

THE INTERACTIVE ANNUAL REPORT: THE FUTURE OF INVESTOR ENGAGEMENT

It wasn't so long ago when the idea of trading in the gloss and glamour of a company's printed annual report for a digitized replica was, for many, unfathomable. At the very least, without the luxury of high-speed Internet, thumbing through an annual report online could be a time-consuming and cumbersome venture. As humorist Dave Barry once quipped, "An entire new continent can emerge from the ocean in the time it takes for a web page to show up on your screen. Contrary to what you may have heard, the Internet does not operate at the speed of light; it operates at the speed of the DMV."

Nowadays much of that resistance has waned. That is not to say print is dead — far from it — but as environmental concerns increased, printing costs mounted, and the number of web-savvy investors increased, more and more companies opted to post their materials online in addition to mailing hard copies. Today, online annual reports are a fact of life thanks to the Security and Exchange Commission's e-proxy rule, which as of January 1, 2009 requires all filers to post their proxy materials online.

Issuers have a bevy of options when it comes to posting their company materials online, ranging from PDFs that replicate the format of the printed version to interactive, multimedia microsites — known as the "interactive annual report." Although the SEC's ruling does not stipulate which format an issuer must use, it is worth noting an often-overlooked amendment that says whichever format (or formats) selected must be "convenient for both reading online and printing on paper."¹ "Convenient" is undefined, perhaps intentionally so, with the minor exception of a footnote (number 35) that advises issuers to take downloading time into consideration.

That said, a quick look back at an earlier draft of the rule — the so-called "voluntary compliance release"² — may provide more insight into what the Commission means by "convenient." A provision that didn't make it into the final ruling seems to endorse the interactive online annual report:

"To take better advantage of the capabilities of the Internet, the materials also must be presented in a readily searchable format, such as HTML. This type of format would make the proxy materials easier to read on a computer screen. In addition, such a version may incorporate additional user-friendly features such as hyperlinks from a table of contents to enable shareholders to quickly and easily navigate through the document. Many Internet Web sites today provide documents in dual formats such as this."

1 Shareholder Choice Regarding Proxy Materials. Release No. 34-56135. 26 July 2007. Securities and Exchange Commission. [<http://www.sec.gov/rules/final/2007/34-56135.pdf>]

2 Internet Availability of Proxy Materials. Release 34-55146. 22 January 2007. Securities and Exchange Commission. [<http://www.sec.gov/rules/final/2007/34-55146.pdf>]

Unfortunately, many companies have overlooked — or perhaps misunderstood — this guidance and, instead, have opted to comply with the ruling by posting digitized replicas of the printed version. As the SEC warned in the footnote of its final ruling, these large files can be time-consuming to download and cumbersome to read on a computer screen. And it's not just a PDF that can prove unwieldy. One format to watch out for — as it may be confused with the interactive report — is the so-called “web-conversion,” a common service included in IR website packages. Although the web-conversion includes HTML code — as the SEC recommends — and provides some browsing and hyperlink capabilities, this type of web-conversion replicates the layout of the printed version, often by converting a PDF document into an image file such as .jpeg. This means that while investors do not need an additional plug-in to read the report, such as Acrobat Reader required for PDF viewing, the image files are still large and often cumbersome to read.

ANNUAL REPORT RANKED MOST IMPORTANT TOOL FOR INVESTMENT DECISIONS

When executed correctly, an annual report ties a company's various lines of business together into a cohesive, compelling story.

Attract new investors: According to the Rivel Research Group's latest study, nearly 70 percent of buy-side analysts surveyed report that the annual report is helpful in terms of deciding which stocks to pick.

Keep the ones you've got — avoid share price volatility: In the same survey, about the same amount of respondents reported the annual report is also helpful when tracking a stock.

Even better news: The survey also found that as stockholders' investment horizon increases, so does the annual report's usefulness.

Source: Rivel Research Phone Interviews, July 2007

This does not mean an online document identical to the printed report should be shunned. On the contrary, a PDF version, for example, can be a convenient format for investors wishing to print out the document. It is not necessarily convenient, however, for investors wishing to read the materials online. In fact according to an SEC survey of retail investors³, more than 60 percent of respondents said that it is at least “somewhat difficult” to find the information they wanted in printed reports. For this audience, a second format that takes full advantage of the web's capabilities, as the SEC suggested, is needed. The user-friendly navigation of an interactive report allows viewers to quickly jump to the information most important to them, creating a personalized experience. Furthermore, the ability to include multimedia, such as a video clip featuring senior management interviews or a slide show offering a virtual tour of a company's facilities, brings the company to life in a richer, more compelling way. Ignoring this is forgoing an opportunity to engage a shareholder, analyst, or stakeholder.

THE NEW BREED OF INVESTOR

More and more, investors are going online for information to help with their investment decisions. According to the same SEC survey of retail investors, 50 percent of respondents reported using the Internet to make investment decisions, and that number will surely continue to grow. Institutional investors are getting in on the action as well. Just a quick Google search shows some of the biggest funds, including CalPERS, AFL-CIO, TIAA-CREF, are active online and on social media outlets like Facebook and Twitter.

