

Reputation, Reputational Crisis and Corporate Social Responsibility of Banks: Measurement and Relationships

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Abstract The chapter focuses on the relationships between corporate reputation and corporate social responsibility. First, the main and most important measurement metrics of corporate reputation are analysed. Second, the focus shifts to CSR and an investigation of the measurement tools most frequently adopted by the scholars. Finally, an interesting analysis on the linkages between reputational crisis and the corporate social responsibility of banks is conducted. In this context, we highlight the role that CSR plays with regard to corporate reputation, the characteristics and the effectiveness conditions for CSR to operate as a reputational driver and, finally, when CSR can resolve the reputational crisis of a bank.

1 Corporate Reputation and CSR: The Measurement Metrics

To enhance and better manage corporate reputation, one must first understand how to measure this asset. Indeed, we cannot increase reputational capital if it is not first properly measured (Gardberg and Fombrun 2002). We apply similar considerations to corporate social responsibility (CSR). For this reason, the current chapter focuses first on the measurement metrics for both reputation and CSR. The aim is to realize a comprehensive overview of the main measurement tools for these assets. Thereby, we can also verify the main similarities and differences between corporate reputation and social responsibility. As will be evident in the second paragraph of this chapter, these two assets (reputation and CSR) are inextricably linked by

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important reciprocal relationships that a preliminary analysis of the measurement metrics certainly allows us to highlight.

1.1 The Metrics for Measuring Corporate Reputation

The issue of measuring corporate reputation has attracted the interest of many scholars who, over time and in various ways, have attempted to provide an answer to this important question (Walker 2010).

A first large classification of approaches to measuring corporate reputation leads to distinction between quantitative and qualitative metrics. The first measures aim to provide a numerical score; they are generally based on financial or market variables and assess reputation regardless of the opinion expressed by the stakeholders. Additionally, they do not provide a quantitative score as a final output, which is a synthetic indicator capable of expressing the total value of corporate reputation. However, the qualitative methodologies represent a barometer of corporate reputation and, thus, indirectly show the level of the bank's exposure to reputational risk. By contrast, quantitative metrics are based on the expectations of stakeholders and aim to synthesize, through an appropriate quantitative score, the opinions expressed at a given time. Therefore, while the quantitative metrics can be equated essentially to a financial value, the qualitative metrics are mostly measures of perceptive character.

1.2 The Quantitative Metrics for Measuring Corporate Reputation

We can distinguish different quantitative approaches for measuring corporate reputation, including the *Intellectual Capital Approach*, the *Accounting—Financial Approach*, the *Marketing Approach* (or approach based on the brand value), the *Market-based Approach* and, finally, the *Reputational Value at Risk* (or *Reputational VaR*) (Gabbi and Patarnello 2010; Soprano et al. 2009).

At present, the approach that is most often used in the banking sector is based on market data (*Market-based Approach*). Indeed, to measure the negative impact caused by the manifestation of reputational risk (that is a negative measure of corporate reputation), several authors use the event study approach, which has led to interesting conclusions. More specifically, this approach seems to confirm the hypothesis that when “reputational sensitive” events occur, i.e., events with high reputational impact caused mainly by operational losses, the bank suffers a financial loss greater than the book value due to the joint manifestation of the reputational risk (De Fontnouvelle et al. 2006; Gillet et al. 2010; Schwizer et al. 2010; Biell and Muller 2013; Fiordelisi et al. 2014; Palmrose et al. 2004; Sturm 2013). However, in

addition to such pioneering studies, there are new research perspectives. Among the latter, the following are worth mentioning:

- a) the practice of conducting a more accurate analysis of reputational events through accumulated knowledge of cases and situations likely to affect the value of reputation. In this way, a “*database of reputational events*” can be built to realize increasingly more accurate predictive investigations;
- b) the improvement of the qualification of reputational events and the creation of an *ad hoc* model for measuring reputational risk to consolidate the approaches taken in the various hierarchical levels;
- c) the need to improve methods of measuring not only the severity of reputational risk (*ex-post view*) but also the frequency, calculating the probability that within a specified time frame, the reputational event could occur (*ex-ante view*);
- d) the need for industry associations or a national and/or international Supervisory Authority to define best practices for management and measurement, including at the sectoral level (Reputation Institute 2015).

1.3 The Qualitative Metrics for Measuring Corporate Reputation: Professional Models Versus Academic Models

We can also discern different qualitative approaches to assessing corporate reputation (Helm and Klode 2011). The literature suggests several classifications; the most important classifications are based on the type and/or number of stakeholders involved in the estimation process.

Indeed, some authors develop measures involving only one category of stakeholder, especially the customers of the company (Walsh and Beatty 2007). Other authors, however, take into account the views expressed by different parties that, for various reasons, gravitate around the company. Consequently, in the first case, the final score will be of *uni-stakeholder character*; in the second case, the estimates will be of the *multi-stakeholders type*.

Conversely, a second proposal distinguishes between objective and subjective instruments that assess corporate reputation (Carreras et al. 2013). The former are based on testing and evaluations conducted by individuals with high expertise (*highly informed experts*) and, thus, aim to produce an impartial value of reputation. The subjective measurement tools, however, are called such because they are based, essentially, on the perceptions and expectations of the other categories of stakeholders. Therefore, whereas the objective tools are designed to determine “*the degree to which a group of stakeholders actually thinks, feels and admires that company with or without reason, and right or wrong*” and, thus, can be assimilated to an excellent certification, the subjective measurement tools aim to synthesize “*the degree to which a group of stakeholders actually thinks, feels and admires that company with or without reason, and right or wrong*” (Carreras et al. 2013:354).

