



---

2015  
RITTENHOUSE RANKINGS

---

# CEO CANDOR & CULTURE SURVEY™

*Leadership  
Powerful Communication Facts Strategy Smarter Decisions  
Integrity Strategy Revolutionary Candor Innovation  
Communication Facts Shareholder Powerful Leadership Authentic*

## Rittenhouse Rankings 2015 CEO Candor Analytics™ Survey

### I. EMERGING FIELD OF FINANCIAL LINGUISTICS

The annual Rittenhouse Rankings Candor Analytics™ Survey is one of a number of analytic tools that comprise an emerging field of investment analysis called “Financial Linguistics”. This body of work focuses on the importance of analyzing words as well as numbers to identify tangible and intangible drivers of shareholder value. It integrates insights from behavioral economics with the principles of financial accounting and valuation.

Financial Linguistics experts use in-depth analyses to help CEOs, investors, boards of directors, customers, and employees gauge the integrity of a corporate culture, the quality of executive leadership, and the reliability of corporate accounting.

#### Other institutions and experts that offer Financial Linguistics research include:

- The Securities & Exchange Commission, which has developed powerful data analytics search tools to analyze MD&As and other corporate reports to identify potential accounting fraud.
- High-frequency traders who use linguistic software to monitor stock market sentiment and position trades.
- Analysts at companies like Valens Securities, Inc. and Business Intelligence Advisors (BIA) who are trained in forensic analysis and scour quarterly earnings teleconference calls to determine if executives are revealing or obscuring important information about accounting results and financial performance, strategy, vision, and stakeholder relationships.

Academic studies have shown that CEOs who communicate candidly in shareholder letters and corporate communications gain competitive advantage. A landmark study by Standard's & Poor's found that exemplary transparency in annual reports was correlated with a lower cost of capital and superior financial performance.

Why does Financial Linguistics provide trusted, actionable insights? Because language is central to human behavior and behavior determines actions that lead to business success or failure. In short: words create the future.

### II. What is Candor Analytics™?

Candor Analytics is a measurement tool created by Rittenhouse Rankings to systematically evaluate executive communications and rank order companies based on high to low candor scores. The coding system is based on the Rittenhouse Model of a Sustainable Business™. This in-depth taxonomy helps researchers to sort executive communications text into meaningful categories. Sorting this text reveals patterns and insights into leadership, corporate culture, competitive advantage, and other measures of corporate performance.

Over the past 10, five and three years, the average compound annual returns of top-ranked quartile companies in the Candor survey (analyzed on a June to June basis) were 18.1 percent, 28.3 percent, and 30.7 percent compared to the S&P 500's 10, 5 and 3 year compound returns of 7.1 percent, 11.5 percent and 10.7 percent, respectively for the same June to June period.

The total annual June to June return of the top quartile of candor ranked companies in the 2015 Survey was 17.6 percent versus the S&P's 1.8 percent return from June to June.

Over the years we have found that companies excelling in both candor and total return are likely to cultivate corporate cultures that exhibit a "Words Matter Mindset". Leaders who believe that words matter tend to prefer clarity to confusion, directness to evasion, and truth telling to truthiness\*.

Expecting their words and actions to create the future, these leaders strive to find the "right words" to communicate strategy, vision and actions. They won't settle for the "almost right" words. This discipline sets an example throughout a company to create communications that are unbiased, balanced, focused and relevant.

Leaders who chose words that transmit positive energy engage in high-quality conversations that reinforce positive cultural values. This energy sparks innovation and builds trust. Such leaders try to avoid words that transmit negative energy which weaken positive values like risk awareness, innovation, collaboration, and accountability.

\*Truthiness is a quality characterizing a "truth" that a person making an argument or assertion claims to know intuitively "from the gut" or because it "feels right" without regard to evidence, logic, intellectual examination, or facts. (Wikipedia).

## V. CANDOR RANKINGS METHODOLOGY

The Rittenhouse Rankings Candor Analytics™ methodology allows researchers to code and analyze key words, phrases and concepts in corporate communications to measure candor, a proxy for corporate trustworthiness.

