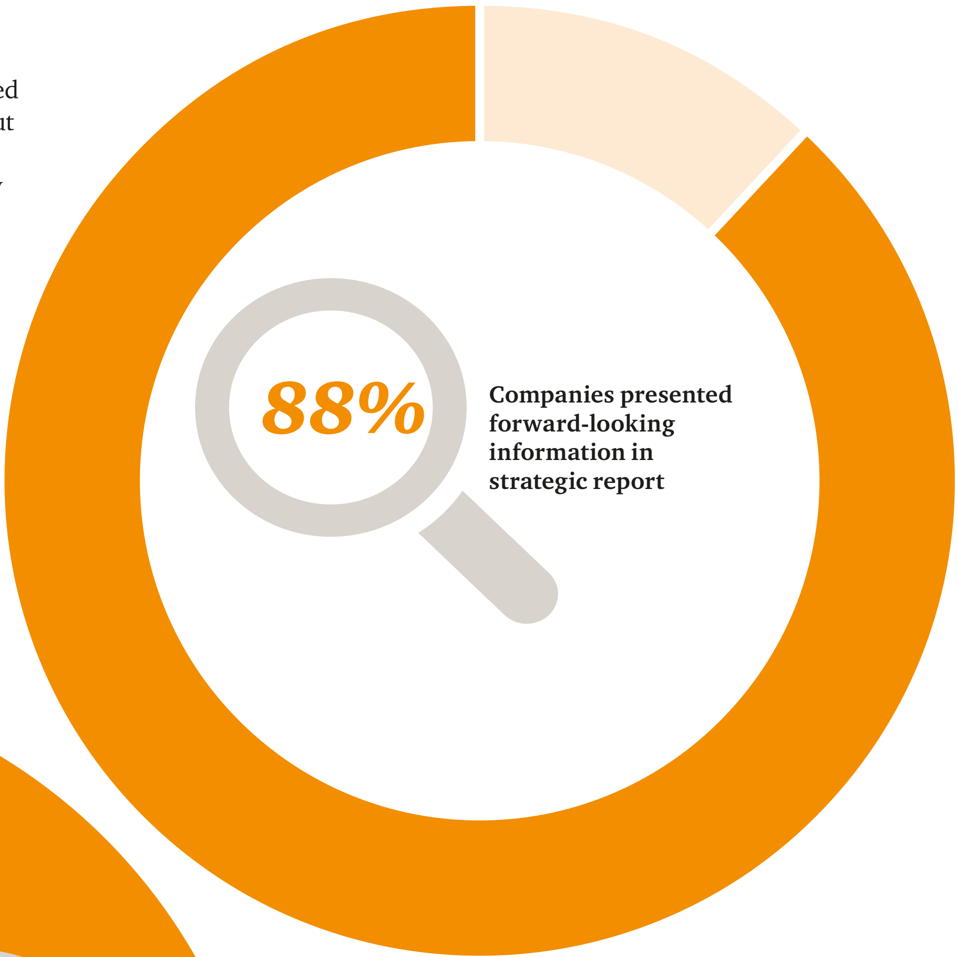
Current trends and practices

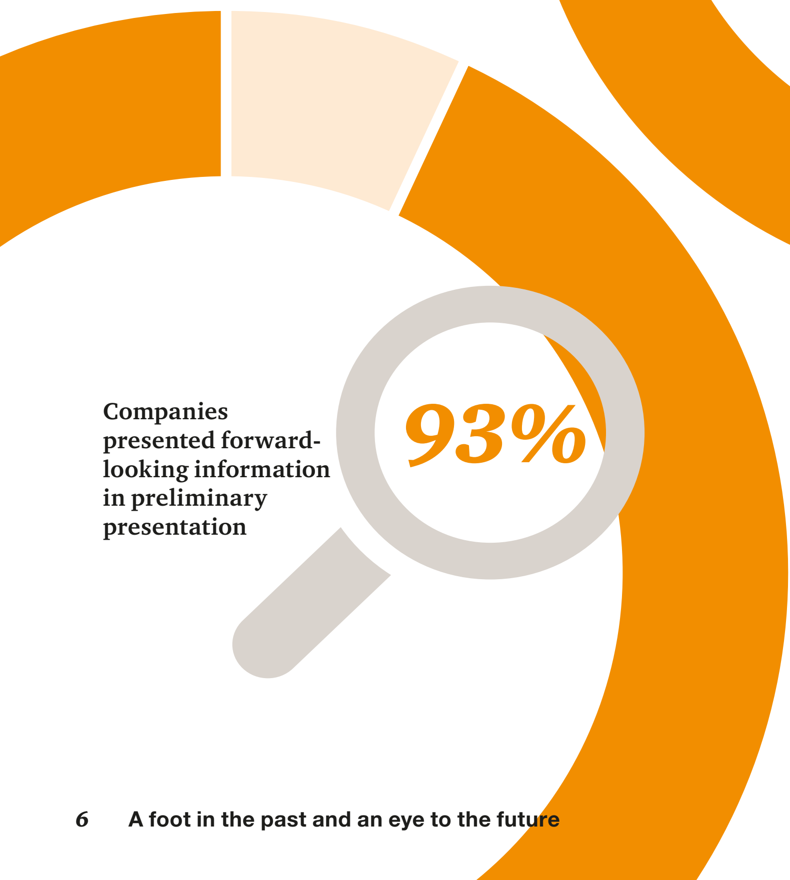
In 2016 we conducted a review of the strategic reports of 52 companies with December 2015 financial year ends from the FTSE 350, looking for any aspects of their reporting that addressed a specific period beyond the current reporting period. In this case, for example, beyond 2016.

We used the strategic report as the primary source, but have also examined preliminary results presentations to put together a picture of how consistent companies are in where and what they say about the future.

Extent and consistency

It is encouraging to see so many companies providing some elements of forward-looking information in their strategic reports (88%) and in preliminary results presentations (93%), however the quality and consistency of this information is not always what investors want. For example, we have seen cases where a strategic report has a clear three-year strategy yet it is not referenced in the preliminary presentation, and another where explicit financial targets have been highlighted in the preliminary presentation but not used in the strategic report. These type of inconsistencies can raise questions about both the quality and validity of information being presented, and management's effectiveness at setting clear strategic priorities.





Types of forward-looking information provided

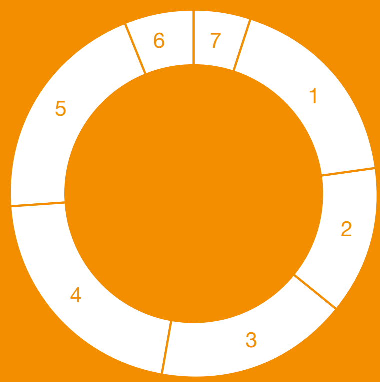
Our review suggests that companies provide a wide range of forward-looking information in their reporting across their different communication channels but that the types of information provided can vary between these.

Strategic reports will typically include forward-looking information in the context of disclosures around corporate social responsibility and financial information/debt maturities. A number of companies are also providing a clear perspective on future market trends, however all of these aspects tend to sit as isolated bits of information within the report and are arguably all areas where company confidence in presenting a forward-looking perspective is at its highest.

Forward-looking financial information is most prominent in preliminary presentations, where companies are speaking directly to an audience of investors and analysts looking for insights and clarity.

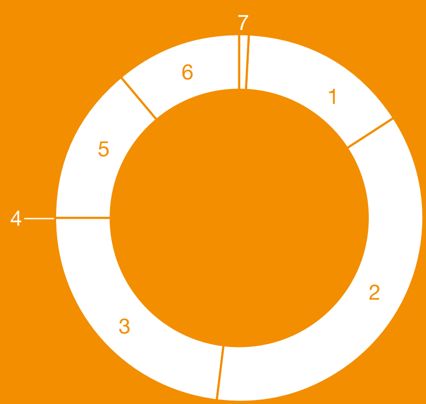
A common misconception is that prelims only focus on getting the financial results out to the market as quickly as possible. Our research dispels this view showing that a number of companies provide strategic insights in their preliminary presentations – perhaps an encouraging sign that companies are no longer just communicating results at this time, but instead taking the opportunity to talk more about the future.

Scope of forward-looking information in strategic reports



1. Debt maturities	**18%**
2. Other financial	**13%**
3. Strategic	**17%**
4. CSR	**21%**
5. Markets	**20%**
6. Orders/Pipeline	**6%**
7. Other	**5%**

Scope of forward-looking information provided in preliminary presentations



1. Debt maturities	**15%**
2. Other financial	**36%**
3. Strategic	**23%**
4. CSR	**0%**
5. Markets	**14%**
6. Orders/Pipeline	**11%**
7. Other	**1%**

Period of forward-looking information

There is a clear inconsistency in the timeframes companies choose to report forward-looking information in their strategic reports and preliminary presentations, and only a small number of companies are prepared to assign clear timeframes to strategic information. Whilst it may be expected that different periods of forward-looking information may make sense for different industry groups or information categories, surprisingly we haven't identified any clear trends of specific industries reporting over the same periods of time – making comparisons difficult.

