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Discussion of

Politically Motivated Corporate Decisions: Evidence from China

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Summary

- This paper studies
  - The nexus between politics and finance in China
  - Impending political tournaments on corporate decisions: inv; tax; employment; wages, cash holdings, debt, stock returns and volatility

- Theories:
  - Uncertainty reducing economic activity
  - Agency-driven incentives increasing economic activity

- It yields interesting findings:

Two years before national promotions for 31 mainland China province heads,

✓ Investment increases by 6%

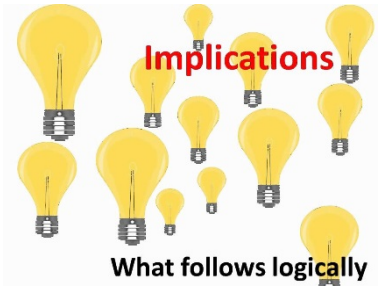
One year before national promotions for 31 mainland China province heads,

✓ Tax increases by 4.1%

Comment 1: Time effects

- The promotion happens at the same time for all the 31 provinces.
  - 2003, 2008, and 2013.
  - No cross-sectional variations.

Firm invest more in 2001, 2006, and 2011 than in other years (2000-2013).



- In theory, this could be easily driven by many other factors:
  - National monetary policy, credit expansion, and etc.;
  - Investment opportunities, business cycles;
  - Political, econ events
- Empirically, you might need to include firm fixed effects.

Comment 2:
China's Five-Year Plans (中国五年计划)

- A series of social and economic development initiatives.
  - China's ambitious Five-Year Plans have been praised for their efficiency, capabilities and importance to growth and development (Xinhua, 2010).
  - Tenth Plan (2001–2005)
    - Achieve an average annual economic growth rate of about **7%**;
  - Eleventh Plan (2006–2010)
    - GDP up **7.5%** annually from 18.2 trillion yuan in 2005 to 26.1 trillion yuan in 2010;
  - Twelfth Plan (2011–2015)
    - The targets were to grow of GDP by around **8%**;

- 2001, 2006, and 2011 are the 1st year of each five-year plan.

How to remedy?

- Cross-sectional (between-province) variations!
  - Heterogeneity tests do not provide much inferences, as most of them are not significant.
  - Even ex post "*Promotions*" are not significant.
- Ex ante? Likely promotions vs. unlikely promotions
  - Could affect province heads' incentives
  - Expect different results in terms of investments and taxes
- Empirically, construct a prediction model for promotion likelihood. E.g., Li and Zhou (2005, JPubE), Chen, Li and Zhou (2005).

Comment 3: "Strategically" important provinces

- Table I.
- Beijing, **Shanghai**, Tianjin, **Chongqing**, **Sichuan**, Guangdong, Jiangsu, Shandong, Heilongjiang, Henan, Jiangxi
- Gansu, Guangxi, Ningxia, Qinghai, Shanxi, Tibet, Xinjiang, Yunan, Hainan
- Historical data on promotions ➔ promotion likelihood

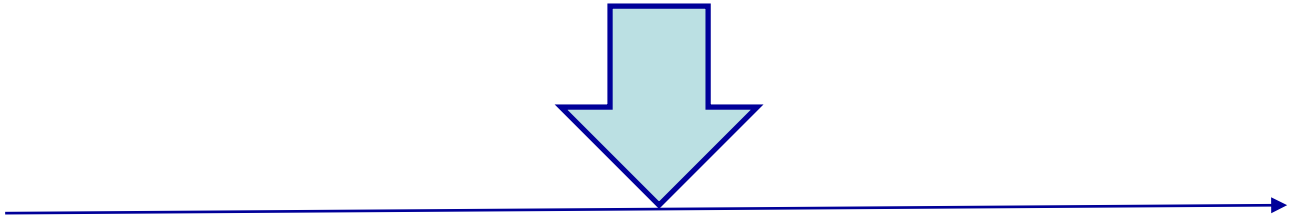
Province	2003	2008	2013	Total
Anhui	0	0	0	0
Beijing	1	0	1	2
Chongqing	1	1	1	3
Fujian	0	0	1	1
Gansu	0	0	0	0
Guangdong	1	1	0	2
Guangxi	0	0	0	0
Guizhou	0	0	1	1
Hainan	0	0	0	0
Hebei	0	0	1	1
Heilongjiang	0	1	1	2
Henan	1	0	1	2
Hubei	1	0	0	1
Hunan	0	0	1	1
Inner Mongolia	0	0	1	1
Jiangsu	1	1	0	2
Jiangxi	0	1	1	2
Jilin	0	0	1	1
Liaoning	0	1	0	1
Ningxia	0	0	0	0
Qinghai	0	0	0	0
Shaanxi	0	0	1	1
Shandong	1	1	0	2
Shanghai	1	1	1	3
Shanxi	0	0	0	0
Sichuan	1	1	1	3
Tianjin	0	1	1	2
Tibet	0	0	0	0
Xinjiang	0	0	0	0
Yunnan	0	0	0	0
Zhejiang	1	0	0	1
Total	10	10	15	35
Mean	0.32	0.32	0.48	0.38

Comment 4: Timeline

Table III

Investment rates tournament years

	2yr before Tournament		Tournament Year		2yr after Tournament
Year	-2	-1	0	1	2
Investment	0.0758	0.0712	0.0746	0.0700	0.0713



Year 1	Year 2	Year 3	Year 4	Year 5
7.46%	7%	7.13%	**7.58%**	7.12%

- A new broom sweeps clean (新官上任三把火). (An et al., 2016; Cao et al., 2015).
- Simply a reversal in Year 4?
- More formal tests might be helpful.

