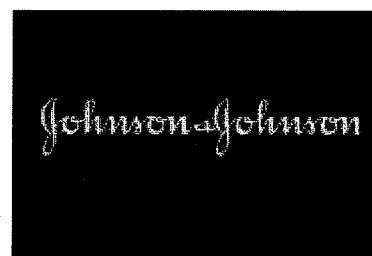


Why Johnson & Johnson's Recall of Children's Tylenol Matters

By AMY BARRETT

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So far the market has largely yawned at Johnson & Johnson's (JNJ) recall of consumer products like Children's Tylenol and Children's Zyrtec -- the shares rose 44 cents Wednesday to \$65.14.



But as the manufacturing problems at the company's Fort Washington, Pa., plant continue to grab headlines, the real pain for J&J could be the tarnishing of its vaunted brand.

On May 4 the Food & Drug Administration released a scathing report about conditions at the Johnson & Johnson facility that makes the recalled products. Among the deficiencies cited in the report: Thick dust in certain parts of the facility and raw materials used in manufacturing that were contaminated with bacteria.

Voluntary Recall

J&J began a voluntary recall of the products made at the Fort Washington plant on April 30.

While FDA Commissioner Margaret Hamburg said in a statement that the "potential for serious health problems is remote," the agency is continuing to investigate and hasn't ruled out criminal penalties. J&J said in a statement that the recall was because of manufacturing problems, not due to reports of any adverse medical events, and that production at the plant has been suspended until problems there are fixed.

"We have committed extensive internal resources to this effort, and brought in independent outside experts to assist us," the company said in the statement.

Still, the most recent recall follows two other similar incidents. Last fall the company recalled

some Tylenol products because of strange odors emanating from them, and in January of this year, J&J initiated another recall in connection with that problem. The company said at the time that the odor appeared to be connected to a chemical applied to the wood pallets that transported packaging material for the products. The FDA slammed the company for not moving aggressively enough to address the problems, which first surfaced back in 2008.

Financial Impact

The financial impact from all this isn't likely to be overly severe. That's because J&J's consumer business isn't the real earnings driver at the company. Last year J&J generated \$62 billion in sales, with 25% coming from the consumer business that includes Tylenol, skincare products under the Aveeno line and baby products like Johnson's Baby Oil. But that unit only contributed 15% of J&J's operating income. The rest came from the higher-margin pharmaceutical and medical device operations.

But the value of the consumer business goes way beyond its bottom-line contribution. "The J&J name is one of the most respected brand names in the world," notes Gary Stibel, founder and CEO of New England Consulting Group. "And it is not by accident. They have invested brilliantly in marketing to patients, physicians and institutions."

Halo Effect

And Stibel has no doubt there is a real halo effect from that brand on other J&J lines of business. "Yes, the drugs and devices have to stand on their own," Stibel says. But with the J&J brand, "there is a trust that gives people permission to believe in the product, whether it is a consumer product, device or prescription drug."

And once that brand takes a hit, it can be a long road to recovery. Think of the tough job ahead for Toyota (TM) and Goldman Sachs (GS) in resuscitating their images. Years ago, of course, J&J set the bar with its stellar handling of the Tylenol tampering incident. And so far Stibel says they have mounted an effective response to current manufacturing problems. But if the company doesn't show that it has solved these woes soon, management may find the J&J halo grow dimmer.

Tagged: Johnson and Johnson, recall, tylenol