Of the 52 companies included in this analysis, less than a third provided clear timelines beyond the current period for strategic information in their reports with marginally more doing so in their preliminary presentations. We conclude that for most companies their strategic statements are just focused on a point in time summary rather than giving real insight into their strategic ambitions for the future. This is contrary to the spirit of the strategic report, which was introduced to encourage companies to provide more forward-focused statements.

Our research also pointed to some clear inconsistencies; 30% of the companies that provided strategic information in their strategic reports failed to provide the same information in their preliminary presentations, and a further 40% that provided that information in their preliminary presentations failed to include it in their strategic reports.

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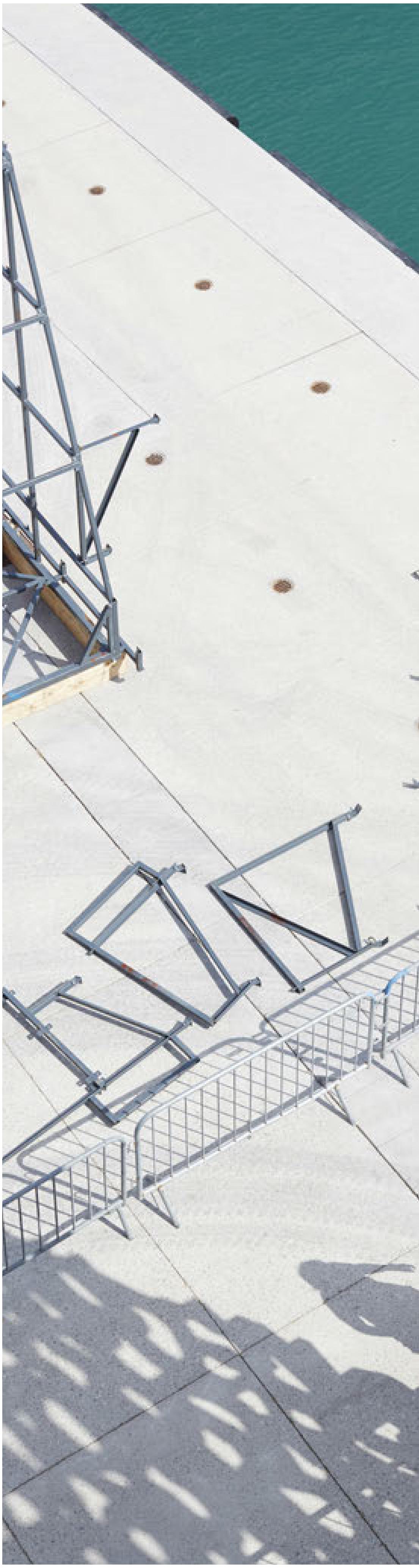
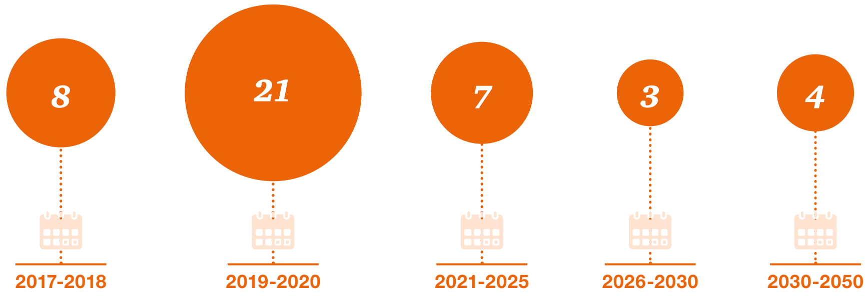
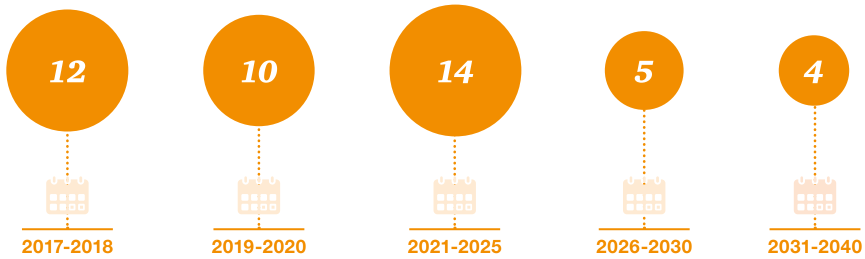


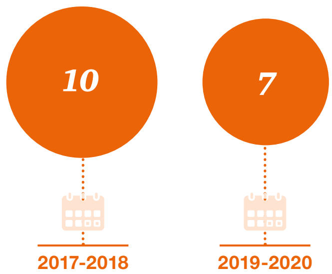
Period of forward-looking information provided by companies in their Strategic report.



Period of forward-looking information provided by companies in their Preliminary Presentation.



Period of forward-looking information provided by companies in their Strategic report for strategy insights.



Period of forward-looking information provided by companies in Preliminary Presentation for strategy insights.

Viability period consistency

The introduction of the viability statement has, for the first time, created an impetus for companies to disclose the period over which they plan and consider the risks to the business. This has made it easier to identify inconsistencies in the messages conveyed or the periods disclosed and significantly, where planning periods do not necessarily match the nature of the business.

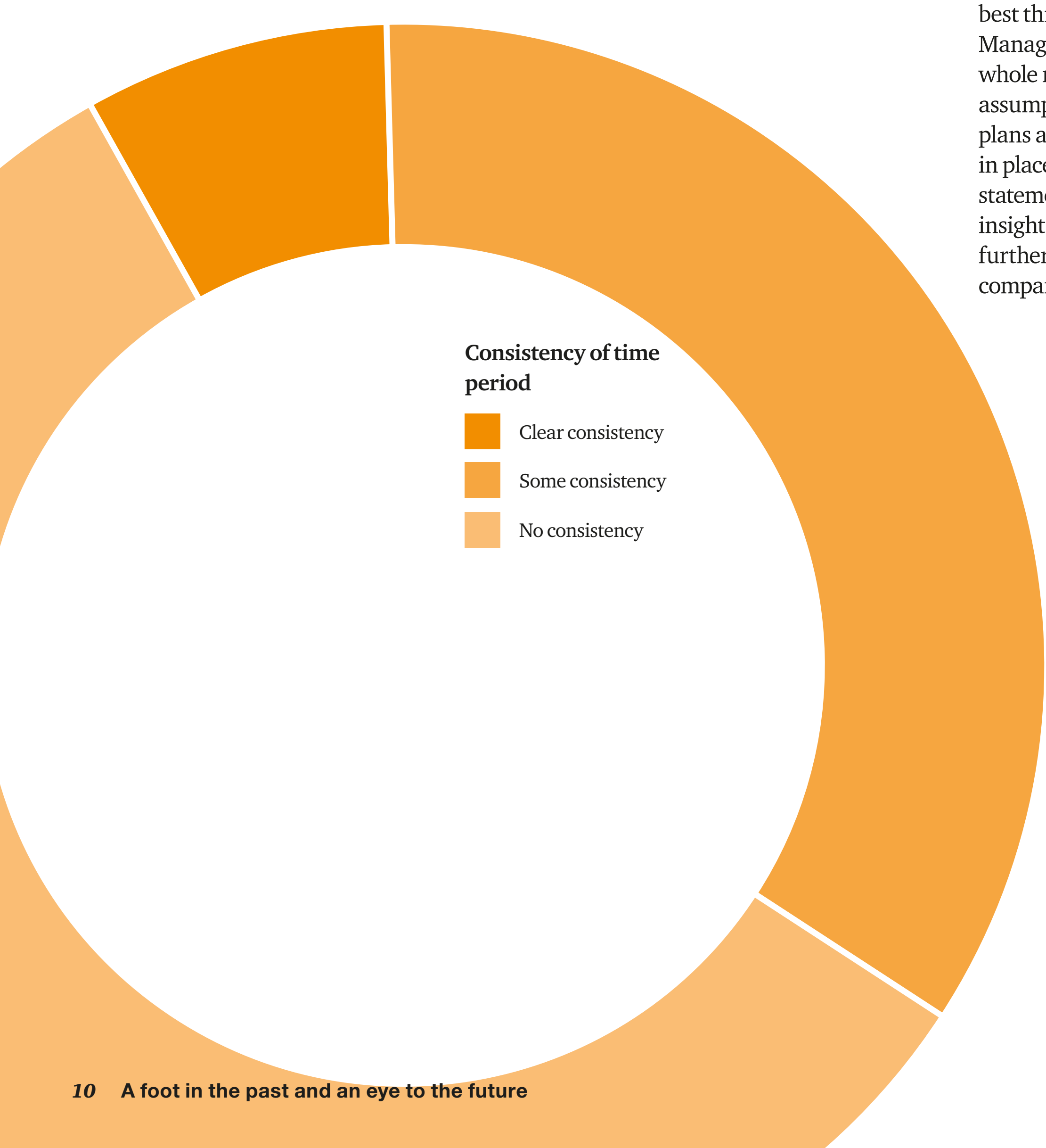
It also provides an impetus to bridge the reporting gap and to provide a clearer explanation of why other elements of reporting, for example strategic messaging, key risks and the business model, are positioned the way they are by the company.

