The impact of corporate reputation on stock value

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Abstract. In the continuous development of the socialist market economy, corporate reputation as an intangible asset provides a unique and sustainable competitive advantage. The study found that in China’s stock market, when companies encounter a crisis, the negative impact on the stock value of companies with good reputation in the short term will be stronger than that of companies with poor reputation. However, in the long run, corporate reputation will have a 'shadow price' role. It will quickly alleviate the negative impact of the crisis on the stock value of the company and will obtain significantly positive abnormal returns. When enterprises encounter benefits such as listing, good corporate reputation such as China's time-honored enterprises can succeed in the financial market with good reputation and are favored by investors. Because its reputation can promote the compatibility of management interests and form a good cycle of consciously maintaining reputation, it shows good market performance and stock value.

Keywords: corporate reputation; crisis situation; stock value; Chinese time-honored enterprises.

1. Introduction

Since the reform and opening up, with the continuous improvement of the market economy, the market has gradually played a decisive role in the allocation of resources, and competition among enterprises has become the internal driving force for improving economic efficiency. In addition to explicit price competition accidents, reputation plays an implicit incentive role in market competition. A good organizational reputation and external image will act on the future income function of the enterprise. Enterprises have incentives to establish a good image to increase long-term returns. On the contrary, when the reputation of the enterprise is damaged due to illegal punishment, negative events and other factors, it will become the 'archives' of the enterprise and will have an inhibitory effect on the future earnings of the enterprise. Reputation theory is a frontier theory of modern western economics. In the study of reputation, it dates back to the middle of the 18th century. Economist Adam Smith put forward this concept. He believed that reputation is an important mechanism to ensure the honest execution of contracts. Even if both parties are self-interested, for reputation reasons, the threat of losing future gains will automatically implement the contracts concluded by both parties, and transactions including potential opportunism will continue. At the beginning of the 21st century, Federal Reserve Chairman Alan Greenspan said in a speech at Harvard University: “In today’s world, the economic value of products is increasingly reflected in intangible assets. As a special intangible asset, the competition of corporate reputation has become the driving force of economic progress in the 21st century.” As an intangible asset, corporate reputation has become one of the core competitive advantages of enterprises. It can be seen that the value of reputation is self-evident.

At present, scholars have two different views on the study of corporate reputation and stock value. The first view is that good corporate reputation can support the rise of stock prices, which can bring higher returns to investors than low reputation. The second research view is that corporate reputation has no significant impression on the performance of companies in stocks. Based on the existing scholars' research, this paper uses the literature research method to explore the listed companies. By studying the relationship between corporate reputation and stock value, it finds out how to enrich the academic research in the field of reputation in China and provides reference suggestions for listed companies in China.
2. Literature Review

The relationship between corporate reputation and stock value has always been a research hotspot in the theoretical circle. At present, most scholars' research supports the conclusion that corporate reputation has a positive impact on future market performance. For the study of reputation, Akerlof believes that reputation can reduce the problem of market efficiency reduction caused by information asymmetry [1]. Represented by reputation trading theory and reputation information theory. Reputation trading theory holds that reputation is the expectation of the production capacity of an enterprise organization. It is a scarce and inimitable valuable resource that can be displayed through the name of the enterprise (Tadelis S, 2002). [2] It affects the choice of stakeholders in all enterprises and can provide enterprises with sustainable competitive advantages. The reputation information theory believes that reputation can effectively limit information blocking and distortion, increase transaction transparency, and reduce transaction costs, so it leaves a deeper impression in the public mind. Reputable companies can send positive investment signals to investors, and investors are willing to invest in companies with better reputations, because these companies can help investors obtain excess returns above average returns (Beatty & Ritterl, 1986) [3]. Some scholars have also shown that corporate reputation is directly positively correlated with the performance of its stock market (Srivastava, 1997) [4], and investors will be more inclined to buy companies with good corporate reputation during the IPO process, because these companies are more likely to receive a higher premium when the stock is issued (Xu Rong, 2023) [5]. When companies receive negative information, corporate reputation can buffer the company's production and operation and stock market, protect the company's existing assets, and is considered a kind of wealth by investors (Richardson, 2000) [6]. With a good image, enterprises can not only be recognized by the society and the public, but also increase the confidence of investors and collaborators. A good corporate reputation can guide customers to self-connect with the enterprise, stimulate the sense of identity to the enterprise, and guide them to generate identity and support for the enterprise. When the corporate reputation management reaches a certain height, employees will have trust in the enterprise, and employees' evaluation of the enterprise will change with the change of corporate reputation. Employees will bring more efficiency to the enterprise when they work. Through the empirical study of corporate social responsibility information, corporate reputation and investment intention, scholars have found that the better the reputation of the company, the more it can encourage investors to make decisions to support corporate profit goals. [7] Some scholars have found that when the company's reputation ranking is published, the company's reputation has no effect on the abnormal return of the company's stock price (Chung, Kristina, 1999) [8]. Some scholars also divide the capital market into three forms, weak efficient market, semi-strong efficient market and strong efficient market. In the former two markets, all public information of the enterprise, including the reputation of the enterprise, will not make investors obtain excess returns (Fama, 1970) [9]. Because scholars choose two different theories and different countries, time and other research samples to explain the relationship between the two, there are different results. So in China's capital market, will corporate reputation affect the value of corporate stocks? Can enterprises with good reputation improve the returns of shareholders and bring higher returns to investors? These are the questions that this article attempts to answer.

