

Political Connections and Financial Resource Allocation: Evidence from China

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Motivation

- Politically connected firms have easy access to financial resources (Sapienza, 2004; Khwaja and Mian 2005; Claessens et al., 2008; Bliss & Gul, 2012; Hasan et al., 2017; Wellalage et al., 2022; Bussolo et al., 2022)
- Results based on observational datasets, however, are mixed (Hasan et al., 2017).
- Challenge: political connections aren't randomly assigned
- Different types of connected firms are studied separately (institutionally connected firms vs. personally connected firms)
- Survey experiment with loan officers in China

Roadmap

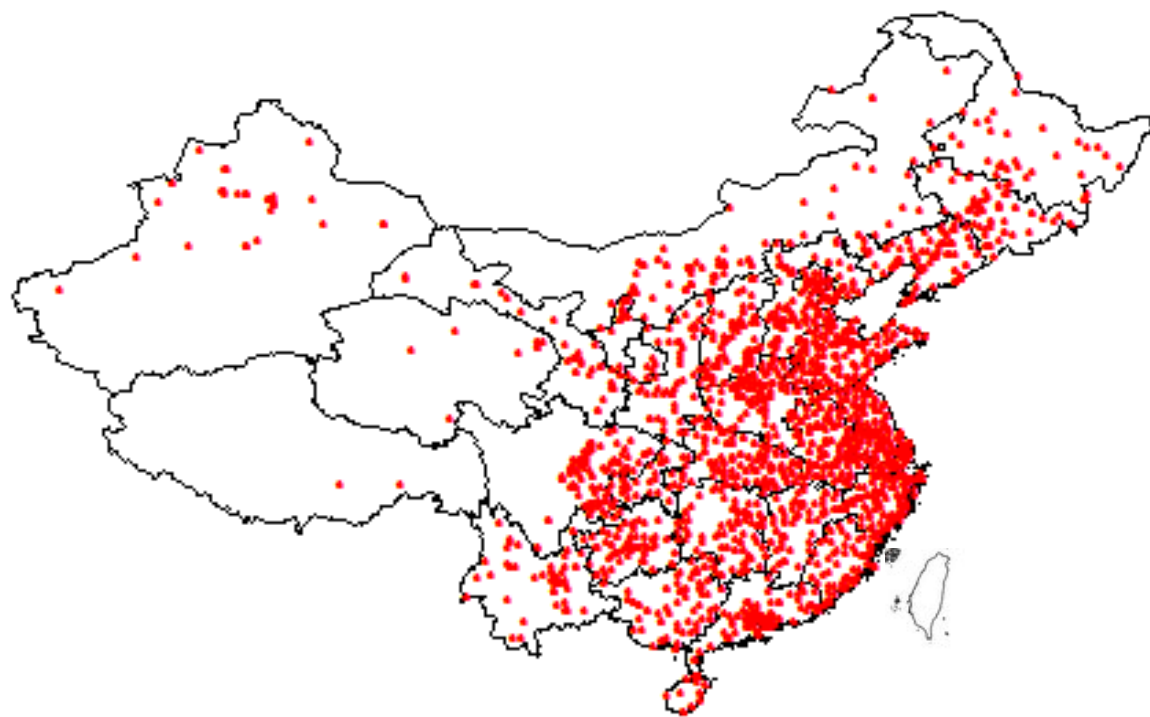
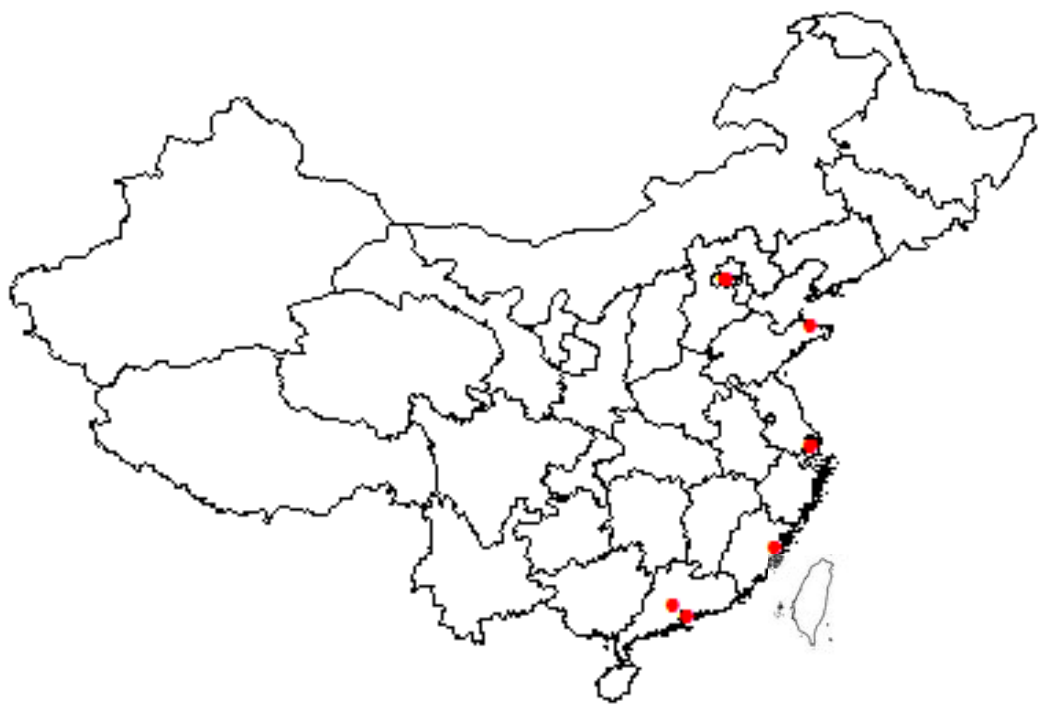
1. Country context
2. Survey design
3. Findings
4. Implications

1. Country Context

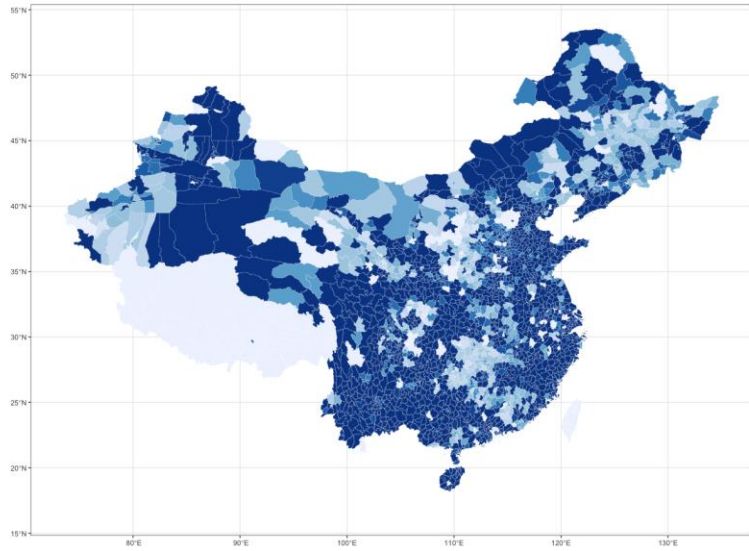
1. Country context

- Proliferation of banks in China since the mid-1990s
- Outcome of political bargaining
- Big 4 central state banks + thousands of “local state banks”
- “As competitive as of that of the US”

