



## A Recent Literature Review on Corporate Political Connections

Irwan Trinugroho 

Faculty of Economics and Business, Universitas Sebelas Maret, Surakarta, Indonesia

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### Abstract

It has always been an interesting issue deliberating the connectedness between corporation and political power. There have been a substantial number of papers in the academic literature empirically studying what so call "corporate political connections" over the last 17 years. Using 81 papers published in 2010-2017 in finance, economics, accounting, management and other journals, in this present paper, I provide a recent literature review on firm political connections particularly with respect to the empirical studies discussing the impact of being politically connected firms. A number of issues related to the effect of political connections on corporate strategy, behaviors and outcomes have been addressed. Few other papers provide different perspective by looking at the antecedents of corporate political connections and the contingency role of such connections. Little is found on the development of new measures of corporate political connections. Finally, it could be suggested that the interaction between political connections and the technological-based business innovation would be an interesting issue to study.

## Telaah Pustaka Tentang Koneksi Politik Perusahaan

### Abstrak

Isu mengenai keterkaitan antara perusahaan dengan politik selalu menjadi topik yang menarik untuk dibahas. Selama 17 tahun terakhir, banyak bermunculan penelitian akademik yang menguji koneksi politik perusahaan secara empiris. Menggunakan 81 artikel penelitian yang dipublikasikan selama 2010-2017 di bidang keuangan, ekonomi, akuntansi, manajemen dan yang lainnya, saya menyediakan resensi pustaka dari berbagai macam artikel yang meneliti koneksi politik perusahaan serta mendiskusikan dampak menjadi perusahaan yang memiliki koneksi politik. Berbagai macam isu mengenai dampak koneksi politik terhadap strategi, perilaku dan kinerja perusahaan sudah banyak diteliti namun belum banyak yang menguji menggunakan perspektif baru mengenai anteseden dari koneksi politik dan berbagai macam faktor yang bisa menjadi kontingensinya. Masih sedikit juga ditemui pengembangan alat ukur baru dari koneksi politik. Terakhir, bahwa dapat disimpulkan bahwa interaksi antara koneksi politik dengan bisnis yang berbasis teknologi akan menjadi sebuah topik yang menarik untuk didalami.

JEL Classification: G3, G30

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## INTRODUCTION

Discussing the connectedness between business and politics is always interesting especially with regards to the link between business entities and political power as it is generally known that anecdotal evidence on this issue is prevalent worldwide (for the detail examples, see the paper of Faccio, 2006). Theoretically, Schaffer (1995) explain that studies on political influences in business could be classified into “micro” and “macro” levels. The micro level, usually directly called as firm level or organizational level, is a dominant level of analysis utilized by management, business and finance scholars. Macro level of analysis, such as communities, industries, social classes and societies, are mostly used in political science, public economics and sociology. In this present paper, the focus of analysis is the micro level perspective more particular with regards to political connections at the firm level<sup>1</sup>.

Since the seminal paper of Fisman published in the American Economic Review in 2001 which estimates the value of political connections for firms by studying Indonesian firms, there has been a growing body of literature on corporate political connections particularly in the fields of finance and economics as well as in accounting. Most of them are empirical papers investigating the impact of being politically connected firms, although there are also few papers provide theoretical explanation on the existing (antecedents) and the outcomes of political relatedness for firms. Nys et al. (2015) and Sutopo et al. (2017) provide literature review on the benefits (access to source of financing, higher firm performance, government privilege) and disadvantages (inefficiency, unqualified board member) of political relations for firms.

Indeed, management scholars (Hillman et al., 1999; Tripathi et al., 2002; Hilman et al., 2004; Ozer et al., 2010) have also introduced the concept of corporate political activity which

to some extent could be considered to be overlapping with the term of corporate political connections.

However, these two could be disentangled by differentiating between activity and embeddedness (Sutopo et al., 2017). Therefore, it could be argued that corporate political activity is more on the efforts, such as lobbying, done by firms to deal with political circumstances (Hilman et al., 2004), while corporate political connection is the extent to which a corporation closes to the political power (Nys et al., 2015). Those management scholars have also empirically examined the impact of corporate political activity on firm outcomes and mostly find that corporate political activity is positively associated with firm performance according to the meta-analysis of (Lux et al., 2011).

In this present paper, I provide a recent comprehensive literature review more particular on the strategy, behaviors and outcomes of politically connected firms by reviewing articles from four fields, 1) finance, economics, 2) accounting, 3) management and business (including strategic, marketing and organization behavior) and 4) other fields.

