

Research on the Influence Mechanism of Reputation on Status

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Abstract:

In recent years, along with our country's capital market and related laws and policies have been continuously developing and improving. VC is faced with the problem of where the capital comes from and where it goes from. On the one hand, investors need to inject their own capital into VC to obtain the increase of capital; On the other hand, more and more incumbent enterprises regard venture capital as an important means of external research and development, maintaining and expanding competitive advantages, and achieving financial and strategic goals, in order to assist their own business development. At this time, the status and reputation of VC will be highlighted, because it can convey positive signals of its good operation and high investment efficiency to the outside world, so as to obtain more choices for investors and startups. However, the research on the relationship between reputation and status, two intangible assets, is still slow and has not reached a unified conclusion. Based on this, this paper studies the mechanism of reputation on status. The results show that impulse plays a positive regulating role in the influence path of reputation on status, while volatility plays a negative regulating role.

Keywords:

Reputation, Status, Momentum, Volatility

1. Introduction

Existing studies have shown that reputation and status bring a lot of benefits to Venture Capital (VC). A good reputation can improve the visibility of VC and show its quality to stakeholders [1], thus reducing the uncertainty of startups about VC's own quality. When reputation reduces the uncertainty of consumers, it increases the possibility of startups introducing VC funds and assets. This is the signaling effect of reputation [2]. VCS with high status can charge higher prices for products or services of the same quality [3], which reflects the strength of their bargaining power. Meanwhile, VCs with high status may be more likely to obtain better trading opportunities than VCS with low status [4]. When VCs invest in startups, they act as quality certifiers. VCs generally face two problems. First, on the capital demand side. Because the market is too crowded, investors will be more strict about where

their money is going when they are faced with multiple choices. So how to promote the raising of funds has become a big problem. Second, on the supply side. Although the number of venture capital institutions is huge, there are very few high-quality entrepreneurial enterprises with good expectations. Faced with this imbalance, entrepreneurial enterprises have more choices in the invisible, making institutions become passive parties. The performance of some head VCs in these two aspects is still strong, such as IDG Capital, Deep Venture Capital, Sequoia Capital, etc., in 2021, the number of project financing reached 272, 152, 138, respectively, and the project IPO exit reached 21, 10, and 24.

Many institutions face difficulties in raising funds, no money to invest, and projects cannot be withdrawn. Comparing the differences between the head VC and the rest of the VC, there are differences in the amount of capital under management, the establishment time of the VC institution, the success rate of the IPO, and its position in the syndicate alliance. These aspects are the reflection of VC's reputation and status. Recently, scholars have turned their attention to the interrelationship between reputation and status [2]. But the black box of this interrelationship is still not fully explored. Therefore, in this study, the path black box of the relationship between reputation and status needs to be opened.

2. Literature Review

The existing researches mainly focus on the source (or construction), function and dynamic evolution of the reputation of venture capital institutions:

In terms of reputation source (construction), investment performance can also be used as one of the indicators to express reputation in recent studies. First, scholars point out that the reputation of VC can be measured by its earnings [4]. Similarly, good investment performance can promote the further improvement of reputation [5], and performance in the IPO market has increasingly become a major factor in the reputation of venture capital institutions. Secondly, the professional knowledge and skills of venture capital institutions have also become factors in the formation of the reputation of venture capital institutions. VC's operating experience and experience in a certain industry can be regarded as a proxy variable of venture capitalists' professional knowledge and skills, and VC's professional knowledge and skills in cultivating enterprises' good growth are obviously an important source of VC's reputation [2].

In terms of reputation, it mainly focuses on two dimensions: one is the impact on venture capital institutions themselves. Gompers(1996)[6] focused on the capital market in the United States. He found that VCS with low reputation had a higher IPO underpricing level than VCS with high reputation in the exit process after the listing of the target companies they invested in, in order to make it easier to raise funds in the future [7]. On the contrary, in the study of the British capital market, there is no difference between the IPO underpricing of low-reputation VCS and that of high-reputation institutions. Baker and Gompers(1996)[6] proposed that VC with high reputation can bridge start-ups and management institutions to improve their internal management quality. On the one hand, a high reputation can provide VC with stronger bargaining power, and startups will compromise in the process of establishing relationships with VC firms, enabling VC to obtain a discount of 10%-14% when purchasing equity. Similarly, VCS with high reputation have a higher probability of successful joint investment when other institutions establish joint investment. This