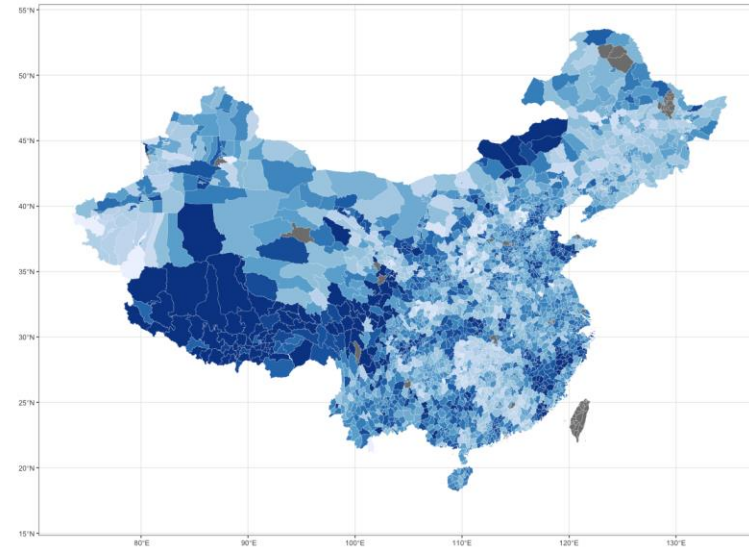
Beijing's Banking Balloon



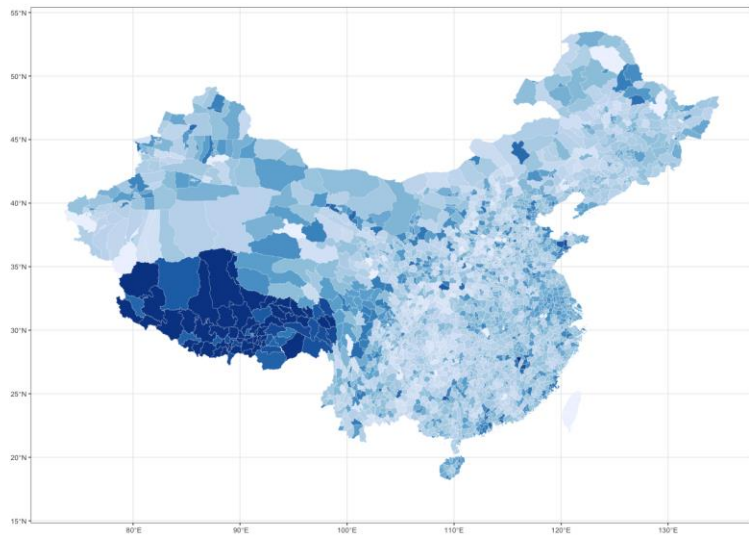
Shrinking Big 4's branch share



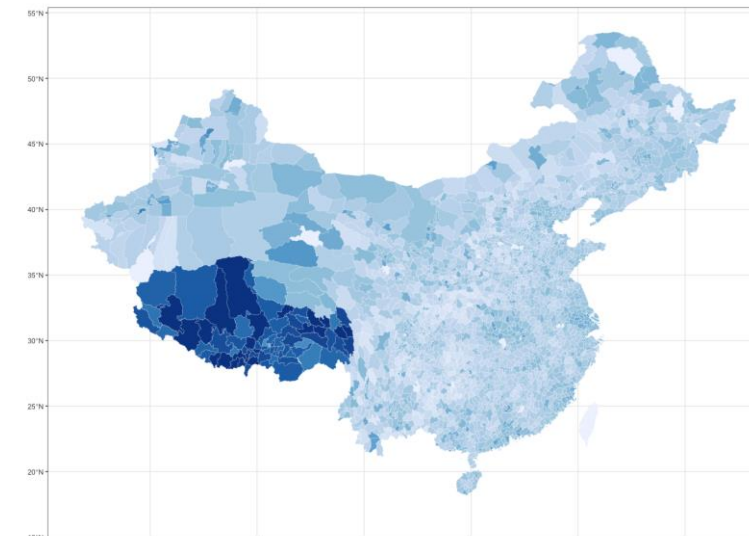
1986



2001



2009



2019

1. Country context

- A variety of firms
- SOEs ([institutional connections](#)) and private ones
- Both SOEs and private firms can possess [personal connections](#) with the party state

1. Country context

		Institutional Connections (SOE)	
		YES	No
Personal Connections	YES	+++	+
	No	++	baseline

The power of connections become more salient when resources are scarcer

2. Survey Design

2. Survey Design

- Conjoint survey experiment with Chinese loan officers
- Multi-dimensional, choice-based research design
- Assess how each firm attribute affects respondent preferences/selections
- Particularly useful in country contexts where respondents might be less willing to reveal true preferences

2. Survey Design

- “This is a study about firm finance in China. You will see the general information about ten sets of firms, such as their sales growth, debt level etc. In each set, there are two hypothetical firms (Firm A and Firm B). Firms in each set belong to the same industry, are of the same size and age, and possess the same amount and kind of collateral, etc. The firms in each choice set are also located in the same region.”

2. Survey Design

Attribute	Firm A	Firm B
Profitability	{high, low}	{high, low}
Sales growth	{fast, slow}	{fast, slow}
Debt level	{high, low}	{high, low}
Institutional connection	{central SOE, provincial SOE, city SOE, county SOE, private}	{central SOE, provincial SOE, city SOE, county SOE, private}
Personal connection	{current NPC/CPPCC member, neither...nor...}	{current NPC/CPPCC member, neither...nor...}
Contribution to taxation	{big, small}	{big, small}
Contribution to employment	{big, small}	{big, small}