The development of this process is described in *Investing Between the Lines (McGraw-Hill)*, a book endorsed by Warren Buffett in his 2013 shareholder letter. Candor is so important that Berkshire Hathaway CEO Warren Buffett included it as one of the 15 key principles that make up the company's Operating Manual. Principle 12 reads:

*"...We will be candid in our reporting to you, emphasizing the pluses and minuses important in appraising business value. Our guideline is to tell you the business facts that we would want to know if our positions were reversed. We owe you no less."*

Buffett prizes candor because it mitigates self-delusion, a key leadership risk: He wrote: *"...candor benefits us as managers: **The CEO who misleads others in public may eventually mislead himself in private.**"*

To measure candor in executive communications, we developed a proprietary analytic model that includes over 100 topics organized into seven categories: 1) Capital Stewardship; 2) Strategy; 3) Accountability; 4) Vision; 5) Leadership; 6) Stakeholder Relationships; and 7) Candor.

Each topic within these categories is defined by a set of rules or protocols. Each is assigned point values that weight its significance in determining corporate success. Points are awarded for both factual details and context. For example, keywords and phrases like cash flow, financial and operational goals, and innovative ideas are all awarded positive points.

Candor topics, however, are awarded point deductions. These examples of negative candor are also known as "F.O.G." or "Fact-deficient, Obfuscating, Generalities." This includes platitudes, clichés, corporate jargon, Orwellian nonsense, and confusing statements that lack important context. Excessive F.O.G. points found in a corporate communication can reveal if a company is at risk for losing focus and direction.

This disciplined methodology instills a discipline that allows analysts to objectively evaluate CEO words and produce comparable Candor Scores and Rankings.

A company's Candor Survey score is calculated by totaling all negative (F.O.G.) points in an executive communication and dividing these by the total positive content points. The resulting F.O.G. percentage is called the Candor Discount Factor (CDF). After the scores are tallied, all 100 companies in the annual Candor Rankings Survey are ranked from lowest CDF to highest CDF.

#### IV. 2015 CANDOR SURVEY RANKINGS

The quartile companies ranked from top to bottom in the 2015 Candor Analytics survey are:

#### 2015 Rittenhouse Rankings CEO Candor Analytics™ Survey

Top-ranked in Candor		Top-ranked in F.O.G.	
Rank	Company	Rank	Company
1	<b>Sherwin-Williams</b>	100	<b>Walgreens</b>
2	<b>Clorox</b>	99	Fiat
3	<b>Costco</b>	98	<b>Emerson</b>
4	<b>Southwest Airlines</b>	97	<b>L'Oréal</b>
5	<b>JetBlue Airways</b>	96	<b>ConAgra Foods</b>
6	<b>CVS</b>	95	<b>Anthem</b>
7	<b>Google</b>	94	Volkswagen <sup>(2)</sup>
8	<b>Thermo Fisher</b>	93	Chevron
9	Hewlett-Packard	92	CSX
10	AMD	91	Humana
11	Travelers	90	<b>Avon</b>
12	Becton, Dickinson	89	EBay
13	ADP	88	<b>Bank of America</b>
14	Whirlpool	87	Wal-Mart
15	Texas Instruments	86	<b>Twenty-First Century Fox</b>
16	<b>Amazon.com</b>	85	Toyota
17	<b>General Mills</b>	84	Lenovo
18	General Motors	83	Capital One
19	Microsoft	82	Abbott Laboratories
20	<b>Honeywell</b>	81	Williams Companies
21	Netflix <sup>(1)</sup>	80	Novartis
22	<b>Edison International</b>	79	Time Warner
23	<b>Charles Schwab</b>	78	Bristol-Myers Squibb
24	Lockheed Martin	77	Siemens
25	Cigna	76	<b>BHP Billiton</b>

(1)(2) Not in 2014 Survey/ Company names in bold indicate repeat top and bottom rankings in the prior year's Survey.

The Candor Analytics system is used to measure candor in earnings teleconference calls, Management Discussion and Analysis (MD&A) reports, CEO speeches and annual shareholder letters.

Why analyze shareholder letters when many investors dismiss their value because they are often written by public relations experts and not the CEO? First, these letters are signed by the CEOs, a symbol of personal accountability. Second, the ability to identify leaders who publish letters that spin information, instead of providing meaningful commentary, gives investors a measure of the integrity of leadership and cultural values. Warren Buffett once told us in an interview that a lot of CEOs don't understand their businesses and this is evident in reading their annual letters.

Over the years, we have found many CEOs who actively collaborate with their annual report teams to draft their shareholder letters. These leaders use their authentic voices to reveal the unique corporate thumbprint. They typically rank in the top of our annual surveys.