Unfortunately, in the first year of the requirements, few companies have taken this opportunity and have attempted to demonstrate a linkage between their new viability statement and the front end of the report. We expect this to be a key area of investor interest going forwards. Management should therefore consider their response to questions such as: What are the milestones in your strategy? Do you assess your risks over the same period? Why is your viability period different from your peers?

Our analysis across the FTSE 350 shows that three to five years has quickly emerged as the default for most companies, whether in fast moving sectors or those with major long-term capital programmes. This is understandable, given the nature of the formal viability statement – where a company demonstrates its ability to meet liabilities as they fall due over the relevant period and the accompanying need for supporting detailed and robust financial forecasts.

It does, however, mean that the real value lies in the disclosures generated around the viability assessment rather than the formal statement of period. And it's here that care needs to be taken with the consistency of what's being said in the annual report. What was the rationale for selecting your specific viability period? Without an explanation investors may make their own assumptions for modelling. Be clear on why the decision was made and then be transparent about how this links to other disclosures made through the narrative. A five year viability period can be confusing for a company that only states a strategic plan for the year ahead with no other explanation provided.

We have seen a number of viability disclosures that focus mostly on process. This is fine if the process is specific, insightful and aligned to other messages, but this hasn't been the case, meaning at best this is a missed opportunity. Management teams and boards make a whole range of judgments and assumptions in arriving at their business plans and the risk management processes in place. A truly valuable viability statement disclosure will provide further insight into those judgments, providing further confidence about how the company is using its investors' funds.



The eight principles of forward-looking information

Through our work with prepares and users we have identified eight key principles of reporting that if addressed, will ensure companies provide a stronger forward-looking orientation to their reporting and encourage users to take a longer-term view of their business. These are outlined below and explored in more depth through the rest of this guide. Each principle is supported by good practice examples demonstrating how other companies are giving more insight into their future.

1

Explore future markets

Use a wide range of data sources to clearly present the market factors that support the strategic plan and put the business model, strategy and risks into context.

2

Set out strategic direction

Demonstrate strategic thinking that looks beyond the next financial year. Reference timeframes and milestones, as well as clearly articulating the strategy in the context of the company's longer-term purpose and impact on its key stakeholders.

3

Keep the business model dynamic

Business models have changed dramatically and face ever increasing disruption. Demonstrate how the company is driving change and how the business model is expected to evolve and remain resilient.

4

Articulate resources and relationships

Clearly articulate the tangible and intangible resources and relationships relied upon by the company, the risks to this reliance and how they are managed and nurtured.

5

Identify lead indicators of performance

Provide an appropriate mix of strategically relevant non-financial indicators to support the financial metrics. These can often act as lead indicators to future financial success. To be useful these should be clearly aligned to the strategic priorities and supported with an explanation of how they impact financial performance.

6

Explain future risks and opportunities

Explain the principal risks and uncertainties facing a company, the changing risk profile and how those risks are managed. Explore the opportunity each risk may also bring.

7

Be clear on financial prospects

Disclosing future prospects does not have to mean providing profit forecasts. Consider a broader range of financial and operational measures milestones and targets.

8

Be consistent

Give investors confidence by ensuring all messaging is clear and consistent within and across annual reports, preliminary presentations and all other company communications.

1

Principle one

Explore future markets

The challenge

Investors invest a lot of time forming a view on the market factors that are likely to have an impact on the future performance of a company. As part of this, they want to understand management's perspective as well. They also need a clear direction and picture of the data that management uses to help them form a view of market conditions that will support future strategic success.

Observations

Our experience has shown that most companies focus on explaining what has occurred in their marketplace in the current period as justification of this year's financial performance and support this with historical or current period trend data, and, for example, market share.

We are seeing some companies speculate more about future market opportunities and aligning this with how they will respond in the future. However, these insights do tend to be largely qualitative.

Those companies that do provide good analysis on their perception of the future market environment usually support their insights with data and some even make use of external perspectives to support their position. But these insights are rarely aligned with their business model and strategic priorities.

PwC recommends

- Show future market forecasts as well as trend data.
- Use a range of data sources that look beyond the current year.
- Support data with a discussion of key drivers.
- Demonstrate alignment of trends to both the business model and the strategic response/period.
- Discuss the strategic response to these trends.

Keir Group Annual Report 2015

Keir Group provide a comprehensive overview of the key elements of the external environment that have relevance for their future success. The overview includes clear data charts that show both prior year and future forecasts. The report also makes clear reference to a number of different sources for the data used.

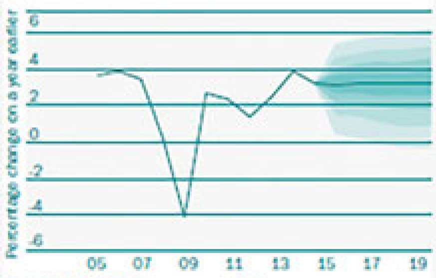
Our markets

We are operating in a generally positive market environment overall, with good pipeline visibility. The following information summarises some of the key macro-economic and market trends affecting our business and contains data and information extracted without material adjustment from publicly available information or sources.[1]

The UK currently provides a positive environment for Kier. The UK economy is growing at a consensus annual rate of 2.6% and is forecast to grow at similar rates to 2020. A new majority Government provides policy stability. Government tax revenues have risen by 25% since 2009/10. Household spending rose by 4.2% in the year to June 2015 and business investment is up by 5.7% year-on-year. The UK was the third largest country for foreign direct investment in 2014 and continues to be attractive.

Overall, the UK economy has proved resilient to the effects of recent global political and economic instability.

Real GDP growth scenarios



Sources: ONS, OBR

UK infrastructure spend has strong visibility. Infrastructure improvement is central to the UK Government's policy, as a means of creating further economic growth and to address historic under-investment. Strategic highways has confirmed spend of c.£21bn to 2021 and, within the regulated utilities, the water sector alone will see £44bn of investment to 2020. Future spend on the rail network, where £38bn of expenditure in the 2014–2019 control period had previously been announced, is now subject to a Government review.

The Budget announcement of a Roads Fund to support a second Roads Investment Strategy, plus additional planned major infrastructure schemes, such as HS2 and Crossrail2, all add to a significant long-term pipeline of opportunity.

The UK Government's austerity programme provides an opportunity to differentiate. The pace of fiscal consolidation has eased, reducing its drag on growth. The austerity programme clearly creates a challenge for our public sector clients, particularly local government, which has an obligation to provide services to the public.

Over the last five years we have worked with a number of clients to develop better use of their property assets and innovative ways of delivering services within the budgets and resources they have available.

Kier offers a breadth of capability. Our breadth means we can help clients to finance, plan, design, construct and maintain their assets, and to optimise whole-life costs. We will continue to engage with the public sector in this way.

Activity in our main international markets remains resilient to commodity market fluctuations. In the Middle East, investment is being driven by fundamental drivers, notwithstanding the fall in oil prices. These include the need to diversify their economies and create infrastructure, healthcare, schools and housing for their growing populations.

The Australian economy is forecast to grow, driven by population growth, improving Government finances, increased freight, and further expansion of the road network. The federal government is focusing on infrastructure spending, and, in particular, transport infrastructure to stimulate the 'post-resources' economy – an A$11.6bn Infrastructure Growth Package was included in the 2014 Budget.

Demographic changes are creating opportunities. In the UK, the number of people aged over 65 has increased by 17% since 2003 and is forecast to increase further. The ageing population will continue to drive expenditure on health, care services and a changing profile to residential property needs.

Almost 60% of population growth for the next 25 years is forecast to come from the net effect of more births than deaths. This population growth will create demand for more schools, universities and better social infrastructure.

At the same time social and lifestyle changes, such as the increase in single person households (5.5% growth over the last 10 years) and older people downsizing, will increase the demand for housing and change the type of housing demanded.

Total infrastructure output

Sources: ONS, Construction Products Association

[1] Sources: HM Treasury; HMRC; Office for National Statistics; UK Trade & Investment; Capital Economics; Al Arabiya/Saudi Gazette; Savills; Construction Products Association; Financial Times; Institute for Fiscal Studies; BDO; CBI.