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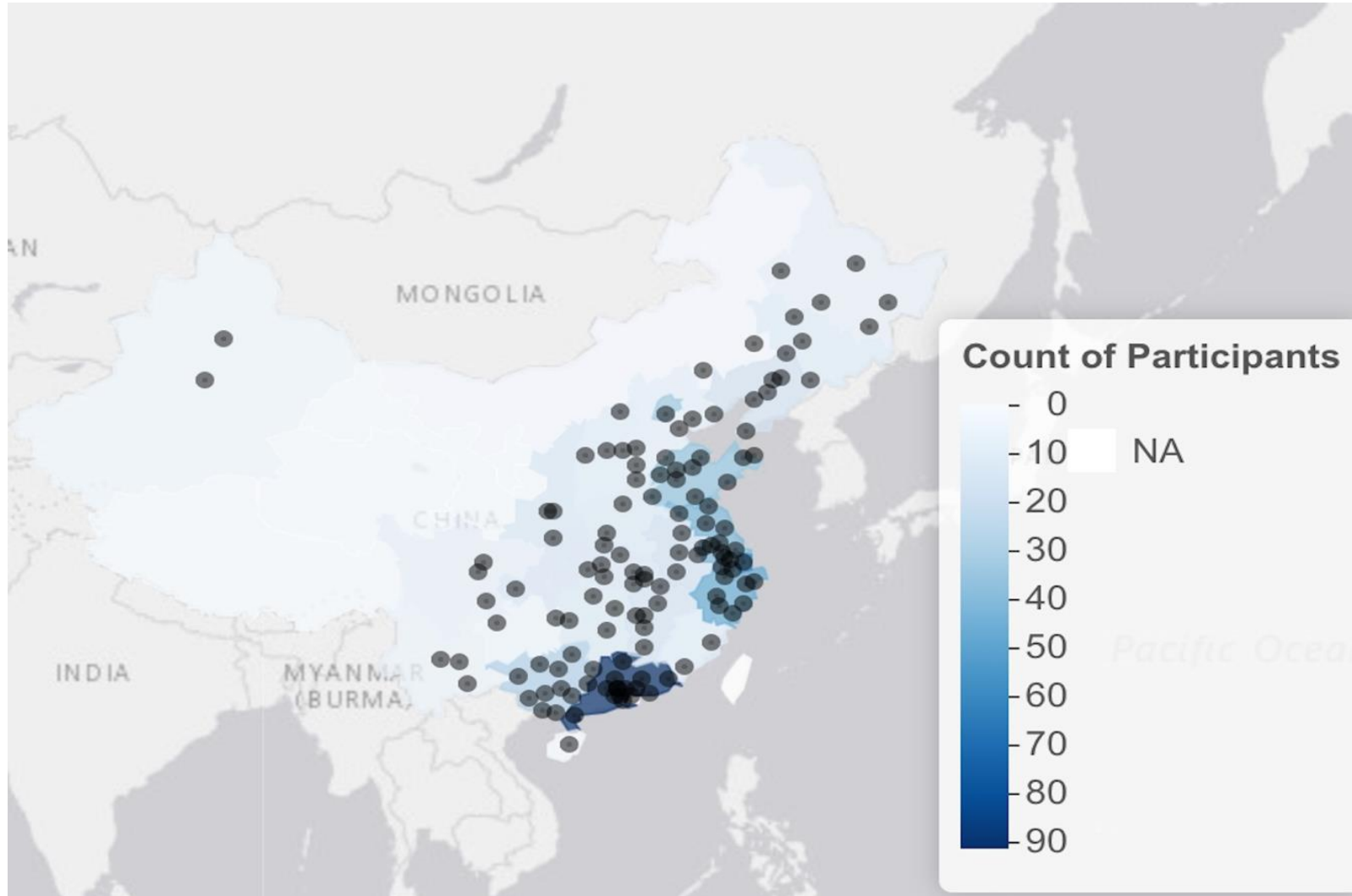
2. Survey Design

1. During normal times, imagine both firms can secure a loan. Which one is more likely to get it at a cheaper cost? (0, 1)

2. Under a tightening credit environment, which firm is more likely to continue to secure lending from banks in their respective localities? (0, 1)

** We understand that loan approval is a long and complicated process. It's also context-specific. You need not worry about the details and specifics; we only need your first reactions.

2. Survey Design



- Snowballing in late 2017 early 2018
- 35% from large central state banks
- A total of 500 loan officers
- A total of 10,000 (500*2*10) hypothetical firms

2. Survey Design

- I obtain the average marginal component effect (AMCE) of each firm attribute on the probability of a firm being chosen by the loan officer under each scenario.

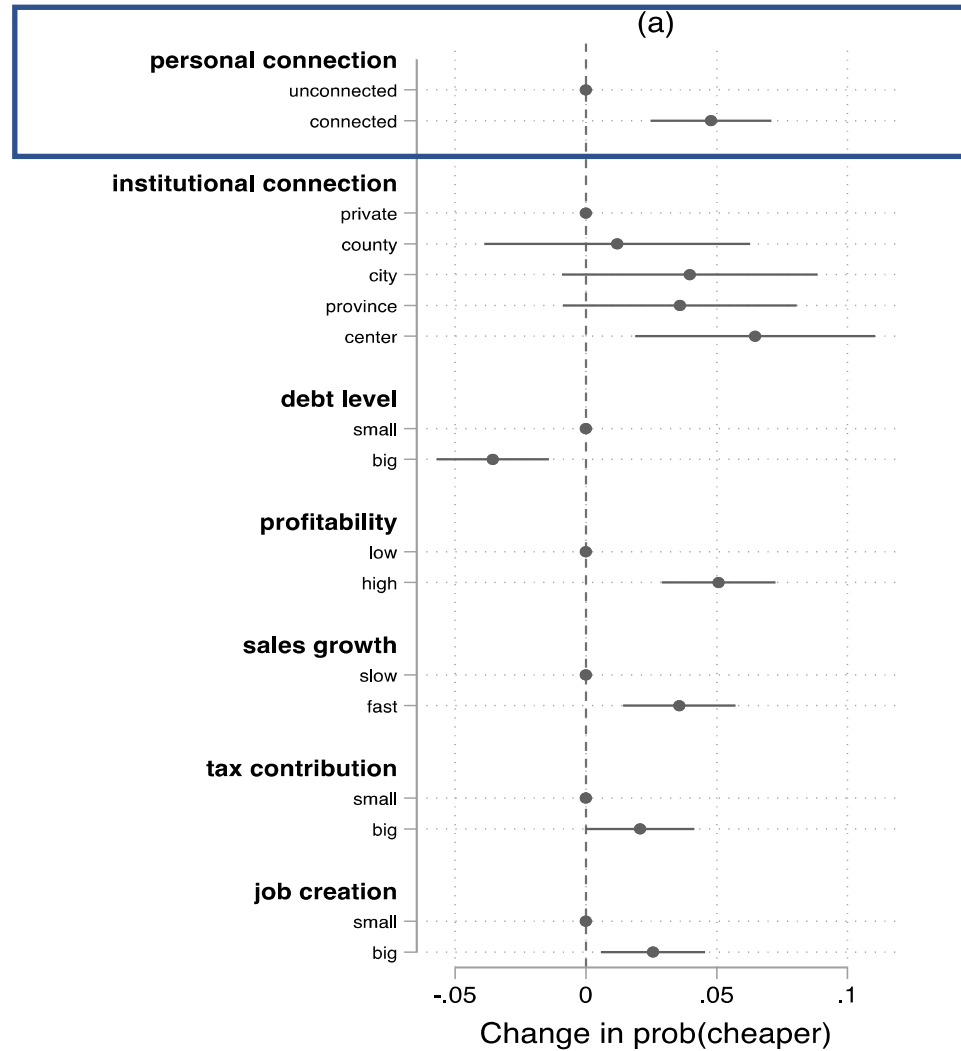
- $$Y_{ijk} = \beta_0 + \sum_{\alpha=1}^7 \sum_{d=0}^{D_{\alpha}} \beta_{\alpha d} X_{\alpha d i j k} + \varepsilon_{ijk}$$

- where Y_{ijk} is the binary outcome variables indicating whether firm j in task k for loan officer i is chosen. $X_{\alpha d i j k}$ represents the d th value of attribute α . $\beta_{\alpha d}$ is the estimated coefficient.

