Quality Impact on Brand and Reputation

A basic understanding on quality value and how to influence

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Quality and Brand

Many people say that management should care more about quality because 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 number 1 priority for management is financially sustaining the business. It is the responsibility of the professionals to provide information that can help management to justify their 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 that most people in business would tell you that 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 brand new phones having reception problems. 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 Steve Jobs fix the problem? He told consumers that "you are holding the phone wrong."

Surviving Brand Damage

The decision Steve 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 correct. 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 Chart 1)*. My observation is that Apple paid the price on the brand, but it still cost less than fixing it would have. 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. It was a disaster because its faulty batteries caused fires when it was introduced in 2017. It was a confirmed quality issue that led to the global recall and re-release 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, 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 that this problem didn't get identified prior to product release. Samsung indeed took the right approach with the recall before even more failures occurred. I can imagine there was a Samsung quality engineer saying that "the global recall may be expensive, but it is the right thing to do to prevent the brand damage" at the time. 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 that Samsung indeed reduced the brand damage with a well justified, but significant, cost *(see Chart 2)*.

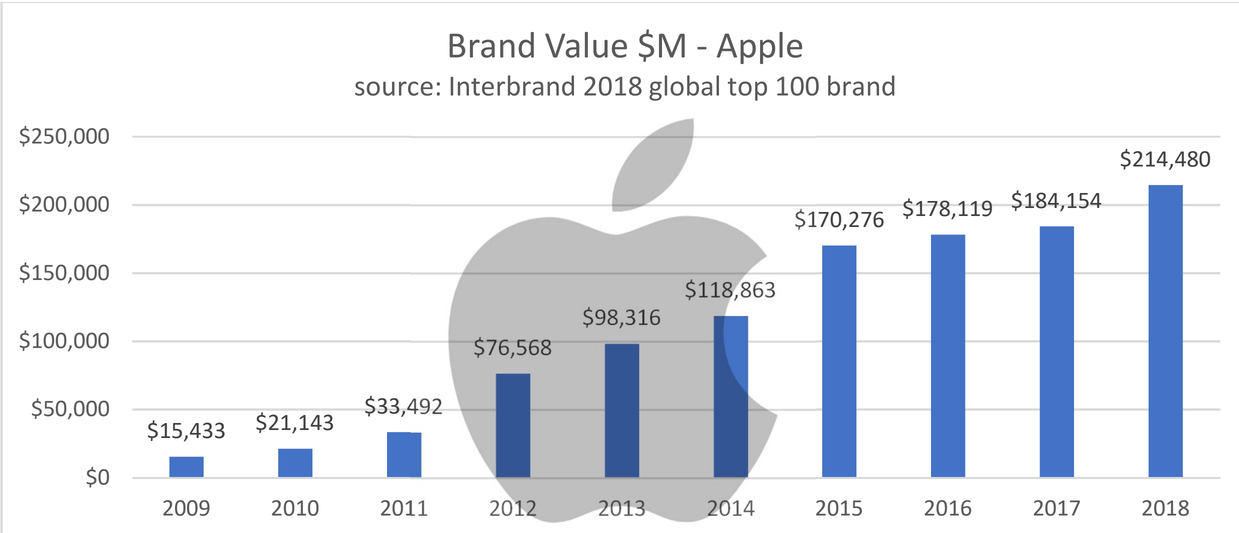

Chart 1

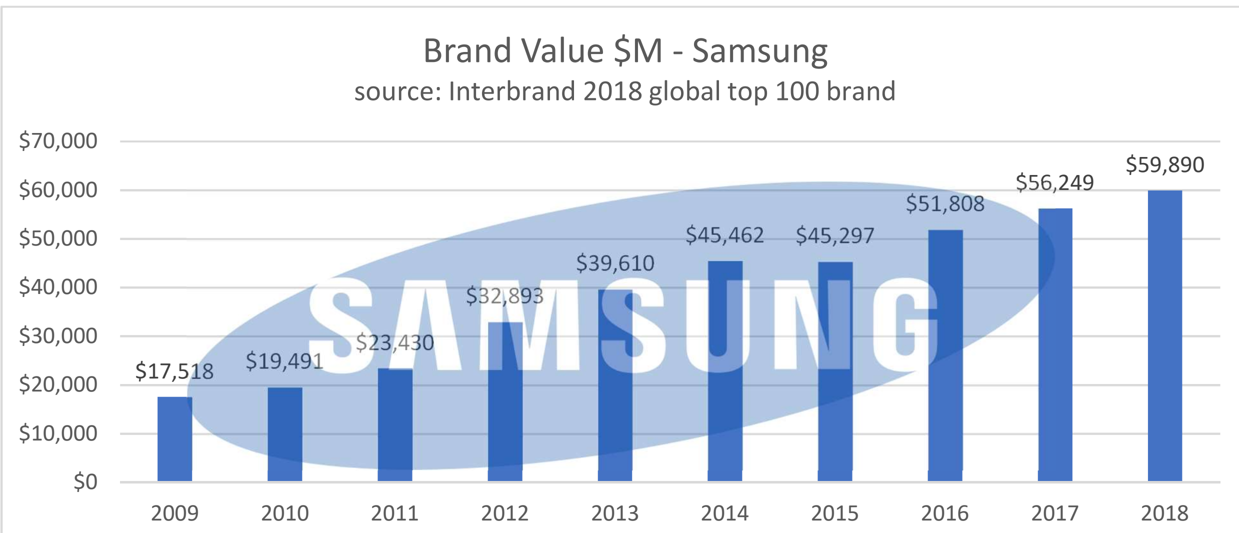

Chart 2

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? It can start from 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 via 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 Table 1) has greater freedom in its pricing strategy to set higher prices. Such an advantage has direct benefits to 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.

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

Table 1

The market approach compares similar brands. It is similar to the housing market, where your sales price is close to similar 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. Using the Samsung Note 7 as an example, the recall cost is 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 is a lot of financial details involved in properly defining a company's brand equity, but for most of us, 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, then it would be a good idea to understand how your investments or projects can add value to the brand.

Leadership and maintaining the brand image

