The impact of quality on brand and reputation

Finding the right balance to sustain value and support the company's bottom line

By Kaiwen Cheng

Many people say management should care more about quality because a lack of quality could damage brand image and brand reputation. The same group of people is also likely to say that management has not done enough to protect the brand.

Of course, I agree 100% that we should protect the brand image and reputation, but not all actions are justifiable. The No. 1 priority for management is to sustain the business financially. It is the responsibility of the professionals to provide information that can help management justify its decisions. Therefore, this is a "two-way" street between management and professionals. It is fair to say that management relies on the quality professionals to demonstrate the relationship between brand and quality.

People take action only where there is justification. I am certain most people in business would tell you brand reputation is critical, but having a sustainable business is critical, too. Therefore, the balance between cost and brand is a critical question.

Using the iPhone 4 reception issue back in 2010, as an example, it was certainly a brand image issue when people were upset about having reception problems with the new phones. There were tons of complaints and sales were suffering. It takes no effort for me to argue this was a quality issue, because it was.

Should Apple have treated this as a product quality issue and demanded that engineers fix the phone? It seems logical. But how did CEO Steve Jobs fix the problem? He told consumers, "You are holding the phone wrong."

Surviving brand damage

The decision Jobs made to survive the crisis during the 2010 launch was a balancing act between brand image and cost. Let's re-examine this case.

Did the brand image get damaged? Yes.

Did the company choose to fix it? No.

Would the cost have been very high if the company had chosen to fix it? Yes.

Did Apple have a strong enough brand that its customers were willing to tolerate it? Yes.

Was the decision correct in the end? Probably. After all, Apple went on to become the company with the highest market capital in 2018 for a short time, and it was considered to be the most valuable brand in 2018 (see Figure 1). My observation is that Apple paid the price on the brand, but it still cost less than fixing it. This is a good case where even if "it is the right thing to do" to fix a quality issue, it still may not be justifiable.

Samsung's premium Note 7 smartphone is a different good example. Its faulty batteries caused fires when it was introduced in 2017, a confirmed quality issue that led to the global recall and rerelease of its phones. Samsung Electronics Co. said its net profit fell 16.8% to 4.54 trillion Korean won ($4.0 billion) in the third quarter of 2017. The company's mobile division reported its smallest quarterly profit since it launched its first Galaxy series phone more than six years ago. The overall recall cost was reported at $5.3 billion.

In this case, there was a clear cost associated with quality defect. It was too bad the problem wasn't identified prior to product release. Samsung took the right approach with the recall before more failures occurred. I can imagine a Samsung quality engineer saying "the global recall may be expensive, but it is the right thing to do to prevent the brand damage." Due to the potential safety concerns, the cost of damage would have been too high to pay, and the brand damage would have become uncoverable.

By looking at Samsung's overall profit and revenue right now, it is clear Samsung reduced the brand damage with a well justified but significant cost (see Figure 2).

FIGURE 1

Apple's core success

The increasing brand value of Apple for a decade prior to 2018.

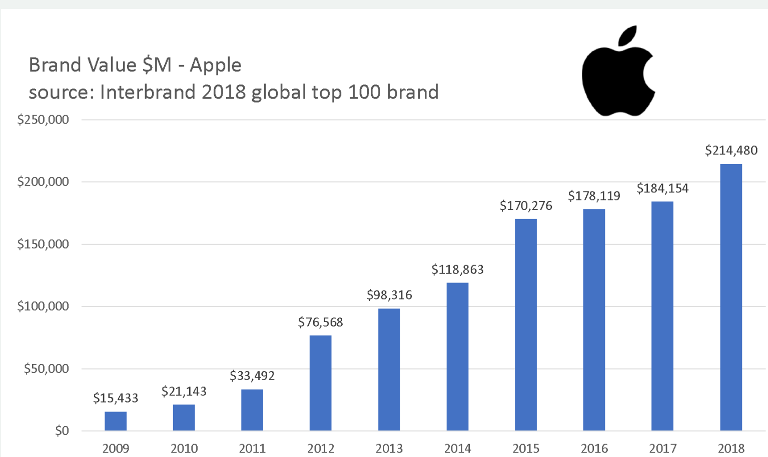
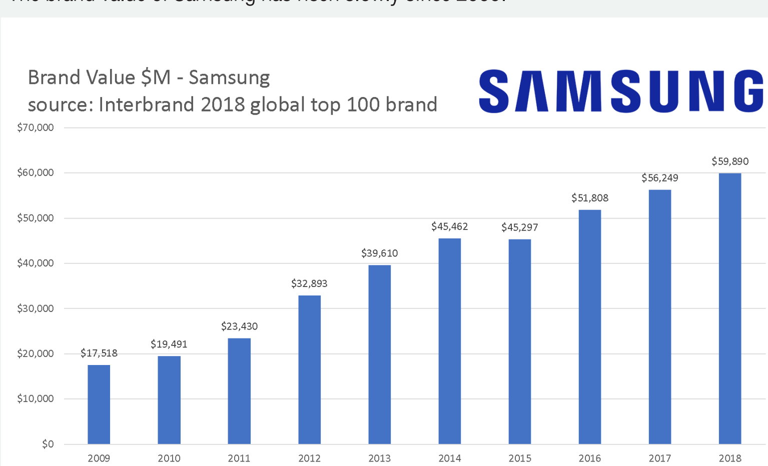


