



# Corporate culture

Do companies not only talk the talk but also walk the walk?

Dr Joanna Nash, Dr Wang Chun Wei

**C**orporate culture is a powerful dynamic in a company. It is the set of beliefs and attitudes about the way things are done in an organisation or, more formally, the “set of values and norms widely shared and firmly held by members of an organisation”.<sup>1</sup> It shapes a firm’s internal environment and influences the decision-making and behaviour of management and employees.

It is widely accepted that corporate culture is driven by the top, that is, the board. The board sets the tone of the organisation, which filters through to management and employees. While not necessarily at the top of a board meeting agenda, we believe corporate culture permeates through an organisation’s decisions and actions.

Further, culture matters to a firm’s performance as it acts as a social control mechanism over employees’ behaviours via peer influence. What do we mean by this? Consider the following example.

A person works in a firm where everyone clocks on at 9 am and clocks off at 5 pm, not a minute earlier or later. If that person comes into the business as someone who is willing to put in extra hours, or arrives early or stays late, as they observe those around them and the common practice, they will sooner or later likely start conforming to the culture and come at 9 am and leave at 5 pm. The culture will set a tone for how that person will work—and they will evolve into that same process.

Likewise, if an employee shirks at work while those around them are diligently working, again the social pressure from the culture will likely mean that they will change their work habits to adapt to this culture and improve their productivity. The way that the employee’s behaviour can change speaks to the power that a good corporate culture can have on a firm.

This makes it a driving factor in an organisation’s success and may be attributable to stock outperformance. Therefore, it is a key consideration for investors, along with the ability to differentiate firms based on those with strong corporate culture and those without.

## The challenge of measuring corporate culture

Despite its importance for a firm’s success, corporate culture is notoriously difficult to measure. In our view, commonly used objective metrics of other aspects of a firm’s performance, such as sales numbers or percentage of women board members, do not provide meaningful insights.

Employee surveys may offer insights, but do not work for cross-company comparisons because methodologies and measures vary, they are not always conducted regularly, and results are often not publicly available. Employee rating sites (for instance, Glassdoor) may give a view of employee happiness, but do not necessarily reveal the true culture of an organisation.

## A unique approach to accurately capturing corporate culture

RQI Investors uses a unique approach to measure the strength of a firm's culture. This method involves assessing conference calls by analysing the way management speaks. We then analyse company attributes related to the language and themes that emerge during these calls, before going on to consider whether we can capture stock outperformance by trading on this information.

To do this, we have used a specialist 'culture' dictionary based on five dimensions of corporate culture: *innovation*, *integrity*, *quality*, *respect* and *teamwork*, identified as the most mentioned company values in the corporate websites of firms in the S&P 500.<sup>2</sup>

## Values and attributes that make up corporate culture and how these are analysed

At a high level, based on this 'culture' dictionary, the values seen at play, as extrapolated from the from the five key dimensions of corporate culture are shown in Table 1.

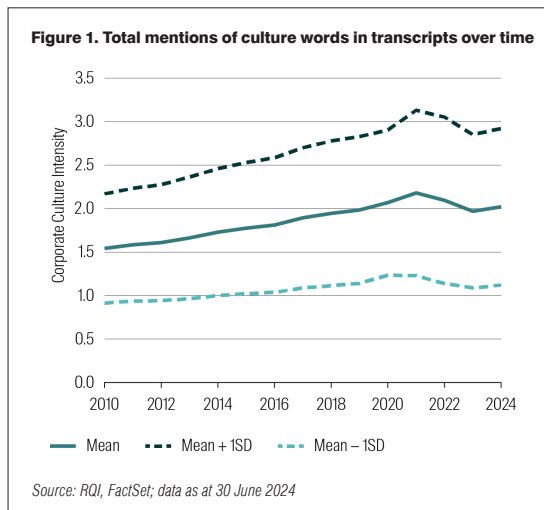
**Table 1. Word associations with different values**

Dimensions	Associations
Innovation	Creativity, efficiency, excellence, passion, pride
Integrity	Ethics, fairness, honesty, responsibility, transparency
Quality	Customer relationships, dedication, product quality
Respect	Leadership, professionalism and talent
Teamwork	Collaboration, cooperation, leadership, professionalism

Source: Li et al. 2021

Using the culture dictionary, we look at different parts of the conference call—the prepared management section, then the Q&A section where analysts can ask questions without notice.

