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# PHILEQUITY CORNER

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## Reputation is an asset

While reputation has no formal entry in the balance sheet of a corporation, it still needs to be viewed as an asset, which can also turn into a liability. It affects the market value of a corporation. The care and protection needed to safeguard a company from attacks on its character and status are classified as “reputational risk”.

Researchers and investment analysts need to pay attention to the track record and reputation of the principals behind listed companies. With the media coverage of business players now at par with their political and entertainment counterparts, reputation has figured in the valuation of the company. Sometimes corporate figures mingle with showbiz personalities ensuring double coverage for the couple, in business and entertainment.

Some positives drive up the premium in pricing. These include a track record like increasing the market cap of the stock through efficiencies, a strong management line-up, clear strategy, or an aggressive cash dividend policy. A character discount may arise from unkept promises on an acquisition, weak second-tier management, lack of a transparent succession planning, or a luxurious personal lifestyle charged to the company.

The structure of Philippine business can be characterized as a concentration of a few names or families controlling large conglomerates in varied fields like banking, property development, utilities, and even food chains. A failure of one company in a particular group can be like the falling domino raising the risk factor for the whole group. This introduces the concept of “reputational risk”.

When reputation turns sour as in the high-flying lifestyle of the principal or the failure to meet loan amortizations and the need to float bonds for “refinancing” then the “reputational risk” becomes another factor in evaluating the value of a company or group.

The importance of reputation has only been highlighted by twenty-four-hour news channels and the rise of social media. Business is now covered by tabloid-type of reporting, spotlighting personalities over debt leverage and capital expenditures.

In business, even more than entertainment, reputation has become an intangible asset (or liability) even when it is not formally reflected in the financial statement. Although in acquisitions, this matter of character is sometimes under the general valuation of “goodwill”.

The value of an actively traded stock is posted daily with its price fluctuations determined by financial metrics as well as reputation. The latter can sometimes figure even larger in the valuation than the level of capital expenditure.

Reputational branding has become a marketing effort. TV interviews are arranged to show the philanthropic side of a tycoon. Celebrity endorsers lend their own good name and popularity to a product or company. Philanthropy too has become more focused on certain advocacies like education, sports, or the arts.

The effect of status on price is more evident in products with a high emotional and discriminatory content such as art. Certain buyers in an art auction bid high for an artwork to expand their collection of a particular artist enjoying a high brand recognition. Art has become a good example for the market value of reputation.

In local business with its small and well-connected grapevine, reputation cannot be ignored. Stocks are associated with their principals and lumped together as the “ABC” group, with that combination of letters representing a person or family. Rumors of the takeover of a sleepy company by a particular character is enough to lift a dormant stock into the stratosphere or fall back in a hard landing when nothing seems to be going on—we are still finalizing the closing conditions. The research analysts’ valuations, based on future cash flows and acquisition synergy is enhanced or devalued by the reputation of the principals involved.

Ours is a business dominated by high-profile business personalities. Sometimes, these same characters cross the line to politics and raise their profiles even higher. Buying shares of a company is a declaration of faith not just on its past financial performance but on the reputation of its leadership. Such perceptions are not static. They swing with a company’s fortune and the scrutiny of regulators and political players.

Reputation indeed has market value. Names associated with quality and reliability through the years enjoy premium pricing and market appeal. This same attribute can also pull down a company’s value if reputational risk is ignored.