To put more simply, according to this view, the Fortune reputational rankings belong to the objective instrument category because they result from the opinions of Top managers and financial analysts, who are persons with high expertise. By contrast, the *RepTrak Pulse* of the Reputation Institute constitutes a subjective measurement tool because it results from the opinions expressed by the consumers of the company and expresses essentially the emotional involvement of these stakeholder groups (see *infra*).

In this context, however, because the intent is not only to achieve an overview of the main tools for assessing corporate reputation but also to identify similarities, differences and difficulties of such measurement models, we decided to simply distinguish between a) professional background models and b) academic models. The main difference between the two approaches regards only the subject that makes the elaboration because while the former are developed by consulting firms, magazines and others, sometimes in partnership with academic scholars, the latter are only performed by the doctrine. Concerning the output, however, the two approaches are equivalent in terms of providing specific reputational scores.

Regarding the models of the professional field, the development of the first rankings dates back to the 1980s. At first, the methodological approach is quite simple: after defining the areas under investigation (reputational dimensions), a selected stakeholder group, which expresses their judgements on a determined sample of companies, is interviewed. The most important of these first reputational rankings is the *American Most Admired Companies* (AMAC), which was developed in 1983 by the US Magazine Fortune. In the future, these ranking will be named the *World's Most Admired Companies* (WMAC) because Fortune has expanded the sample of companies under investigation. Over time, other similar initiatives were created to develop parallel indicators but relative to other geographical areas (Fombrun 2007; Carreras et al. 2013).

Subsequently, to overcome some important criticalities raised by these first measurement proposals, the professional field, in partnership with academia, has sought to improve the methodological approach by developing new reputational indicators. One such indicator is the *Reputation Quotient* (RQ), developed in 1999 by a team of professors (Fombrun et al. 2000a) in collaboration with the consulting firm *Harris Interactive* and now revised in a new version, which was developed only by the consulting firm. The principal value of this indicator is that it has expanded both the range of stakeholders involved in the analysis and the number of evaluation criteria. Indeed, unlike the Fortune score, which is based on only a few items (initially, there were seven items but now there are nine), the *Reputation Quotient* (RQ) not only is a multi-stakeholder score but it also focuses on 20 indicators that are grouped into six reputational dimensions that were selected through a bottom-up approach, i.e., by conducting a series of pilot studies (Fombrun et al. 2000a). Moreover, a further important aspect regards the introduction of the “emotional factor” in addition to the more rational dimensions: the *emotional appeal factor*. The basic items of this factor are as follows: *good feeling*, *admiration* and *respect*, *trust*—note that corporate reputation is not simply the result of

objective assessments; it also derives from the emotional involvement of the company's main stakeholders (Davies et al. 2004).

Finally, compared to the first reputational rankings (still elaborated), with the introduction of the RQ, the methodology has been enriched by a rigorous conceptual background. Indeed, while the elaboration of *Fortune's* WMAC is not based on a detailed definition of corporate reputation or what is measured, since the construction of the RQ, the analysis has also incorporated such components (Fombrun et al. 2000a).

Rather similar to the RQ, but constituting an advanced version, the *RepTrak™ Pulse* was developed by Reputation Institute in 2006. This ranking is a “*simplified emotion-based measure of corporate reputation*” (Ponzi et al. 2011:16) because its implementation focuses on an appropriate balance between emotional factors (*esteem, good feeling, trust, and admiration* that consumers feel towards a company) and more rational elements linked to six reputational dimensions. The theoretical framework is strong; developed on the basis of *signalling theory* and the *resource-based view* (RBV), the score aims to “*conceptualize corporate reputation as beliefs about companies and disentangle the drivers of reputation from the construct itself*” (Ponzi et al. 2011:16). However, what differentiates the ranking of the Reputation Institute is mainly the stakeholders interviewed. The stakeholder reference group does not relate to the managerial figures but to the general public or consumers, appropriately balanced with respect to age and gender.

Finally, the *MERCO index* (*Monitor Empresarial de Reputación Corporate*), whose main advantage is that it is based on a multi-steps and multi-stakeholders methodology, is worth noting. More specifically, such ranking not only involves several stakeholders groups, including both the Top managers and the consumers (and, therefore, the general public) in the analysis process, but also is developed in two different evaluative phases, with the aim of perfecting the final score. The aim of the implementation of a second step of analysis is to confirm or reject the result obtained from *previsional ranking* which is the output of the first phase (Carreras et al. 2013). Additionally, the final score of this ranking, unlike the previous rankings, is certified by the KPMG auditing firm on the basis of the *International Standard ISAE 3000*.

Restricting the analysis only to the banking and financial sector, all the rankings mentioned offer interesting information and allow the use of industry and geographic area filters. Among all ranking institutions, *Fortune* produces the most disaggregated information because, as regards the financial sector, it proposes the ranking of approximately seven different areas: 1) *Consume credit card and related services*, 2) *Financial data services*, 3) *Insurance: Life and Health*, 4) *Insurance: property and casualty*, 5) *Megabanks*, 6) *Securities and Asset Management*, and 7) *Superregional Banks*. In all areas, the ranking distinguishes between companies with higher reputation and the so-called “*contenders*”, which have obtained a score lower than the industry average.

In addition, the Reputation Institute produces several sectoral reports annually, including the ranking of American banks with higher reputations in collaboration with the financial daily “*American Banker*” (2014 *US Most Reputable Banks*).