The difference in how company management talks between these sections is informative in determining if



corporate culture is truly embedded in the firm or simply lip service.

Our corporate culture score focuses on consistency of corporate culture in different sections of the call.

In our view, the more spontaneous and less scripted the language used, the more likely it will accurately reflect the culture of the company compared to other potential data sources such as company websites, annual reports and so on, which contain more scripted 'PR' talk.

Looking firstly at some of the basic data analysis, Figure 1 shows that total mentions of culture words within conference calls have increased over time.

Going further, when we look at the five underlying corporate values, we can also see that different industries have a focus on different corporate values. This is not surprising.

For example, IT firms and communication services have more mentions of innovation, but financials talk more about integrity (probably to address previous issues). The distribution of mentions by sector for the five corporate values are shown in Figures 2 to 6.



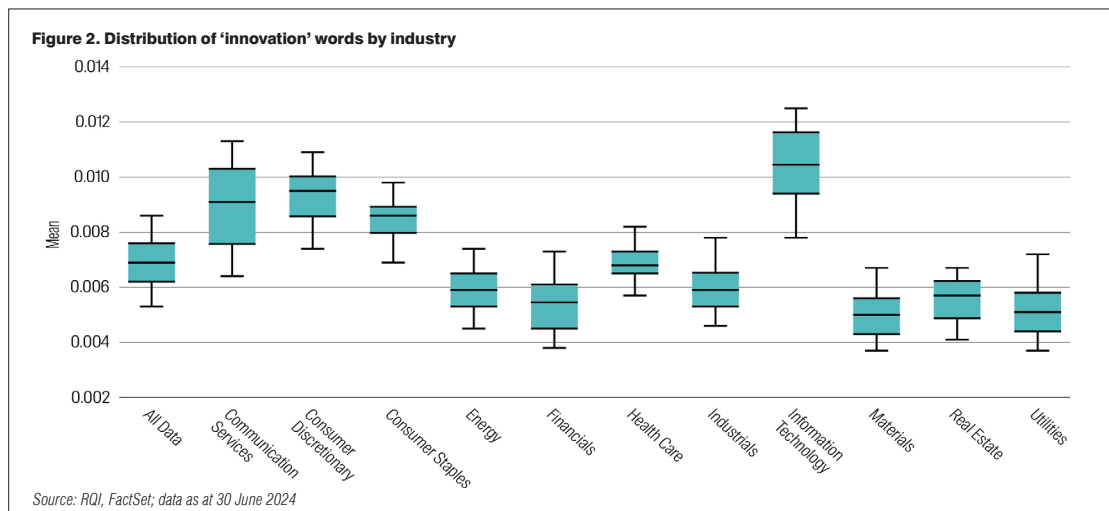
**Dr Joanna Nash, RQI Investors**

Joanna is a senior quant portfolio manager and head of portfolio management at RQI Investors. She holds a PhD in Economics from Yale University, a Bachelor of Laws and Economics (Honours) from the University of New South Wales, and is a CFA charterholder.



**Dr Wang Chun Wei, RQI Investors**

Wang Chun is a quantitative portfolio manager at RQI Investors. His qualifications include a Bachelor of Commerce (Honours) in Actuarial Studies from the University of Melbourne, a PhD in Finance from the University of Sydney, and is a CFA charterholder.

