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# MARKET THEORIES ANALYSIS FOR THE WEB MARKET AND INCORPORATION OF REPUTATION AS A COMPETITIVE FACTOR FOR WEB COMPANIES

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**Abstract:**

*The goal of this paper is to familiarize the reader with the way reputation is mainly treated as well as the way it could be treated for web companies when they are focusing on selling to other markets than their own. This paper covers the reputation concept as a competitive advantage, as well as the treatment of this for a web company that wishes to sell abroad.*

**Key words:** *Reputation; Web market; Reputation if going abroad*

## **1. Introduction**

The reputation as a concept is treated by researchers as posing a competitive advantage for companies and their products. Customers would rather choose companies with a good reputation, as the latter presents the good or bad opinion about the company or the company's products by other customers.

Reputation as a competitive advantage for the companies allows them to become more flexible in terms of their prices. This is due to the fact that prices in an economy tend to be sticky, according to the Keynesian theory. This is true in terms that a higher reputation a company has the more it can hold prices at a certain level, which usually is above average market level.

The web market being a market strongly based on information we could presume that it also responds to reputation, very well. Though reputation can play an important role even for the real market companies, it is crucial for a company which sells something that a potential customer can't feel at the moment of purchase.

This paper presumes that reputation is a very important factor for the web market theory. It could explain the way competitive collusion works on this market as well as help us understand why people from other companies when buying online prefer certain companies to others.

## **2. The concept of Reputation in Competition**

As explained in some sources reputation presents a competitive advantage on the real market. This reputation can be associated with a brand or a specific retailer in some cases.

Even on the real market reputation can influence a consumer's willingness to buy from a specific retailer or to choose a specific brand. This is due to the fact that reputation incorporates the company's previous experiences. These in turn helps potential customers see the company as a trustworthy place to make their purchases.

Researchers often associate good reputation of a brand to the competitive advantage of its products. This in turn brings us to another conclusion that a bad reputation can pose a competitive disadvantage of the products, thus leading to the decline of the company's sales figure.

Michael E. Porter (1998) determines that we can speak of a global market, and the companies that operate on this market are grouped into clusters. This diminishes their costs and leads to a high quality and innovative product. In some way this can be thought of as being a kind of reputation of regions. I.E. people consider the Silicon Valley as being an innovative cluster, this is due to its reputation of doing so in the past periods.

David M. Kreps and Robert Wilson (1981) show that in a two stage game reputation plays a crucial role since sellers try to build up reputation in the first stage as to appear benevolent and this in turn brings to better sales in the second period.

Paolo Vanin (2007) stated that nowadays competition is hand in hand with reputation since the disregard for a company's promises might lead it out of the market. This is shown due to the fact that if buyers pay a higher price for high quality and area cheated, the company that cheated them, thus gaining bad reputation, will have a hard time making sales in the second term. This could lead for companies to intend to become trustworthy as by Klein and Leffler (1981). Paolo Vanin in his paper from 2007 does not use in his analysis such factors as brand image and advertisement in order to make the model easier to predict.

However reputation is not accepted by all economists as a factor that influences competition. One strong point that reputation is given by Matthias Sutter, Uwe Delleck and Rudolf Kerschbamer in their paper from 2009, where they studied a large experiment of 936 participants for efficiency in credence goods markets. This research had as a conclusion that allowing sellers to build up reputation had little influence.

Although reputation can pose a competitive advantage its use in the analysis of companies on the real market is of limited value, due to the fact that Fortune ratings are made by the financial performance of the company. The financial performance of the company although it might rely to some extent on reputation it has more important factors incorporated [David L. Deephouse 2000].

Reputation as a competitive advantage allows companies to be more flexible. This flexibility is expressed in terms of prices that can be thought of as sticky and thus

they do not completely and immediately reflect the fluctuations in supply and demand. I.E. the reputation of a company or its products is high therefore customers will buy it even if the price is relatively high as compared to the other competitors that are led by the supply demand ratio.

From this example we can understand that the higher the reputation of a company or a company's products the more this company will be chosen by client in disregard to their possibly higher prices. Therefore the reputation can be thought of as being a factor that can allow a company to receive higher mark-ups without decreasing their sales.

Reputation can be thought of a company's asset, and as any other asset it has specific particularities. The main particularities of reputation consist of the fact that reputation is harder to earn than to lose.

