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The Role of Reputation Management and Sustainable Corporate Governance in Enhancing Financial Resilience

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Abstract. Constantly evolving business environment accretes the complexity of operation for corporations in the modern era. Firms strive to maintain financial resilience, especially in the face of adversities and systemic challenges like the COVID-19 pandemic, banking collapses, and geopolitical crises. This paper underscores the importance of reputation management and sustainable corporate governance in mitigating financial volatility and fostering long-term stability. Through a mixed-method analysis, such as an event study on the collapses of Credit Suisse using financial models and regression analyses, the study evaluates the impact of market sentiment, media exposure, and stakeholder trust on corporate performance. Additionally, to minimize market shocks and restore confidence, integrating sustainable managerial initiatives such as corporate social responsibility (CSR) and Environmental, Social, and Governance (ESG) has been found to be contributive as a proactive risk mitigation. Considering trade-offs, such as the financial costs of sustainable projects and the unpredictability of public reactions, corporations should adopt reputation management strategies with a focus on authenticity, transparency, and timely execution. By combining short-term crisis management to address emergent scandals with the integration of sustainable governance for long-term stakeholder alignment, firms can effectively enhance financial resilience and navigate modern economic challenges.

Keywords: Reputation management, financial resilience, event study, ESG, CSR.

1. Introduction

Economic contingency over the past decade has proliferated due to a ceaseless evolving business environment, elaborate financial structure, and intricate technological interaction [1]. Drastic financial crisis and economic fluctuation were witnessed by various sounded events, namely the COVID pandemic, G-SIB bankruptcies, wars, and energy crisis. Effective corporate governance, under such a context, is necessary to mitigate the external risk and strengthen financial resilience. During systemic crises, such as the collapse of SVB and Credit Suisse, a series of financial downturns in banking sectors led to millions of market value evaporating due to the contagious scandal influence [2]. Historical lessons highlight alarming calls for corporate management, urging the need for proactive risk management not only for mitigating short-term contingent problems but also for fostering long-term resilience.

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Among various considerations under management scope, there is a prevalent trend of adopting reputation management, including the incorporation of sustainable initiatives [3]. Specifically, reputational management refers to a strategic process to shape, maintain, and enhance firms' public image, establishing credibility and trust among stakeholders [3]. Some strategies include transparent communication, monitoring public sentiments, and risk management to prevent prevailing scandals. Present approaches also include active corporate involvement in corporate social responsibility (CSR) and Environmental, Social, and Governance (ESG) principles in their sustainable operations, addressing negative feedback constructively [4].

However, even acknowledging the merits of these approaches, firms vary in the extent of adoption. As witnessed by past crisis windows, remarkable performance fluctuation is not yet effectively contained. Hence, this paper aims to investigate the relationship between reputation management, sustainable corporate governance, and financial resilience. By analyzing examples of real-world crises, the study seeks to identify the specific extent to of these practices are used in addressing the financial volatility and stakeholder concerns. Through these inquiries, critical analysis will be provided with effective measures to strengthen corporate resilience, benefiting corporations both in the short term and long-term sustainably within an increasingly volatile economic environment.

2. Corporate management and financial resilience

2.1. Impact of market sentiments and need for reputation management

The performance of a corporation is measured not only on the basis of its fundamental operations and revenues, but also the brand value and stability play a prime role. The perspective of how the market, consumers, and investors perceive a brand creates transformative power in driving market sentiments, which ties to the performance of a firm [5].

There are copious cases where stock prices can be highly volatile or even deviate from the fundamental measures due to capricious market sentiment. GameStop and AMC, for instance, are exposed to more than 100% of the implied volatility due to the constantly evolving ambivalent market speculations, which curbs potential investments by vitiating investor confidence [6]. Moreover, negative news exposure can aggravate the situation. As shown in Figure 1, for instance, since the inception of scandals about Credit Suisse's "spying on former employees" and "Chairman violating Covid lockdown rules", the events that are irrelevant to corporate performance have heightened the stock volatility of the firm by damaging the brand image [2].