Comment 5: Channels

- How exactly do they influence corporate decisions? How to communicate?
  - Esp. for the private firms.
  - Larger firms? Firms with political connections?

- The authors find that SOEs do not respond.
  - Because leaders of SOEs are relatively powerful???
  - Then we would expect to see different effect for central and provincial SOEs. But no difference…

- Political incentives???
  - "*Private entrepreneurs elected to the NPC have gained legitimacy to participate in gov circles*"…
  - this likelihood should be very small.

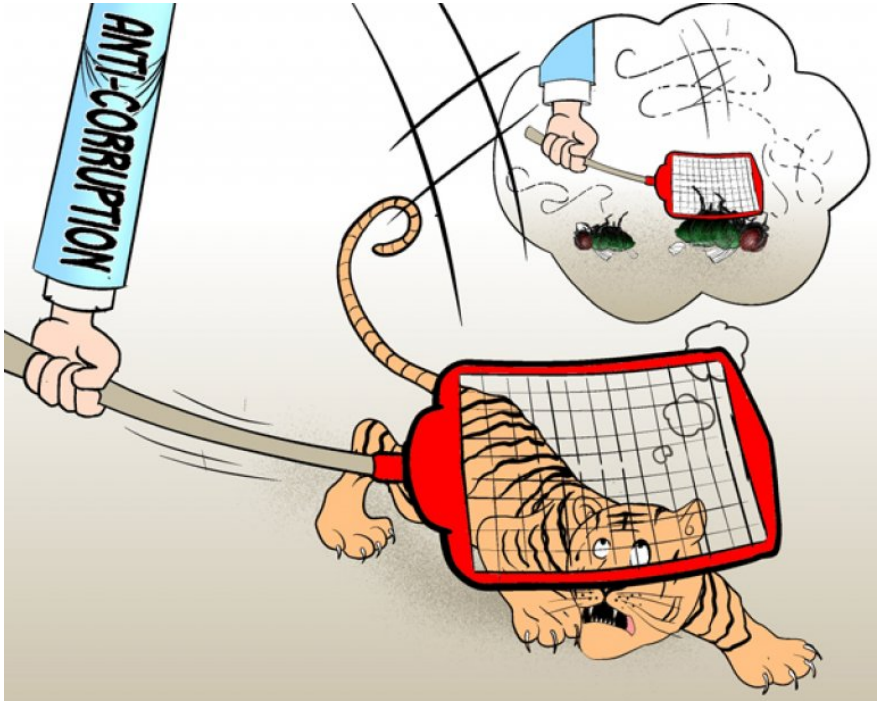
- Soft power??? More direct evidence is needed.

Comment 6: Firm heterogeneity

- What kinds of firms are more likely to cater to the demand of provincial leaders? Invest more, pay more tax. Incentives?
  - Benefit…? (or any cost if not complying?)
  - Cost – stock price drops.
- Firm size
- Firm age
- Firm profitability
- Investment opportunities
- Firm with credit access
- Firm distance to the capital city of the province?
- **Political connections?**

Comment 7: Anti-Corruption Campaign since 2012

- 2003, 2008, 2013
- 2013 different?
- Might not be feasible for investment analysis, but ok for tax and other analysis.



A Quibble

- Table II.

Firm Level Characteristics

Variable	N	Mean	Median	Standard Deviation
Investment	16380	0.0725	0.0454	0.0817
Tax	16965	0.2257	0.1703	0.2351
Employment Growth	16162	0.1264	0.0181	0.5605
Wages Growth	16156	0.4268	0.1085	1.5668
Cash	16305	0.0208	0.0202	0.0643
Debt	16305	0.2494	0.2260	0.2022
SOE	17527	0.4314	0.0000	0.4953
Tobin's Q	17360	1.6891	1.3484	1.0569
Cash Flow	16378	0.0629	0.0567	0.0792
Market Return	16965	0.2649	-0.1209	0.7440
Market Volatility	16965	0.0058	0.0044	0.0042

Other minor issues

- The inclusion of fixed effects is inconsistent:
  - Some tables with only province fixed effects;
  - Some tables with firm fixed effects

- The discussion of the effect of political uncertainty in Section 2 seems to be redundant (pp. 5-8).

- Missing references in the reference list, e.g., Bo (2007); Han and Yan (1999); etc.

- P17. Possible wrong reference of Piotroski and Zhang (2013); Zhang and Scase (2013); etc.

TAKE AWAY

- **Table VI: Impact of political tournament cycles on pricing of 51 dual-listed firms (A-share – H-share)**

Price Premium	1
1yr before Tournament	0.029**
	(2.03)
Year of Tournament	-0.029*
	(-1.86)
1yr after Tournament	-0.148***
	(-8.32)

- Buy the 51 A-share stocks and short the 51 H-shares, 1 year before the Tournament, *t-1*;
- Buy H-shares, short A-shares in the year *t* and *t+1*.
- 2018 is the Tournament year!

Overall

- Very interesting paper
- Well written
- Good implementation and extensive tests

- Good luck to publication!