2

Principle two

Set out strategic direction

The challenge

By definition, a company's strategy is forward-looking, providing a framework or set of objectives and goals that the company wish to achieve. Companies face the following challenges when setting out their strategic direction:

- Investors look for strategic depth and detail, whereas companies all too often focus their reporting on the here and now.
- There is a growing appreciation that companies must have a clear purpose and consider the needs and expectations of a wider group of stakeholders and the impact they have on them if they are to retain their licence to operate.
- Investors want companies to explain their understanding of market trends/developments and the actions being taken to ensure their strategy is resilient enough to respond and to exploit the opportunities.
- Adherence to regulatory requirements can make it difficult for companies to demonstrate the strategic relevance of some information included in their reporting.

Observations

BlackRock CEO and Chairman Larry Fink said in 2015 that "annual shareholder communications are too often backwards-looking and don't do enough to articulate management's vision and plans for the future". He also said that this "perspective on the future is what investors and all stakeholders truly need, including, for example, how the company is navigating the competitive landscape, how it is innovating, how it is adapting to technological disruption or geopolitical events, where it is investing and how it is developing its talent".

Our review supports this perspective and shows that only a few companies are taking the opportunity to clearly set their strategic agenda for more than the forthcoming period. We believe setting the strategic tone is essential for good reporting.

Statements all too often provide a 'point in time' position on strategy, rather than how it might evolve or too often provide multiple, siloed, or conflicting strategic priorities (corporate, financial, corporate responsibility etc.) in one report. These statements often fall short in demonstrating the quality of internal strategic thinking. Similarly, many companies set out strategy as a standalone disclosure in the report making it difficult to understand the relevance of some of the other information included or to get a complete insight into management's strategic vision.

PwC recommends

- Investors want confidence that a company is focused on the long-term journey and not just short-term gains and losses. Balance strategic depth and detail together with a clear timetable.
- Articulate the strategy in the context of the company's longer-term purpose and impact on its key stakeholders.
- Provide a clear link between the company's overall strategy and other supporting financial or corporate responsibility priorities.
- Use strategy to underpin reporting to ensure readers appreciate the strategic relevance of disclosures made. This can be done explicitly through the use of strategy symbols inserted through the report or implicitly with the clear repeated use of key strategic terms.

Micro Focus Annual Report 2016

Micro Focus provide the reader with a clear overview of their four stage strategic plan explaining the clear actions both for prior stages and for upcoming ones. The actions also indicate where investors can expect an upturn in performance and profit.

Pearson Annual Report 2015

The Pearson report provides a good example of a company looking more holistically at their strategic planning and clearly incorporate their social commitment. They are also explicit with their action plan that has targets for the period to 2025 and the alignment to wider strategic goals.

Our four phase plan

Implementation: four phase plan whilst delivering sustainable shareholder returns

Phase 1 **FY15:** Assessment ✓	Phase 2 **FY16:** Integration ✓	Phase 3 **FY17:** Stabilization	Phase 4 **FY18:** Growth
Actions:	Actions:	Actions:	Actions:
— Deliver plans for FY15	— Standardize systems	— Stabilize top line	— Top line growth
— Detailed review of combined businesses	— Rationalize properties	— Improve GTM productivity	— Standardize systems
— Invigorate Product Management	— Rationalize legal entities	— Growth from new areas	— Rationalize legal entities
	— New Go to Market ("GTM") model	— Improved profitability	
	— Maintain/improve cash conversion	— Standardize systems	
	— Rationalize underperforming elements	— Rationalize legal entities	
	— New market initiatives		

The Plan

By 2025, Pearson commits to empower the lives of 200 million learners annually, more than doubling our current reach and doing it through the delivery of more effective products and services.

	Access	Success	Progress
Our goals To meet our commitment to empower the lives of 200 million learners annually, we have set three goals.	Enhance access to high quality education that leads to meaningful outcomes	Help more learners gain the knowledge and skills required for life and career success in the 21st century	Help more people make measurable progress in their life and career through learning
2025 targets We are building on our efficacy work to set ourselves ambitious growth targets.	› We will help 10 million primary and secondary learners annually access high quality education › We will help 2 million post-secondary learners annually access high quality education	› We will help increase literacy and numeracy for 50 million learners annually › We will help 50 million learners annually gain the knowledge and skills required for study and employment › We will help advance the English language skills of 75 million learners annually	› We will help 25 million learners annually transition into the workforce after further or higher education › We will help 20 million learners advance their career prospects annually
Strategic alignment Our goals and targets align with our core strategic priorities. For more see strategic overview on p04	Online degree and virtual school programmes can improve learner access to quality primary and secondary education; currently those programmes are helping 1.8 million learners to annually access quality education. By 2025, we aim to help 10 million.	Our products that support adult English language learning can provide learners with the skills required for success in a global workforce. Products such as MyEnglishLab and many others allow us to help advance the English language skills of 30 million learners annually. By 2025 we aim to help 75 million learners annually.	Our workforce readiness products support learners to make measurable progress in their lives and careers. Products such as MyITLab help approximately 15 million learners to transition into the workforce annually. By 2025 we aim to help 25 million learners annually transition into the workforce after higher or further education.

3

Principle three

Keep the business model dynamic

The challenge

Business models have changed radically over the past decade. The natural evolution of a company and the disruptive impact of the digital age will mean that business models continue to be re-evaluated and changed as companies seek new and better ways to engage with, and create value, for key stakeholders, including clients and customers, employees, suppliers and wider society.

Companies need to consider how their reporting can support this dynamism and reflect the growing importance placed on understanding the relationship with, and impact on, key stakeholders.

Observations

Companies are without doubt extremely good at embracing change – their very survival often depends upon it. Not all companies, however, are so good at reporting how their business model has changed and how it is likely to continue to evolve and remain resilient into the future.

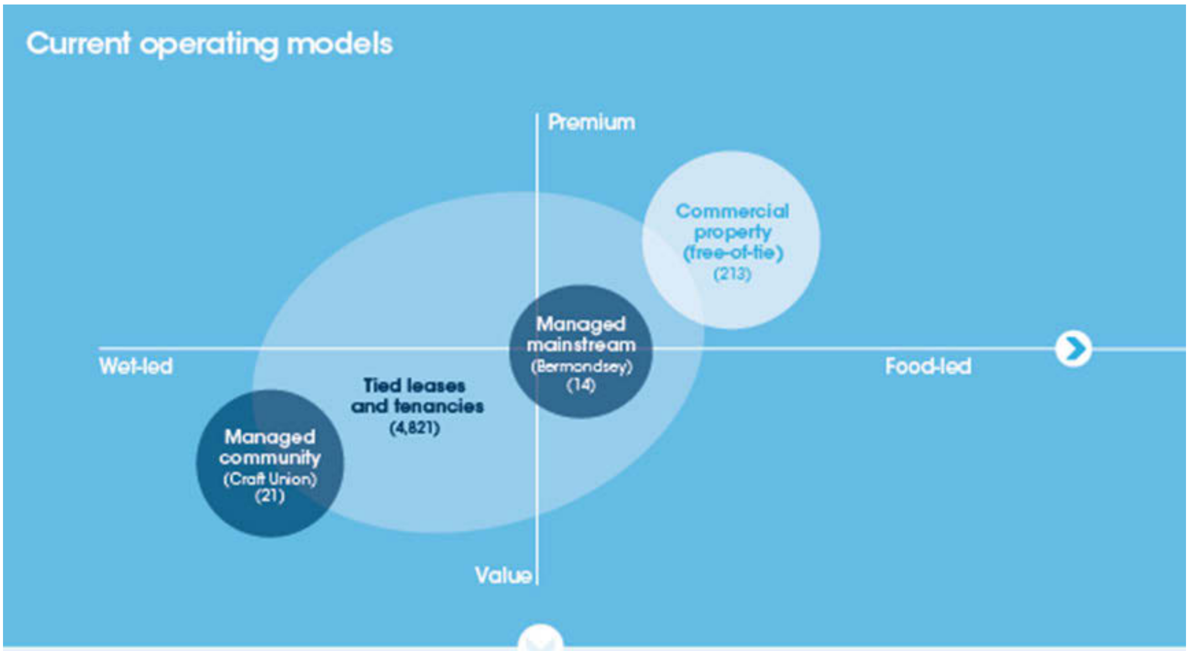
Our research suggests that whilst reporting of business models is evolving there is still a real inconsistency over what is presented. On the whole, while the reporting is becoming more comprehensive and outward-facing, it is largely generic, and set at a static point in time. Very few companies offer any perspective of how the model may need to change to respond to future customer needs or connect their business model with their discussion around market trends, strategy, risks and KPIs.