#### IV. CANDOR RANKINGS AND MARKET PERFORMANCE

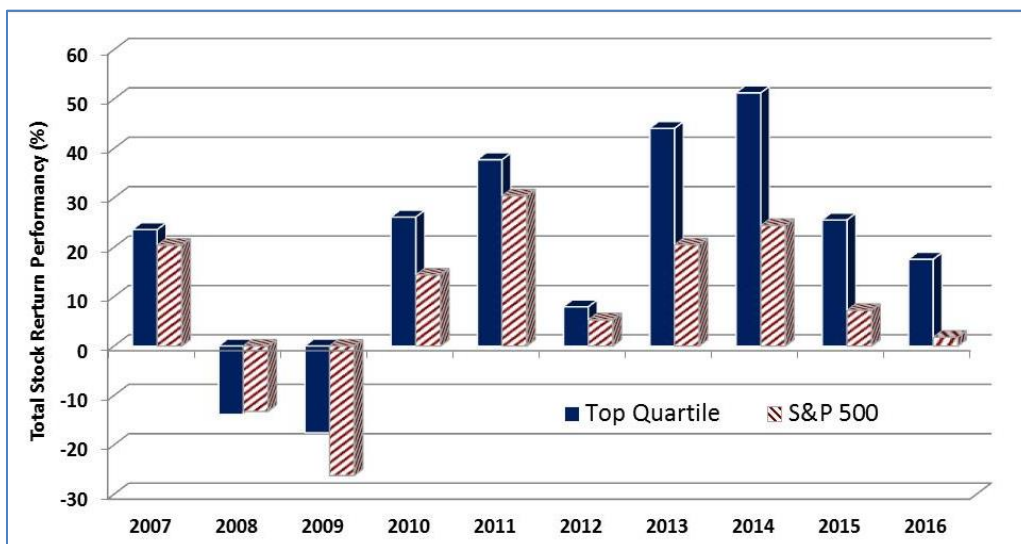
##### Annual Total Return Performance of 2015 Top and Bottom Quartiles Ranked in Candor

To correlate Candor Rankings with market performance, we calculate the total return of top and bottom quartile-ranked companies each year from the period ending June 30 to June 30.

The total return of the top quartile-ranked companies in the 2015 Candor Analytics™ Survey averaged 17.6 percent, substantially outperforming the S&P 500 of 1.8 percent and the bottom quartile-ranked companies which averaged a negative return of 19.2 percent.

This pattern of highest-ranked companies outperforming the market and lowest-ranked companies underperforming the market is a trend seen below that has persisted for over the past 10 years as seen in the chart below.

**Companies Top Ranked in Candor vs. S&P 500 (June 30 to June 30)  
2015 Rittenhouse Rankings CEO Candor Analytics™ Survey**



Of note is the widening gap between the performance of high candor-ranked companies and the market over the past four Surveys, compared to the period leading up to and including the financial crisis and global recession from 2007 to 2012.

Why has this performance gap widened? We believe it illustrates the connection between investor fear and stock valuation. During the recession, investor fear was at all-time highs. As a result, investors were less likely to discriminate between companies with strong, trust-based cultures and those with fear-based cultures.

As the economic recovery progressed, investors grew more confident and discriminating in their assessments. By 2013, we began to see the spread widen between top-ranked companies in candor and the market. What connects candor and market performance? In a word, "Trust".

Executives who lead with candor are more likely to create trusting relationships with employees who in turn create trusting relationships with each other and with customers. This is more likely to produce winning results which in turn, builds investor trust.

Conversely, executives who choose to obfuscate and lead with truthiness will be handicapped in building trusting relationships with key stakeholders. Their employees will be more likely to hide out and give less on the job than they are capable of giving. They are less likely to raise their hands if they see problems that need addressing. They will be handicapped in building trusting relationships with customers. This mistrust can lead to disappointing financial results.

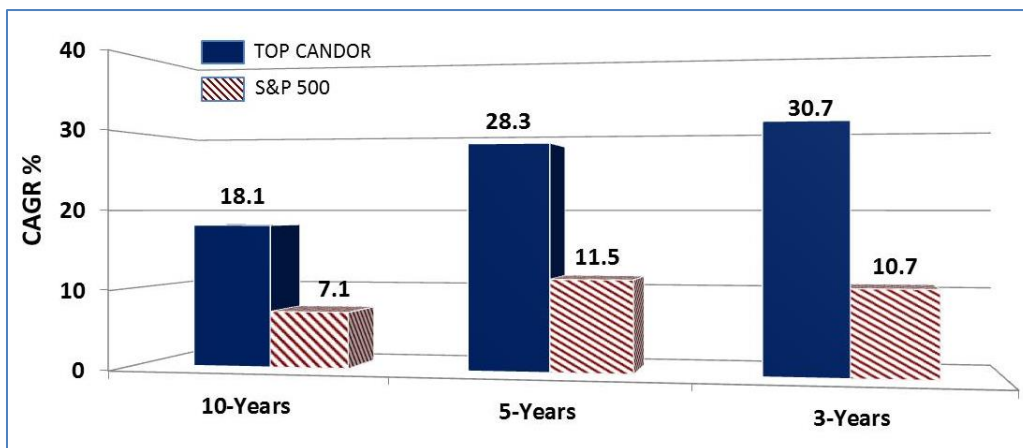
Over time, we believe that a continuing and persistent lack of candor will likely foster the development of toxic performance cultures that can significantly erode shareholder wealth.

