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How corporate reputation influences the value of businesses in the age of social media

> "It takes twenty years to build a reputation and five minutes to ruin it."

Warren Buffett

Reputation has always been a quality cherished by business leaders. However it has arguably never been more volatile. The internet, consumer generated feedback and social media have created an environment in which seemingly modest transgressions can have widespread consequences, and where a single serious incident can cause long-term or perhaps terminal damage to a firm. Today's news is no longer tomorrow's chip paper – the online corporate testament lasts a good deal longer.

Against this backdrop there is a growing awareness in the boardroom of the importance of understanding and measuring a company's reputation. However, despite this, active strategies to track, protect or enhance corporate reputation are still not the norm. Recent research undertaken amongst FTSE 350 companies by YouGov for SIFA Strategy, in conjunction with Deloitte LLP, suggests that only a third of large corporates in the UK use reputation as a key business driver integrated across all stakeholders, with only half of them measuring it and linking it to business outcomes.

SIFA's findings echo a US survey[1] which found that "*95% of chief executives surveyed believed that corporate reputation plays an important or very important role in the achievement of business values, yet only 19% had a formal system in place to measure the value of their corporate reputation*". The Reputation Institute's 2014 study of reputation leaders[2] found that only 16% of business leaders felt that their organisation had the full capabilities to manage reputation, despite 65% of business leaders saying that reputation was a top priority for executives and the Board of Directors.

Ben Morton, Director of SIFA Strategy, notes: "*Research clearly shows that businesses are increasingly aware of the importance and the value of reputation. The crucial next step is enabling companies to better manage and understand reputational performance and to link this to business outcomes and shareholder value creation*."

1 Kim Harrison, Why a good corporate reputation is important to your organization, Burson-Marseller

2 The Reputation Institute, Playing to Win in the Reputation Economy, 2014 Annual Reputation Leaders Study, June 2014

Part of the problem with taking this next step relates to the difficulty of pinning down the contribution of reputation to profits and value. While some existing services (such as YouGov's Brandindex) provide a way of assessing the public perception of brands, which can be closely related to reputation, they do not provide a translation of the concept across to hard financial metrics. Respondents to SIFA's survey typically estimated that between a third and a half of their company's value is accounted for by its reputation. Across the FTSE350 this represents a huge pool of value that management teams believe is linked to reputation. But what is the form of this link, and where on the balance sheet does this value lie?

The inconvenient answer is that it is highly complex, and varies company by company. Large corporates will have many stakeholders, each with a different perception of the firm's reputation and a different route through which this will affect value. For example, for a business led by strong consumer brands, there is an obvious connection between reputation and the value of the brand and associated intangible assets. However, the same company's reputation with suppliers will also be critical. This may manifest in better terms of business, or a more secure supply. The company will also have important relationships with retailers, the longevity and terms of which affect the value of the customer relationship intangible. The company's reputation with other stakeholders such as debt providers, regulatory bodies and even the Taxman will all contribute positive or negative influences on value in different ways.

A company's sensitivity to changes in one or all of these factors will influence how much value is related to reputation. Some sectors (e.g. those where product switching barriers are low) will be more sensitive to changes in reputation (both positive and negative). On the supply side, enterprises with significant market presence may be relatively immune from a changing reputation amongst their suppliers.

The key to understanding the value of reputation to an enterprise is to understand the range of stakeholder factors, the assets affected, and their sensitivity to changes in reputation. This can then be mapped onto a fully inclusive balance sheet using slight modifications to standard (usually intangible) asset valuation techniques[3]. This can be used to provide both the aggregate value related to reputation and also granular information regarding the level of value related to different reputational factors and their influence on different assets.

Although this appears a complex approach, much of the analysis is that which is already done for different purposes. As Doug Eastman, intangible asset valuation specialist at Deloitte comments, "*Historically, enterprises would typically only formally calculate the value of brands and trade names for post-acquisition accounting, which requires the valuation of the intangible assets of a purchased business. Recently, we ind ourselves working more and more with enterprises in assisting them to determine the value associated with their internally-developed intangible assets for strategic planning purposes. We find that when clients quantify the value of these existing intangible assets they reveal intriguing characteristics they had not previously observed.*"

Once the connection between value and reputation is made, it can then be tracked and used for targeting strategy (for example, price optimisation) or linked to boardroom remuneration. If the results of the analysis support the value of reputation estimated by respondent's to SIFA's research, it will also serve to sharpen the focus in the boardroom on protecting reputation and taking steps to limit the risk of becoming tomorrow's social media viral victim.

3 A fully inclusive balance sheet differs from an accounting balance sheet in that it reflects the market value of all assets, tangible and intangible, as well as goodwill. It would be the equivalent to the balance sheet recorded for an acquired business unit under International Financial Reporting Standards

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