PwC recommends

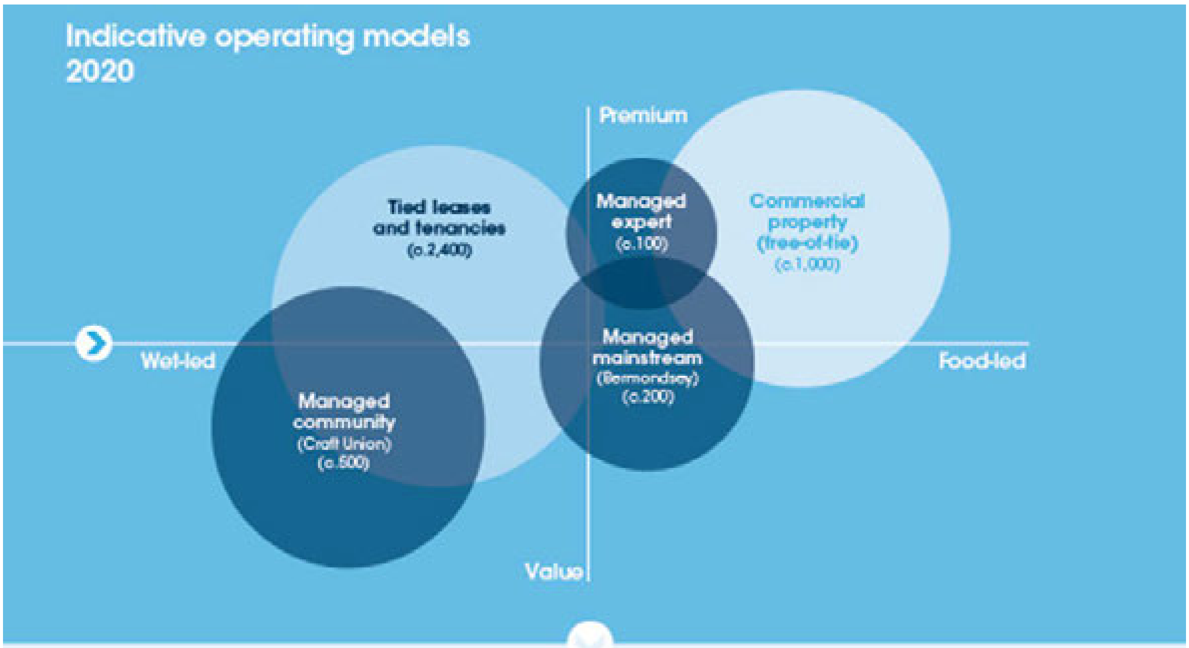
- Present a view of the business model that considers both your internal operations as well as the key resources and relationships upon which you rely.
- Link the business model to market drivers.
- Use a dynamic narrative that is relevant and updated for the period and not just rolled forward from the last.
- Focus on the particular elements of the business model that are more material now and/or will be in the future.
- Clearly articulate management's view of how the business/operating model will evolve to respond to market drivers.

Enterprise Inns Annual Report 2015

Enterprise Inns presents a picture of its current operating models and what they might look like in five years' time. With this picture it explains how 'extending the range of operating models available to the Group gives optionality and serves to increase the ability of the Group to respond more quickly to changing markets, consumer needs and regulation'.



The core operating model of tied leases and tenancies is currently supplemented by 213 commercial free-of-tie leases. The commercial leases trade both as pubs, where the Group has assessed it will achieve greater returns on a free-of-tie lease basis, or non-pub conversions, such as convenience stores.



Our strategy for the estate is to have a broader mix of operating models, offering flexibility in order to optimise value. Tied leases and tenancies will still make up the majority of the future estate, but these will be supplemented by additional commercial properties and directly controlled managed houses within our managed mainstream, managed community and managed expert operating models.

4

Principle four

Articulate resources and relationships

The challenge

A key pillar of providing a forward-looking orientation to reporting is a clear explanation of the tangible and intangible resources and relationships that a business relies upon to maintain its business model. Investors are looking for more than bland, high-level statements because they want to obtain a clear picture of those factors enabling the company to ensure the quality and sustainability of financial performance.

A critical component is to understand what the key resources and relationships are that make an organisation distinctive and those that it relies on for success. These may be distinctive strengths, but may also relate to potential weaknesses or exposure to critical resources or relationships. Aligned to these are the key risks and opportunities these elements present and how the business manages and develops them.

Observations

All too often, we see statements of process or activities that are not grounded in strategic direction and that fail to identify the resources and relationships upon which a business relies and how they will be managed in the future. Similarly, there is often little relationship between the highlighted resources and relationships and strategic priorities for how they're managed, key risks to their continued availability, or real quantified measurement of their management and development or how they impact directly, or indirectly, financial performance.

PwC recommends

- Clearly identify the most material resources and relationships for your business.
- Demonstrate how these are present within the business model and explain what the risks or opportunities faced by relying on them are.
- Include key priorities for these assets as part of strategic discussion.
- Provide sufficient information to understand how they're being managed and whether the priorities are being delivered on.
- Report appropriate KPIs to allow progress to be measured.
- Where insights are included within CSR reports, ensure that there is clear consistency and cross referencing to the corporate strategy and business model.

Berkeley Group Holdings Annual Report 2016

Berkeley Group include a clear overview summary outlining the importance of people to their business and explaining how they manage this key resource. This information is supported by everyday principles of working, longer-term strategic goals and clear measures used to monitor success.

OUR PEOPLE

> We are committed to developing a highly skilled workforce who run autonomous businesses, operate in a safe and supportive working environment and contribute to wider society.

WHY FOCUS ON OUR PEOPLE?

Our people are key to the development process, from the identification and purchase of land through to the sale of our homes and ongoing customer service.

To run any business successfully it is vital to ensure that the workforce is highly skilled and motivated. We understand the importance of supporting all our employees to allow them to work in a safe environment and to continue to advance their knowledge and skills. Developing and retaining our workforce enables us to deliver our objectives and grow as a business.

OUR APPROACH

A devolved business structure is at the heart of our strategy. Our recognised brands and autonomous operational teams carefully manage each individual scheme to ensure that the entrepreneurial spirit of the business continues. Recruiting and retaining a high calibre workforce is crucial to our approach. We must support both our direct employees and the wider workforce of the contractors working on our sites. We are proud to be safe; safety continues to be a key focus area across all of our operations, in addition to enhancing health and wellbeing. We also aim to have a positive impact on society and enable young people to get into work through our support of the Berkeley Foundation.

2016-2018 HEADLINE COMMITMENTS

- Launch and implement a new programme to promote the wellbeing of our staff and create healthy workplaces
- Invest in training and development through our talent management programmes to realise the potential of our people across all areas of the business

2014-2016 HEADLINE COMMITMENTS

- Pay at least the Living Wage to all direct employees ✓
- Reduce energy costs by up to £500,000, investing 50% of the saving in new health and wellbeing initiatives 63%
- Encourage and support every member of staff to be involved with the Berkeley Foundation each year ✓
- Launch a talent management programme which develops new ideas to enhance the business ✓

2016 PERFORMANCE HIGHLIGHTS

NHBC Health and Safety Awards 2015:
National Best Site Awards for Ryewood (Large Builder) and Saffron Square (Multi-Storey Builder)

Payroll Giving Platinum Award 2016 achieved as over 30% of employees donate through the GAYE scheme

2.40
Accident Incident Rate (Industry average: 4.20, HSE October 2015 figure)

68%
employees involved with the Berkeley Foundation

Learn more about Our People at www.berkeleygroup.co.uk/about-berkeley-group/our-vision/our-people

5

Principle five

Identify lead indicators of performance

The challenge

Historically, companies have presented performance indicators based solely on traditional financial information. This is increasingly becoming insufficient to fully meet investor needs. Companies should ask themselves how they can present a balanced set of financial and operational KPIs to support their strategic discussion and provide an indicator of future financial success.

Observations

Our 2016 survey of investors, *Redefining business success in a changing world: Global survey of investor and CEO views,* reported that over 70% of CEOs and 60% of investment professionals believe that in the 21st century business success will be redefined by more than just financial profit. This is echoed by McKinsey whose report highlighted the importance of companies communicating long-term metrics to help investors make decisions about long-term value creation: ‘Focusing on metrics like 10-year economic value added, R&D efficiency, patent pipelines, multiyear return on capital investments, and energy intensity of production is likely to give investors more useful information than basic GAAP accounting in assessing a company’s performance over the long haul’.