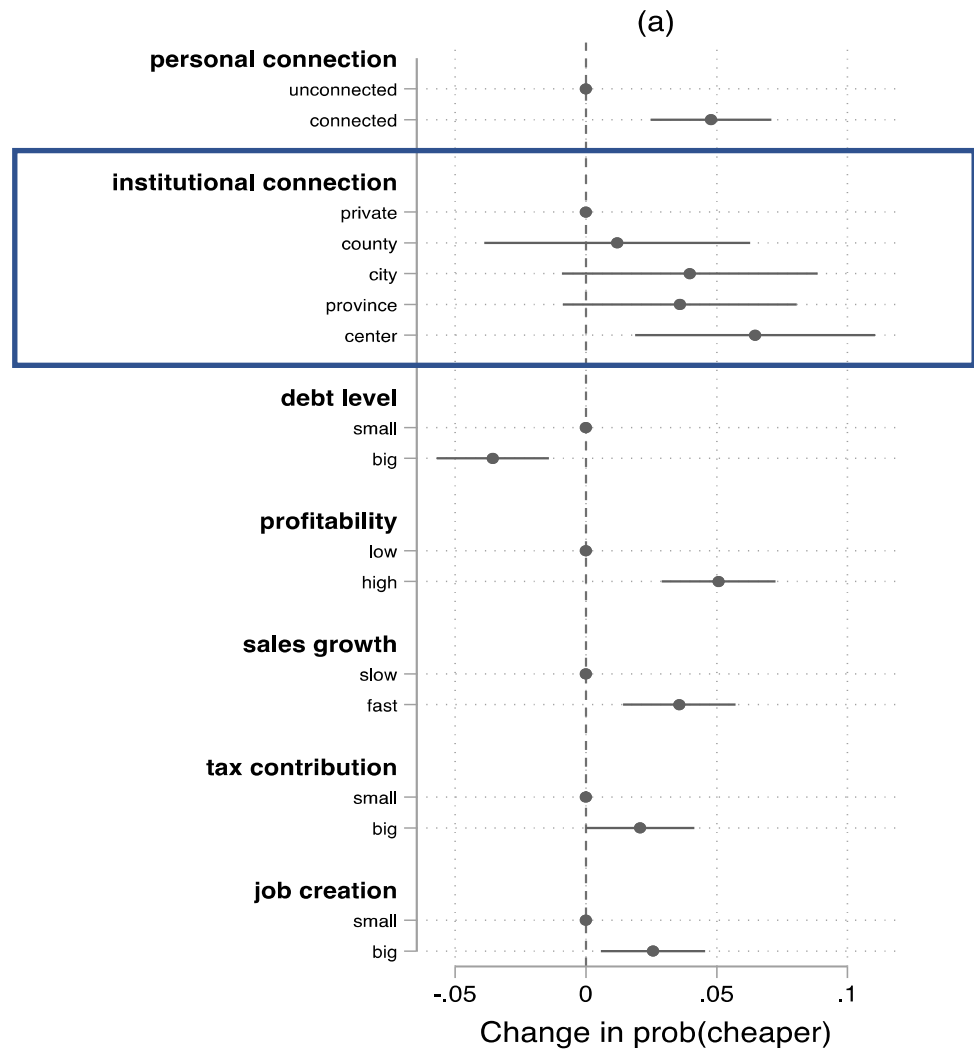
3. Findings

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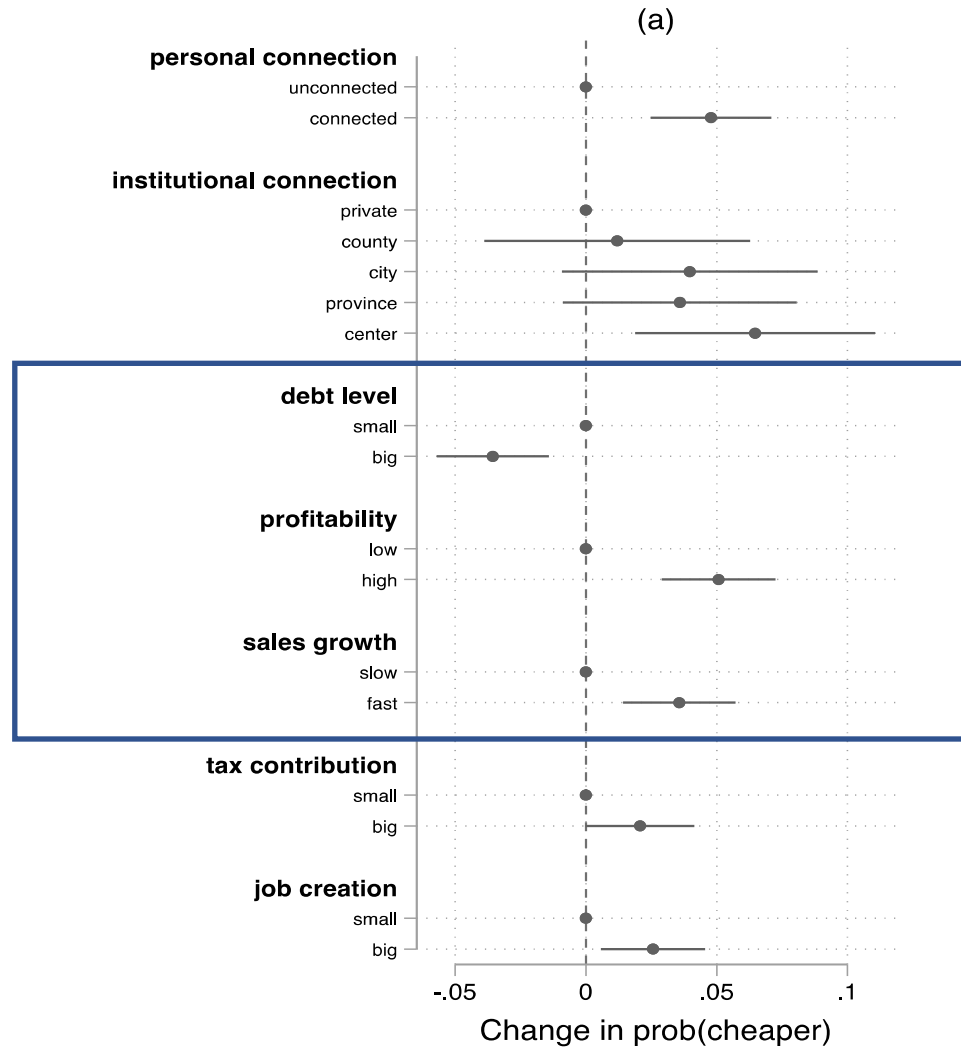
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