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Creating reputational value through organizational resilience

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When it comes to growing a thriving business, reputation is the most valuable asset one can have — and must protect. Andrea Bonime-Blanc of GEC Risk Advisory L.L.C. and Nir Kossovsky of Steel City Re discuss how organizational resilience can help mitigate the risk of losing this important intangible asset.

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The direct and indirect costs of fines and restitutions, regulatory compliance, impaired credit ratings and third-party relationships have been instrumental in helping C-suites and boards better understand the materiality of what The Economist magazine in 2005 called the "risk of risks": reputation risk.Since reputation is nothing more than a forward-looking expectation, reputation risk is best understood financially as the cost of disappointment.While loss is one approach to determining the value of reputation, a "Big Yellow Taxi" strategy — you don't know what you've got 'til it's gone — makes for a memorable Joni Mitchell folk song but a terrible business practice. We now have more than a decade of data affirming the upside — that is, the value — that can be created when companies exceed stakeholder expectations. Because reputation is an expectation that affects every line of a company's profit and loss statement, and because those expectations are reflected in open source conversations, we have been able to set big data analytics loose on this information, yielding indices of reputational value. For the past 12 years, the reputation value metrics used by some underwriters at Lloyd's of London have been used to select Standard & Poor's 500 index companies deemed likely to exceed stakeholder expectations, be upgraded and produce excess returns. The annual equity portfolios selected from the S&P 500 on the basis of these reputation metrics outperformed the S&P 500 index 86.1% of the time. In 629 serial samples of trailing 12-month returns, the reputation-linked portfolio generally outperformed the S&P 500, returning an excess of 9.5% on average (median 4.7%). In 91% of the cases of outperformance, the excess trailing 12-month returns were greater than 2%. The cumulative price returns through Jan. 15, 2015, are 362.5% for the reputation-linked portfolio and 69.9% for the S&P 500.Underpinning the reputation value metrics used to find equity opportunities is an understanding that reputation value is best evidenced by what people are expected to do rather than by what they say they will do. Marketing professionals — and their specialized colleagues in election polling — are painfully aware of this distinction.All things being equal, reputation value results from expectations of corporate behaviors associated with quality, ethics, safety, security, sustainability and innovation. It leads stakeholders to behave in financially relevant ways — how customers respond to prices, how effectively employees work, how creditors set borrowing rates, how suppliers set terms and how severely regulators impose penalties. Better reputations should lead to stakeholder behaviors that create greater enterprise value through shorter sales cycles, larger unit volumes and customer willingness to accept premium product pricing, better terms from employees and vendors for services, and terms for capital from creditors and equity investors.Regulators should be less aggressive as well. Reputational Value Metrics calculated by Steel City Re, being the oldest purely algorithmic value indicators, are indexed measures of the expected value of the above behaviors, evidenced by the telltale signatures left by what stakeholders are expected to do before they are reflected in a company's financial statements.Reputation value is managed best by harmonizing communications and operations, and success is evidenced by a company's realization of fair market value, minimal stakeholder disappointment with consequent P&L impairment, and organizational resilience in the setting of an adverse event.Therefore, the key to organizational resilience is the creation and implementation of internal programs, controls and processes directly connected to the strategy of the business, and enabling stakeholders to appreciate and value them.This means that an oil and gas company will have appropriately well-developed environmental, health, safety and third-party management programs, for example. A financial institution will invest properly in anti-money laundering, anti-corruption and cyber security governance and compliance. And the average global consumer product or retail chain will ensure that it has strong quality, safety and supply chain governance programs in place, all designed to meet and mitigate known or expected high risks. In all this, it is imperative that these programs strengthen an organization to not only withstand risks to reputation and crises, but also to develop new opportunities and create value. Only in this way will a company achieve sustainable reputational resilience. *Andrea Bonime-Blanc is CEO of GEC Risk Advisory L.L.C. and author of "The Reputation Risk Handbook: Surviving and Thriving in the Age of Hyper-Transparency." 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