### Compound Annual Growth Rate

As the chart below shows, if you had invested \$100,000 in the portfolio of candor-advantaged companies over the past ten years, your initial investment would be worth \$529,150 in 2016. This equates to a compound annual growth rate of 18.1 percent. The same investment in the S&P 500 ten years ago today would be worth \$198,280, representing a compound annual growth rate of 7.1 percent.

If you invested \$100,000 in the portfolio of candor-advantaged companies over the past five years, your initial investment would be worth \$347,000, representing a compound annual growth rate of 28.3 percent. The same investment in the S&P 500 five years ago would be worth \$172,320 in 2016 representing a compound annual growth rate of 11.5 percent.

**Compound Annual Growth Rate (June-June)**  
**Top-ranked Candor Companies Outperform the Market**



A \$100,000 investment in candor-advantaged companies over the past three years would be worth \$223,150 in 2016. This equates to a compound annual growth rate of 30.7 percent. The same investment in the S&P 500 three years ago would be worth \$135,780, a compound annual growth rate of 10.7 percent.

### **III. THE VALUE OF MEASURING CANDOR**

Candor-advantaged leaders respect the DNA or the energetic origins of words. For example, the origin of the word “candor” comes from the Latin word “candere” which means to illuminate or shine like a candle. Candor embodies human qualities of honesty and being straightforward in attitude and speech; qualities that are important to build trust.

The word “transparency” is often considered to be synonymous with candor, but its origin is different. Coming from the word “parere,” it means how things appear; the ability to see through them. So while candor’s DNA is defined as refers to light shining from a flame and behavior that is honest and straightforward, the DNA of transparency refers to whether or not we can see through something.

Investors, CEOs, corporate communicators and boards of directors use Candor Analytics rankings and scores to gauge how much they can trust a company’s accounting numbers and leadership. Because words create the future, precision in word selection is vitally important.

Why do investors rely on numbers over words when making investment decisions? It is because numbers appear to be more precise than words. And while, this is true, investors tend to forget that financial reporting numbers result from countless judgments that are made in a company about where and when to report incoming and outgoing cash, how much to report and when to turn cash into profits.

Investors who can identify the cultural values that shape these judgments will gain an investing advantage. They can protect their capital when they know if these values are conservative such as those in a Berkshire Hathaway company, or aggressive, even reckless, as was true at Enron.

Companies rich in positive candor are more likely to produce reliable financial accounting than companies that are deficient in candor.

### **VII. CONSTRUCTING A REPRESENTATIVE SURVEY SAMPLE**

Early in the development of the Candor Rankings system, Rittenhouse Rankings selected 100 companies for inclusion in the annual CEO Candor Benchmark Surveys. The selection was based on three factors: 1) capitalization of \$1 billion or more; 2) broad industry representation; and 3) high and low placement on Fortune magazine's list of Most Admired Companies and BusinessWeek's list of companies ranked by financial performance grades.

The companies that comprise the Candor Survey have remained relatively constant. This consistency allows us to observe continuing patterns as well as disruptions in patterns over time. Over the past 10 years, 25 companies were dropped from the Survey due to mergers and acquisitions, bankruptcies, and/or failure to publish a shareholder letter.

They were replaced by comparable companies matched by industry, capitalization, and reputation. Twelve companies are not domiciled in the U.S.: Air Canada, BHP Billiton, CIBC, FIAT, Lenovo, L'Oréal, Novartis, SAP, Schlumberger, Siemens, Toyota, and Volkswagen.

