CHAPTER I

INTRODUCTION

Corporate reputation builds strategic value for a company by granting it a competitive advantage against the rival. A good reputation means higher investment and more customers and higher profit. Corporate reputation can be defined as how an entity (private or public) is perceived by each of its stakeholder. It needs consequently to measure and monitor corporate reputation since it involves numerous factors such as credibility, reliability, responsibility and trustworthiness, customer loyalty. Corporate governance mechanisms seek to protect investors and maximization of corporate value, as well as increasing confidence on capital markets. On the other hand trust is the confidence that customers have on the provider of services to fulfil their needs. Finally customer loyalty is defined as promise of buyers to purchase particular products, services and brands of an organization over a consistent period of time.

After sub-prime lending crisis and trading mistakes nearly sank the global economy, leading private sector banks in India like, HSBC and Standard Chartered banks are again charged with money laundering charges and Multi-billion dollar trading losses at JP Morgan. Most of all, over the still-emerging LIBOR (London Inter-Bank Offered Rate) scandal of Barclays bank. Banking is an industry where trust is exceptionally important, even more than most businesses, banking is a business built on faith—the faith of depositors, the faith of investors, and the faith of counterparties. Any one of those away and the whole business stands to falter.
Banks have acted as if corporate governance and trust didn’t have much value to them. Such wrong steps as making and losing enormous financial front, and received a huge government bailout. Biggest reason to feel optimistic is that even after the many scandals of the past six years, customers don’t really hate banks, and they just want to feel that they are being treated fairly. They don’t mind their bank making a profit or that some wrong decisions lose their invested money in wrong hands.

Lot of studies suggest that many corporate reputation related risk can be avoided simply by creating a structure to evaluate and manage them. Just as a well-run bank will monitor their corporate reputation and its governance practices, smart banking companies are now learning to manage and monitor their corporate reputation by eliminating the sources of potential reputation disasters. Banks and companies today have varying degrees of expertise when it comes to managing their corporate reputation. This research study focuses on the Impact of corporate governance, trust and customer loyalty on corporate reputation among bank investors and customers in Chennai.

This Chapter presents the concept of corporate governance, trust and customer loyalty as an independent variable and the corporate reputation as dependent variable for the research study. Statement of the research problem, significance of the research study, objective of research study, research questions, conceptual framework of the research study, variables of the research study. Finally it provides an overview and contents of various chapter in the research study

1.1. Corporate reputation

“Corporate Reputation” is the perception of the corporation by the public and it is a function of triggering events that reveal to the public unknown corporate practice or a new facts regarding products and services sold by the firm.
A common understanding of this concept is pivotal to any fruitful discussion on the practical role that the board can play in overseeing the protection and enhancement of the company’s reputation. Corporate Reputation forms part of intangible assets, which include brand, human capital, goodwill, and knowhow. Corporate reputation has a significant impact on investor’s behaviour. Research by Earnest and young suggests that about 35% of investment decisions are based on factors such as corporate reputation and image of banks.

Corporate reputation is a valuable intangible asset for companies. Good reputation draws more customers, repeated purchases and favourable treatment by suppliers, bankers, the media and investors. Many factors can contribute to the accumulation of corporate reputation over time, like customer satisfaction, quality products and services, corporate culture, management and staff expertise, brand position, advertising, public relation, corporate social responsibility. Another key factor is corporate governance, even though it’s more often thought as a regulatory necessity. A strong linkage between corporate governance and corporate reputation, companies can turn a good corporate governance structure into competitive advantages. Corporate reputation plays a vital role in a business’s future value by influencing stakeholder’s behaviour and, future earnings potential and prospects. The “corporate halo” effect of a reputable business can help to differentiate products in a highly competitive sector, it may allow premium pricing and can be the ultimate deciding factor for a prospective purchaser of services.
A strong reputation can help to attract and retain high-quality employees and can deter new competitors by acting as a barrier to market entry. Reputation can also shape the attitude of regulators, pressure groups, and the media towards a business and can affect its cost of capital. “Understanding Reputation Risk and Its Importance by (Jenny Rayner, 2003).