This is consistent with our experience that increasing regulation and stakeholder interest has encouraged companies to present a broader picture. Our research shows that sitting alongside financial measures companies are reporting an increasing number of non-financial indicators. In our latest review of reporting practices in the FTSE 350 we found the average number of KPIs to be 8, split 5 financial, 3 non-financial. But the reality is scratch away at the surface and these non-financial KPIs tend to point to the reporting of data that is either required or readily available rather than strategically relevant. These non-financial indicators can be lead indicators of future financial performance but to do so they need to be relevant and clearly related to strategic priorities and financial success.

A number of companies support their KPIs with specific performance targets but these can be sporadic – provided for some KPIs but not all – or are set without any indication of timescales leaving it unclear as to the real expectations of management.

PwC recommends

Investors will look for transparency on both financial and non-financial performance indicators. We would recommend that a business:

- Examine and clearly articulate an appropriate mix of KPIs that clearly align with strategic priorities.
- Explain how the different measures interrelate.
- Where possible, set explicit targets and associated timelines.
- Demonstrate measurement of the outcome and impact of activities, not just the input/output in order that investors can determine how effective initiatives taken actually are. For example not just the number of training days provided but the skills uplift this had.

Reckitt Benckiser Annual Report 2015

Reckitt Benckiser have set explicit targets for their KPIs and have associated a clear time period with this. They have also adopted milestone targets for some measures allowing progress to be monitored and interim performance assessed.

Barclays Annual Report 2015

Barclays have provided a clear summary of both financial and non-financial indicators that they believe will demonstrate success across the 5C’s element of their strategy which is explained throughout the report. Explicit targets are provided for the period to 2018.

KEY PERFORMANCE INDICATORS

Proportion of total Net Revenue from Health and Hygiene

74%

2014: 72%

Target to 2020: 80%

Like-for-like Net Revenue growth

+6%

2015 target: +4%

2016 target: +4-5% at constant exchange rates

Target to 2020: Total Net Revenue growth which outperforms the markets in which we operate

Operating margin Expansion

+210bps

2015 target: Moderate to 'nice' expansion

2016 target: Moderate margin expansion

Target to 2020: Moderate margin expansion

We have agreed eight key measures categorised into the 5Cs against which our stakeholders can hold us to account.

	Metric	Actual 2014	Actual 2015	Target 2018
Customer and Client Page 12	Personal and Corporate Banking (PCB), Barclaycard and Africa Banking weighted average ranking of Relationship Net Promoter Score® (NPS) vs. peer sets	4th	4th	1st
	Client Franchise Rank: Weighted average ranking of wallet share or customer satisfaction with priority clients in the Investment Bank	5th	5th	Top 3
Colleague Page 13	Sustained engagement of colleagues score	72%	75%	87-91%
	% women in senior leadership	22%	23%	26%
Citizenship Page 14	Citizenship Plan – initiatives on track or ahead	11/11	10/11	Plan targets
Conduct Page 15	Conduct Reputation (YouGov survey)	5.3/10	5.4/10	6.5/10
Company Page 16	Adjusted Return on Equity (RoE)	5.1%	4.9%	N/A[a]
	Fully Loaded CRD IV CET1 ratio (Capital Requirements Directive IV Common Equity Tier 1)	10.3%	11.4%	N/A[a]

Note
a Please refer to the new financial targets set out in the Chief Executive's review on page 4.

6

Principle six

Explain future risks and opportunities

The challenge

A clear, specific and dynamic explanation of the risks/opportunities faced by a business and how they are being managed helps the user form a view of the resilience of a business, the potential threats to success in the future and whether management and the board are on top of them. These should be given due attention if the annual report is to be 'fair, balanced and understandable'.

Equally, risks arise because companies make strategic decisions in response to opportunities, and the scale of the opportunity and action taken will be considered in light of whether it falls within the parameters of the agreed risk appetite. There has been more focus on this internally than any other aspect of risk in recent times because of its inclusion in the Governance Code. It drives all the decision making around how risks will be managed and what level of investment is needed in internal control systems, but it's complex and difficult to express.

Observations

In this year's review of narrative reporting practices in the FTSE 100 we saw an increasing number of companies providing more insight into their overall risk profile, through the use of heat maps (19%) and how the risks have changed during the year (56%). We have also seen a smaller number of companies talk about emerging risks that are on the board's radar but have yet to make it to their principal risk statement.

But fundamentally there remains less clarity on what those risks actually are. Too many are not specific to the company, and a wide range of different materiality levels are used to identify them. It is difficult to talk meaningfully about how a risk is changing or what corrective action has/may need to be made if the risk itself is generic.

Similarly, the discussion of risk management tends to be a generic summary of what was planned rather than what transpired for each specific risk in light of market trends or strategic decisions made.

Risk appetite disclosures are either not given or are poorly done, reflecting the struggle that we know has been taking place within many organisations. This is becoming increasingly apparent for many companies outside the financial services sector.

PwC recommends

Risk profile will vary from company to company. The individual circumstances will determine how best to present that information. We consider good practice an approach that:

- Is very clear about the nature of the principal risks and why they are the right ones for the company.
- Explains the changing risk profile, including changes in the status of a risk, emerging risks, how the risk is being managed and, if it is outside of the set parameters/appetite, what is being done about it.
- Shows how the board and its committees are involved in dealing with risk and exercise governance over management.
- Provides a link between the risks and commentary around the business model, strategy, viability statement or the effectiveness of the systems of risk management and control.

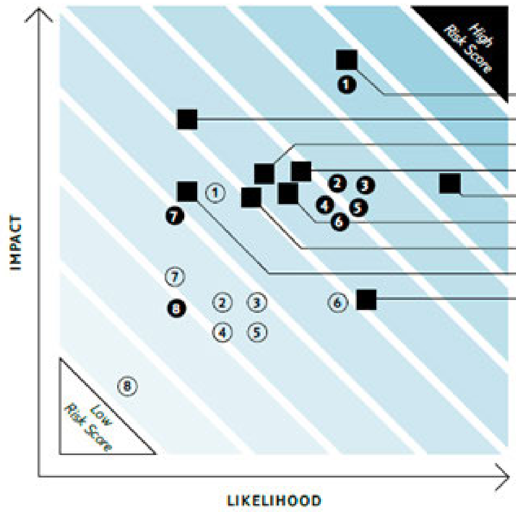
TUI AG
Annual Report 2015

TUI's reporting presents a comprehensive risk heat map that goes beyond simply listing risk profile and instead articulates where the company would like each risk to sit in the future.

Rio Tinto
Annual Report 2015

Rio Tinto use a tabular structure to demonstrate clear alignment of their risks with the opportunities these also present for the company. They also take a further step by reporting how this might impact on the company's viability.

RISK POSITION



INHERENT RISKS

■ CURRENT RISK POSITION

Macroeconomic Risks
Health & Safety
Seasonal Cash Flow Profile
Competition and Consumer Preferences
Destination disruption
Input Cost Volatility
Legal & Regulatory Compliance
Joint Venture Partnerships
Supply Chain Risk

AKTIVE RISKS

● CURRENT RISK POSITION ○ TARGET RISK POSITION

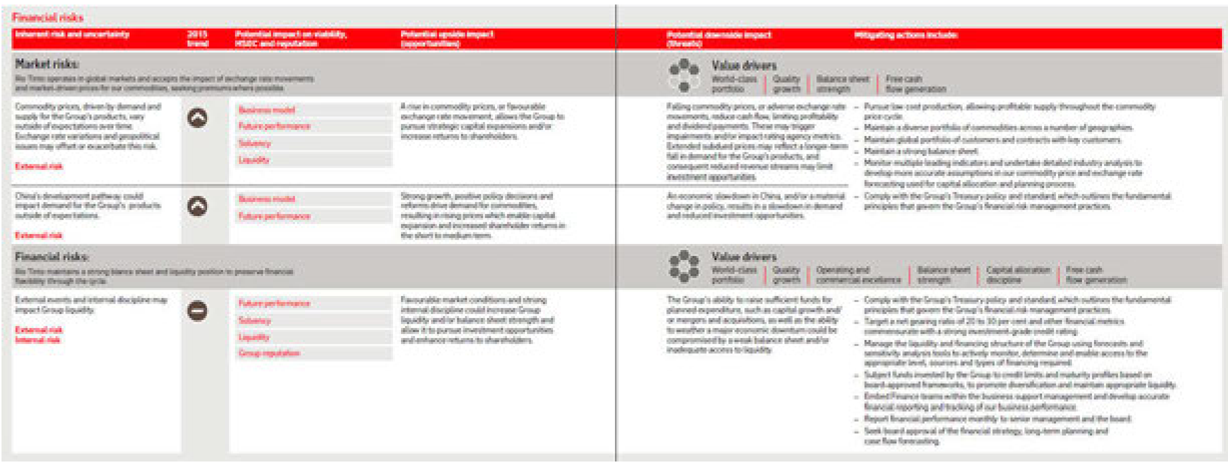
1 *IT Development & Strategy*
2 *Brand Change*
3 *Growth Options*
4 *Integration Oportunities*
5 *Sustainability Targets*
6 *Cyber Security*
7 *Talent Management*
8 *Corporate Streamlining*

CURRENT RISK POSITION

This shows the current level of risk faced today after taking in to account the controls that are in place and which are operating as intended.