The latest reports indicate that the banking sector has not yet bridged the reputational gap that other industries have bridged because it is still suffering the effects of the international crisis, of which it is considered the main culprit. The reputational drivers on which banks should invest more are related to the products and services provided, the governance processes and the CSR strategies (Reputation Institute 2015).

1.4 The Qualitative Metrics for Measuring Corporate Reputation Proposed by the Doctrine

Qualitative academia models are elaborated only by the doctrine. The first attempts by scholars to measure the reputational asset date back to the 1970s. At that time, the attention focused mainly on the concept of the credibility of the enterprise (Newell and Goldsmith 2001). Only later, since the 1980s, specific studies on the measurement of corporate reputation have been conducted. The models proposed by the doctrine are quite heterogeneous (Helm and Klode 2011) with respect to the theoretical base (*institutional theory*, *resource-based view* and *signalling theory*, see Walker 2010), the derivation process of the model (*reflective model* versus *formative model*, see Helm 2005; Carreras et al. 2013:381) and, finally, the operating and managerial implications achievable (Walker 2010; Carreras et al. 2013). The following are among the best-known approaches:

- a) the *Reputation Index* of Cravens et al. (2003), which is based on 4 reputational dimensions (*leadership*, *strategy*, *culture* and *innovation*) and 21 elementary items;
- b) the *Corporate Personality Scale* of Davies et al. (2004), which is based on seven reputational qualitative dimensions related to characteristics of human personality (*Agreeableness*: honest, socially responsible; *Competence*: reliable, ambitious; *Enterprise*: innovative, daring; *Ruthlessness*: arrogant, controlling; *Chic*: stylish, exclusive; *Informality*: easy going; *Machismo*: tough);
- c) the *SPIRIT model* of MacMillan et al. (2004), which is based on three reputational dimensions: *experiences* (sub-dimensions: communication, material benefits, experience of outside influences), *feelings* (sub-dimensions: trust and positive emotions), *intentions* (including sub-dimensions of supportive behaviours, advocacy and retention of stakeholders);
- d) the *CBR—customer based reputation* of Walsh and Beatty (2007), which is based on five reputational dimensions related to *customer orientation*, *good employer*, *reliable and financially strong company*, *product and service quality*, *social and environmental responsibility*.

Unlike professional models, these approaches are characterized by limited empirical utilization because they are mostly usable only as part of the scientific research that developed them.

1.5 The Metrics for Measuring CSR

As with corporate reputation, there are different corporate social responsibility (CSR) measurement approaches aimed to express a synthetic assessment of the ethical performance of the company. With regard to the banking sector, the solutions most frequently used in the literature can be differentiated in two macro groupings:

1. *Ethical ratings*: mostly elaborated by consulting firms or external agencies, such as *Eiris* (de la Cuesta-González et al. 2006), *SAM*, *Ethibel* and *Axia* (Soana 2011), *KLD* (Goss and Roberts 2011; El Ghoul et al. 2011), *Standard Ethics*, *Vigeo*, *IW Financial*, *Calvert*, *Jantzi Research Inc.*, *RiskMetrics*, *Investissement Responsible*, *Accountability Rating*, and *Thomson Reuters* (Ioannou and Serafeim 2012; Ciciretti et al. 2015). Additionally, we can also discern academic ethical ratings, which are scores elaborated by the doctrine with regard both to banks (Scholtens 2009; Birindelli et al. 2015) and other organizations (Sotorrió and Sánchez 2008; Turker 2009).
2. *Ethical indexes*: groups of securities of listed companies characterized by high ethical performance. They are produced by the company specializing in the creation and management of stock market indexes that, for the case of CSR indexes, is generally assisted by an external ethical rating agency (see *supra*). In this case, the measurement of a bank's ethicality is made by simply verifying whether the bank can be found on the selected ethical index (Chih et al. 2010; McWilliams and Siegel 2000).

1.5.1 Ethical Ratings

Similar to the traditional rating, which synthetizes the creditworthiness of the company, the ethical rating reflects an assessment that, in this case, concerns only the social performance of the firm. More specifically, the ethical rating represents a barometer of the intensity by which the firm puts in place corporate social responsibility policies and strategies. At a methodological level, the ethical ratings are processed by content analysis approach (Abbott and Monsen 1979; Beattie and Thomson 2007): first, the evaluation criteria are selected (KPI, *Key Performance Indicators*) and, then, the company's compliance with these criteria is assessed. This verification takes place by administering a questionnaire to the company (Turker 2009), by viewing directly the corporate documents (Birindelli et al. 2015) or by examining information from Supervisory Authorities, media and other communication channels (Scholtens 2009; Sotorrió and Sánchez 2008). Frequently, these cognitive tools are used in an integrated manner. The evaluation standards, which generally are based on a combination of positive and negative criteria, can vary widely and be quite numerous depending on not only the approach taken by the ethical rating agency but also the type of score that will be processed. More specifically, we can distinguish between the following two types of ratings:

- a) *multi-dimensional ethical ratings*;
- b) *mono-dimensional ethical ratings*.

While the former ratings aim to evaluate simultaneously multiple CSR dimensions of a company, the latter simply check only dimension. Examples of the first type are the “*ESG ratings*” issued, for example, by KLD and ASSET4 and designed to assess, at the same time, the environmental, social and governance performance of the company. The *RepRisk index* (RRI), which was developed by *RepRisk* consulting firm is always multidimensional. Unlike the other scores, it does not indicate the most ethical companies; rather, it indicates those most exposed to the ESG risks. Indeed, a high value on the index reflects a firm's lower level of ethicality. Examples of one-dimensional ethical ratings, however, include the *Pollution Performance Ranking* and the *Carbon Performance Leadership Index* (CPLI) because they only evaluate the environmental performance of the firm and the *CSR Online Awards Europe 10*, which focuses on only the disclosure of social reporting tools.

