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The name's the game: Does marketing impact the value of corporate name changes?

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ABSTRACT

Each year, thousands of firms change their names, many in the absence of an accompanying M&A event. Existing research reveals significant heterogeneity in the stock market response to such pure name changes. Why do some firms reap greater stock market rewards for changing their names? Our study of name change announcements by 180 publicly listed U.S. firms reveals that marketing-related factors play a critical role in the value of corporate name changes: Firms with high marketing influence in their C-suite, high marketing investments, and high marketing capability receive greater stock market rewards for changing their names. Firms that change their names to leverage a strong brand in their portfolio, or to proactively communicate a change in their scope of business (i.e., a future change in their product portfolio or geographical markets), are also rewarded more than firms that change their names to retroactively align their names with a new scope.

1. Introduction

Each year, thousands of firms across the globe change their names (Standard & Poor's Capital IQ database), many in the absence of an accompanying merger and acquisition (M&A) event. Prior scholars (e.g., Wu, 2010) have classified name changes unrelated to M&As — the type of changes we focus on in this article — as *pure* name changes. Examples include RIM's name change to Blackberry, Apple Computer Inc.'s name change to Apple Inc., and Federated Department Stores Inc.'s name change to Macy's Inc.

A firm's name change is a major strategic action that usually comes with significant tangible costs associated with communicating the change to various stakeholders, and intangible costs associated with loss of the existing name. One wonders whether the benefits of these changes actually justify their costs. Surprisingly, some researchers (e.g., DeFanti & Busch, 2011) find a positive, some (e.g., Karbhari & Sori, 2004) highlight a negative, and others (e.g., Bosch & Hirschey, 1989) report no association between corporate name changes and shareholder value. Research that sheds light on these inconclusive results and explores the boundary conditions under which name changes increase shareholder value is limited on at least two fronts.

First, little work has gone into understanding whether certain types of name changes are rewarded differently than others, and if so, what explains these differential rewards. Second, existing research on corporate name changes (e.g., Bosch & Hirschey, 1989; Cooper, Dimitrov, & Rau, 2001; Howe, 1982; Karpoff & Rankine, 1994; Kot, 2011), focuses mostly on finance-related contextual variables such as prior firm performance and firms' classification as financial or non-financial institutions. Notable for their omission are studies exploring the role of marketing-related factors in the value of corporate name changes. This omission is highly surprising, given that understanding whether the existing name has lost its appeal with customers, selecting a name consistent with the intended firm image, and communicating a name change all require significant marketing expertise.

We address these limitations by conducting an event study of pure name change announcements by 180 publicly listed U.S. firms. We first classify different types of name changes, and explain why we expect the stock market to react less positively to one particular kind. We then explore the impact of three marketing variables on the valuation of name changes.

2. Theory

2.1. Common types of pure name changes

Content analysis of the press releases accompanying name changes unrelated to M&As helps reveal two common motivations for pure name changes: (1) Leveraging a strong existing brand in the portfolio, and (2) communicating a change in the scope of business (i.e., a change in the firm's product portfolio or geographical markets).

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Federated Department Stores' adoption of the Macy's name, can be classified as an example of a firm leveraging a strong brand in its portfolio:

"*By aligning our corporate name with our largest brand [Macy's], we will increase the visibility of the company with customers, leverage the world-famous Macy's brand name, and get more credit for our accomplishments in the marketplace.*" (CEO Terry J. Lundgren)

In the case of Chinadotcom changing its name to CDC, however, the firm, as revealed in its press release, intended to communicate a change in its scope of business — a change involving greater product and geographical diversification:

"*The new name, without 'dotcom' signals the shift of our business focus away from a heavy reliance on the Internet sector. In addition, the new name without the clear reference of 'china' symbolizes the company's more geographically diversified revenue and customer mix.*"

Similarly, the motivation behind Immtech Inc.'s name change to Immtech Pharmaceuticals, as revealed by the company's press release, was to communicate a new business scope that involved the launch of the firm's first oral drug and an entry into the pharmaceuticals market:

"*This name change signifies the start of a new era for our company as we move our first oral drug candidate … toward commercial launch and marketing.*" (CEO and Chairman Eric L. Sorkin)

We broadly consider Chinadotcom and Immtech Inc.'s name changes as examples of firms communicating a change in their scope of business. However, we use another factor to subclassify this latter category of name changes even further: the timing of the name change.