means that VC with high reputation can leverage more funds to participate in investment [5]. On the other hand, scholars have also found the negative effects of reputation. Since reputation is an expectation of the future based on past performance, institutions with a high reputation tend to suffer more criticism when they are seen to show inconsistencies. For example, when the invested enterprise is suspected of fraud, the reputation of its related VC will be reduced, and its exit performance will be affected [7]. The second is the impact on the invested enterprises. Generally speaking, venture capital institutions with high reputation can improve the IPO probability of the target enterprises, promote the innovation of enterprises, and promote the management level of enterprises. Gomper(1996) [6] proposed that investee enterprises can make use of VC's high reputation to improve the possibility of cooperation with other high-quality underwriters. In turn, it is more likely to succeed in reaching the target of going public [8]. Xiao Fang (2021) [12]proposed that the reputation of venture capital institutions has a significant positive promoting effect on the innovation of target enterprises. Shu et al. (2011) [13]believe that VC with a high reputation can bring better business results when establishing relations with target enterprises, which is mainly reflected in the higher level of financial indicators such as ROA.

In terms of the dynamic evolution of reputation, Chanlder et al. (2013)[2] argued that reputation should be unstable and multi-dimensional, which is based on the perception of the quality and performance of the target company. Kim et al. (2021)[13] expanded and researched in this direction, adding the definitions of impulse and momentum to study the potential energy and volatility of reputation. Impulse refers to the expectation brought about by the momentum of reputation in a period of time, and momentum refers to the fluctuation degree of reputation in a period of time [13]. This paper provides a theoretical basis for the study of the co-evolution of reputation and status.

With the maturity of the capital market, the competition in the venture capital (VC) industry has become more intense. In such an environment, the reputation of a VC becomes a key differentiator between different institutions. Reputable VC institutions are more likely to attract high-quality startups, because for these companies, getting the support of well-known VCS is not only an injection of capital, but also a recognition of their potential and development prospects. For start-ups, the lack of a reliable financial history and market performance often makes it difficult to justify their value through traditional financial reporting. As a result, they tend to seek VCS with good reputations as backers as an indirect quality assurance and market signal. At the same time, VC institutions themselves are paying more and more attention to maintaining and enhancing their own reputation. A VC with a high reputation will not only have easier access to quality investment opportunities, but will also be able to build a broader social network and gain access to more resources and information. These factors work together to make reputation the key to the long-term survival and success of VC in the market. A high reputation also means a high degree of market recognition, which can help VC institutions obtain more favorable conditions when negotiating and cooperating. Therefore, the importance of venture capital reputation has received increasing attention in both academic research and practice. Scholars study the impact of venture capital reputation and explore how to effectively build and maintain that reputation. At the same time, stakeholders, including investors, start-ups, partners, etc., are also beginning to pay more and more attention to the reputation of VC. This trend reflects that in today's highly competitive capital market environment,

the reputation of venture capital institutions is not only key to their success, but also an important asset for them to continue to attract quality projects and maintain their market position.

3. Research Design

3.1. Research hypothesis

The reputation of the company also needs to be continuously strengthened and maintained. Research shows that there is a positive correlation between the previous reputation and the current reputation [9], and with the growth of VC's age, the influence of the change of reputation on the current reputation will not be weakened. Reputation must be constantly strengthened, making it more susceptible to previous changes in reputation [10]. At the same time, high status can bring more information, higher quality opportunities and resources, thereby enhancing the performance and reputation of the VC. Based on this, the following hypothesis is proposed.

H1: The reputation of venture capital institutions promotes status.

Considering the dynamic characteristics of reputation, two important concepts, Momentum of reputation and Volatility of reputation, are introduced. As a supplement to reputation, these two concepts make the concept of reputation more complete, and also provide important guidance for us to study the influence path of reputation on status.