In order to create a good brand reputation it takes a series of successful promotions, events and satisfied customers. The post sales service can help the company build up their reputation, thus encouraging more customers to make their purchases from a certain company or a certain company's products.

Although it is hard to build up a good brand reputation and recognition, it is rather easy to obtain bad reputation for the company, because all it takes to spoil a company's reputation is a couple of bad practices. Due to this fact companies are more inclined to research and develop around practices that were successful in the past, without trying anything conceptually new.

Thus, though, reputation can pose a competitive advantage, but at the same time it encourages companies to come back to practices that proved efficient in the past, with just some improvements on the latter. This fact can explain why, the majority of the products even though they pose the same level of reputation there are still not many companies willing to innovate conceptually.

The main market theories do not give reputation enough value in the market analysis, this being due to its limited role in the financial indicators of the companies. Although, nowadays, reputation started being researched at a higher scale as a competitive advantage factor, it is still not too common to come by, in the analysis.

### **3. Reputation as an important competitive factor on the web market**

Although the web market is a relatively new market, it has some characteristics which do not differ greatly from the classic markets [Sută-Selejan 1996], thus making some of the concepts from the neoclassic theories apply to this one as well.

The web market has specific segments, some of which do not have counterparts on the real market. This and another number of particularities makes the web a more specific market to analyze with the classic market theories.

The reasons, why the classics cannot be applied to the web market, number elements such as goods exchange values and unfortunately even the "invisible hand" principle cannot fully apply to the web market. Although the web market has the possibility to auto regulate and to come to the normal prices, but since the prices on

the web market tend to be sticky it sometimes takes time. The governmental regulation is again not a very attractive option, if it were to be implemented on a country level.

As a market theory we could combine some of the aspects of the classic and neoclassic theories to make them more feasible for the web market. Thus we are to define some basic concepts of the market and how we could define them in terms of the existent theories.

Firstly the web market doesn't differ in terms of the market regulation as in market freedom. The web market is known for its freedom as compared to the real market, where some regulations may apply without favoring some companies over others, but as the web market companies compete on a global level, thus the local regulations could generate some benefits of detriments.

The market has a possibility to auto regulate to a normal state, though it has to be regulated in terms of mergers. The market auto regulation is possible due to the active competition and the rivalry for a larger market share. While the market can auto regulate and it might not seem necessary to be regulated in terms of antitrust policies, it isn't so. For the real market when the institutions analyze mergers they view their financial data as well as market shares, to determine whether the merger could be malefic for the market. In terms of the web market while the merger might not seem to distort the competition in any obvious way by financial figures, it might do it by potential. So on the web when a merger was to be analyzed not only financial figures should be researched, but the amount of visitors as well, because if a website has a large number of visitors or users, but doesn't profit from the fact it because they do not have means and in the case such a website would be overtaken by an advertisement agency, it would surely give them an advantage against their competition.

So the regulation of the web market should indicate that the institutions that analyze mergers and other antitrust cases they should also take into account the amount of users than merger has gained, not only market share, which doesn't necessary mean the same thing. I.E. youtube.com has a high number of users [Xu Cheng, Cameron Dale, Jiangchuan Liu 2007], but not whole of its users create its market share, as it generates revenue by advertisement.

The second aspect which we should cover would be the entry barriers, as apparently there are few to enter the market. Although in order to be competitive you should make your potential consumers be aware of the fact that you are present on the market. After awareness there are a number of other steps in order to be competitive. These steps were described in the previous chapter. The steps progress as follows first the potential consumers have to be aware of the company's presence on the market, then they have to trust the company and then the reputation starts playing a crucial role and only after all of these steps are achieved price becomes an important factor.

The amount of companies on the web market is large, while the market cannot be exactly called a perfect competition, as the market shares of these companies differ greatly. There are a number of extremely large companies that own a lot of websites, via mergers that hold the majority. (I.E. google, amazon etc.)

A very important characteristic of the web market is that the companies try to gain a competitive advantage through advertisement which is most frequently used to make the potential customers aware of the services that come post-purchase. Therefore the market itself relies a lot on the post-sale services, as well as different delivery terms, customer support services etc. Being a service based market means that customers would choose one web company over the other according to the services that these companies provide.

