THE REAL VALUE OF REPUTATION

It takes just a single incident to shatter a company’s reputation. To avoid such situations, communicators need to take a strategic role in shaping public perception

by Charles J. Fombrun and Jonathan Low

Our purchasing decisions are governed by two factors: our perceptions of the features of the products or services we are interested in buying, and our perceptions of the companies that stand behind them. Marketers have spent their careers (and virtually all of their advertising budgets) trying to influence the first of these two factors. However, evidence is mounting that the second factor may be even more influential than the first.

Each year Reputation Institute measures consumer perceptions of the world’s largest companies. The results are scored using the RepTrak model, which aggregates consumer perceptions based on their assessments of a company’s products/services, innovation, workplace, leadership, governance, citizenship and financial performance. Statistical analysis of the results in 2011 showed that product perceptions explained only 39 percent of people’s purchase intentions. In contrast, 61 percent of their purchase intentions were explained by their perceptions of the companies behind those products. A similar pattern was found when Reputation Institute’s analysts examined consumer advocacy—the likelihood they would recommend a company’s products and services. Only 42 percent of consumers’ recommendations could be explained by product perceptions, whereas 58 percent could be derived from perceptions of the companies standing behind those products.

These findings speak to the growing value of corporate reputation as a strategic tool that can create tangible economic value for companies by influencing the degree of support they receive, not only from consumers (the products they buy), but also from investors (the investments they make) and from other stakeholder...
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Reputations develop from stakeholder perceptions about companies. To build reputational assets, companies are increasingly involved in measuring the strength of those perceptions using carefully calibrated and comparative scorecards. These scorecards can then be used to benchmark how perceptions across a company’s stakeholders, markets and divisions compare with selected rivals. This kind of research is increasingly relied upon by the C-suite to examine the underlying factors that drive the purchase decisions of consumers, the investment decisions of investors and the workplace choices of employees.

Armed with a precise understanding of their target markets, heads of marketing are in a strategic position to develop relevant communication platforms and optimize allocations to the paid and earned media coverage they get for their companies and brands. So too are the heads of finance and human resources. A strategic investor relations program can be developed to generate favorable perceptions of the company from current and potential investors. A strategic employee relations program can be designed to convey the attractiveness of the company’s workplace to existing staff and potential recruits.

Overall, a strategic reputation management program integrates all of these efforts across the company, and when effectively implemented, is the driving force behind tangible economic returns.

—C.J.F. & J.L.

An integrated program can help create a positive corporate image

Accounting for reputation capital

The value of a company resides in its stock of physical and financial capital, as well as in the human, organizational, intellectual and brand-based assets it possesses—what accountants describe as the company’s intangible assets. Economists estimate that intangibles may account for up to 80 percent of a company’s market value. Institutional investors have reported in a well-cited survey of 575 analysts released by Capgemini Ernst & Young back in 1996 that more than 35 percent of their portfolio allocation decisions were based on intangibles. A Forbes report on the “25 Most Valuable U.S. Corporate Brands” (a list that included such companies as P&G, Coca-Cola and General Electric) demonstrated that some corporate brands are even more valuable than their parent companies’ market capitalization—the total value of the company’s shares traded on the world’s stock exchanges.

Several recent examples illustrate the interrelationship between reputation and financial performance. On the negative side, News Corp., Citigroup, BP and Toyota have suffered stock price, earnings and market-share erosion as a result of events that have seriously damaged public perception. On the positive side, Ford, Tata, Apple, Petrobras and LVMH are showcase examples of the financial benefits—and reputation gains—that can be traced to improved public perceptions of both their products and companies.

Consider BP, which crafted and promoted the message that its two initials stood for “beyond petroleum” and that it represented the responsible, forward-thinking face of contemporary energy policy. But the April 2010 Deepwater Horizon explosion and the massive oil spill that
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followed for weeks afterward in the Gulf of Mexico belied the company’s claims of heightened concern for safety and environmental awareness. Self-destructive communications from the company reinforced impressions of arrogance and evasiveness. A toxic concoction of weak public relations and images of befouled wildlife sanctuaries further damaged BP’s reputation.

The demands of global markets, with their emphasis on comparability of data, adoption of standards and increased transparency, are requiring institutions in the private, public and nonprofit sectors to provide ever more information about their allocations of people and capital. In this acutely competitive environment, where knowledge is capital, perceptions matter more than ever—and so have become the new battlefields on which companies and stakeholders are waging war. Because perceptions are malleable, they are also subject to strategic influence and manipulation. The fact that most companies have only a superficial understanding of the perceptual components of their reputations is a significant risk. The sustainability of an organization—its very license to operate—may depend on how financial, reputational and human capital markets come to perceive and value the decisions and investments they make.