Herbig and Milewicz (1993) have defined Reputation as an estimation of the consistency over time of an attribute of an entity. An organization can therefore have numerous reputations (like price, product quality and innovativeness reputations) and / or global reputation. Banks and Financial institutions were once the first port of call for companies seeking funding. Now companies have lost faith in their financial support. In effect, the damaged reputation of the banks as corporate lenders is now leading to a major shift in behaviour by corporate borrowers. A damaged reputation can cost an organisation in terms of decreased brand value; reduced share price; lost customers, partners, strategic relationships; and difficulty in recruiting and keeping top notch employees. After the crisis banks are now emerging with operations and systems put in place, covered by in house teams saying ‘we are covered from a risk perspective’. All this considered, it will be a long wait before the country’s banks reach parity and as Warren Buffet (2011) said: “It takes twenty years to build a reputation and five minutes to destroy it.”

1.2. Corporate Governance

In a developing countries and economics, the need to fund economic growth and to attract Investors, impose to companies to adopt good corporate governance standards. Surveys have shown that investors are willing to pay more to acquire the shares of companies with good corporate governance especially in developing countries and economies characterized by the shortage of governance traditions and weak external control markets (McKinsey & Company, 2002).
Indeed, well-governed companies and socially responsible, enjoy a better reputation in their environment, enabling them to develop a sustainable competitive advantage (Hillman and Keim, 2001). Corporate governance mechanisms seek to protect investors and maximization of corporate value, as well as increasing confidence on capital markets. Previous empirical research has investigated corporate governance relationship with information quality, earnings management or internal controls (Klein, 2002, Cohen et al., 2004, Davila & Penalva, 2006). From a corporate governance point of view, (Tonello, 2007) provides recommendations on how boards of directors can protect corporate reputation, as it claims that the board should have an oversight function in protecting and enhancing reputation.

According to Fombrun (1996, 2000) companies that have better governance practices have a better image and are more valued in terms of reputation. Reputation builds competitive advantage (Weigelt & Camerer, 1988, Fombrun & Shanley 1990, Hall, 1993) and improves financial performance (Roberts & Dowling, 2002.) Several authors have stressed and pointed out that the ultimate responsibility for the achievement and maintenance of a good reputation lies on the Board of Directors and the CEO (Kitchen & Laurence, 2003, Dowling, 2004,Tonello, 2007).

1.3. Trust:

Trust is defined as a belief of one party that other party will be fulfilling their needs and wants. As far as services are concerned, trust is the confidence that customers have on the provider of services to fulfil their needs. Generally trust can be defined as confidence that one party has on another, because of honesty and reliability of the other partner (Morgan & Hunt, 1994). Trust shows consumer commitment and satisfaction with particular brand.
An organization uses trust in brand as a risk-reduction mechanism (Doney and Cannon, 1997). Further they have stated in their study that trust is formed of two aspects, perceived credibility and benevolence. Authors also suggested two levels of trust. The first level is trust of customer on an individual and the second level represents the trust of customer on an institution. Trust is a significant intervening factor between behaviour of customers before and after the purchase of particular product. It results in the long-term loyalty and makes stronger the association between the two parties. Trust is considered as a special psychological state of mind. When a customer trusts a firm, he or she has the strong confidence in their quality of product and services of the organization.

1.4. Customer Loyalty:

Customer loyalty is defined as promise of buyers to purchase particular products and services and brands of an organization over a consistent period of time, irrespective of competitor’s new products and innovations and these customers are not compelled to switching behaviour to other competitors. (Oliver, 1999).

It is similar as the maintenance of long term relationship between customer and the organization (Gundlach, Achrol & Mentzer, 1995, Anderson and Weitz 1992). The term loyalty behaviour can be used in several different terms but basically it is considered as the intention of the buyers to make the purchases again and again to build a continuous relationship with the organization (Dick and Basu, 1994, Fornell 1992).