FIGURE 2

Samsung's steady tune

The brand value of Samsung has risen slowly since 2009.



Brand value 101

The clear pattern between these examples is in the balance between the cost of fixing quality issues and potential brand damage. Therefore, it is extremely valuable to develop a cost estimate of the potential impact on brand value, even if it is not precise.

But how? Start by ensuring your organization has an understanding of brand equity or brand valuation. ISO 10668 "Brand valuation – Requirements for monetary brand valuation" is a great starting point that helps organizations assess or understand their own brand values.

A brand value can be assessed by three different approaches: income approach, market approach and cost approach. The income approach primarily focuses on assessment through evaluation of the brand impact on sales, acquisition or pricing that is reflected in cash flow. For example, a premium brand such as Gucci or Mercedes-Benz (see Figure 3) has greater freedom in its pricing strategy to

FIGURE 3

Pricey ride choices

Mercedes-Benz's status as a premium brand gives it more flexibility in pricing strategy than its competitors.

Midsize Sedans Price Difference		
	**Mercedes-Benz E-Class**	MSRP $52,950 - $104,400
	**BMW 5 Series**	MSRP $53,400 - $74,450
	**Toyota Camry**	MSRP $23,845 - $34,600
	**Chevrolet Malibu**	MSRP $21,680 - $30,974

set higher prices. Such an advantage directly benefits a company's income level. In other words, for two companies with the same level of operating efficiency, the premium brand would have a higher profit margin.

The market approach compares similar brands. Think housing market, where your sales price is close to comparable houses sold in your neighborhood. Therefore, businesses can use deals among similar brands to establish their own brand valuations. The cost approach measures the value of a brand based on the cost invested in building the brand, its replacement cost or its reproduction cost.

In the Samsung Note 7 example, the recall cost was reported as $5.3 billion. Considering that the recall avoided potential lawsuits resulting from human and property damage, it prevented further deterioration of its $59 billion brand value. This cost estimate can be used as the basis to confirm the brand valuation.

There are a lot of financial details involved in properly defining a company's brand equity, but for most, the focus would just be on the concept of brand valuation itself. If you plan to make a point by using the brand image or brand reputation as a justification for anything, it would be a good idea to understand how your investments or projects can add value to the brand.

Leadership and brand image

Brand valuation studies have clearly confirmed that a brand is an intangible asset. Then why doesn't management always take action to prevent damage to its brand or reputation? The most logical explanation is that it can't justify the cost of action to prevent damage.

Here is a made-up example based on my experiences. Let's suppose Company X is a supplier for a simple sheet metal bracket. The risk of the application of this bracket is low, and the worst-case failure would result in customer dissatisfaction but will never hurt anyone. In this example, the quality engineer identified that the newly produced brackets had discoloration with slight dimensional defects. The appearance was poor, but the bracket would assemble and function without issue. Should leadership allow them to inquire with their customer about accepting these products?

There are at least two scenarios that would lead to different approaches. Scenario one: Company X understands it is chosen based on price and this customer is not one of Company X's core customers. In this case, the brand won't have an impact on its future business because the decision was based on price. Company X has a good chance to be replaced by another low-cost supplier, especially since there is low or no liability for product failure. I am sure there are many managers who would take the chance and ask their customer to accept subpar products.