When changing its name to communicate a new scope, a firm may change its name either proactively, whereby it changes its name *prior* to initiating changes in its business scope, or retroactively, whereby it changes its name *after* initiating a transition in its business scope. Immtech Inc.'s name change to Immtech Pharmaceuticals can be classified as a *proactive* name change, as the name change announcement preceded Immtech's entry into the pharmaceuticals market. Chinadotcom's name change to CDC, on the other hand, can be classified as a *retroactive* name change. The word *diversified* used in the past tense in the press release ("… the new name … symbolizes the company's more geographically diversified revenue and customer mix") reveals that the company had already diversified beyond the Internet product and the Chinese market at the time it decided to adopt the CDC name.

Given these three classifications of name changes, then, one wonders whether some types of name changes are likely to reap greater stock market rewards than others.

2.2. Investigating the financial valuation of different types of name changes

Prior researchers (e.g., Horsky & Swyngedouw, 1987; Karpoff & Rankine, 1994) have highlighted two mechanisms by which name changes help firms: (1) inherent value and (2) signaling value. Inherent value involves the new name *itself* increasing the firm's cash flows by improving customer awareness or perception of the firm. Signaling value, on the other hand, involves the firm's act of changing its name providing a promise to investors that the company is likely to make value-generating changes in its business operations.

A firm that adopts the name of a strong brand in its portfolio is expected to benefit from both inherent and signaling value. By making its link with a prominent brand more explicit, a firm is likely to increase customer awareness of the firm and improve customer perception of its other brands. Furthermore, investors are likely to be reassured that a firm's top executives are unlikely to risk diluting the adopted brand without being confident about their firm's future prospects.

A firm that changes its name to communicate a new scope (whether retroactively or proactively), assuming the new name is appropriate, is also expected to gain inherent value by changing its perception in customers' eyes. For example, Chinadotcom's name change to CDC is expected to help change customer perception of the firm to a more globalized one, thereby attracting new customers from outside China. Similarly, Immtech Inc.'s name change to Immtech Pharmaceuticals is likely to help attract customers who may otherwise not have been aware of the company's entry into the pharmaceuticals market.

With regard to signaling value, when a firm proactively changes its name to communicate a forthcoming change in scope, the name change helps communicate relatively *unexpected* news to investors. The efficient market hypothesis would then dictate that investors would update their expectations of the firm's future cash flows, and the expected value of the new strategy would be incorporated into the firm's stock price quickly. However, when a firm retroactively changes its name, investors are expected to have already tracked the firm's gradual transition in scope. Most of the value of the new scope would then have already been incorporated into the firm's stock price. Any limited value that the name change announcement provides would then be reflective primarily of inherent value and the limited *additional* confidence to investors about the potential of the firm's new scope. Thus:

H1. Relative to a firm that changes its name to retroactively align its name with a new scope of business, a firm is likely to be rewarded more by the stock market if it changes its name (a) to leverage a strong brand in its portfolio or (b) to proactively communicate a new business scope.

2.3. Investigating the role of marketing in the financial valuation of name changes

We believe three marketing factors help answer some important questions investors may have while evaluating a name change announcement: (a) Does the choice of the new name, and the strategic shift that the name change may communicate, make sense from a customer perspective? (b) Is the firm likely to make sufficient marketing investments while implementing the name change process? (c) Does the firm have the capability to use its marketing resources *efficiently* while changing its name?

2.3.1. Investigating the role of marketing's influence in the C-suite

Investors are likely to be uncertain about the inherent value of a new name because names that are adopted whether to leverage an existing brand or to reflect a changed scope differ significantly in regard to such intrinsic features as memorability, meaningfulness, aesthetic appeal, transferability, adaptability, and associations (Yorkston & Menon, 2004); differences in such name characteristics are in turn related to differences in customer perception of a firm. Thus investors may be uncertain whether a new name is in line with the intended firm image, and whether it will succeed in changing customers' perception of the firm to a more globalized or more diversified firm.

Similarly, investors are expected to have at least some uncertainty about the value-generating potential of a change in scope that the new name may foreshadow. This uncertainty occurs because, while venturing into new product segments or geographical markets may help firms stimulate growth (Campa & Kedia, 2002), changes in scope may also hurt firms by making them move away from their core competencies (Denis, Denis, & Sarin, 1997). Furthermore, investors may be uncertain about the TMT's ability to effectively manage the strategic