TARGET RISK POSITION

This shows the target level of risk deemed to be an acceptable, tolerable and justifiable risk position after further actions have been implemented to mitigate the risk.



Managing our risks, embracing our opportunities

By managing risk effectively and embracing opportunities, we will be in a stronger position to deliver our strategy and enhance shareholder value.

Our key focus areas in 2015

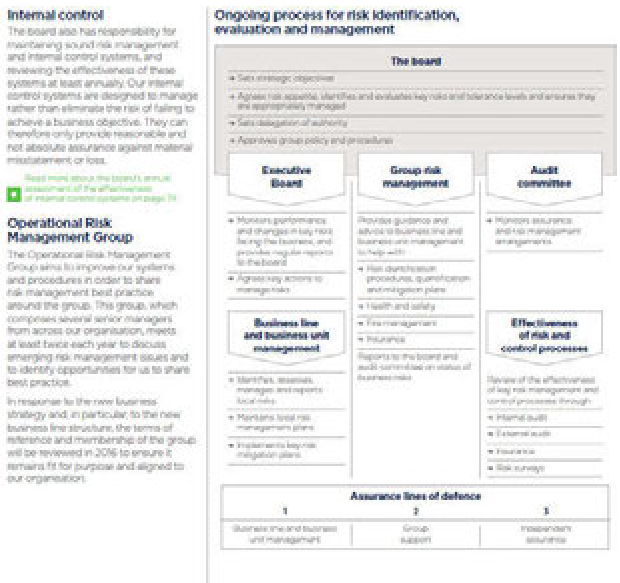
Next steps and key priorities for 2016

Risk appetite

Inherent attributes

Risk culture

Identification, evaluation and management of principal risks



Internal control

Operational Risk Management Group

Ongoing process for risk identification, evaluation and management

The board

Executive Board

Group risk management

Audit committee

Business line and business unit management

Effectiveness of risk and control processes

Assurance lines of defence

Berendsen Annual Report 2015

Berendsen clearly demonstrate management's oversight of the risk management process providing a much wider narrative than commonly seen. The report provides good commentary on the role played by management around risk in the period and also the future plans they have going forwards.

7

Principle seven

Be clear on financial prospects

The challenge

Companies will often raise concerns that communicating future financial prospects will attract regulatory attention and resulting pressure to meet those forecasts will outweigh any benefits achieved. For example, many have criticised earnings guidance as encouraging short-term outlook and investment. The recent changes to the Market Abuse regulations reiterates the existing requirements in the Disclosure Transparency Rules (DTR 2.2.1), that publishing price sensitive information may require ad hoc communications to the market on previously released targets, which have further led to companies being reluctant to state the targets to start with.

Observations

Whilst many companies have a natural reluctance to provide forward-looking financial numbers, we believe that investors are much more understanding of them if they are supported by the underlying assumptions, methods and other sensitivities that are involved in their development. The new European Securities and Markets Authority (ESMA) guidelines on alternative performance measures (APMs) support this approach, setting out requirements that APMs be used transparently, their relevance explained, and that clear reconciliations to GAAP be shown in order to be meaningful.

It's also useful to know what the parameters are for assessing corporate success and progress. For example, is a small gain to be applauded given expectations or derided? This can only be properly understood through clear disclosure on management's intentions.

PwC recommends

- Use a broad range of measures to ensure investors understand the full picture.
- Provide specific targets, milestones or target ranges for performance.
- Consider the use of both short and longer-term timeframes to encourage longer-term investment.
- Be clear on why management believe this performance is both desirable and achievable.
- Provide a clear link to market information on growth, opportunities and uncertainties.

Thomas Cook Annual Report 2015

Thomas Cook provide a clear set of financial targets over a three year period. The relationship between these targets and the success of the wider operating model is also made clear helping to demonstrate the wider relevance of the disclosure.

Babcock International Annual Report 2016

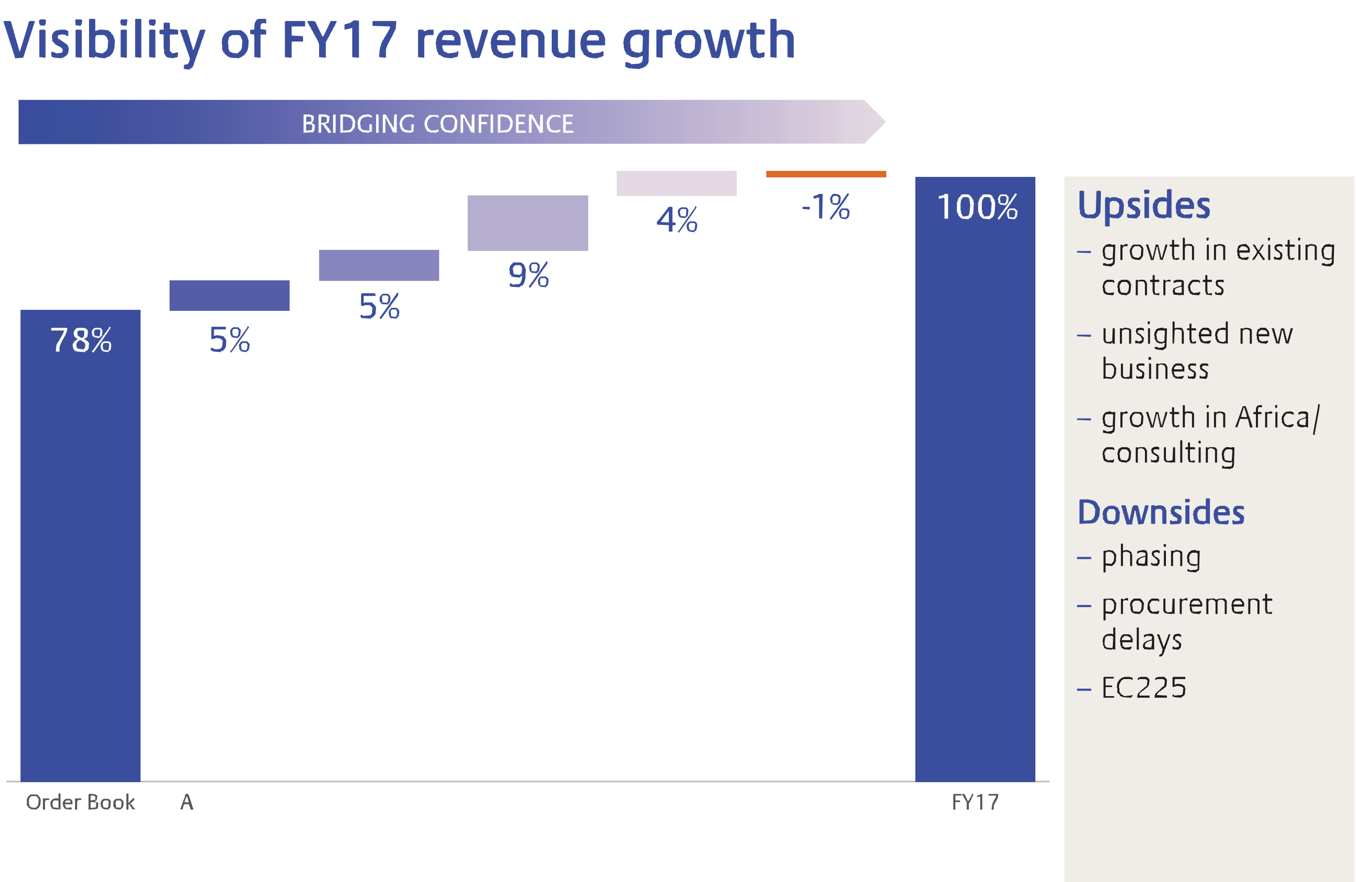
Babcock make good use of a bridge chart to clearly show the elements that will contribute to revenue growth over the forthcoming period.

These initiatives aim to generate significant, sustainable, long-term profit growth, including revenue growth through a better quality proposition that attracts more customers at higher price points, and margin improvements through better yielding and cost efficiencies.