Scenario two: Company X wants to have a long-term relationship and grow with this customer. It wants to be considered as the vendor for future business with more complex parts and bigger margins. In this case, the brand would have an impact on future income. It is important to build the image of the company to be one that won't ship subpar products to their customers. In this situation, leadership is likely to take action and fix the problem to maintain the brand image.

I use these scenarios to contrast decisions. Taking action to protect the brand is not only based on internal factors. A company's brand can be influenced by many external factors as well as the strategic direction defined by the senior leadership. To avoid frustration on why leadership "is not doing the right thing," you must understand the underlying drivers that influence the decision, especially when you have a desire to change the course of action.

Action plan to build brand

Let's say you are a leader in your organization who wants to promote a quality culture to improve the brand. What would you do? Below are few actions that can increase your chance of success.

1. Identify if quality is a key element of the brand.
2. Establish the multiplier for business benefit estimation.
3. Utilize the multiplier to justify projects for improvement.

Identify if quality is a key element of the brand. Quality is a measure of how closely our products and services meet customers' expectations. Based on this definition, I believe everyone would say quality is for sure an element of the brand. The reality is that this is not universally true. If you realize your company doesn't believe quality should be a key element of the brand, but you believe it should be, then my only conclusion is you probably are in the wrong company.

Establish the multiplier for business benefit estimation. Using a multiplier for project justification or prioritization is more practical because brand value is complicated to capture. A multiplier is used against the tangible direct benefits from each project or investment. Such benefits might include scrap reduction, cycle reduction or inventory reduction. The overall estimate benefit would be calculated based on the tangible benefit times the multiplier.

The logic behind this approach is each employee can be directed to perform value-added, routine or nonvalue-added tasks. By investing in quality improvement, we can refocus resources on tasks that would add value for the company or brand. There were academic studies stating the overall business benefits of quality projects could be six times as high as the tangible benefits.

There is no practical reason to lock in an exact number for the multiplier. In general, most managers expect their employees to generate benefits equaling one to four times their salaries. This is an easy concept for management.

In my own case, we presented the idea to senior leadership. Their answer was they believed six times would be a rare case, but four times is acceptable. Since then, four to six times has been used as the multiplier to performance sensitive analysis on potential return on projects, which has accelerated the project approval process significantly.

Utilize the multiplier to justify projects for improvement. After completion of step 2, this becomes very straightforward. Again, you would want to have a range of multipliers that is acceptable in your organization. The selection of multiplier(s) within the range would depend on the projected potential and the confidence. Therefore, once tangible benefits have been identified, we apply the multiplier(s) to define actual benefits to justify projects. Keep in mind there is no substitution for having data and concise communication to support a justification.

In summary, professionals can be more effective by understanding the factors of management decisions, especially for quality professionals. The seemingly right thing to do, such as protecting the brand, may not bring tangible benefits for business. The logic of brand evaluation provides a tangible measurement as a financial benchmark.

Such an approach would allow projects with intangible benefits, including quality or brand image, to be compared side by side with tangible projects. Since management's No. 1 priority is to ensure financial sustainability for the business, this approach provides a transparent and objective cost-benefit analysis without ambiguous arguments. ❖

Top-rated brands for 2019

Here are the top 25-ranked brands in Brandirectory's Global 500 2019 at *https://brandirectory.com*:

1. Amazon, United States, $187,905 million
2. Apple, United States, $153,634 million
3. Google, United States, $142,755 million
4. Microsoft, United States, $119,595 million
5. Samsung, South Korea, $91,282 million
6. AT&T, United States, $87,005 million
7. Facebook, United States, $83,202 million
8. ICBC, China, $79,823 million
9. Verizon, United States, $71,154 million
10. China Construction Bank, China, $69,742 million
11. Walmart, United States, $67,867 million
12. Huawei, China, $62,278 million
13. Mercedes, Germany, $60,355 million
14. Ping An, China, $57,626 million
15. China Mobile, China, $55,670 million
16. Agricultural Bank Of China, China, $55,040 million
17. Toyota, Japan, $52,291 million
18. State Grid, China, $51,292 million
19. Bank of China, China, $50,990 million
20. WeChat, China, $50,707 million
21. Tencent (QQ), China, $49,701 million
22. Home Depot, United States, $47,056 million
23. Taobao, China, $46,628 million
24. T (Deutsche Telekom), Germany, $46,259 million
25. Walt Disney, United States, $45,750 million

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