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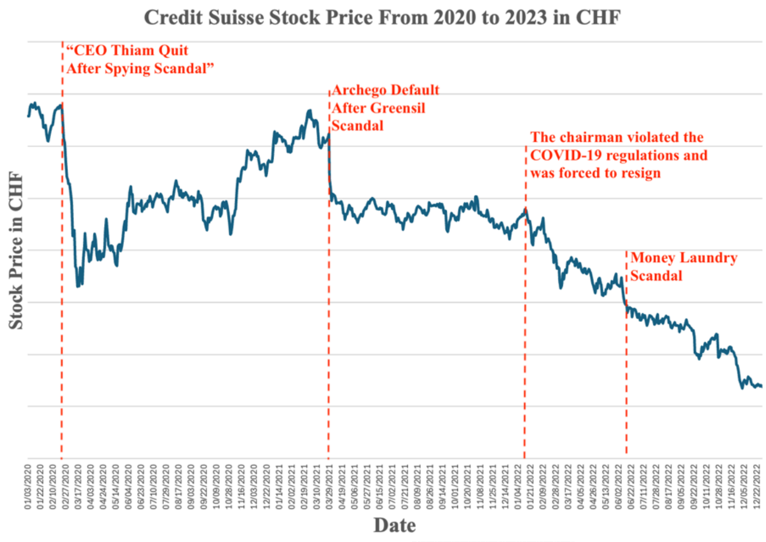

Figure 1. Scandals and stock price reactions for Credit Suisse from 2022 to 2023 [7].

As shown in Figure 2, for the event window within [5,15] days around "CEO Thiam quits after spying scandal", the cumulative abnormal returns (CARs) conducted via the CAPM model demonstrate a significant decline, signifying adverse stock response and heightened volatility as a reaction to scandals. Evidently, the financial resilience of companies can be seriously threatened by various scandals and versatile market sentiments, stressing the need for proactive reputation management to absorb shocks and restore investor confidence.

Figure 2. Event study for "CEO Thiam quits after spying scandal" and CAR

Event study for "CEO Thiam quits after spying scandal" and cumulative abnormal return response for Credit Suisse. CAR computed via the CAPM model using European Stock 600 as the market index and 10-year US treasury as the risk-free asset over the past year from the event window.

Apart from idiosyncratic impact, systemic sentiments are also a vital consideration for building financial resilience. Modern finance and business environment as an elaborate mixture implies a close association among different stakeholders. Banks are interconnected by deposit borrowing and derivatives, while firms are mutually impactful by their operational environment and production processes [2]. Illustrated by the previous example, the collapse of Credit Suisse – a G-SIB – led to a

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serious contagious effect in the banking sector [2]. The fear of a systemic banking crisis generalized to other European banks, even though the scandals were idiosyncratic and irrelevant to them [2]. In addition, the dynamic of the business environment is another consequential systemic risk. Globally influential events like the outbreak of COVID and lockdown policies in China restricted capital mobility and diminished overall confidence in investing and consuming [8]. As a corollary, industrial firms suffered from skepticism about a shortage of sales and factor supply. Conceivably, without direct communication clarifying the concerns, low market confidence deters investment prospects over the sector as a whole [9]. On the contrary, certain firms demonstrate strong resilience during systemic crisis and share similar characteristics of proactively avoiding skepticism either by transforming the production with situationally advantageous factors, such as the production of medical-related products, or effectively communicating to report the functionality of current operation [10]. Without the mitigation of systemic risk, the weakness can easily spread and worsen the financial resilience of corporations.

Another factor that fueled the process is the media. Over the past decades, media exposure was accelerated by the prevalence of mobile devices like laptops and phones, creating a multiplier effect for messages with an ease in transmission, especially for astonishing scandals with captivating content about familiar brands [11]. This magnified the negative influence on reputation and brand image. According to statistics, corporations, particularly those with high public exposure, have their problem reported more frequently in news, headlines, and papers, gaining considerable views, affecting market sentiments [11]. Consequently, market volatility is heightened by the spotlight attention, exaggerating the influence. For instance, there is a tractable proliferation in stock volatility after the CEO of Tesla – Elon Musk – posts a single tweet [12].