Finally, the ethical rating can be represented by a numerical score or a synthetic assessment via letters. In most cases, these scores are shown; in other circumstances, however, the provider only publishes the ranking and omits the score assigned to each company.

At present, there is a wide range of ethical rating/score solutions offered by the professional world. This range has raised some confusion and many questions. Indeed, in some cases, a company is excluded from an ethical rating but is still judged as good by another consulting firm. Moreover, the approach taken by different ethical agencies may be quite different. Often, the criteria and weighting system used vary considerably. For this reason, the project known as the *Global Initiative for sustainability ratings*, which is still in the implementation phase, was developed with the objective of defining a standard model of ethical rating elaboration that can be shared and accepted at the international level.

1.5.2 Ethical Indexes

Equity ethical or socially responsible indexes represent an important tool of business ethics (*Social Responsible Investment*). Indeed, when we compare them with the traditional indexes, we can immediately check the performance that this sector can offer over the traditional one. In addition, as a measurement tool for CSR, ethical indexes allow us to identify immediately the most ethical companies (that are the constituents of these indexes) without providing a summary measure of their level of ethicality. In reality, membership on an ethical index may be treated as a type of quality certification regarding the company's social and environmental commitment and a type of recognition of the company's social activities.

Concerning the methodology, ethical indexes are constructed in the same way as ethical ratings, i.e., using a combination of positive and negative criteria designed to assess the social performance of the company. While the negative criteria aim to

exclude all the companies operating in productive sectors in contrast to the corporate social responsibility principles (such as alcohol, tobacco, weapons, pornography and gambling), the positive criteria assess the commitment of the company in terms of environmental, social (respect for human and civil rights) and governance concerns. Often, the starting point is a traditional index. By applying a proper screening policy, we delete issuers that do not meet the requirements of social corporate responsibility previously defined. Moreover, ethical ratings are frequently used to more easily identify the undertakings to be included among the indexes.

However, in addition to ESG criteria, the ethical indexes must observe other composition criteria, especially in terms of maximum weight to be assigned to the securities with the highest capitalization. This method also ensures the comparability of any ethical index with a traditional index, *condicio sine qua non* so that the performance comparisons (between ethical and traditional finance) result fair and correct.

Finally, even in this case, it is possible to distinguish between the following two types of indexes:

- a) *multi-dimensional ethical indexes*, which are used to assess the social performance of the company in several respects, including the environment, the relationships with stakeholders and the corporate governance system;
- b) *one-dimensional ethical indexes*, which are used to highlight the social performance of the company in regard to a single dimension (environment, social or corporate governance) or industry sector.

For example, examples of the first type of ethical indexes are the *MSCI KLD 400 Social Index* and the *MSCI World ESG index*, while a mono-dimensional ethical index is the *FTSE CDP Carbon Strategy*, which aims to assess only the environmental performance of the enterprise. This index, indeed, includes companies that, for various reasons, incur costs and take initiatives to address the emergence of toxic emissions.

As previously mentioned, in the case of ethical indexes, we do not obtain an ordinal measure of the CSR level attributable to each firm (as in the case of ethical ratings whose output is constituted, mainly, by a numerical score); rather, it is possible to only discern the companies that best meet the sustainable finance principles. In the empirical literature, dummy variables are used to select the organizations included on ethical indexes and, therefore, characterized by the best social performance.

1.5.3 Other Measurement Approaches for CSR

Finally, other less important approaches to measuring CSR used by scholars concern the verification of the firm's adoption of relevant international standards (such as the *Equator* or the *Wolfsberg Principles*, see Scholtens and Dam 2007; Chih et al. 2010); the attainment of ethical certifications and compliance with

guidelines on ethical conduct, such as those approved by the *United Nations Global Compact*, the *OECD*, the *Global Impact*, the *UNEP Finance Initiative*, the *Carbon Disclosure Project* and, finally, the *GRI (Global Reporting Initiative)*. Furthermore, in these cases, scholars frequently use dichotomous dummy variables to discern banks that are compliant with selected ethical standards. Indeed, if the bank is compliant, it is given a value of one; otherwise, it is given a value of zero.

1.6 The Measurement of Corporate Reputation and CSR: Can We Hypothesize an Integrated Approach?

One aspect that certainly unites the corporate reputation and CSR concerns the large number of metrics proposed in the literature or by economic and professional fields. On the one hand, this shows the extreme accuracy of and the great interest that the scientific and professional community has in these issues. On the other hand, this aspect also involves a degree of uncertainty and confusion (Carreras et al. 2013). Indeed, the proliferation of measurement instruments, which are often quite different from each other, implies the need to make a choice in an attempt to use the tool most appropriate to one's knowledge needs. Moreover, this selection is not without implications. Frequently, the use of one approach to measuring corporate reputation and/or CSR over another approach affects the research results by supporting the investigation objectives to a greater or lesser degree. For this reason, given the absence of an ideal evaluation model, in the previous paragraphs, we provided an overview of the main measurement instruments for both corporate reputation and CSR with the aim of realizing some critical reflections on their adoption to develop metrics that are increasingly complete and effective.