The service aspect of any good bought from the web leads us to the idea of the advertisement that is done by the means of online ads, as well as mouth to mouth transmission. This can be attributed to good reputation, as positive reputation reflects the opinion of the customers' about the service or the truthfulness of the statement that the company provided, be it after purchase or prior to one. I.E. if a customer buys from a company that states that the goods will be delivered free of charge at a certain date and fulfills this promise, then the customer would be more tended to praise the company to his friends, and even post positive feedback on the website itself that might determine other potential customers to buy precisely from that website.

The types of consumers that buy from the web market could be categorized as having bounded rationality. Their rationality is bounded by the fact that they do not see the whole market and make their decision based on the image a certain web company has created. I.E. one of the most used and well known e-commerce websites is amazon.com, this is due to the fact that it has a large number of satisfied customers.

A completely rational consumer would rather go for the lowest possible price for a certain good. While on the web market we can see that clients prefer to pay more but on a website with a good reputation and on the one they trust. So in this the web market tends to follow the market theories of the Harvard School of Economic thought that states that consumers have bounded rationality. This can be due to their preferences or to the insufficient information on the market.

Now we can speak more in depth about the reputation factor and its potential impact on the supply and demand effect on price setting. Due to the fact that web market consumers make a decision to buy from the web judging by the fact that they either trust the market or they don't, we can say that trust and reputation can have an impact on the decision to buy. In this manner this market is pretty similar to the mass media segment of the real market, in terms that it relies on information [David L. Deephouse 2000].

A good reputation of a certain web market company can influence consumers to use their services or buy their products even if the price set by them isn't necessarily the lowest from the market. Thus if demand drops the ones that will be forced to lower their prices are the companies with lower reputation or trust. On the other hand the companies that have a high reputation will still have their sales volume at the same level. Although we have to mention that if the demand drops drastically on the most important market for the web company then even the companies with a high reputation would have to lower their prices. Another important aspect is that if the demand is to

drop on the market that is of secondary importance to the web company, then the company won't have to decrease their prices.

The demand drops on the web market may not affect directly their prices, but if the demand drops on the real market, and real market companies lower their prices, than the web market in turn would have to lower them as well. This is due to the fact that the web market companies gain their competitive advantage from the fact that they have lower prices than the real market and sometimes better service. However if the web market would have the same prices as the real market it might lose sales, because it wouldn't seem as attractive to customers.

Another important aspect of reputation is that when a web company is viewed from another market than that of its origin, then the reputation of its country of origin is very important as it might set a competitive advantage on that market. Let us have a company A, which is situated in country A<sup>1</sup>, then the reputation scheme, can be viewed in the table 1.

**Table 1: Country Reputation against Company reputation, competitive advantage analysis**

		Reputation of Company A in Country A <sup>1</sup>	
		High	Low
Reputation of Country A <sup>1</sup>	High	A high competitive advantage	No Competitive Advantage
	Low	No Competitive Advantage	A competitive Disadvantage

*Source: Developed by the author*

As we can see from table 1, the competitive advantage is seen even if the company A is being viewed from another market than that of its origin country. A reputation of a country however means that it is regarded as being good in the field that the company A operates.

When the company has a high reputation on a market that is considered unqualified or regarded poorly in the field of the company, then this reputation is annulled by the fact that the country doesn't instill power in the field. I.E. if a company sells shoes and is from a country that is not highly regarded for shoe sales, then it will be regarded as a poor company on another market, and won't be chosen in favor of more powerful competitors. The same situation would arise in the case that if a company has a low reputation on a qualified market.

While if we are to analyze the impact of reputation on the competitive advantage of a company on another market, if the market has low reputation as well as

the company from that country, then the company would be faced with a competitive disadvantage.

In conclusion we could say that the web market is a market characterized by bounded rationality from the customers, it has low entry barriers, it can be thought of as being global and at the same time this type of market is highly dependent on reputation.

#### **4. Conclusion**

In conclusion we can state that reputation plays a crucial role in competition on the web market. It also plays an important role when web companies are to be approached by customers from another country than their country of origin.

On the web since the client cannot feel the good in its proper sense, companies have to rely on their reputation in order to make a sale. Not to mention that the majority of times the payment is perceived by the company before the customer receives the goods.

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