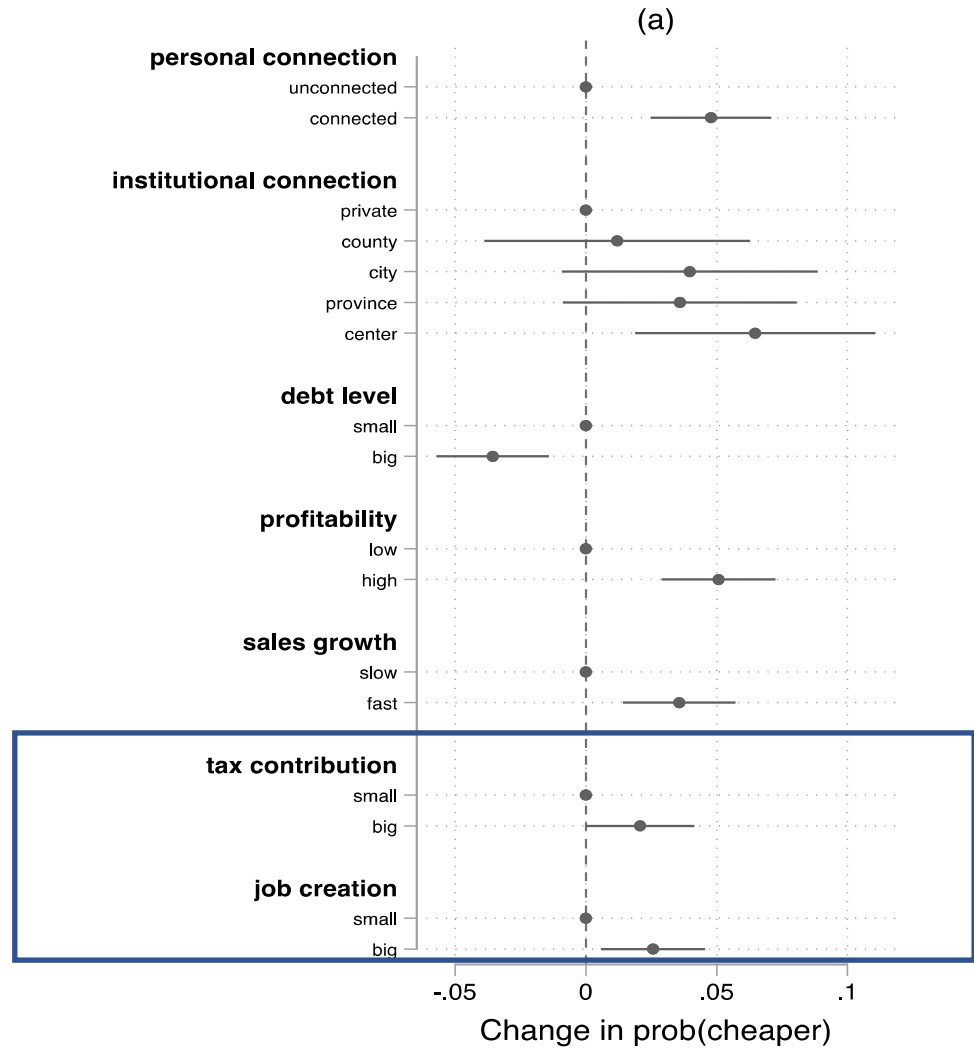
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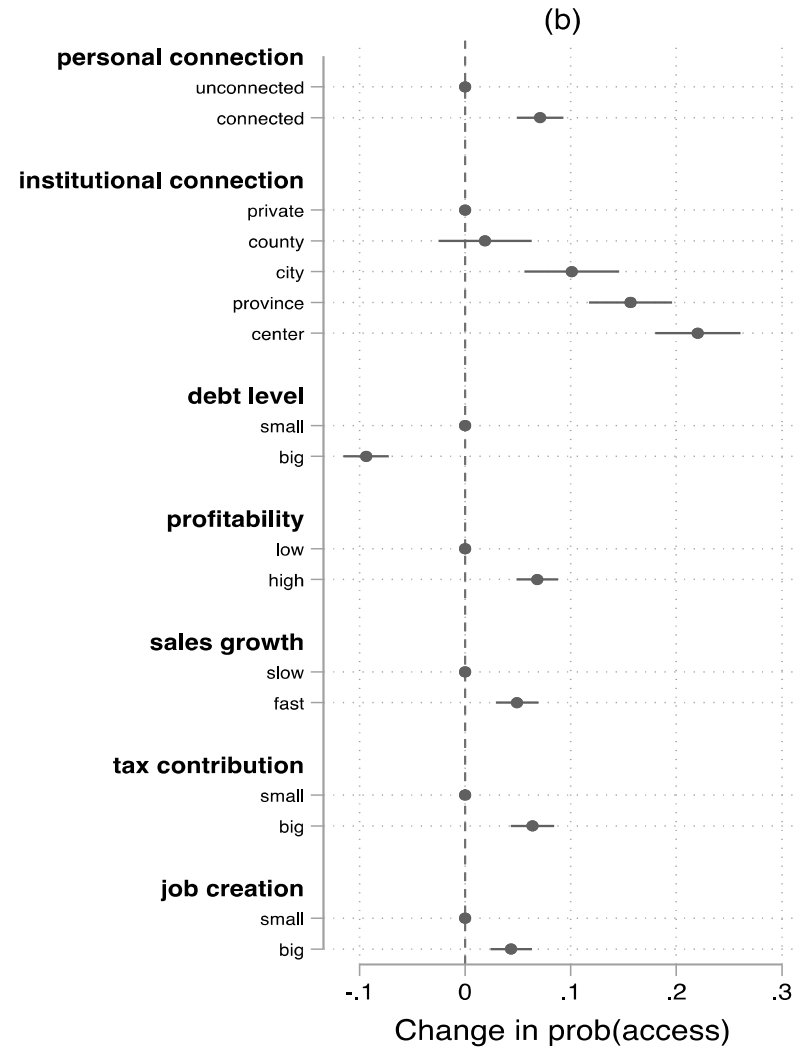