## METHOD

To provide a more recent literature review, I use 81 published papers in Elsevier's journals (available in ScienceDirect) over the period of 2010-2017 (including articles in press) that specifically designed to empirically study “corporate political connections” or “corporate political ties” or “corporate political relationship”. I divide those papers into four categories according to the specific areas which are 1) finance and economics, 2) management, 3) accounting and 4) others. It is then resulting to 56 finance and economics papers, 13 accounting papers, 6 management papers and 6 papers are categorized as others. The composition of papers based on the year of publication and the particular field

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<sup>1</sup> Nys et al. (2015) differentiate political influences in business at the micro level into three channels which are rent-seeking behaviors, grabbing hand behaviors and corporate political connections. However, the latter is my focus in this paper.

is presented in Table 1, while the composition of papers based on the sources (journals) is presented in the Appendix 1.

With regards to the institutional setting, most papers (76 papers) are single-country

studies. It is understandable because the information (dataset) to measure corporate political connections is mostly manually-collected which then creates difficulties to broad it into a cross-country study. Exceptions are the papers of

**Table 1.** Composition of Papers Based on the Year of Publication and the Fields

<b>Year of Publication</b>	<b>Finance and Economics</b>	<b>Management</b>	<b>Accounting</b>	<b>Others</b>	<b>Total</b>
2017 and in press	17	3	4	2	26
2016	9	1	1	1	12
2015	7	1	4	1	13
2014	7	0	1	1	9
2013	8	1	1	1	11
2012	6	0	1	0	7
2011	1	0	1	0	2
2010	1	0	0	0	1
<b>Total</b>	<b>56</b>	<b>6</b>	<b>13</b>	<b>6</b>	<b>81</b>

**Table 2.** Composition of Papers Based on Institutional Setting and the Fields

<b>No</b>	<b>Setting</b>	<b>Finance and Economics</b>	<b>Management</b>	<b>Accounting</b>	<b>Others</b>	<b>Total</b>
1	China	32	4	5	4	45
2	Indonesia	2	0	2	0	4
3	Malaysia	5	0	2	0	7
4	Bangladesh	0	0	1	0	1
5	Turkey	1	0	0	0	1
6	US	3	0	1	0	4
7	Poland	1	0	0	1	2
8	Spain	0	1	0	0	1
9	Philippines	0	1	0	0	1
10	Japan	1	0	0	0	1
11	Israel	1	0	0	0	1
12	Taiwan	3	0	0	0	3
13	Egypt	1	0	0	0	1
14	Italy	1	0	0	0	1
15	Ghana	1	0	0	0	1
16	Thailand	1	0	0	0	1
17	Denmark	1	0	0	0	1
18	Cross country	2	0	2	1	5
<b>Total</b>		<b>56</b>	<b>6</b>	<b>13</b>	<b>6</b>	<b>81</b>

Boubakri et al. (2012), Boubrakri et al. (2013), Braam et al. (2015), Al-Hadi et al. (2016) and Brown (2016). China is the dominant institutional setting to study corporate political connections in which more than half of papers on firm political connections studying Chinese firms. The remaining also mostly takes place in emerging countries (Table 2 for the details).

## RESULT AND DISCUSSION

### Recent Issues

Table 3 exhibits the composition of papers based on type of firms to study which is divided into financial and non-financial firms. Table 4 presents the summary of specific issues discussed in reviewed papers. The number of issues in Table 4 exceeds 81 due to there are some papers that discourse more than one issue. Finally, I identify 29 issues that are discussed in the 81 reviewed papers.

### Market Discipline and Bank Failure

As presented in Table 3, only four papers are specifically dedicated to study politically connected financial institutions. As mentioned by Nys et al. (2015), indeed, very few studies focus on political connections of banks compared to non-financial firms. Basically, there are two main issues discussed on the bank political connections. The first one is regarding the market discipline by depositors and the likelihood of failure.

Two papers published in the Journal of Financial Stability (Disli et al., 2013 using Turkish banks' data; Nys et al., 2015 using Indonesian banks' data), stress on the impact of political

connections of banks on depositors' behavior under the framework of market discipline.

Generally, they provide evidence that politically connected banks are less disciplined by depositors. It is argued that depositors could be considered to have less effort in monitoring politically connected banks as they may perceive that those banks are less risky than non-politically connected banks. The other paper (Polsiri & Jiraporn, 2012), in the context of Thailand, also reveals that banks having political connections are less likely to fail. The second issue discusses the performance difference between politically connected and non-politically connected banks (Hung et al., 2017). In the context of China, they find that politically connected banks have higher performance than that of non-connected banks.