The impulse of reputation is defined as strength or power gained through movement or a series of events. Given the different trajectories of reputation evolution, organizations with the same level of reputation may still have different reputation impulses. Viewers judge whether the momentum of an organization's reputation is positive or negative, and to a greater or lesser extent, based on the observed trajectory of improvement or decline in the organization's reputation over time due to its recent behavior and performance [11]. Based on this perception of motivation, audiences can form expectations about the organization's future behavior and performance [8]. For example, if an organization has a good reputation momentum, its potential partners may perceive that it is performing better and better and expect to continue to do so for some time in the near future [8]. When an organization gives a good expectation that its reputation has steadily increased or decreased in the past period of time, it means that the momentum of the organization's reputation is reducing the impact of market noise on the audience, and it is also conveying the information that it is running well to the outside world, so as to reduce the asymmetry of information. Then the reputation of the institution will have a more significant impact on the status under the adjustment of this expectation. If the momentum of an organization's reputation is positive, the audience can easily observe the level of its reputation and retrieve information from these observations, which will strengthen the impact of reputation. Based on this, the following hypothesis is proposed:

H2: The impulse of reputation has a positive moderating effect on the influence of reputation on status

The momentum of reputation means that momentum is defined as a rapid and unpredictable trend of change. To the extent that the irregularity or randomness of a variable limits our ability to accurately predict its value, momentum increases the uncertainty of the variable. On the one hand, in extreme cases, when audiences don't change their opinion of an organization, its reputation doesn't fluctuate at all. On the

other hand, if there are some fluctuations in an organization's performance, or if there are some unexpected events, such as accidents or scandals, then its reputation may be more volatile. [3] In venture capital institutions, the fluctuation of reputation is more affected by their investment behavior. When the investment behavior of the institution is abnormal, the noise received by the audience will be increased. When the noise level increases, it becomes more difficult to interpret the original signal. As a result, noise tends to weaken the impact of the signal. The momentum of a variable prevents us from observing other (dynamic or static) features of the variable. For example, if the value of a variable changes over time, with high frequency and large amplitude, compared to the opposite case where the variable remains constant, in which case it can be confusing to determine whether the value of the variable is generally high or low, and whether it is increasing or decreasing. As a result, the audience is unable to clearly receive and interpret the signals associated with these reputational characteristics. In this case, the effect of reputation on status will be affected. Based on this, we propose the following hypothesis:

H3: The momentum of reputation has a negative moderating effect on the influence of reputation on status

3.2. Variable measurement

Reputation: Referring to the construction of the reputation indicator by Lee et al. [12], we use a rolling five-year window to calculate the annual reputation of each VC firm.

Status: is the centrality of eigenvector.

Area diversification: Regional segmentation is determined according to the data of funded startups on Zerodata network, and regional diversification is realized using entropy measurement.

Early-stage preference: This variable reflects the degree to which venture capital firms invest in early-stage ventures.

Direct tie. Refer to the study of Kumar and Zaheer. We control the degree centrality of focus firms by calculating the number of binary connections between focus firms and their substitutes in the network at time t .

Indirect tie. The number of companies indirectly connected by focus companies in the whole network in t years is counted to obtain knowledge sharing through informal channels in the network. In addition, the annual dummy variable (Year) is also set to control the possible influence of the annual change trend on the co-performance.

3.2. Model Selection

The relationship between status and reputation is discussed by referring to the regression equation (1) of previous literatures. Regression equations (2)(3) were used to measure the moderating effect of reputation impulse and reputation momentum. The specific regression equation is as follows:

$$Status_{i,t} = \phi_1 Reputaition_{i,t} + \phi_2 Control_{i,t} + \mu_{i,t} \quad (1)$$

$$Status_{i,t} = \phi_3 Reputaition_{i,t} + \phi_4 Reputaition_{i,t} * Momentum_{i,t} + \phi_5 Momentum_{i,t} + \phi_6 Control_{i,t} + \mu_{i,t} \quad (2)$$

$$Status_{i,t} = \phi_7 Reputation_{i,t} + \phi_8 Reputation_{i,t} * Volatility_{i,t} + \phi_9 Volatility_{i,t} + \phi_{10} Control_{i,t} + \mu_{i,t} \quad (3)$$

3.3. Data Sources

208,206 VC investment events in China from 1996 to 2020 were collected from Zero2IPO data network; Excluding individual investors and non-disclosed investment events, the remaining 120,094 investment events; Then collect the amount of capital management and total investment of each VC; The total amount of investment; Number of IPO exits; VC age of the current year, after deleting the missing data of the above indicators, 97701 observed values were obtained; Then, according to the reputation index, the value of missing management capital is excluded, and the remaining reputation observation value is 34190. Then, according to the needs of the construction of status indicators, the value of a single institution investing in a single start-up enterprise is eliminated, and the final remaining observation value is 20,433, including 3,773 venture capital institutions, and all variables are 1% tail reduction treatment.