However, through the joint analysis of the two measurement approaches (reputation and CSR), an interesting aspect emerged: in many cases, the dimensions analysed are indistinguishable from one another because they aim to analyse roughly the same aspects, including, in particular, *corporate governance*, the *quality of products and services*, and the *level of corporate innovation*. Moreover, in most cases, CSR is included among the reputational drivers due to a strong correlation with respect to reputational asset (Reputation Institute 2014). Similarly, some providers include reputation among the ethical dimensions to be analysed to develop a CSR indicator. Finally, it is not uncommon to find the use of reputation scores to synthesize the level of ethics of an organization in the literature (Turker 2009), although this method has not entirely shared (Liston-Heyes and Ceton 2009).

This overlap leads us to reflect on the possibility of developing an integrated approach to jointly measure the ethical and reputational performance of a bank. However, for this to happen, it is necessary to refine the two measurement approaches. Indeed, if there is a clear similarity in “*what*” reputation and CSR metrics measure, significant differences emerge on “*how*” the measurement is conducted. More specifically, the reputational scores are constructed by reworking

the perceptions that one or more stakeholder groups have of a company. In contrast, the ratings or ethical indexes are based mostly on the analysis of corporate documents, failing to examine the sentiment surrounding the organization. In other words, with regard to governance processes, if the goal is to build a corporate reputation indicator, the assessment will focus on how stakeholders judge that system; however, if the focus moves to the CSR, the analysis will be more objective because it will be conducted by consulting the corporate documents, interviewing the managerial class, or administering a questionnaire to the company (Turker 2009). It is obvious that these two measurement systems will make use of different data and information but may be integrated. More specifically, it is possible that stakeholders make judgements based on aspects other than the objective characteristics of the company. This may depend on the type and quality of publically available information, how these are spread and filtered by the company, and aspects related to the personality of the stakeholders involved in the analysis, such as their degree of education, age, skills and preferences, etc.

For this reason, it is not improper to assume the development of an approach that combines and integrates the subjective assessments, which characterize the measurement of reputational asset, and the most objective measures, which distinguish the CSR analysis, into a single synthetic judgement. Such an attempt would also overcome some of the critical issues related to reputation scores, including the excessive reliance on subjective assessments and, therefore, on the target stakeholders selected for the estimation of the indicator.

Certainly, a combination that is properly balanced between subjective and objective assessments could generate an indicator that is not only more complete but also less random because it is subjected to a testing process and empirical evidence. To this end, we could assume a *multi-steps approach*: first, the subjective measures should be implemented to verify how the company's behaviour is perceived and judged by the public; then, we may proceed with the objective estimates to integrate, validate and refine those related to the performance reputation. The final output of this combination will be a numerical score that can be understood as a synthesis of the "*ethical reputation*" of the company.

2 Reputational Crisis and the Corporate Social Responsibility of Banks: What Are the Relationships?

A cross analysis of the reputational crisis and CSR is still not widely debated in the literature (Melo and Garrido-Morgado 2012; Esen 2013). However, such an analysis is very important for several reasons.

The link between reputation and CRS started long ago. For banks, this relationship represents two aspects of the same coin (Hillenbrand and Money 2007), although there is still debate on how to develop that connection and its management

implications (Hillenbrand and Money 2007; de Quevedo-Puente et al. 2007; Esen 2013).

The logical link between the two issues is represented by the fiduciary bank relationship and the social function of banks. In the broadest sense, the corporate social responsibility of a bank is nothing more than an effective exercise of its objective function. Careful planning of business processes, together with the supervision of banking business, a detailed organizational structure and an efficient system of internal controls could enable the customer relations—which are governed and solidified in function of the trust relationship—to contribute positively to building the bank's good reputation on the market in the medium-long term. Conversely, a reputational risk can be symptomatic of a loss of customers' confidence; in turn, the latter may result from several factors. In summary, when the cornerstones on which the banking business rests are weakened, we can say that the social function of the bank is no longer apparent, which may cause the manifestation of reputational risk (Walter 2013).

Therefore, although they are not always analysed in the literature in an integrated manner, the issues of corporate reputation and corporate social responsibility in the banking sector are easily attributable to common goals (Hoepner and Wilson 2012).

In fact, there are banking entities oriented toward ethics and social responsibility and for which the link with the company's reputation becomes almost unavoidable and binding, revealing a very strong identity. In these cases, it is the same business (for example, ethical mutual funds, the business of green economy, social and sustainable investments, etc.), strongly oriented towards CSR issues, that requires a risk management planning process that can estimate the negative effects of a possible failure of the business, with negative consequences on reputation. Indeed, in these cases, the reputation of the financial intermediary is nothing but its sense of social responsibility.

However, for other banks, a strong orientation towards CSR issues serves as a “*protective barrier*” against adverse events not only of external origin, such as an economic crisis (Xifra and Ordeix 2009), but also of internal origin, such as a reputational crisis (see *infra*, Box 1 on *Société Générale* reputational crisis).