Customer loyalty can be attained by recognizing the client needs, organizing them, and accomplishing those. Customer loyalty and customer satisfaction both are known as an instrument to build up and achieve consistent competitive advantage (Ali et al.2010).
Oliver (1999) defined brand loyalty as ‘‘a deeply held commitment to re-buy or
re-patronize a preferred product/service consistently in the future, thereby causing
repetitive same-brand or same brand-set purchasing, despite situational influences and
marketing efforts having the potential to cause switching behaviour.’’ This emphasizes
the two different aspects of loyalty described in prior studies—behavioural and attitudinal.

Chaudhuri and Holbrook (2001) stated that behavioural or purchase, loyalty
consisted of repeated purchases of the brand, whereas attitudinal loyalty included a degree
of dispositional commitment, in terms of some unique value associated with the brand.
Thus, customer loyalty here was considered bi-dimensional, including both attitudinal
commitment and behavioural re-purchase intention.

1.5. Statement of the Research Problem

‘‘Loss of reputation is seen as the biggest threat to business. Contrast to this, with
the finding that only 22% of companies have a formal strategy in place to manage brand
& reputation risk, and the complicated nature of this risk and the enormity of the challenge
become apparent’’ (PricewaterhouseCoopers) Reputation has intrinsic current value as
an intangible asset. Although reputation will not appear as a discrete balance sheet item,
it represents a significant proportion of the difference between a business’s market and
book values (less any quantifiable intangibles such as licenses and trademarks). Since
intangibles usually represent over 70% of market value, reputation is often a business’s
single greatest asset. Reputation also plays a pivotal role in a business’s future value by
influencing stakeholders behaviour and hence, future earnings potential and prospects. A
good or bad reputation can affect stakeholder’s decisions to maintain or relinquish their
stake—be they are investors, customers, suppliers, or employees.
The “corporate halo” effect of a reputable business can help to differentiate products in a highly competitive sector, may allow premium pricing, and can be the ultimate deciding factor for a prospective purchaser of services. A strong reputation can help to attract and retain high-quality employees and can determine new competitors by acting as a barrier to market entry. Reputation can also shape the attitude of regulators, pressure groups, and the media towards a business that can affect its cost of capital. “Understanding Reputation Risk and Its Importance” by Jenny Rayner (2003).

The researcher believes that reputation of the corporate influence the investment decision, though the Impact may vary on the factor and change will persist. The researcher proposes to choose bank’s Investors and customers for his research study.

Reputation is the most important aspects of banks as a study intend to understand the corporate governance, trust and loyalty factors affects the reputation of the bank and the decision on the Investment. The research intend to study the impact of governance factors, trust and customer loyalty on corporate reputation.

1.6. Need for the study

Liberalization and de-regulation process started in Late 90’s has made a big change in the banking system. From a totally regulated environment, Indian banking gradually moved into a market driven competitive system. Globalization would gain greater speed in the coming years particularly on account of expected opening up of financial services under WTO. Major trends change the banking industry world over, globalisation of operations, universalisation of banking. We can expect great changes in the banking scene in the coming years. The move towards universal banking has already begun.
This will gather further momentum bringing more non-banking financial institutions (NBFC’s), micro finance companies into an integrated financial system. The advent of new technologies could see the emergence of new financial players like payment banks, small finance banks in the Indian banking industry.

Globalization would provide opportunities for Indian banking corporate’s to expand their business in other countries. Similarly greater presence of international players in the Indian financial system. Corporate governance in banks and financial institutions would assume greater importance in the coming years and this will be the key role in attracting the customer and investors for the banks.

In a totally de-regulated and globalised banking scenario, a strong regulatory framework would be needed. The role of regulator would be critical for ensuring soundness of the system by fixing benchmark standards for capital adequacy and prudential norms for key performance parameters. Adoption of good corporate governance practices will lead to confident to investors as well as to customer. (Vadhar, Bipinchandra T, 2011).