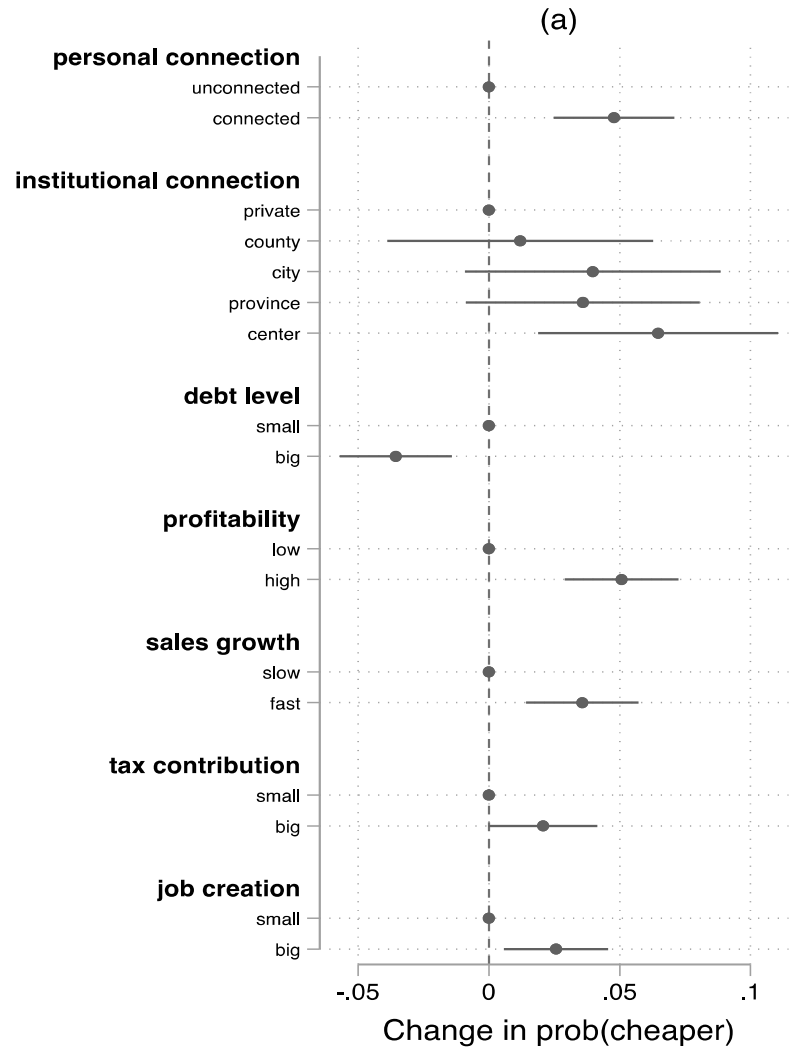
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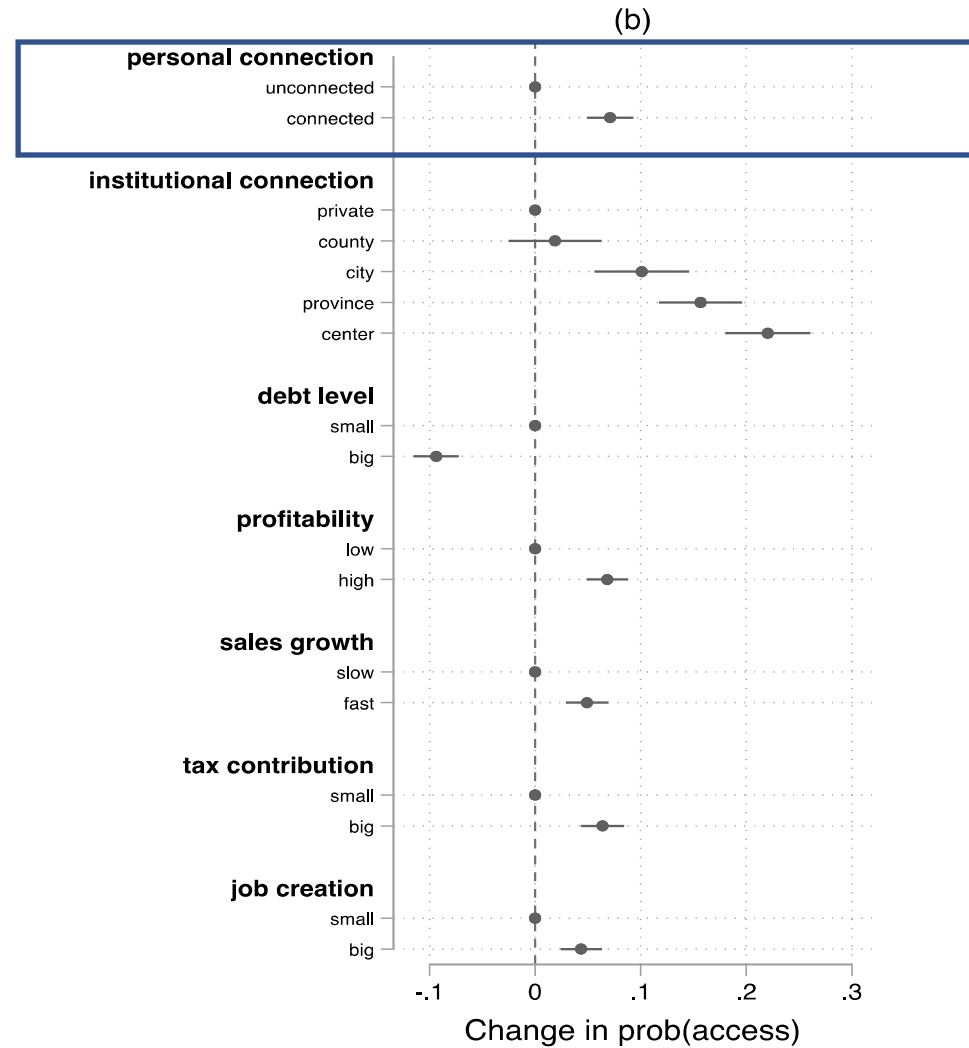
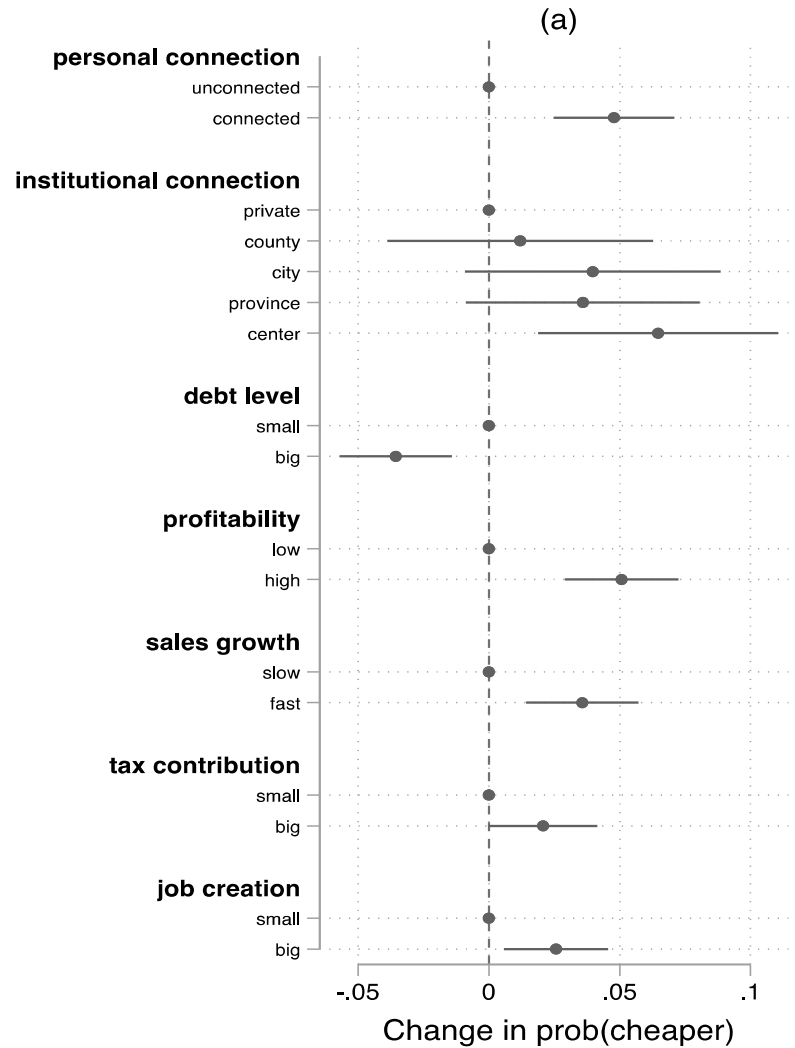