2.1 Reputation and CSR: A “Triple” Consequential Relationship

From the point of view of an enterprise, there are many reasons to adopt CSR practices (Fombrun et al. 2000b; Esen 2013). Indeed, the doctrine has long showed significant benefits, including the development of increasingly strong customer relations (Lin et al. 2009; Mulki and Jaramillo 2011). More specifically, customers show a greater predisposition to buy products (Smith and Alcorn 1991), a greater willingness to pay a higher price (Creyer and Ross 1997) and, finally, less sensitivity to supporting the costs associated with the change of the brand to sustain,

mainly, the companies involved in ethical activities. Then, the relationships with economic performance are not less important: indeed, the main research studies (Simpson and Kohers 2002) report a positive connection, noting that the development of social responsibility practices will promote businesses' profitability, especially in the long term (Beurden and Gössling 2008; Scholtens 2009; Callado-Muñoz and Utrero-Gonzalez 2011). Often, the link between ethical and economic performance is not evaluated assuming a direct relationship; rather, it is mediated by another intangible asset, which is also strongly linked to CSR (Vitezić 2011; Esen 2013; Walker and Dyck 2014). More specifically, research states that the implementation of social responsibility strategies, by increasing the value of corporate reputation, also enhances the economic value creation. In other words, the profitability of the company would result from the development of the reputational capital, which, in turn, would constitute the main (positive) result of the implementation of social responsibility practices (Fombrun et al. 2000b; Esen 2013).

The consequential link between ethical and reputational performance appears, therefore, unequivocal (Walker and Dyck 2014). However, if we analyse the various metrics for measuring corporate reputation, we can easily see that corporate social responsibility is always mentioned because it represents one of the main reputational drivers (Esen 2013; Walker and Dyck 2014). However, it may happen that this relationship is manifested with different intensities depending on the industrial sector (Williams and Barrett 2000), the economic cycle (Jacob 2012) or the different socially responsible activities (Brammer and Pavelin 2006). More specifically, Brammer and Millington (2005) show that the growth of reputational capital, which is associated with the increase of expenses for philanthropic activities, varies significantly in the different industrial sectors. Indeed, these authors observe that philanthropy greatly affects the reputation of those companies linked to sectors with significant social externalities, such as the alcoholic beverages and tobacco sectors. This finding suggests that philanthropy (expression of the CSR practices) can help companies to expiate behaviour that is not socially responsible. Philanthropy acts as a "*protective barrier*" against the negative perceptions of stakeholders. Similarly, Jacob (2012) notes that the link between CSR and reputation is influenced by the economic environment in which the firm operates. Indeed, the author, observes that during the recent sub-prime mortgage crisis, the influence of the working conditions (workplace) on the reputational capital of a company became more marginal. This is due to the deterioration of working conditions, which was the main consequence of the crisis and made employees and their expectations less influential at a reputational level (Jacob 2012).

Overall, therefore, considering the relationship with corporate reputation, a triple role can be assigned to CSR. First, corporate social responsibility is a tool that increases the value of corporate reputation (Esen 2013). Such awareness began in the 1990s (Fombrun and Shanley 1990) but only later received greater consideration (Gardberg and Fombrun 2002; Brammer and Pavelin 2006; Esen 2013; Walker and Dyck 2014) with regard to emerging economies (Rettab et al. 2009) and at different stages of economic instability (Xifra and Ordeix 2009). The reason for this link is found under signalling theory, in which social performance represents an

antecedent of corporate reputation (Turban and Greening 1997; Janney and Gove 2011; Maden et al. 2012). Indeed, by developing CSR practices, the company would send signals to meet the stakeholders' expectations and, thus, increase the value of its reputation.

Additionally, social responsibility is ascribed the function of protecting the value of corporate reputation (Fombrun et al. 2000b). Indeed, the risk of incurring reputational losses is one of the main reasons that lead companies engage in social responsibility practices (Fombrun et al. 2000b; Pelozo 2006). Klein and Dawar (2004) believe that CSR represents, for the enterprise, a form of "*insurance policy*" against negative events. More specifically, these scholars argue that consumers' high perception of the CSR activities of the company minimizes the attributions of guilt for any faults in products sold (Minor and Morgan 2011). Therefore, even in the absence of a direct impact on corporate profitability, CSR produces value because it can help to mitigate the negative effects of a detrimental event, safeguarding the value of the reputational asset (Klein and Dawar 2004). If then, in addition to good ethical and reputational performance, major and effective disclosures are provided, the protection level against financial scandals will be maximized and the market's reaction will be less harmful (Janney and Gove 2011).

Finally, another function that we can attribute to corporate social responsibility regards the recovery phase of reputation loss. Indeed, when a reputational crisis occurs, CSR can certainly help to minimize the reputational damage by mitigating the negative impact of fraudulent behaviour. However, in this case, it is good to make a clarification because the ethical commitment of a company can be a double-edged sword. High involvement in social responsibility practices can expose companies to more severe judgement if they become responsible for fraudulent conduct (Janney and Gove 2011). Specifically, when a company has a high reputation for a given dimension of CSR, violations connected with this dimension are likely to be severely punished. In other words, if a company is known for having a good corporate governance system, a scandal that affects this system will be severely punished by the market. Conversely, if the governance system of the firm already suffers from a poor reputation, any flaws in this sector will certainly have less reputational impact (Janney and Gove 2011).

A further implication of the controversial relationship between reputation and CSR concerns the influence that these assets have on the behaviour of investors, especially on shareholder activism. Recent studies show that the development of corporate social responsibility practices leads to a better reputation but, at the same time, creates some negative externalities (King and McDonnell 2015). Companies with better reputations, which are more well-known and visible, are also likely to more easily become the target of operations boycotts by activists. Indeed, to give more emphasis and visibility to their protests, these stakeholders will choose businesses with better reputations because these firms are the most known to the public. In turn, these companies will tend to satisfy the activists' expectations to avoid triggering an adverse reaction by the market and losing economic value. Thus, a vicious circle is created in which, rather than constituting a form of

insurance, CSR is likely to make companies more vulnerable (King and McDonnell 2015).

