Promoting a Reputation for Quality*

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Abstract

I consider a model in which a firm invests in both product quality and in a costly signaling technology, and the firm's reputation is the market's belief that its quality is high. The firm influences the rate at which consumers receive information about quality: the firm can either promote, which increases the arrival rate of signals when quality is high, or censor, which decreases the arrival rate of signals when quality is low. I study how the firm's incentives to build quality and signal depend on its reputation and current quality. The firm's ability to promote or censor plays a key role in the structure of equilibria. Promotion and investment in quality are complements: the firm has stronger incentives to build quality when the promotion level is high. Costly promotion can, however, reduce the firm's incentive to build quality; this effect persists even as the cost of building quality approaches zero. Censorship and investment in quality are substitutes. The ability to censor can destroy a firm's incentives to invest in quality, because it can reduce information about poor quality products.

KEYWORDS: Reputation, Advertising, Promotion, Censorship, Dynamic Games
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