In the emerging banking and financial environment there would be an increased need for self-regulation. Development of best practices in various areas of banks” working would evolve through self-regulation rather than based on regulatory prescriptions. Evolution of corporate governance being adopted by banks, particularly those who have gone public, will have to meet global standards over a period of time. In future, corporate governance will guide banks, the way they are to be run. As stated by J.Wolfensohn, Ex- President, World Bank – “Corporate governance is about promoting corporate fairness, transparency and accountability”. 
In order to enlist the confidence of the global investors and international market players, the banks will have to adopt the best global practices of financial accounting and reporting. This would essentially involve adoption of prudent corporate governance practices which will eventually lead a good reputation to the banks. The focus on corporate governance is particularly crucial in financial services and, most of all, in the banking sector since this sector has lately become highly exposed to public scrutiny and has learned, in a costly manner, the risk of attracting adverse publicity through failings in corporate governance resulted in huge loss of reputation for the banks.

Hence the researcher would like to study and establish the relationship between the corporate governance and its dimension, trust and customer loyalty on corporate reputation with respect to banks in Chennai, Tamilnadu state, India.

1.7. Significance of the Study

Significance of this research study is presented in a detailed manner with respect to the following:

(A) Functional Heads, policy and process makers.

This research study would bring out the impact of corporate governance factors on corporate reputation. This research study would also provide suggestion to functional heads and policy makers of the organisation and key factors affects the corporate reputation. There are numerous studies has been undertaken on the above said area in other countries. There is paucity of studies on corporate reputation in India. Hence, the significance of this present research study lies in carrying out the research on corporate reputation of banks in Chennai, Tamilnadu state, India.
(B) Heads and top Level executives

This research study intend to study the impact of trust on corporate reputation. The research will make suggestion to heads and top level executives about the importance of trust building on their products and services and impact of corporate reputation development.

(C) Product team and Service Heads

This research study will bring out the impact of customer loyalty on corporate reputation. The research will make suggestion to product development and service management team on the importance of customer loyalty and importance of customer loyalty factor in building a strong reputation on the products and services.

(D) Board and Senior Management of the Organisation

Board and senior management of the organisation would know from this research study about the impact of corporate governance and its factors, trust and loyalty on corporate reputation. This research study would provide suggestion and bring out the importance in implementing corporate governance practices, policies and strategies to sustain and improve the corporate reputation of the organisation.

This research would provide suggestions which would enable the senior management to effectively design the strategies and policies handle corporate reputation. Research will provide the importance of corporate governance and provide inputs of good governance practices leads to development of corporate reputation.

1.8. Research Questions

This research study intend to study the following questions.

(1). What is the relationship between corporate governance and its dimension with respect to corporate reputation of a bank?
(2.) What is the impact of discipline as a dimension of corporate governance on corporate reputation and its relationship?

(3). What is the Importance of independence of director’s on corporate governance as well in corporate reputation development?

(4). How transparency and fairness with relevant to corporate governance influence’s the corporate reputation developments?

(5). How the accountability and responsibility dimension of corporate governance impact corporate reputation of banks?

(6). How the social awareness dimension of corporate governance influence the corporate reputation developments in banks

(7). What is the relationship between trust, customer loyalty and its Impact on corporate reputation among the bank’s Investors and customers?

1.9. Aim and Objectives of the Research Study

The aim of the research study is to examine the influence of corporate governance and its dimension like discipline, independence, transparency, fairness, Accountability, responsibility, social awareness and trust & customer loyalty on corporate reputation among banks and NBFC’s in Chennai.

Objectives of the Study

The various objectives of this research study are as follows:

- To assess the relationship of corporate governance and it dimension affects the corporate reputation.
- To examine the effect of “discipline” of corporate governance on corporate reputation of the bank.
- To find out the effects of “fairness and transparency” on corporate reputation.
- To find out the change in boards “independence” impacting factors of corporate reputation.
• To find out the effects of “accountability and responsibility” on bank corporate reputation.
• To find out the “social awareness” effects on bank’s corporate reputation.
• To know about demographic variable pertaining to respondents of the research study.
• To assess the relationship of trust on corporate reputation.
• To find out customer loyalty effects on corporate reputation.
• To provide suggestions based on the findings of the study.