The 2015 Candor Survey included the following 100 companies:

1. 3M	35. Dow Chemical	69. Marriott International
2. Abbott Laboratories	36. DuPont	70. McDonald's
3. ADP	37. Eastman Chemical	71. Microsoft
4. AIG	38. Eaton Corp	72. Netflix
5. Air Canada	39. eBay	73. NIKE
6. Alcoa	40. Edison International	74. Novartis
7. Amazon.com	41. Emerson	75. PepsiCo
8. AMD	42. Entergy	76. Pfizer
9. Anthem	43. Estee Lauder	77. Pitney Bowes
10. AT&T	44. Exelon	78. SAP
11. Avon	45. ExxonMobil	79. Schlumberger
12. Bank of America	46. FedEx	80. Sherwin-Williams
13. Becton, Dickinson	47. Fiat	81. Siemens
14. BHP Billiton	48. Foot Locker	82. Southern Company
15. Boeing	49. Ford Motor	83. Southwest Airlines
16. Bristol-Myers Squibb	50. Franklin Resources	84. Starbucks
17. Capital One	51. General Mills	85. Target Corporation
18. CBS	52. General Motors	86. Texas Instruments
19. Charles Schwab	53. Google	87. Thermo Fisher
20. Chevron	54. Harley Davidson	88. Time Warner
21. Chipotle	55. Hewlett-Packard	89. Toyota
22. CIBC	56. Home Depot	90. Travelers
23. Cigna	57. Honeywell	91. Twenty-First Century Fox
24. Cisco Systems	58. Hormel	92. UPS
25. Citigroup	59. Humana	93. Volkswagen
26. Clorox	60. IBM	94. Walgreens
27. Coca-Cola	61. Intel	95. Wal-Mart
28. Colgate	62. JetBlue Airways	96. Walt Disney
29. Comcast	63. Johnson & Johnson	97. Wells Fargo
30. ConAgra Foods	64. Lenovo	98. Whirlpool
31. ConocoPhillips	65. Lockheed Martin	99. Williams Companies
32. Costco	66. Loews	100. Xerox
33. CSX	67. L'Oréal	
34. CVS	68. Lowe's	



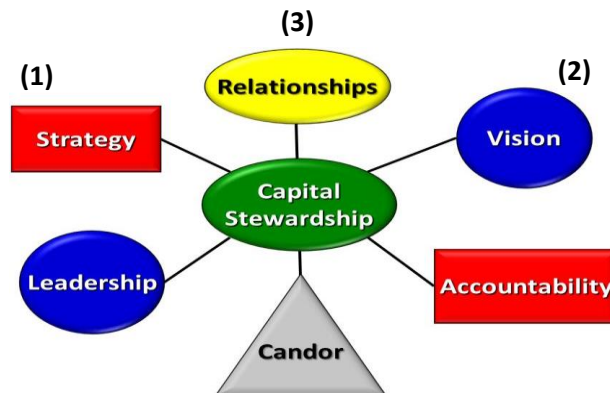
### Rittenhouse Rankings Corporate Culture and Candor Model™

Financial and candor analysts use the Rittenhouse Rankings Model below to score content in executive communications. By comparing peer companies we can find those companies whose communications reveal topics that CEOs ignore or obscure and those which are reported in detail and with exemplary context. These “GAP analyses” are a vital corporate culture diagnostic tool.

As well, changes in rankings over time may signal important positive and/or negative events that impact results and shareholder value.

As seen below, the hub of the culture and candor model is Capital Stewardship. It includes topics such as cash flow, goals, capital discipline, and operating metrics. Topics in each of the systems are defined by scoring protocols, so analysts can systematically and objectively code communications to calculate measures of positive and negative candor.

#### The Seven Systems of a Candor-Advantaged Business



The remaining six systems are organized into three vectors. The **red vector or left-brain system (1)** combines Strategy and Accountability systems. Strategy topics include business opportunities, markets and competitive advantages. Accountability topics include meeting goals and reporting financial results. Strong Accountability scores reveal a CEO’s commitment to create a culture of ownership and responsibility.

The **blue vector or right-brain system (2)** combines Vision and Leadership. Vision topics include the corporate purpose and value proposition, and statements about innovations. Leadership topics include investor skepticism, and what CEOs learned in addressing problems and failures. Strong, credible leadership supports the realization of a credible and compelling Vision.

The **third vector or backbone of the system (3)** combines Stakeholder Relationships and Candor. The category of Stakeholder relationships includes topics that describe customer needs, employee programs and stakeholder empathy. While strong customer relationships are supported by positive trust, Candor topics are awarded negative or F.O.G. points, not positive points. Therefore, companies which have high F.O.G. scores are considered to have low trust with their stakeholders and companies having low F.O.G. scores are expected to have high trust with stakeholders.

The power of candor in the model is evident in its triangle shape which appears as a fulcrum on which the balance of the corporate entity teeters.