### Access to Finance

Easier access to sources of financing is generally considered to be the benefit of being politically connected firms. Pioneered by Khwaja and Mian (2005), A substantial number of papers have empirically investigated the difference in access to finance between politically connected and politically connected firms. Consistently, in this review, there are 8 papers that specifically address this issue. Generally, they find that politically connected firms are benefitted by having easier access to finance. For example, Yang et al. (2014), by studying non-listed firms in China, document that political connections help firms to obtain long-term loans. Moreover, they introduce a contingency factor-media monitoring-which is found to lessen the relationship between political connec-

**Table 3.** Composition of Papers Based on Type of Firms to Study

Field	Financial Institutions	Non-Financial Institutions
Finance and Economics	4	52
Management	0	6
Accounting	0	13
Others	0	6
<b>Total</b>	<b>4</b>	<b>77</b>

**Table 4.** Summary of Specific Issues Discussed in Reviewed Papers

No	Issues	Finance and Economics	Management	Accounting	Others
1	Market Discipline	2			
2	Failure/ Default	1			
3	Access to Finance	6		1	1
4	Financial Performance	7		3	2
5	Market Value	11	1	2	
6	IPO (Process and Performance)	7			
7	Capital Structure	4			
8	Cost of Capital	2			
9	Government Policy and Bailout	2			1
10	Corporate Social Responsibility	2			1
11	Employee Salary	1			
12	Expropriation	2			
13	Corporate Investment	2	2		
14	Corporate governance	6	1	1	
15	Tax Benefits			2	
16	Privatization			1	
17	Related Party Transaction			2	
18	Financial reporting and Earning Management			3	
19	Audit			2	
20	Innovation	1			1
21	R&D Intensity				1
22	Business Strategy		2		
23	Venture Capital	1			
24	Dividend	1			
25	Managerial Turnover and Succession	2			
26	Business Environment	1			
27	Family Firms	1		2	
28	Merger and Acquisitions	2			
29	Liquidity Management	2			

tions and access to bank loans. Similarly, Yeh et al. (2013) reveal that in Taiwan, political connections of firms are positively associated with access to bank loans. More recently, by studying Indonesian firms and disentangling firms into large and medium and small enterprises, Fu et al. (2017) politically connected loans have more access to loans from state-owned banks particu-

larly for small and medium enterprises, the effect of political connections is higher.

**Financial and Market Performance**

Corporate outcomes, more particular financial and market performance, are the most studied issue when discussing political connections of firms. The seminal paper of Fisman

(2001) basically also measures the value of political connections by looking at the stock price of highly connected firms when the President's health worsened. In the reviewed papers, there are also 12 and 14 papers that empirically study the effect of corporate political connections on financial performance and market performance, respectively.

Generally, most of them conclude that political connections lead to higher financial performance or higher market value of firms. For instance, Wu et al. (2012) find that Chinese private firms having politically connected managers have better performance than non-connected firms. Ding et al. (2014) partially find that having politicians on the board help improve firm performance particularly in the state-owned enterprises. Similarly, A paper of Brown (2016), studying air transportation firms, reveals that firms with intensive political activity and political connections, subsequently, have higher profitability. Taking different perspective, Luo et al. (2016) find that politically connected firms is less risky in the stock market compared to non-politically connected firms.

### **Government Policy and Bailouts**

The other issue that is studied by a number of papers is related to the link between corporate political connections and government policy. It basically refers to the study of Faccio et al. (2006) which find that politically connected firms are more likely to be rescued by the government than non-connected firms. among the reviewed papers, there are three papers that specifically discuss the impact of political connections on government policy.

Using the data of 2008 TARP in the US, Blau et al. (2013) find that politically connected firms are benefitted by more likely to receive TARP fund with a greater amount and earlier than non-connected firms. On a different matter, Zhang et al. (2014), by studying wind energy manufacturing firms, stress on the impact of government subsidies on firm performance with political connections as the moderating effect. Arguably, the effect of government subsidy

on firm performance is different depending on how politically connected the firms.

### **Financial Reporting, Earnings Management, Audit and Tax Benefits**

An influential paper of Faccio (2010) reveals that one of the differences between politically connected firms and non-connected is that the connected ones pay lower taxes than the latter. Likewise, given the nature, some accounting papers in this review, stress on the link between political connections and some aspects related to tax benefits, financial reporting and earnings management. For example, Wu et al. (2012) provide evidence that politically connected private firms in China enjoy tax benefits. Similar issue is also studied by Platikanova (2017). Wang et al. (2017) study the interaction between managerial ability and political connections and their effect on likelihood of financial reporting fraud. In a cross-country study, Braam et al. (2015) find that politically connected firms tend to move from real earnings management to accrual-based earnings management compared to non-connected firms.

### **Business Strategy, Innovation and R&D Intensity**

It is generally known that a substantial number of management scholars have studied the link between political connections and business strategy. In this review paper, it is also found some papers that empirically investigate the effect of corporate political connections on business strategy, innovation and R & D intensity. For instance, Wang et al. (2016) study how family firms with political connections transform their business and adopt M & a strategy. Linking political connections and corporate innovation has also been studied by some papers not only in management field (Song et al., 2015) but also in corporate finance (Hou et al., 2017).