4. Result

4.1. Regression analysis

Table 1. Regression analysis.

	(1)	(2)	(3)
VARIABLES	Status	Status	Status
Reputation	0.322*** (4.11)	0.207** (2.56)	0.325*** (4.18)
Momentum		-0.075*** (-5.22)	
Reputation*Momentum		0.338*** (9.28)	
Volatility			0.030*** (4.14)
Reputation*Volatility			-0.124*** (-4.78)
direct	-0.003*** (-5.13)	-0.002*** (-4.18)	-0.002*** (-4.78)
Area diversification	-0.001 (-0.14)	-0.001 (-0.24)	-0.001 (-0.10)
Early-stage preference	0.074 (0.77)	0.074 (0.77)	0.070 (0.73)
Indirects	1.395*** (22.82)	1.354*** (22.13)	1.373*** (22.05)
Constant	5.934*** (9.37)	6.071*** (9.63)	6.102*** (9.53)
Observations	20,433	20,433	20,433
R-squared	0.583	0.587	0.584
Number of id	3,773	3,773	3,773

Robust t-statistics in parentheses

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

In this paper, the dynamic factor of reputation is considered in the mechanism of influence of reputation on status, and the impulse of reputation and momentum of

reputation are incorporated into the model as dynamic measurement factors in combination with previous studies. As shown in column (1) of Table 1, the influence of reputation on status is significantly positive, and hypothesis H1 is confirmed. As shown in column (2) of Table 1, the cross-multiplication term of reputation and reputation impulse has a significantly positive influence coefficient on status ($\beta=0.338$, $p<1\%$). This shows that the impulse of reputation plays a positive moderating role in the influence of reputation on status, and hypothesis H2 is proved. In column (3), the influence coefficient of reputation and momentum of reputation on status is significantly positive ($\beta=-0.124$, $p<1\%$), which indicates that momentum of reputation plays a negative moderating role in the influence of reputation on status. Hypothesis H3 is proved.

4.2. Robustness test

As there are few alternative variables to be found in the measurement of reputation and status adopted in this paper, the robustness test of this part will be divided into selecting one of the subsamples (VC with local capital source) for testing. The results are shown in Table 2, which are consistent with the above regression results and further demonstrate the robustness of the above regression results.

Table 2. Robustness test.

	(1)	(2)	(3)
VARIABLES	Status	Status	Status
Reputation	0.219***	0.118***	0.186***
	(11.32)	(5.05)	(8.82)
Momentum		-0.048***	
		(-5.19)	
Reputation*Momentum		0.183***	
		(7.27)	
Volatility			0.008
			(1.59)
Reputation*Volatility			-0.074***
			(-4.63)
Direct	-0.001**	-0.000	-0.000
	(-2.09)	(-1.50)	(-1.55)
Area diversification	0.006*	0.007**	0.007**
	(1.72)	(2.18)	(2.14)
Early-stage preference	-0.003	-0.002	-0.002
	(-0.14)	(-0.07)	(-0.07)
Indirects	1.185***	1.165***	1.175***
	(53.86)	(52.72)	(53.23)
Constant	3.873***	3.943***	3.923***
	(25.49)	(25.92)	(25.76)
Observations	17,695	17,695	17,695
Number of id	3,405	3,405	3,405

5. Conclusions

In this study, this research examines the impact of the dynamic characteristics of reputation, momentum and volatility on status flows. We believe that both may have additional signaling effects that affect the perception of the audience and thus the position of the organization itself, and that volatility may also act as noise that interferes with other signaling effects. The empirical results show that impulse plays a positive moderating role in the co-evolution of reputation and status (hypothesis 2),

while volatility plays a negative moderating role (hypothesis 3). This result shows that the impulse and momentum of reputation can transmit significant signals. The impulse of reputation conveys to the audience the stable state of the institution's reputation over a period of time, and this kind of information transmission makes the audience more comfortable. So the role of reputation is also obvious in such conditions. The momentum transmission of reputation reflects the volatility of reputation. Research shows that people are unwilling to see the volatility of reputation, because reputation volatility often represents inconsistency, which transmits more noise to the outside world and will affect the role of reputation on status.

Conflicts of Interest

The author declares that there is no conflict of interest regarding the publication of this article.

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