It's difficult to talk about the Internet these days without also mentioning social media. Social media is a force to be reckoned with and can no longer be dismissed as a passing trend. It has the potential to bring a lot of attention to your company. Now for example, individuals can become your company's evangelist

³ “Mandatory Disclosure Documents Telephone Survey.” Securities and Exchange Commission. July 30, 2008. [<http://www.sec.gov/pdf/disclosuredocs.pdf>]

by sharing your annual report with their Facebook or Twitter followers. They can also post your materials on content-sharing sites like Docstoc, which houses more than 2,500 annual reports. Docstoc has proven particularly fruitful for companies such as Chesapeake Energy Corporation. The company's 2006 annual report has racked up more than 15,000 views since its first posting in 2008.

This can be a double-edged sword. Information can easily “go viral,” as those in the online community say when a site or video spreads rapidly, and this means a weak annual report can spread just as quickly — if not more so — as a strong one. As a company you will want to take ownership of your corporate story, rather than allowing often-anonymous third parties to frame your story for you — not to mention that assuming ownership for a posting is a refreshing change within the generally anonymous virtual world. Although social media may not yet play an influential role in investment decisions, a vast majority of analysts and investors surveyed by corporate communications specialist Brunswick Group believe social media will indeed play an increasingly important role in investment decisions in the near future⁴. This means it is important for issuers to start familiarizing themselves with the various outlets now, so as not to get left behind.

PERSONALIZING THE INTERACTIVE ANNUAL REPORT EXPERIENCE

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Fueled in part by the social media revolution, one online medium that is growing particularly quickly in popularity is video. YouTube, for example, surpassed 100 million viewers in 2009; and in January of 2009 alone, 147 million people watched, on average, 101 videos each⁵. Videos are particularly effective tools when it comes to creating an engaging online annual report. Allowing investors to see and hear from the people who run the company can be a particularly effective method of engagement. It humanizes the company's story; not to mention that people are more likely to retain information that they have seen and heard. An additional benefit is that videos are 53 times more likely to appear on the first page of search results than text-only pages, which drives traffic⁶ to the website.

NOT ALL FORMATS EQUAL

Perhaps not surprisingly, investors do not give equal weight to all formats of online information. Web users are becoming increasingly sophisticated and they are no longer always content to passively consume information. Rather, the growing demand is for an interactive, multimedia-fueled, personalized experience. In fact an “investor wish list” compiled by investment management firm Reed Conner & Birdwell included “new communication methods” in the five-item list of what investors want to see from companies as they are making investment decisions⁷.

4 “Brunswick Group Survey Findings on New Media Usage by the Investment Community.” Brunswick Research. September 2009.

5 “YouTube Reaches 100 Million US Viewers.” YouTube Report 2009: A Marketers' Guide to Understanding and Using the YouTube for Business. March 5, 2009. [<http://www.youtubereport2009.com/youtube-reache-100-million-us-viewers>]

6 Gannes, Liz. “The Great Video SEO Frontier.” BusinessWeek.com. Bloomberg LP. February 13, 2009. [http://www.businessweek.com/technology/content/feb2009/tc200990212_136831.htm]

7 2010 National Investor Relations Institute panel session. “How Investors Make Investment Decisions.” June 7, 2010.

This means that, for an increasing number of investors, a PDF replica of the printed version does not always do the trick. As early as 2004, studies were showing that investors were already demonstrating a preference for personalized, multimedia annual report experiences. One academic study of online investor behavior analyzing website traffic logs⁸ showed that 60 percent of visitors who identified themselves as retail investors opted for the interactive, HTML version of the annual report instead of the PDF. And of those who identified themselves as professional investors, 40 percent chose HTML with, an additional 20 percent using both HTML and PDF versions. These studies suggest that a substantial, growing population is looking for an interactive experience, and those companies that cater to these people will likely be more in tune with the needs of their shareholder base.

TIPS FROM THE EXPERTS

- / Start early
- / Create a strong story/theme
- / Provide simple, clear, intuitive navigation
- / Provide easily accessible financials
- / Feature powerful, well-placed visuals (graphics, videos, photography, Flash animations)
- / Provide print, search, and download functions

It is not too great of a stretch to understand why this new breed of web-savvy investors are shying away from printed or PDF versions: the SEC's recent rash of new disclosure requirements, including greater explanations of directors' qualifications, carbon emissions, compensation, and risk management, have made proxy materials longer and more complex than ever. And this may be where the benefits of the interactive online annual report really shine. For the investor, the navigation capabilities allow for a personalized viewing experience, as they can quickly jump to the information most relevant to their needs. For companies, this means decreased printing costs. It also means savings in terms of environmental costs. Thus, by adopting the interactive online annual report, issuers can position themselves not only as technologically savvy and forward-thinking, but also as eco-friendly and environmentally conscious.