Hence, according to the historical performance, clearly, market sentiments and scandals play an influential role in worsening the financial resilience as they are associated with more market volatility and speculative market behaviors. This influence is further moderated by media exposure and news effects, making negative news far more alarming for large corporations by causing widespread fear and loss of confidence, urging the need for reputation management.

2.2. Role of sustainable corporate governance

Apart from the issues with the negative brand image resulting from reputation crises, proactive campaigns to improve public image and corporate dedication to social and public interest are paramount. Corporate Social Responsibility (CSR) projects combined with Environmental, Social, and Governance (ESG) concepts are vital for building financial resilience [4]. Considered as a shield against external shocks, ESG methods are gradually seen as lowering risks and providing long-term financial stability [4]. Beginning in 2020, several nations like China and the US are tightening control over environmental issues [13]. Corporate efforts of switching to sustainable energy sources, such as electric automobiles, were subsidized, benefiting bureaucratically and monetarily [13]. On the other hand, companies with high carbon emissions were fined and had their operating accessibility threatened [13]. National rules, therefore, provide an anticipation effect that changes consumer and investor attitudes toward the prospect forecasting for various companies, expecting actions consistent with the ESG criteria. For example, the Dieselgate Volkswagen emissions scandal resulted in heightened stock volatility of approximately 40%, signifying €30 billion in fines and court settlements due to the dishonesty over emission tests, turning the scandal into financial losses [14]. Furthermore, evidence supporting this also comes from the trend that ESG-aligned companies usually show better operational efficiency and reduced capital costs. There is a significant correlation between ESG scores and financial performance indicators like return on equity (ROE)

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[15]. Hence, these findings demonstrate how strategic tools that reduce vulnerability to environmental, social, and governance risks increase organizational resilience, enhancing ESG practices from ethical imperatives.

Apart from risk mitigation, high stakeholder interaction and loyalty can be achieved via CSR initiatives, which are vital to cushion crises. During Covid and the financial crisis, the corporate and stakeholders' relationship is fragile due to the conflict of interest between employees' and shareholders' welfare [16]. When the economy witnesses low productivity and demand, to reduce the variable cost and maintain operational efficiency, managers are inclined to lay off employees and marginalize the welfare of employees or customers in extreme cases [17]. As depicted by unemployment and payroll statistics provided by the World Bank, there was a significant decline during 2008 and 2020 [18]. Companies weaken the stakeholder connections, facing a loss of intellectual capital and corporate loyalty. On the contrary, Starbucks's employee-first initiatives during the COVID-19 epidemic, for instance, including more perks and job security, produced better retention rates and created a positive social image [19]. Reflected by employee retention rates, Starbucks was performing in a leadership position relative to its comparative peers [19]. By strengthening stakeholder ties, CSR-minded businesses can help to offset the negative consequences of economic shocks.

Moreover, during economic hardships, community-based CSR integration as a management tool provides advantages in recovery performance and enhances corporate social image. It is found that businesses that actively engage in disaster relief programs, community interaction initiatives foster goodwill that accumulates brand equity, which is considered a financial safety net [20]. This is because devoted consumers and supportive communities demonstrate a higher inclination to develop long-term connections with brands, especially during a crisis [20]. When enterprises reported helping society and delivering goodwill to communities, contrary to prevalent negative news during the crisis, it captured attention and established preference. For example, Walmart promised to deliver disaster relief efforts, like contributions to recovery from Hurricane Katrina, and donations of over $20 million in cash and over 2400 truckloads of emergency goods to the affected area [21]. This deliberate contribution was verified to be a significant source of positive exposure that improved customer perception, which was materialized by strengthening of financial capital, as Walmart reported around 4.6% growth in same-store sales following the event, higher than the industry average, rooting the market position and financial stability [22]. Accordingly, this underscores the importance of ESG and CSR incorporation in reputational enhancement, aiding the risk management practices.