In BP’s case, weak answers to questions about its handling of mundane operational issues metastasized into a figurative indictment of its attitude toward the environment and its commitment to safety. This spiraled into a challenge to its competency, its management capability and, ultimately, its corporate culture. Suddenly, the much-dreaded “license to operate” phrasing began to be heard, questioning the legitimacy of the company’s operations not only in the U.S., but around the world, particularly in Russia, where the company’s joint venture, TNK-BP, was threatened. (Never secure in this partnership, BP’s Russian financial partners in the deal sensed the company’s weakness and moved to exploit it, eventually negotiating a deal with government-controlled Rosneft, and wresting effective control of the joint venture from BP.) In due course, BP CEO Tony Hayward, who was evidently ill-prepared to deal with all of these reputational exigencies, had to be pulled out.

BP’s annus horribilis is reminiscent of Shell’s conflict with the activist NGO Greenpeace in 1995 over the sinking of the outdated Brent Spar oil rig in the North Sea. It also mirrors the experience of Coca-Cola in 1999, when a small batch of carbon dioxide used in the drink allegedly caused some Belgian schoolchildren to feel sick. Both Shell and Coca-Cola watched their share prices fall precipitously as a result of these crises, and had to deal with boycotts of their operations, delays in their implementation of strategic initiatives and wholesale shifts in their leadership.

Global forces are causing shifts in public perceptions of companies that in turn drive changes in regulatory, political and financial structures around the world. Companies that enjoy strong and favorable reputations have a competitive advantage in these global markets. Iconic brands and exemplary reputations help companies “translate” their offerings to new customers, because the values they embody provide a shorthand interpretation of what they have to offer.

Corporate communication, therefore, has a strategic role to play in shaping public perception, and thereby indirectly influencing value creation. Since the returns to communication and transparency are increasing, investments in reputation building and management are becoming strategic contributors to the bottom line.

Reputation and brand, however, require continued and costly upkeep if they are to deliver results. Failure to maintain the connection between corporate action and corporate communication is a risky proposition.

Apple makes a positive case for reputation management. The company tied Google for the No. 1 spot in the RepTrak 100, a global rating by more than 50,000 consumers across 15 countries that Reputation Institute released in June. Apple has triumphed by continuously exceeding expectations as an innovator. From the Macintosh to the iPod to the iPhone to the iPad, the company has repeatedly introduced products that anticipated market needs with well-designed and exceptional technology. With each product introduction, consumers have paid a premium for the privilege of owning a product that redefined not just the category they were in, but entire industries. The iPod changed the way people thought about acquiring and playing music. The iPhone reinvented telecommunications by
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blending phones and computers, and the iPad has redefined the notion of computerized mobility. These strategic coups have eliminated numerous competitors and reduced related businesses to the role of supplicants.

As Apple’s reputation for innovation has grown, so have its financial results—and the financial markets have followed suit. Eye-catching design and exceptional functionality supported premium pricing that created profits. Profitability, in turn, enabled accelerated research, more innovation, market share expansion and competitive dominance, and delivered outsized financial results. On 19 July, Apple announced its second-quarter results: an astounding sales growth of 83 percent and profit growth of 92 percent. The company exceeded financial analysts’ projections by almost 34 percent, and conveyed the promise of future growth in an as-yet untapped market, China.

Reputation management is strategic management
As we have described here, reputation can be a vital source of intangible value that, if optimized, can contribute significantly to creating tangible financial value. Although intangible, reputations are, in fact, quantifiable, measurable and manageable. Failure to properly account for reputation—both literally and figuratively—is very likely to damage a company’s results and prospects.

Reputations are, therefore, a vital component of strategic management—and, not surprisingly, top-rated companies have begun to manage them as such. For these vanguard firms, reputation is a key component of a value-creating cycle: When properly managed, it represents the economic returns of past investments made to create value and build competitive advantage. Once established, a good reputation acts like a magnet in attracting stakeholder resources and solidifying a company’s competitive strategic position. When damaged, however, a weak reputation drives away customers, repulses investors and mars performance. BP’s multiple stumbles over the past decade demonstrated the dangers of failing to manage reputation strategically. Apple’s impressive ascendancy showcases the benefits of actions that have built both reputation and performance.

about the authors
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