1.10. Conceptual Model of Research study

Figure 1.1 shows the conceptual model of study by depicting the influence of Corporate Governance with Discipline, Independence, Transparency, Fairness, accountability, responsibility and Social Awareness as its dimension. Further it shows the influence of Trust and Customer Loyalty on corporate reputation (DV). This framework indicates Corporate Governance (with all dimensions), Trust and Customer Loyalty as Independent variable (IV) and corporate reputation as dependent variable (DV).

Figure 1.1 .Conceptual model of the Research study

Corporate Governance
(a). Discipline
(b). Independence
(c). Fairness
(d). Transparency
(e). Accountability
(f). Responsibility
(g). Social Awareness

Customer loyalty

Trust

Corporate Reputation
1.11. Variables of the Research Study

**Dependent variables:**

The dependent variable of this research study is **Corporate Reputation.**

**Corporate reputation:** defined as reputation as an estimation of the consistency over time of an attribute of an entity. An organization can therefore have numerous reputations (i.e. price, product quality and innovativeness reputations) and or global reputation

**Independent variables:**

The Independent variable of this research study are **Corporate Governance.**

**Corporate Governance:** defined as “the relationship among various participants in determining the direction and performance of corporations”. (Monks and Minnow, 2004).

(a).**Discipline:** The contractual governance approach proposes a monitoring role for the board through a disciplinary orientation. The board monitoring role can reassure stakeholders about the proper use of the resources provided and the protection of their legitimate interests.

(b).**Independence:** is defined as “the Chairman an independent, non-executive director are independent, and their decisions are independent in nature keeping the organisation growth, reputation in mind”.

(c).**Fairness:** considers the fairness through two different perspectives, protecting all the shareholders interests and ensuring equitable treatment of the stakeholders. In fact, the board must ensure the fairness in the execution of contracts between the company and all their resource providers.

(d).**Transparency:** Transparency means that the company provides adequate disclosure and timely information to its stakeholders regarding its operations and activities.
(e). **Accountability**: is defined as “the predisposition of an organization to provide explanations and justifications for the key stakeholders, concerned by its judgments, intentions, acts and omissions.”

(f). **Responsibility**: Responsibility refers to “the recognition of all stakeholders’ rights such as provided by law and the promotion of active cooperation between the company and main stakeholders to create wealth and sustainable enterprises”.

(g). **Social Awareness**: is defined as “company explicit environment conscious and social responsibility.”

**Trust** and **Customer Loyalty are** independent variable.

**Trust**: trust has been defined as a “set of specific beliefs dealing primarily with the integrity, benevolence, and ability of another party”.

**Customer Loyalty**: Customer loyalty has been defined as a “deeply held commitment to repurchase or re-patronize a preferred product/service consistently in the future, thereby causing repetitive same-brand or same brand-set purchasing, despite situational influences and marketing efforts having the potential to cause switching behaviour”.
1.12. Chapters in details

This Ph.D. research thesis has five chapters:

(1) Chapter I: ‘Introduction’ chapter enlightens on variables of the research study. Statement of the research problem, significance of the research study, need for the study, research questions, objectives of the research study, conceptual framework of the research study, variables of the research study, operational definitions of variables used in the research study and chapters covered.

(2) Chapter II: ‘Review of Literature’ chapter presents both the conceptual literature as well as empirical reviews on variables, Indian context of corporate governance and previous researches pertaining to variables of the research study.

(3) Chapter III: ‘Research Methodology’ describes the methodology used to carry out this research. This chapter contains research design, source of data and unit of analysis, universe, sampling, sample size, hypothesis, and tool of data collection, pilot study, data collection and statistical tests used in the research study.

(4) Chapter IV: ‘Results and Discussion’ chapter presents the statistical findings of the research study and discussion pertaining to the findings of the research study.

(5) Chapter V: ‘Findings, Suggestions and Conclusion’ chapter presents the summary of statistical findings pertaining to the research study, suggestions, limitations and scope for future research. This is followed by the references and the appendices.

The next chapter ‘Review of Literature’ portrays both the conceptual literature as well as research studies relevant to variables of the research study.