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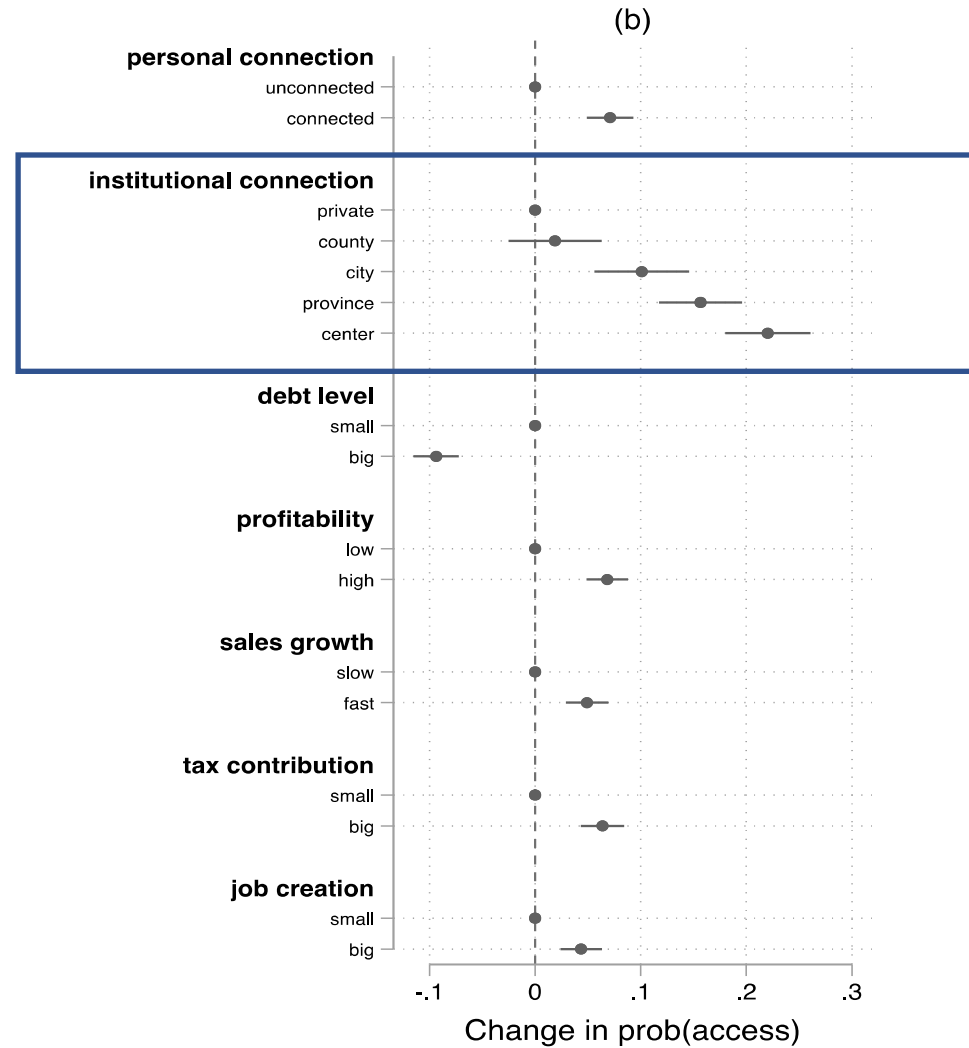
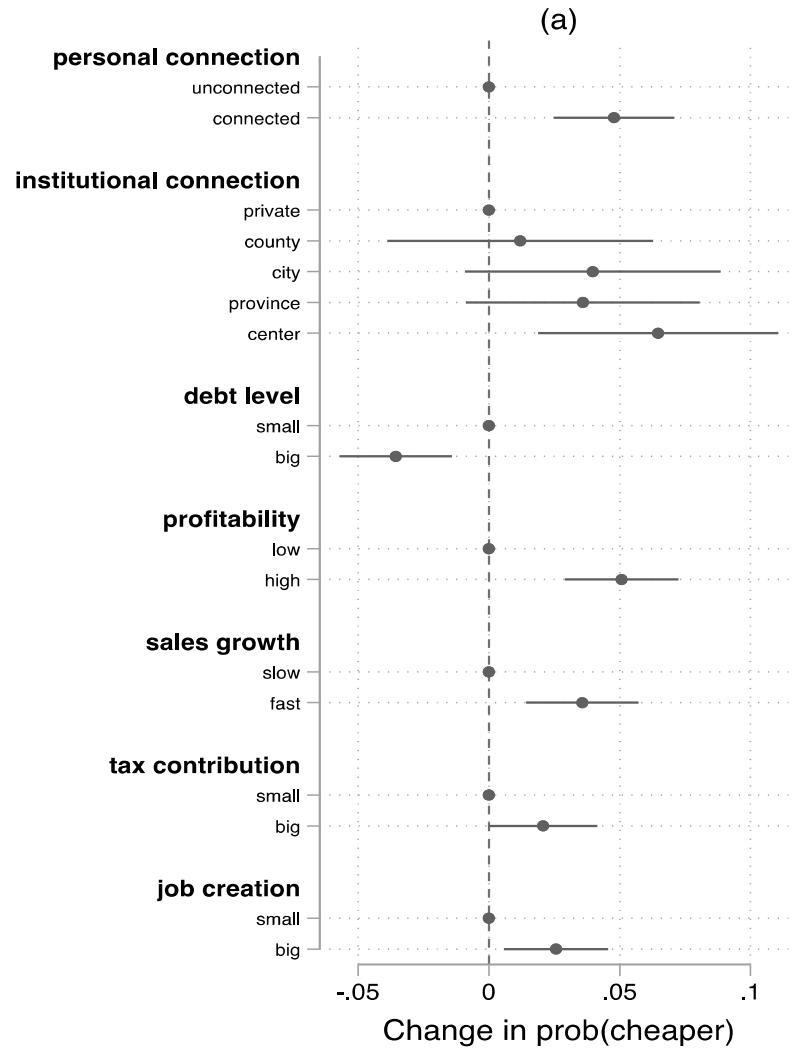
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