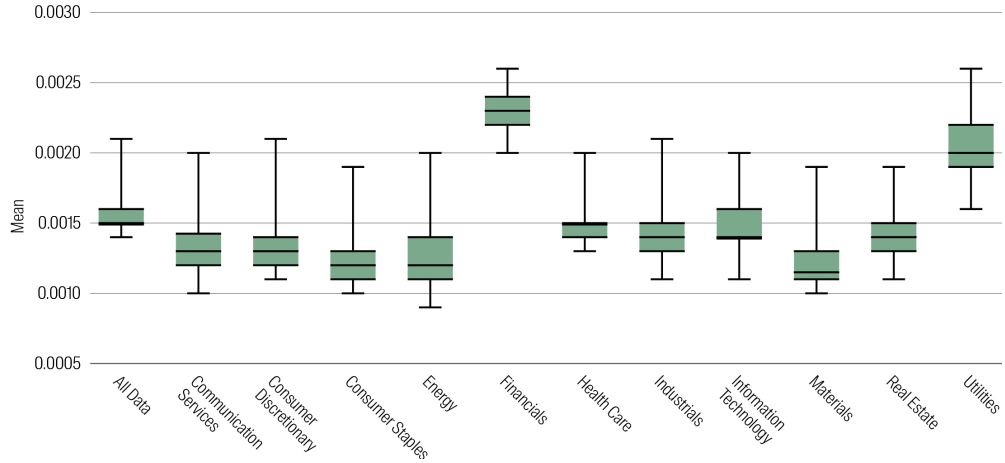




**The quote**

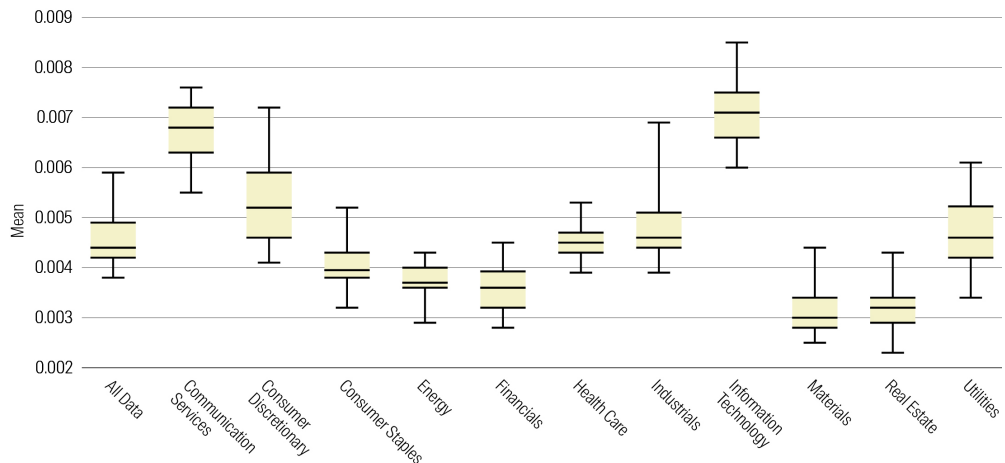
*Despite its importance for a firm's success, corporate culture is notoriously difficult to measure.*

**Figure 3. Distribution of 'integrity' words by industry**



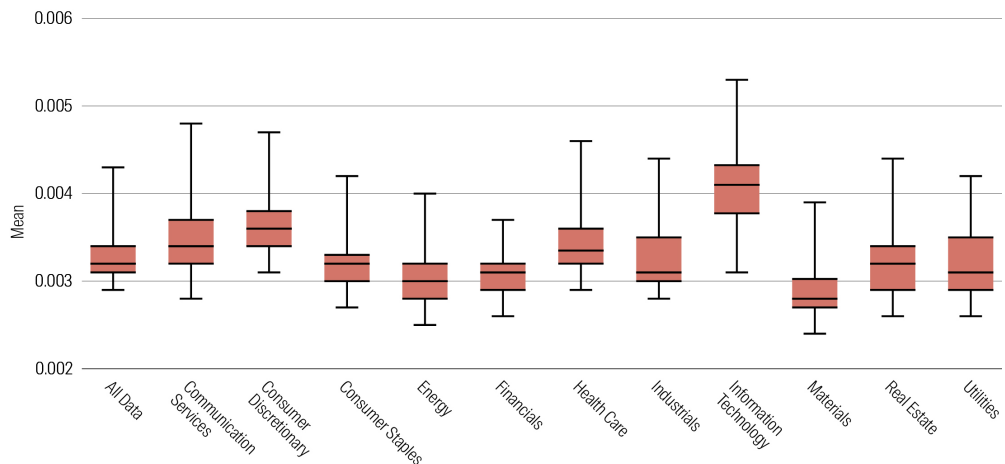
Source: RQI, FactSet; data as at 30 June 2024