### **Capital Structure, Cost of Capital, Dividend and Liquidity**

A number of papers that are included in this literature review empirically examine the ef-

fect of corporate political connections on some traditional corporate finance issues such as capital structure, cost of capital, dividend policy and liquidity. Bliss and Gul (2012b), by studying Malaysian firms, conclude that politically connected firms have higher leverage than non-connected firms.

Moreover, Bliss and Gul (2012a) document that firms with political connections are charged higher interest on debt to cover their higher risk. Similarly, Liedong and Rajwani (2017) find that in Ghana, politically connected firms have higher interest rate. On a different matter, Boubakri et al. (2013), in a cross country study, reveal that firms with political connections more cash than firms without such connections. Related to dividend policy, Su et al. (2014) conclude that having political connections lead firms to pay higher cash dividends.

### **Corporate Governance and Equity Ownership Structure**

Linking political connections and corporate governance as well as equity ownership structure has also been explored especially in corporate finance and accounting. Consistent with previous studies, it also revealed by Shen et al. (2015) that political connections are more prevalent in poor governance firms. Some papers look at the interaction between ownership structure (or type) and political connections (Chan et al., 2012; Al-Hadi et al., 2016). Issue on the link between corporate political connections and related party transaction as an expropriation mechanism is also discussed in some papers. Habib et al. (2017), using data from Indonesia, find that related party loans is exploited by politically connected firms as a tunneling mechanism. Similar issue is also explored by Su et al. (2014).

### **Other Issues**

There have also been other issues studied with regard to corporate political connections. For example, if most papers attempt to investigate the impacts of being politically connected

firms, White et al. (2017) take differently in which they also investigate the antecedents of corporate political ties by focusing on the business environment. Some articles also study the link between political connections of firms and their social responsibility performance (Gu et al., 2013; Lin et al., 2015). Another interesting issue is a paper by Song et al. (2016) which study the effect of corporate political connections on employee wage.

### **Measuring Corporate Political Connections**

As it has been discussed, corporate political connections could be defined as a special relationship between a firm and those who hold powers in the place where firm operate. There have been a number of measures of the degree of corporate political connections. Some papers consider that it is a continuous scale, however, some others use dummy variable to disentangle between politically connected and non-politically connected firms.

Several measures that have been introduced in the literature such as politically connected CEO or boards (Agrawal & Knoeber, 2001), government bureaucrats or former bureaucrats on the board (Fan et al., 2007), closeness with president evidenced by sharply decrease in stock price when the president was getting sick (Fisman, 2001; Leuz & Oberholzer-Gee, 2006), non-market activities for example lobbying and campaign contribution (Keillor & Hult, 2004; Claessens et al. 2008) and ownership by politicians (Li et al., 2008)

The issue of measuring firm political connections has not been a central discussion in most 81 reviewed papers. those papers adopt the measures that have been employed in the previous studies. An exception is a paper of Li and Zhao (2015) which introduce a new measure of corporate political connections which is the amount a firm spends to socialize with government officials. It could be considered that the more the firm spending for socializing with bureaucrats, the higher the level of political connections.

## CONCLUSION AND RECOMMENDATION

To some extent, the issue of corporate political connections has been considered to be mature subject to study. Many issues spreading from characteristics, strategy, behaviors and outcomes of politically connected firms have been explored and empirically been examined. Therefore, it needs more efforts to provide a strong contribution to the existing literature on this particular area. However, the interaction between corporate political connections and the advancement of technology which has led to disruptive innovations could be an interesting issue.

On the one hand, it could be argued that technology would lessen the value of political connections. Sutopo et al. (2017) mention that political connections are less valuable for foreign banks as those banks have performed efficiently resulted from relatively advance technology that they have. On the other hand, some could also argue differently. Although technological-based business innovations have led to major changes in business environment, however, regulatory support is strongly needed in the adoption of such technological-based innovations especially during the transition period. Therefore, political relatedness could still play more important role.

In this present paper, I provide a recent literature review on corporate political connections which have been an interesting issue over the last two decades by reviewing 81 published papers in 2010-2017. By doing so, I am also able to discuss some recent issues related to corporate political connections, the issue in measuring political connections of firms and future research direction in this particular field. Generally, A number of issues related to the effect of political connections on corporate strategy, behaviors and outcomes have been addressed.

On the other hand, few other papers provide different perspective by looking at the antecedents of corporate political connections and the contingency role of such connections. Little is found on the development of new measures of corporate political connections. Finally, it could

be suggested that the interaction between political connections and the technological-based business innovation would be an interesting issue to study.

Nevertheless, some limitations are admitted. First, as mentioned earlier, I only take papers published in the Elsevier's journals. Therefore, some important papers in this particular topic may not be captured in this paper. Second, the period is limited to the papers published in the period of 2010-2017. Obviously, it would be better to deliver a literature review starting from the first published paper in this particular topic.

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