We believe the New Operating Model will enable Thomas Cook to achieve the following, between FY15 and FY18:

- **Revenue growth** at least in line with the European leisure travel market, which is estimated to grow, on average, at between 2% and 3% per year
- **Annual EBIT benefits** of between £100 million and £120 million by FY18, with one-off implementation costs totalling approximately £100 million, of which £25 million was incurred in FY15
- **Cash conversion** in excess of 70% per year, based on a revised definition of cash conversion, being the percentage of underlying profit before tax that is converted into free cash flow
- **Fixed-term debt reduction** of at least £300 million over the next three years

We expect these benefits to be generated by business improvement initiatives which focus on the areas below are embedded in our strategy as described on the following pages. Further details were provided at our analyst presentation on 25 November 2015, a copy of which is available at www.thomascookgroup.com



8

Principle eight

Be consistent

The challenge

Investors make decisions from a wide range of information sources. Steps need to be taken to ensure all messaging under management's control is clear and consistent, giving investors confidence in the forward-looking information provided and also in the internal dynamics of the business. Where different periods make sense for a company, these should be clearly explained, for example how does a three year planning cycle align to a 5-10 year sustainability strategy and what is the stewardship over this?

Observations

The introduction of the viability statement has forced companies to disclose a viable period and to explain their reason for that period. However, we have found that the period chosen often seems to exist only in the viability statement with little supporting evidence of the company giving consideration to such a period elsewhere in the report. Investors look for evidence that the period chosen is meaningful and realistic to their knowledge of the business and its industry, and that it ties in with other reported information but currently there is little for them to work with.

Consistency, however, extends far beyond this and impacts on many areas of the report. For example, we have seen companies identify KPIs that don't appear to measure strategic progress, and companies that report CSR issues to be seen as a good green citizen rather than because they are consistent with the social principles of the business. Inconsistent reporting can sometimes be the product of a large number of writers focused on different agendas pulling the document together and a lack of clear oversight to join the dots.

PwC recommends

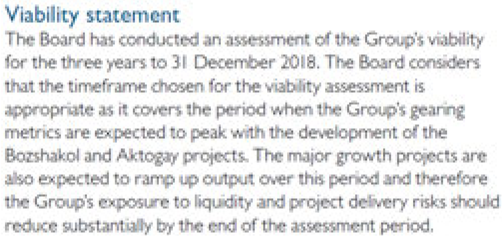
- Ensure that transparency over the period by which strategy is assessed is matched by explicit discussion in the strategic statements.
- Where differences occur, be sure to clearly explain them.
- Make use of clear cross-referencing and signposting within a report to underline the relationship between strategy, risks, KPIs, business model and markets.
- Ensure that disclosures and periods are consistent in the report and through different reporting channels.
- When developing the annual report, ensure one person has clear oversight of all messaging to identify inconsistencies early in the process.

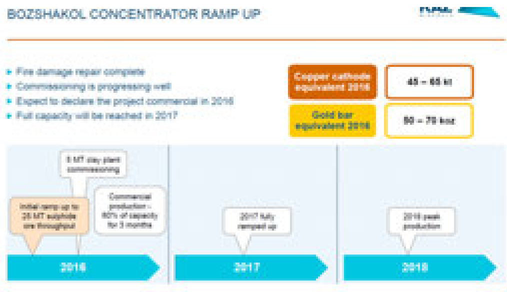
Kaz Minerals Annual Report and Preiliminary Presentation 2015

Kaz Minerals clearly demonstrate common themes on forward-looking insights throughout their strategic report, viability statement and preliminary presentation by using a consistent time period and common terminology allowing the reader to clearly see the relationship across different reporting channels.

Lonmin Annual Report 2015

Lonmin's viability statement is a good example of the relationship between their viability period and their longer-term planning period. This insight helps investors to properly understand the relevance of the period for the company and demonstrates the role that management have played in determining this.


Viability statement
The Board has conducted an assessment of the Group's viability for the three years to 31 December 2018. The Board considers that the timeframe chosen for the viability assessment is appropriate as it covers the period when the Group's gearing metrics are expected to peak with the development of the Bozshakol and Aktogay projects. The major growth projects are also expected to ramp up output over this period and therefore the Group's exposure to liquidity and project delivery risks should reduce substantially by the end of the assessment period.



How we assess the Group's prospects

The Board Strategy Review is performed on an annual basis where the Board and executive management discuss and debate the Group's strategy. The Board Strategy Review considers scenario analysis to encompass a wide spectrum of potential outcomes for key global uncertainties. Executive management prepare a Life of Business Plan (LoBP) which spans in excess of 40 years detailing operational plans to exploit the Group's long life mineral resources. The LoBP forecasts total mining production volumes and costs over the life of mine based on geological modelling and capital expenditure budgets. Capital allocation is determined based on portfolio optimisation models with the aim of ensuring that capital expenditure is invested only in the most valuable ore reserve development and expansion projects that are available to the Group.

Mining production and cost forecasts are then aggregated with concentrating, processing and overhead costs. Key financial assumptions including PGM prices, Rand Dollar exchange rates and cost escalations are reviewed and incorporated into the LoBP. The LoBP output is incorporated into a Working Capital Model (WCM) which produces short and medium term financial forecasts. A detailed annual budget covering the following year is prepared and reviewed by the Board on an annual basis.

The key assumptions applied in the LoBP and WCM are disclosed on note 31 to the financial statements under impairment of non-financial assets on pages 173 to 174. Executive management has gone through an extensive process of arriving at appropriate assumptions to apply including the use of external expects such as SFA Oxford for a review of PGM markets and SRK Consulting to review the operational aspects of the Business Plan. Market analyst and consensus views on PGM price and Rand Dollar exchange rate outlook were also taken into consideration. During the Board Strategy Review described above, the Directors have interrogated the key assumptions and have satisfied themselves that they are appropriate.

The financial forecasts from the WCM are then subjected to stress testing using the key downside risks listed below:

- Weaker USD PGM prices
- A stronger Rand/US Dollar exchange rate
- Lower than planned production
- Higher than planned cash costs

The period over which we confirm longer-term viability

Given the inherent uncertainty involved in setting key financial assumptions, specifically PGM prices and Rand Dollar exchange rates, the period over which the Directors consider it possible to form a reasonable expectation as to the Group's longer term viability, based on the planning and the stress testing described above, is the 3 year period to November 2018. Within the context of the planning cycle described above, the Directors have tested the scenarios that threaten the solvency and liquidity of the Company. While there are clearly not implausible combinations of prices and foreign exchange that would threaten the solvency and liquidity of the Company over the next three years, the Directors believe that there is a sufficiently large gap between the most likely assumptions and those that threaten the Company's solvency and liquidity to conclude that the Company is viable over that period.

Confirmation of longer-term viability

As detailed in the Going Concern section of the Financial Statements on pages 135 to 136, the Rights Issue and therefore the amended debt facilities which only come into effect if the Rights Issue is completed, are conditional, among other things, on Resolutions being passed by shareholders at the General Meeting. The need for shareholders' approval of the planned Rights Issue therefore represents a material uncertainty that may cast significant doubt about the Group's and Company's ability to continue as a going concern and viability such that they may be unable to realise their assets and discharge their liabilities in the normal course of business.

Nevertheless, based on the Group's expectation that the conditions of the Rights Issue will be met, and the robust assessment of the principal risks facing the Group and their stress testing described above, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to November 2018.

Further reading and contacts

Contacts

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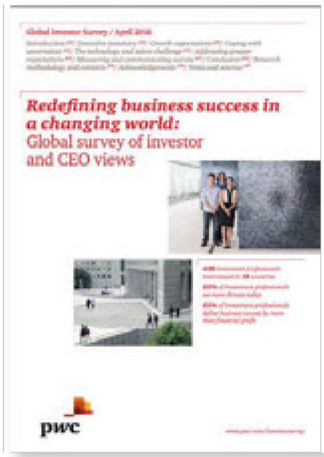
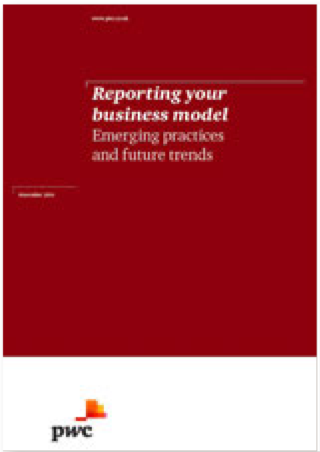
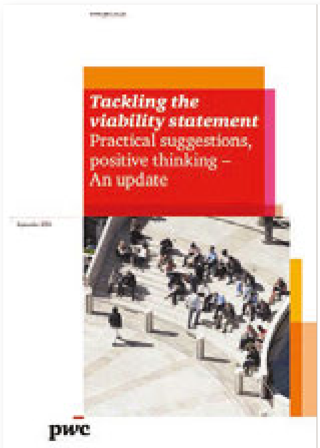
Further reading



Redefining business success in a changing world: Global survey of investor and CEO views



Reporting your business model: Emerging practices and future trends



Tackling the viability statement, practical suggestions, positive thinking – An update

Tackling risk reporting, practical suggestions, positive thinking

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