3. Hypothesis and Research

The improvement of corporate reputation requires a period of planning and accumulation. By the end of 2021, the number of enterprises and organizations on enterprise WeChat has exceeded 5.5 million, and 80% of the top 500 enterprises have opened enterprise WeChat. Enterprises disclose information through social platforms such as WeChat, with the main purpose of realizing the maintenance of enterprises or brands. In the market where the product difference between enterprises is getting smaller and smaller, improving corporate reputation is an effective behavior for enterprises to improve their competitiveness. If the enterprise is good at managing reputation, then based on the
perspective of stakeholders, reputation will create a lot of value from all aspects, make the enterprise develop for a long time, and make the company’s performance and stock show a good trend. Therefore, the hypothesis of this paper is that corporate reputation can play a buffer role in the crisis of stock value, and enterprises with good reputation can improve the return of shareholders. The crisis situation and the listing of Chinese time-honored enterprises are more able to test the impact of corporate reputation on stock value. When the enterprise is in crisis, whether people support the enterprise will be largely affected by the reputation of the enterprise and the managers of the enterprise before the crisis. In other words, a bad corporate reputation can signal to investors that there may be a potential crisis in the company, and when such a crisis erupts, these companies will not receive the support they need to eliminate the adverse effects of the crisis (Brown, 1998) [10]. However, some people believe that a good reputation may have an insignificant or even negative impact on the stock price of the company, because people have higher expectations and requirements for it. When a crisis occurs, the market’s punishment will be more stringent, that is, expectations violate the theory. The time-honored listed brand is a unique corporate reputation asset, which can provide a better identification environment for the study of corporate reputation value (Xu Rong, 2023) [5]. This paper uses the literature research method to study the relationship between the two. In the context of crisis, most scholars selected the melamine crisis in China’s dairy industry as the background to study the relationship between corporate reputation and corporate stock prices (Cheng, 2015 [11]; Xu Qiuqi, 2019 [12]; Lin Zhongyue, 2011 [13]). The study found that after the crisis, the stock prices of companies affected by the crisis showed significantly negative abnormal returns, but the relationship between the medium and long term was not significant. When seriously affected by the crisis, enterprises with better reputation have a stronger impact in the short term than those with poor reputation. However, after a period of adjustment, the "shadow price" of corporate reputation reappears, and the stocks of enterprises with good reputation will obtain significantly positive abnormal returns. It can be seen that in the short term, enterprises with good reputation will be 'cursed' when they are in crisis, because the public and the market pay more attention to them and have higher expectations. However, after the crisis, reputation will play a 'crisis reservoir' project to alleviate the negative impact of the crisis on the stock value of enterprises. China’s time-honored listed companies have also been tested by scholars and found that companies with time-honored brands have significantly lower IPO underpricing rates, and have less post-IPO financing constraints and better stock market performance. The internal mechanism is that the first reputation has an information authentication effect, which can help time-honored companies gain a competitive advantage in the consumer market. Second, the possibility of the time-honored companies to improve their performance before listing is very low, and there is a reputation maintenance effect. Third, rational company managers will strive to maintain the company’s reputation, standardize the company’s internal governance and systems, and strengthen the virtuous circle of reputation and company quality.

4. Conclusion and Implication

In China’s A-share market, there are periodic differences in the impact of corporate reputation on stock value in crisis situations. In the short term, investors conform to the expectation violation theory, and reputation is regarded as the potential commitment made by the organization to its stakeholders. The behavior of the organization will be consistent with its expectations. When negative information is received, it will be particularly valued, while enterprises with relatively poor reputation have no such constraints (Fan, 2022). [14] Therefore, in the short term, the negative impact on the stock value of enterprises with good reputation will be stronger than that of enterprises with poor reputation, but over time, corporate reputation will have a 'shadow price' effect, which will quickly alleviate the negative impact of the crisis on the stock value of enterprises. Will get significantly positive abnormal returns. In the IPO context, good corporate reputation, such as China’s time-honored enterprises, can succeed in the financial market with good reputation and are favored by investors. Because its
reputation can promote the compatibility of management interests and form a good cycle of consciously maintaining reputation, it shows good market performance and stock value.

The enlightenment of this paper is that enterprises should pay full attention to the impact of corporate reputation from the perspective of stakeholders. The good reputation of enterprises can promote the improvement of financial performance of enterprises. This promotion may be because good reputation can attract talents more easily, cultivate higher loyalty, increase customers' confidence in products, and attract more investment. The performance of the enterprise shows the competitiveness of the enterprise to the outside world, and makes the positive cognition, evaluation and emotional connection of the various stakeholders to the enterprise. If a company can develop a strategic system with a sense of social responsibility and a strong sense of corporate citizenship, and use the corporate expectations based on this strategic system to successfully integrate the company’s self-identity and corporate image, then the company will establish a good reputation.

References


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