2.3. Evaluation of trade-offs and value creation

Regardless of the aforementioned benefits for reputation management and sustainable incorporation, those practices also come with a cost. For public relations management via media or public platforms with high accessibility, a prepared and elaborate investigation into specific events needs to be carried out before the announcement to counter scandals. This is because authenticity is essential for building a reliable perception of enterprises [23]. One example of fraudulent reputation management can be illustrated by Luckin Coffee Inc. The corporation managed to fabricate $310 million in sales in 2019 to sustain its lucrative and profitable image, which was found to be deceptive [24]. Consequently, not only was it fined $180 million, but also its stock collapsed by more than 80% on NASDAQ, which inversely affected its financial resilience [24]. Therefore, reputation and public relations management necessitate time and effort to deliver a response in a veritable manner; time lag can sometimes exist when treating an emergent public relations crisis.

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Moreover, although carefully managed, market response and sentiment are unpredictable in many cases. The change of CEO, for instance, triggers different investors' responses. When Starbucks announced new CEO Brian Niccol, its stock price surged more than 20% within a day [25]. On the contrary, Wells Fargo's CEO replacement triggered an adverse market response. Constant changing authority and deep-rooted financial problems result in a decline in stock price [26]. Therefore, corporations need to investigate both immediate and long-term implications, making sure public announcements are timely, transparent, and align with market expectations.

While sustainable management of ESG and CSR involvement creates risk-mitigation and long-term stakeholders' benefits, its short-term impact on financial resilience can be asymmetric. It is found that for corporations with an initial low-ESG rating, the cost of implementing and promoting an ESG score exceeds the potential losses from ESG scandals, especially for SMEs (small and medium-sized enterprises) [27]. The average expected return on investment (ROI) on many sustainable projects was less lucrative than productive main business [27]. Therefore, corporates need to balance the expenditure over ESG investments in the short term without affecting their operational efficiency and liquidity measures, while demonstrating their commitment to sustainable practice for long-term reputational and political welfare.

3. Implications and recommendations

Implicated by prior analysis, reputational management is pivotal for financial resilience and counteracting the effects of systemic shocks from crises. In the short run, emergent scandals and public relations crises need to be effectively managed to stifle immediate shocks from spreading and amplifying through media exposure. Companies must prioritize timely communication and authenticity through transparent reporting to maintain stakeholder trust.

For the long-term financial resilience of the corporation, proactive integration of sustainable initiatives like ESG and CSR concerns is essential. These measures act as moderators to resilient corporate operations, avoiding fines and political violations while enhancing stakeholder loyalty. Moreover, in terms of funding for growth, high ESG scores attract sustainable and mutual fund investors, as growing ESG stock portfolio preference.

Furthermore, the essence of performance resilience also lies within financial fundamentals. Corporations should balance the short- and long-term investment trade-offs, effectively manage their main operations and asset allocation to sustain healthy cash flow growth, which prevents insolvency and liquidity problems during crisis and funds shortage.

4. Discussion

Most analysis within this paper is conducted via case study and event study, which challenges the generalizability to corporations with different characteristics and operational environments. Future studies may conduct controlled experiments to collect primary data and examine the causal impact and the extent of effectiveness of specific reputation management to counteract scandals, which gives implications for specific reputation management methods for practical suggestions. Moreover, moderation analysis may be conducted to quantify the relationship between event exposure and financial volatility while identifying moderators like GDP per capita, market shares, and corporate financial data, such as liquidity ratio, revenue growth, and leverage ratio, to provide a more holistic analysis.

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5. Conclusion

Through conducting an event study and analyzing the historical performance of different firms under crisis windows such as pandemics, natural disasters, and systemic bankruptcy, there is a close association between market sentiments and disturbance over financial resilience for corporations. Financial volatility is amplified by changing market perspectives and business environment, further moderated by the prominence of media exposure. This highlights an urgent need for reputation management to offset the influence of short-term market panic led by shocks and scandals and restore stakeholder confidence. In the long term, integrating CSR and ESG initiatives in sustainable management was found to be effective in aligning with public and political expectations. By proactively social activities through providing public welfare and securing employee benefits, stakeholder interaction and loyalty are secured as a cushion for economic shocks. Nevertheless, tradeoffs such as the financial cost of sustainable projects and unpredictable market reactions need to be considered, which implies the importance of authenticity and timely decision-making. By combining short-term crisis management with long-term sustainable governance, corporations can effectively enhance their financial resilience in an increasingly interconnected and volatile global economy.

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