**Figure 4. Distribution of 'quality' words by industry**



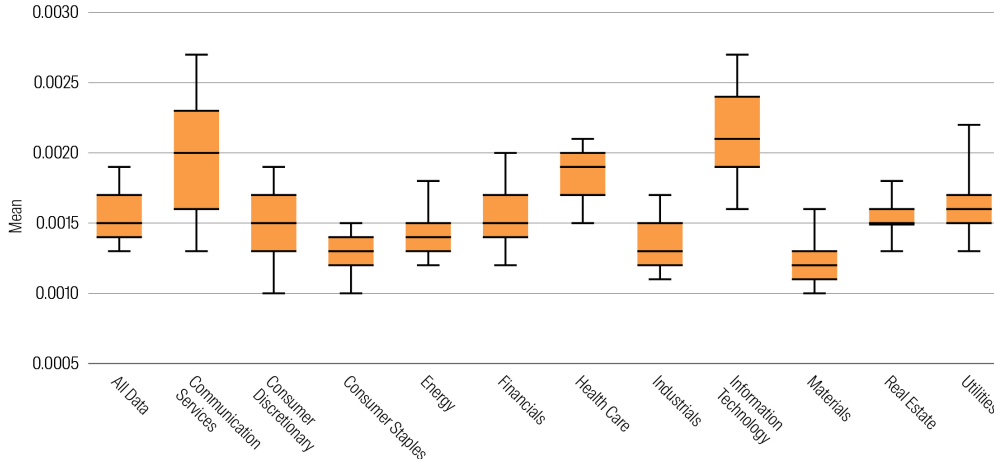
Source: RQI, FactSet; data as at 30 June 2024

**Figure 5. Distribution of 'respect' words by industry**



Source: RQI, FactSet; data as at 30 June 2024

**Figure 6. Distribution of 'teamwork' words by industry**



Source: RQI, FactSet; data as at 30 June 2024

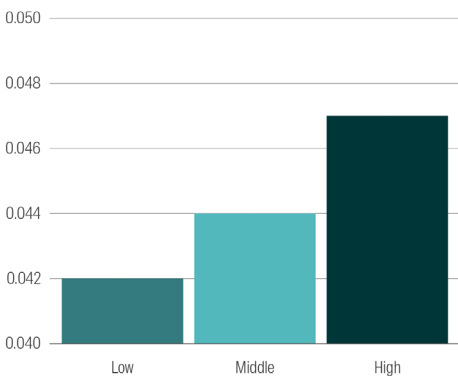
These figures show the distribution of the mentions, with the box representing where the middle 50% (also known as the interquartile spread) of the mentions lies.

### Stronger culture can be equated with higher quality and lower risk

Having determined a way to measure corporate culture, we naturally follow the data to assess if better culture is, in fact, a characteristic of higher-quality, less-risky and lower-volatility companies.

To do this, we split companies into three groups, those with low, middle and high culture scores, and looked at the average return on assets (ROA) as a proxy for quality, and volatility as a proxy for risk. The results are shown in Figure 7.