Brand valuation studies have clearly confirmed that a brand is an intangible asset for a company. Then why doesn't management always take actions to prevent damage to its brand or reputation? The most logical explanation is that they 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, their 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 that they are 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 their 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 that there are many managers 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. They want 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 that they 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 based on the strategic direction.

I want to use these two scenarios to represent a contrast between 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 their decision, especially when you have a desire to change the course of action.

Conclusion and action Plan

Let's say you are a leader in your organization that 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.

Step 1: Identify if quality is a key element of the brand

Step 2: Establish the multiplier for business benefit estimation

Step 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

Use 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 tangible benefits might include scrap reduction, cycle reduction, or inventory reduction. The overall estimate benefit would be the 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 non-value- 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 6 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. Therefore, this is an easy concept for management to use. In my own case, we presented the case to our senior leadership. The answer we got is they believed 6 times would be a rare case, but 4 times is acceptable. Since then, 4 to 6 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 for the justification of 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. Utilizing such an approach would allow projects with intangible benefits, including quality or brand image, to be compared side by side with tangible projects. Since the number one priority for management is to ensure financial sustainability for the business, this approach provides a transparent and objective cost-benefit analysis without ambiguous arguments.

About the author

After a successful career of over 20 years in corporate America, Kaiwen Cheng switched his focus to share what he has learned to benefit others with his company, KC Business Consulting, LLC.

Kaiwen has working knowledge in multiple industries span from household product, OEM equipment, to automotive. He has witnessed raise and fall of brands and their impact on life of people. He used this knowledge to driven business cases in improving quality on product and services in order to achieve greater customer satisfactions.

As a business leader, Kaiwen has multiple successful turn-around improvements in process and quality. His practical approach of tying quality with business performance has played the key role in getting buy-in with effective executions. Examples of his success stories include record-breaking warranty performance for the most complicated tier V engine in the history of our engine lines. His recent successes include leading a supplier quality team to deliver a 60% reduction on external complaints within 20 months.

Kaiwen has a master's degree in industrial engineering from University Missouri – Columbia. He holds a bachelor's degree in physics and has MBA education. He is also a certified Six Sigma Black Belt. More information available on www.kcbcweb.com