CASE STUDY

One company that has capitalized on — and reaped the benefits of — interactive online annuals is Stanley Black & Decker. Last year Stanley tasked its Director of Investor Relations, Kate White, with assessing the effectiveness of its investor communications. White's first target: the annual report — a hefty, glossy 40-page document bound to a 10K. To help save money — and the environment — and engage the new breed of web-savvy investors, White decided to create an interactive online annual review.

"I didn't want this to be just a brand piece," she told *IR* magazine in an interview⁹. "I wanted investors to see the 10K brought to life, to see the numbers and the charts and the graphs, and to see the people who really drive it all. That's what investors want time after time: to hear from the people who run the business day to day."

The result of her labor, and in collaboration with Suka and their partner, Tribe Pictures, is a microsite with video, interactive charts, slide shows, and — for those who do prefer to read — easily accessible links to full-length documents. Users can decide how they would like to consume the information by selecting tabs to learn more about the various aspects of the company including Stanley's business segments and growth

8 The Use of Online Quarterly and Annual Report Information: Who Uses What and When? July 2004. Frank Hodge, University of Washington Department of Accounting, and Maarten Pronk, Tilburg University Department of Accounting and Accountancy

9 Stewart, Neil. "Stanley Black and Decker Launches Video Annual Review." *IR* magazine. p.8. June 2010.

strategy. The site even includes a tab for the company's financials, which includes the CFO in a video segment explaining past performance and strategy moving forward.

And speaking of video, the site actually includes nine video segments that really do bring the company to life, as was White's goal. The clips feature the senior management team and various business heads.

The clips are shot documentary-style with scenes of the company — shots of life on the factory floor, etc. — inserted behind those speaking on film. The first video features Stanley CEO John Lundgren, who sums up the benefits of the interactive report: "We've created the site to give you access to information in a way that's more interactive, cost-effective and better for the environment."

STANLEY BLACK & DECKER BY THE NUMBERS: REAPING THE BENEFITS

Drove traffic to website:

More than 6,600 visits in the first three weeks after launch, and now is raking in 220 visits each day on average.

Environmentally friendly (from letter to shareholders):

"We estimate that reducing the size of this report and using recycled paper has saved approximately:

- / 191 trees
- / 81,211 gallons of water
- / 8,981 pounds of waste
- / 17,684 pounds of net greenhouse gas
- / 135,417,920 BTUs of energy

HURDLES

Making the transition to an interactive report requires senior-management buy-in. White's advice is to remember that "Every executive holds onto something different about the printed annual report," she explains. "Our CEO, for example, saw the annual report as a great recruiting tool, so we had to remember that when working on the videos."

Remember that your executives may not feel comfortable speaking in front of the camera, so it's important to be sensitive to that and budget plenty of time for rehearsal. It's a delicate balance, however, between appearing comfortable on camera and looking like you're performing a recitation in 10th-grade English class. In White's case, senior management was given access to approximately 80 percent of the questions before the shoot; enough to make them feel prepared while still allowing for some spontaneity.

Buy-in from the legal department is important as well, in order to avoid running afoul of any material omissions or disclosure rules. You need to be careful that what is said on video does not require filing a script or the so-called "fair and accurate description" of the multimedia, as it can be difficult and time-consuming to do so. In advance of any filming, scripts should be approved by the legal department. This will also prevent wasting management's time with re-shoots.

ANNUAL REPORT AS CORPORATE CAMPAIGN WEAPON

The past two years or so have seen a slew of regulatory and legislative changes that have companies worried about retail voters. Traditionally, at the annual meeting, retail voters vote with management. Depending on the makeup of an issuer's shareholder base, this population of investors helps ensure that dissident proposals are voted down and do not disrupt the running of the company. Dwindling participation among retail investors could give activist investors a louder voice at the proverbial ballot box.

These changes put increased pressure on companies to step up their outreach efforts to ensure the retail community is voting come time for the annual meeting. This means, as a campaign tool, the annual report is more important than ever. Given the large number of retail investors online, a well-executed annual report could be the key to getting out the vote, so to speak.

The bottom line is that demand for web-based annual reports is growing, and shareholder outreach is as vital as ever. That does not mean print is dead. But, as the SEC's e-proxy rule noted, two distinct formats are needed: one for those who prefer to print the report and one for those craving an online, interactive experience. When it comes to an online version that resembles the printed report, Dilbert may have articulated it best when he quipped, "Bring me a hard copy of the Internet! I need to do some serious surfing."

In all seriousness, when you are creating the print and interactive versions, it is important to ensure the company's message remains consistent across both channels. The annual report is perhaps the company's most important tool when it comes to communicating its message, and in today's noisy online world, the interactive report cuts right to the chase. Print should still remain a key component of your communications strategy, but the growing online audience cannot be ignored. ///

Suka is an award-winning strategic marketing and design firm based in New York City. A thought leader in corporate branding and design for almost 20 years, the Suka team has engaged clients in longtime partnerships to deliver award-winning annual reports and interactive solutions for a wide range of industries, including Fortune 300 companies, financial firms, not-for-profit organizations, and institutions of higher education. For more information about Suka Creative, please visit www.sukacreative.com or contact Susan Karlin, President at skarlin@sukacreative.com or 212-219-0082, ext. 123.

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