2.2 Reputation and CSR: A More Complex Relationship

In fact, the relationships between CSR and corporate reputation are not just consequential. Numerous studies reveal more complex connections characterized by interdependence, reciprocity and/or interactive effects (Trotta et al. 2011). More specifically, it is claimed that business reputation represents not only a consequence of a good CSR strategy but also an antecedent of this practice. It increasingly appears that reputation is a prerequisite for the success of a CSR strategy, that is a *conditio sine qua non* to be more socially responsible.

In particular, the doctrine highlights two basic conditions. The first is the possession of a good reputation, without which the company's implementation of CSR practices may not be effective (Schuler and Cording 2006). The second condition, however, concerns the compatibility of the ethical and reputational performance. In other words, to develop economic and reputational value, CSR strategies must not only be implemented by companies that already have a good reputation but also be consistent with the company's image. Otherwise, if the image projected by implementing CSR practices is not aligned with the firm's reputation, the firm is likely to produce dis-value caused by the incurrence of costs that are not offset by economic value creation (Schuler and Cording 2006; Du et al. 2010).

Servaes and Tamayo (2013) have the same opinion. They observe that the cost of promoting CSR activities can have a negative impact when such strategies are not consistent with the full value of corporate reputation. In other words, "*CSR efforts have to be aligned with the firm's prior reputation to create value*" (Servaes and Tamayo 2013: 1058). Therefore, companies with a bad reputation run the risk of not achieving any benefit from implementing CSR strategies because "*such activities may appear disingenuous and may well have the opposite effect*" (Servaes and Tamayo 2013: 1059). To change this trend, it is necessary to intervene in customer engagement policies to understand why such stakeholders have negative perceptions and, thus, elicit a positive change. Finally, Du et al. (2010) corroborates these considerations by supporting the notion that the preliminary possession of a good reputation amplifies the positive effects associated with the communication of CSR policies.

In summary, it is evident that CSR is not always a good strategy and produces value by improving the company's image. This may depend on the reasons underlying the implementation of such strategies and how they are perceived by the stakeholders. When the company does not enjoy good credibility, CSR policy implementation can feed the suspicion of hidden or selfish motives rather than enhancing the company's reputation; therefore, it can be counterproductive. This risk can be mitigated when neutral external sources give the company a good ethical rating or when the relationship between CSR/advertising is high or when the

company promotes its ethical commitment continuously and pertinently (Yoon et al. 2006) through relevant public relations activities (Esen 2013).

Ultimately, we can state that trust in a company is a key driver of social responsibility, the indispensable condition for CSR practices to be valued positively and have the desired effects. In the absence of trust (and, therefore, of reputation) in the company, any CSR strategy could be futile (Osterhus 1997) or even counter-productive (Strahilevitz 2003).

2.3 CSR as a Reputational Driver: Characteristics and Effectiveness Conditions

As previously mentioned, among the reputational drivers, there are both qualitative and quantitative factors (Esen 2013). Among these, CSR is centrally located because it is considered the most important reputational driver (Esen 2013). Additionally, especially for certain stakeholders, CSR would have a reputational impact far greater than the economic performance (Walker and Dyck 2014). This qualification derives from some characteristics that distinguish CSR policies and attribute the reputational potentialities analysed in the preceding paragraphs to them. More specifically, it can be stated that the CSR is:

- a) *A multivalent driver* with regard to the different stakeholder categories. As previously mentioned, the process of measuring corporate reputation is greatly influenced by the category of stakeholders involved in the estimation process and, therefore, the expectations of each of them. Compared to other reputational drivers, CSR maintains its importance and effectiveness for all stakeholders groups considered for estimating corporate reputation. In other words, regardless of the corporate reputation measure developed, CSR will always have a central position because this driver keeps its positive potentiality regardless of the type of stakeholder (Fombrun et al. 2000b; Esen 2013).
- b) *A cross driver* regarding the business organization. Good CSR practices can (and must) be developed by all the firm's staff, from the senior management to the front office employees. This aspect gives CSR a greater potentiality of impact and higher levels of penetration and diffusion both inside and outside the business organization.
- c) *An easily communicable driver* because CSR is measured and announced with an *ad hoc* reporting tool, which is the Social Report.
- d) *An easily measurable driver*. As we have shown (Sect. 1.5), the doctrine and the commercial practice have long since developed numerous ethical ratings that can certainly be used as reference by the company to elaborate in-house independent indicators of ethics or to monitor the importance of its social performance over time.
- e) *A multi-directional driver* whose management and activation does not require special skills or expertise. Any company can develop CSR practices within

multiple business dimensions (corporate governance, workplace, stakeholders' engagement, the market relationships, etc.) without incurring conflicts or overlapping.

