

Is the Chinese Anti-Corruption Campaign Effective?

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The Economics of Corruption

- Corruption is an exchange of official power for personal gains
- Corruption could be either “grease” or “sand” for commerce and economic development in a partial equilibrium model, but the “sand” view will dominate in a general equilibrium story (Kaufman and Wei, *IMF* 2000)
- The secrecy of corruption leads to substantial distortionary incentives (Shleifer and Vishny, *QJE* 1993)
- Negative effect on growth and development (Murphy, Shleifer, and Vishny, *AER* 1993; Mauro, *QJE* 1995; Wei, *REStat* 2000; Acemoglu et al., *AER* 2001)

The Economics of Corruption

- Anti-corruption strategy may include removing the top corrupt heads through elections or impeachment (Brazil in August 2016 or South Korea in March 2017)
- However, corruption may be pervasive in most developing countries
 - Deng, Wei and Wu (2016) reported about 56% of Chinese officials are likely to have illegal income and the proportion also rises with rank; the most senior officials in their data at the rank of *zheng ju* (Director General) may have unofficial income that is more than 430% of their legal income.

What is the Paper About?

- Is China's anti-corruption campaign led by Mr Xi Jinping's CCP leadership effective?
- Is the anti-corruption campaign actually targeting corrupted officials from more corrupt firms?
- Does the campaign contain political favoritism?
- Is the campaign effective at reducing corporate corruption?

What is the Paper Not About?

- The value of the destruction associated with the corruption.
- The value (social welfare) created from the anti-corruption campaign.

Key Takeaways

- Executives of the firms with corporate self-dealings are more likely to be invested in anti-corruption campaign
- Executives with general political affiliation to past leaders are more likely to be invested in anti-corruption campaign
- Executives with same university affiliations of the current top leaders are less likely to be invested in anti-corruption campaign (element of political favoritism)
- The anti-corruption campaign significantly decreases the highly visible business entertainment expenditure
- Self-dealing and accounting manipulation exhibit no improvement across SOEs, Non-SOEs and benchmarking with Hong Kong firms
- Earnings discontinuity is rampant after anti-corruption campaign
- Reform of the legal, institutional, and press freedom environment are necessary to achieve substantial reduction in corruption

Comment on Measurements

- Measurements for the effectiveness in corruption reduction
 - Individual related measures (regulation breaches and entertainment expenditure) are effective and significant
 - Firm/business operation related measures (profitability, accounting manipulations, related-party transactions) exhibit no effect
 - It will be interesting to compare the savings from the entertainment expenditure to the gain or loss of the profitability (profit margin, sales growth minus income growth) to see the welfare of the anti-corruption campaign has brought to the economy
 - After the event of investigation, whether the productivity (sales volume) and profit margin increase or decrease in the following years

Comment on Regression Design

- Probit regression and matching data construction
 - A one-to-one matching sample is constructed based on following criteria:
 - *For each event firm, we identify a matched firm by first selecting a subsample of firms satisfying the following conditions:*
 - *In the same industry as the event firm;*
 - *Have the same SOE status as the event firm; and*
 - *Market cap is within the range of 50% and 150% of the event firm.*
 - *We then choose from this subgroup a matched firm that has the closest book-to-market ratio to the event firm.*
 - Don't understand the rationale of such one-to-one matching sample construction for Probit regression
 - Why not using the standard propensity score matching to generate a matching sample with similar distribution of the key variables?
 - Why not just use the full sample and control for industry, SOE status, market cap and book-to-market ratio?

Comment on Identification Strategies



- Alternative identification strategies
 - Instead of looking at before/after 2012, may test the impact of the event (investigation) of firm i at time t to other non-event firms with similar firm characteristics or locational similarity, whether it is a temporary or permanent impact.
 - After event of investigation occurs in firm i in province (or county or city or industry) j at time t , whether it shocks firm $-i$ in province (or county or city or industry) j at time $t + 1$ in the corruption measures (or more specific to the corruption related to the investigation) comparing to the control group of firms in province (or county or city or industry) $-j$

Comment on Identification Strategies



- Alternative strategy for testing the political favouritism
 - Break the sample into two: the first has political connection with the current top national leaders through workplace relation, hometown relation and university affiliation; the second has none
 - Estimate the corruption models listed in Table 4 using the second sub-sample, with no political connection with the current top national leaders
 - Apply the estimated coefficients to the first sub-sample with political connection with the current top national leaders and compute the predicted risks of corruption
 - Plot the distribution of mis-matches, i.e., firms with predicted high risks of corruption, but not investigated in the sub-sample with political connection with the current top national leaders

Other Minor Comments

- Indicators for university affiliations of the current top leaders (Xi Jinping from Tsinghua and Li Keqiang from PKU) may simply show the alumni from China's top two universities (Tsinghua and PKU) are less likely to be corrupted, which might have nothing to do with the favouritism of the current top leaders.
- For workplace/birthplace connection, it's better use county level rather than provincial level.
- Page 2 – *“The sample firms have a total market capitalization of RMB 5.29 trillion (USD 805 billion), and account for 5.6 percent of China's listed firms in terms of number, and 18.1 percent in terms of market capitalization.”*
- The World Bank report shows that market capitalization of listed domestic companies in China shows USD 6.005 trillion (2014), and USD 8.188 trillion (2015). So that sample firms of USD 805 billion account for 13.4 percent (2014) or 9.8 percent (2015)