**Figure 7. Average ROA of firms split by corporate culture score**

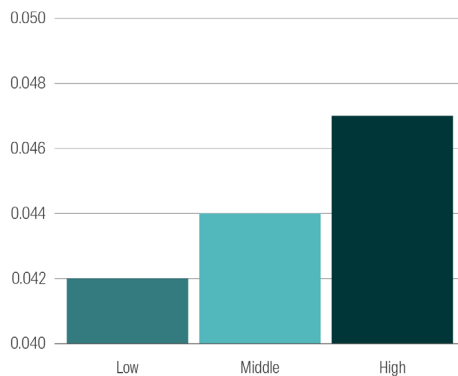


Source: RQI data, January 2010 to June 2024

What we found is, that as the score for culture increases so, on average, does the return on assets (ROA) for those firms, showing that organisations with better culture tend to be of better quality. In our study of firms

within the MSCI All Country World Index that trade in North American or European markets, we also saw that firms with higher culture scores had lower volatility, showing that they are lower risk. This is seen in Figure 8.

**Figure 8. Average volatility of firms split by corporate culture score**



Source: RQI data, January 2010 to June 2024

### Trading impacts: Tilts to strong culture can support outperformance

Having established the link between corporate culture and positive attributes regarding quality and risk, we went further, backtesting<sup>3</sup> to see how this information would play out in real market conditions.

To do this, we constructed an optimised portfolio tilting toward firms with strong culture and away from those with weaker culture. Given the culture dictionary used is in English, our universe included stocks within the MSCI All Country World Index that trade in North American or European markets,<sup>4</sup> comprising around 1,000 stocks and covering approximately 80% of the relevant market cap. This is what was used as the benchmark in Figure 9.



**The quote**

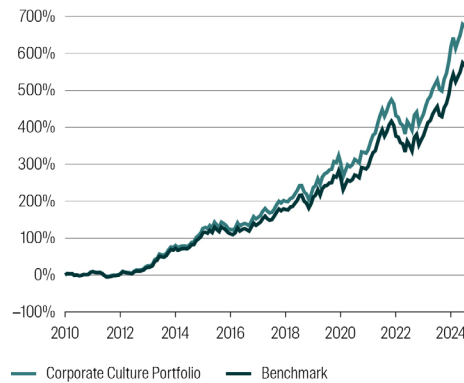
*The more spontaneous and less scripted the language used, the more likely it will accurately reflect the culture of the company...*



### The quote

Over the nearly 14-year period in question, the corporate-culture-tilted portfolio outperformed the benchmark.

**Figure 9. Backtest performance of long-short portfolio**



Source: RQI data as at 30 June 2024

Over the nearly 14-year period in question, the corporate-culture-tilted portfolio outperformed the benchmark. Such consistency of performance shows that strong corporate culture is indeed a company attribute that is rewarded by the market. This outperformance amounts to just over a 1% excess return p.a. over close to 14 years.

### Conclusion

The insights outlined clearly show that firms with the strongest cultures, analysed using a curated dictionary of words proven to be linked with important corporate values, perform better than their counterparts. This superior performance can be seen not only in terms of quality and risk, but also in a pattern of consistent out-performance relative to the market.

RQI Investors is confident that the approach described here represents an effective methodology to measure corporate culture and use the resulting insights to help guide better investment decisions. **FS**

*Previously published on RQI Investors' website. Please see [here](#) for the full disclaimer. Suitable for institutional and wholesale investors.*

### Notes

1. O'Reilly C, 'Corporations, culture, and commitment: Motivation and social control in organizations', *California Management Review*, vol. 31, issue 4, July 1989, pp. 9–25.
2. Li K, Mai F, Shen R, & Yan X, 'Measuring corporate culture using machine learning', *The Review of Financial Studies*, vol. 34(7), July 2021, pp. 3265–3315; using word2Vec (Mikolev et al. 2013); Guiso L, Sapienza P, & Zingales L, 'The value of corporate culture', *Journal of Financial Economics*, vol. 117(1), pp. 60–76.
3. Backtesting is a quantitative method used primarily to evaluate the historical performance of a trading or investment strategy by applying it to past market data.
4. As we currently only have English conference call transcripts, there was limited coverage for Asia and the emerging markets.