However, for CSR to increase the reputational asset value, certain conditions are necessary. More specifically, the CSR strategy must:

- *be congruent with respect to the business and/or production process put in place by the company.* In other words, if the firm belongs to the mining industry, where working conditions are generally more demanding, it should pay special attention to the claims of the employees such that stakeholders render their work in a healthy environment that respects their rights. Therefore, it is not sufficient to develop CSR practices; rather, it is crucial that these practices have an aim and are more consistent than the negative externalities produced by the corporate business;
- *involve all stakeholder categories, informing them of the ethical commitment of the company properly and continuously.* In doing so, it is extremely important to achieve a balance between an overly lengthy communication that is likely to create only scepticism (Morsing and Schultz 2006) and the transmission of minimal information. Indeed, the CSR processes are very important and should be made with foresight and resources by taking care of the content and the timing of realization;
- *be implemented by a company that already has a good reputation.* If the company does not have a good reputation, has a bad reputation, or has an ongoing financial scandal, the development of CSR practices can produce scepticism and be seen only as an expedient to mask some corporate misdeed (Yoon et al. 2006);
- *be credible in the eyes of all stakeholders, which must be given the opportunity to test the feasibility and practicality of the strategies.* Otherwise, the company runs the risk of being considered misleading, with deleterious effects on the building and growth of its corporate reputation;
- *be able to satisfy all stakeholders without damaging any of them.* In other words, to be very effective and have a positive impact on the reputational asset, a CSR policy should develop a “win-win” logic so that the company's efforts to improve its social performance benefit all stakeholders and are equally shared and supported by them;
- *be able to listen and involve all stakeholders at the same time.* By listening, the company will be able to know and understand the real expectations of its stakeholders. By developing engagement practices, it may also receive active and positive support to make CSR strategies increasingly effective and influential.

Finally, we can state that CSR positively impacts corporate reputation (see the Santander case study by Xifra and Ordeix 2009). Likewise, CSR has a positive influence in the case of a reputational crisis because it contains and minimizes the negative effects of the detrimental event (Dell'Atti et al. 2012). An example derives

from the reputational crisis of the French bank *Société Générale*. The resolution of the crisis is ascribable to the interaction of several factors. Certainly, the capital strength of the French bank must be included, together with the management capacity of its Top managers, who understood the seriousness of the crisis immediately and put in place an action plan to wisely resolve and foresee the serious damage to the image of one of the most important European banks (Dell'Atti et al. 2012). However, a positive and purposeful role in the resolution of the reputational crisis was also played by CSR. As evidenced by Box 1, the CSR commitment of the French bank had a central role in minimizing the negative effects of the bank's reputational crisis.

Box 1 The Reputational Crisis of Société Générale and the Role of CSR

The reputational crisis of *Société Générale* resulted from a sensational financial scandal caused by an employee of that bank (a trader). Using various fraudulent operations (usurpation of codes to access computer controllers, falsification of documents, etc.), *Jérôme Kerviel* (the name of the trader) made, over time, a series of highly speculative and arbitrage operations on derivatives that subsequently proved incorrect and caused *Société Générale* to lose approximately 4.9 billion euros. This situation was announced to the press on January 24, 2008. However, despite the major economic loss suffered, the French bank was able to solve its problems in a short time by minimizing reputational impacts related to not only the collapse of the shares price but also the downgrading of the main economic and reputational rankings (Dell'Atti et al. 2012).

According to an analysis of financial statements, *Société Générale* appears to have long been engaged in building a good image in the market to become “a major reference in Corporate Social Responsibility (CSR) and one of the leading European financial establishments in this field” (*Société Générale* 2009: 139). This commitment has led the French bank not only to be included in the main stock (CAC 40, STOXX Europe 50, EURO STOXX 50, Euronext 100, MSCI PAN EURO) and ethical indexes (including, FTSE4Good and ASPI Eurozone) but also to be selected by the major French ethical funds as a target firm (*Société Générale* 2009, 2010, 2011). Additionally, it is noteworthy the decision to integrate CSR policies at all hierarchy organizational levels to avoid these strategies were disconnected from the other parts of the business. Indeed, the 2009 Annual Report stated that: “the CSR management framework forms an integral part of the Group's structure, and comprises a number of different tools and structures at various levels of the Group's hierarchy (the corporate governance system, the compliance framework, the Risk Committees, the New Product Committees, Internal Regulations, Code of Conduct, Audit Charter, etc.)” (*Société Générale* 2009: 139).

(continued)

Box 1 (continued)

Of similar importance for reputational goals is the independent compliance function, implemented by the French bank since 2006. Over the years and on an ongoing basis, this structure has been expanded to take into account the presence of new sources of risk and the changes in the environment and regulatory framework. The last renovation of this function dates back to September of 2010, likely in response to the reputational crisis of 2008. On that occasion, the French bank decided to replace the previous structure with a new department (*Compliance Department*) by extending the functions and assigning a larger staff (Société Générale 2009). Among the responsibilities assigned is the management of reputational risk, for which the French bank has not chosen to set up an *ad hoc* monitoring unit. However, an internal directive is aimed at all employees to define the policy for the management, minimization and prevention of reputational risk. For *Société Générale*, the management of this risk is a key objective to which all employees must contribute (see, more specifically, Société Générale 2011: 168). Finally, a further contribution to the resolution of the reputational crisis is the absence of previous adverse and harmful events that could have damaged the bank's image. At the time of the crisis, the reputation of the French bank seemed very solid and not at all compromised. As argued by the doctrine (see *supra*), the preliminary possession of a good corporate reputation not only serves as a "protection barrier" against adverse events but also allows the CSR strategies to best perform their reputational driver function to reconstruct the deteriorated image. This also explains why the internal consequences (on profitability and equity) of the reputational crisis have been marginal. Indeed, neither the funding of the bank nor its total capitalization suffered a relevant decrease. Both the traditional customers and some more important financial distributors showed a loyal attitude, thereby safeguarding the amount of bank funding. Additionally, the support received from some important investment banks was very important and decreed the success of the capital increase. Finally, customer complaints were contained, and the penalties imposed by authorities have involved only some bank managers and not the highest corporate officers.

Source: Our elaboration from Société Générale Registration Document (2009) and website.

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Managing Reputation in The Banking Industry
Theory and Practice

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