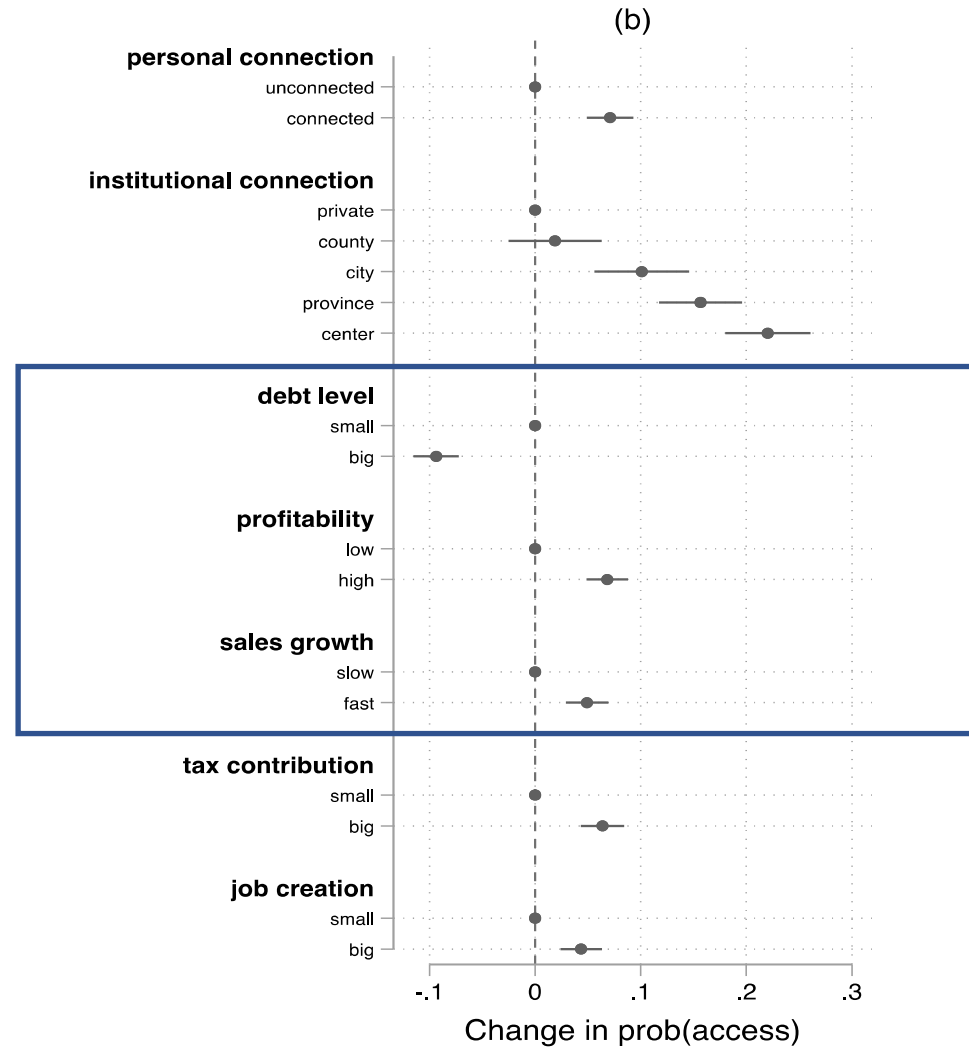
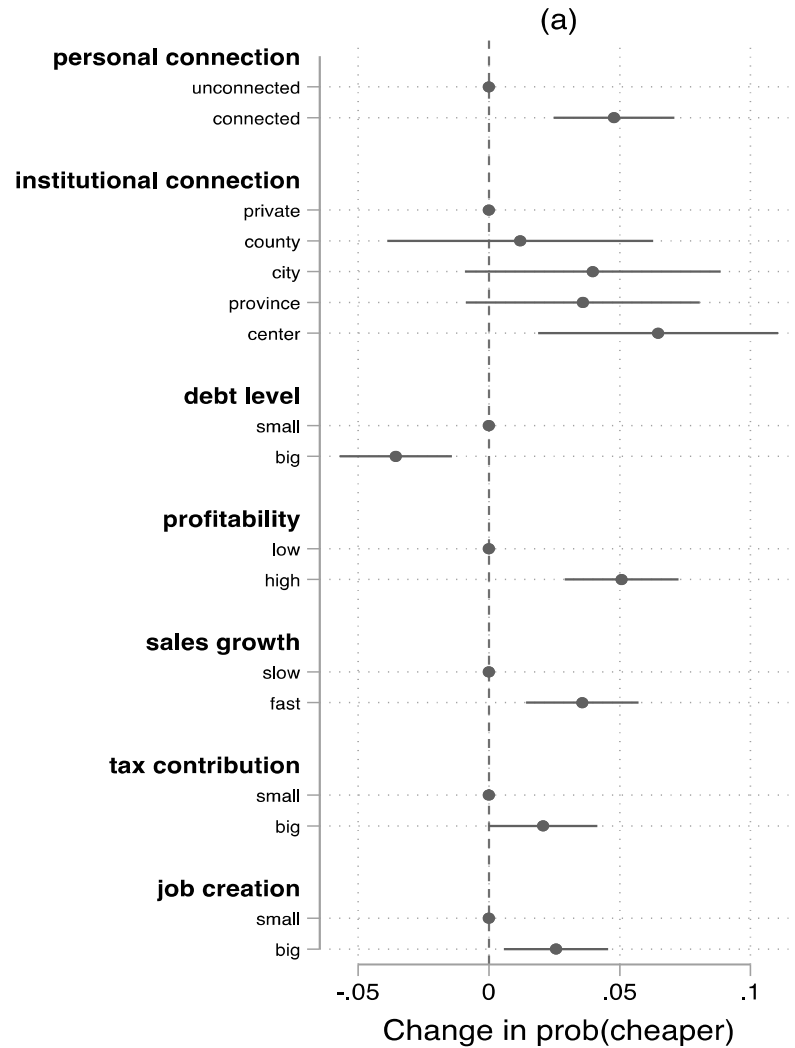
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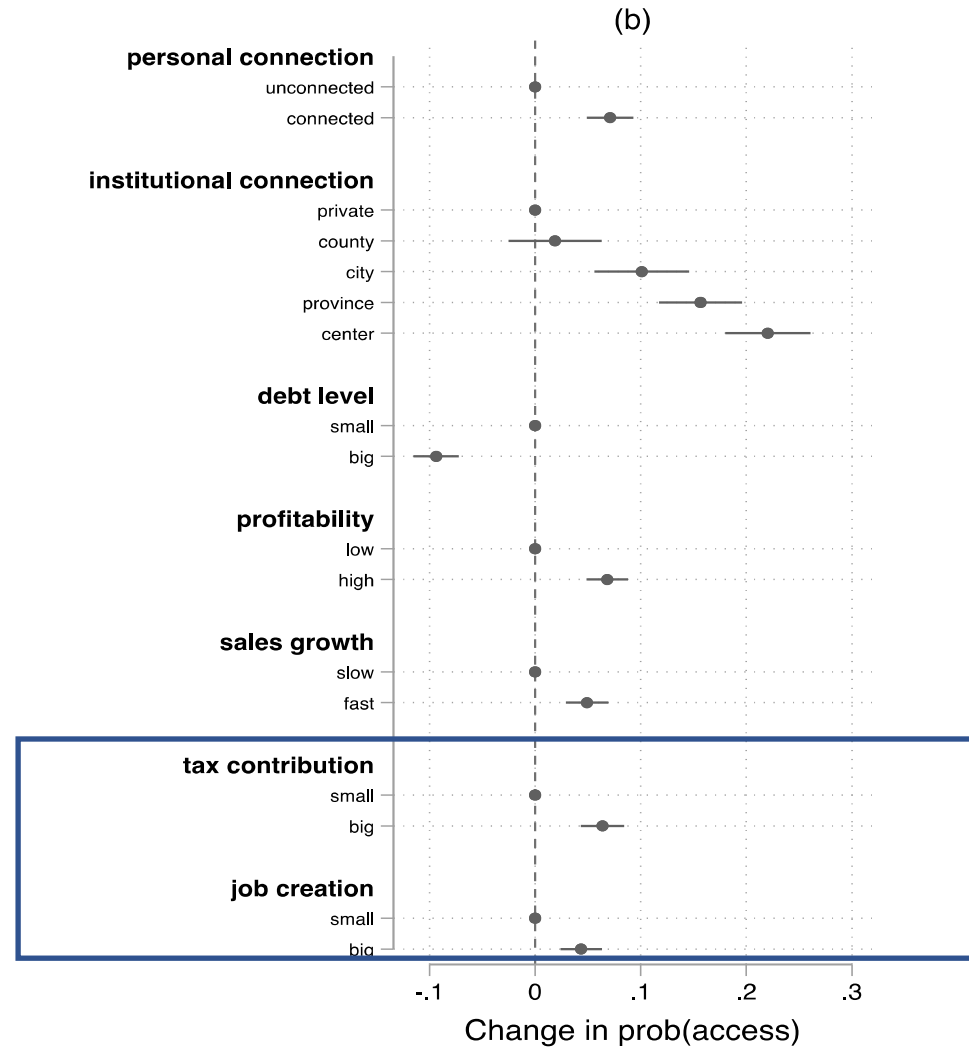
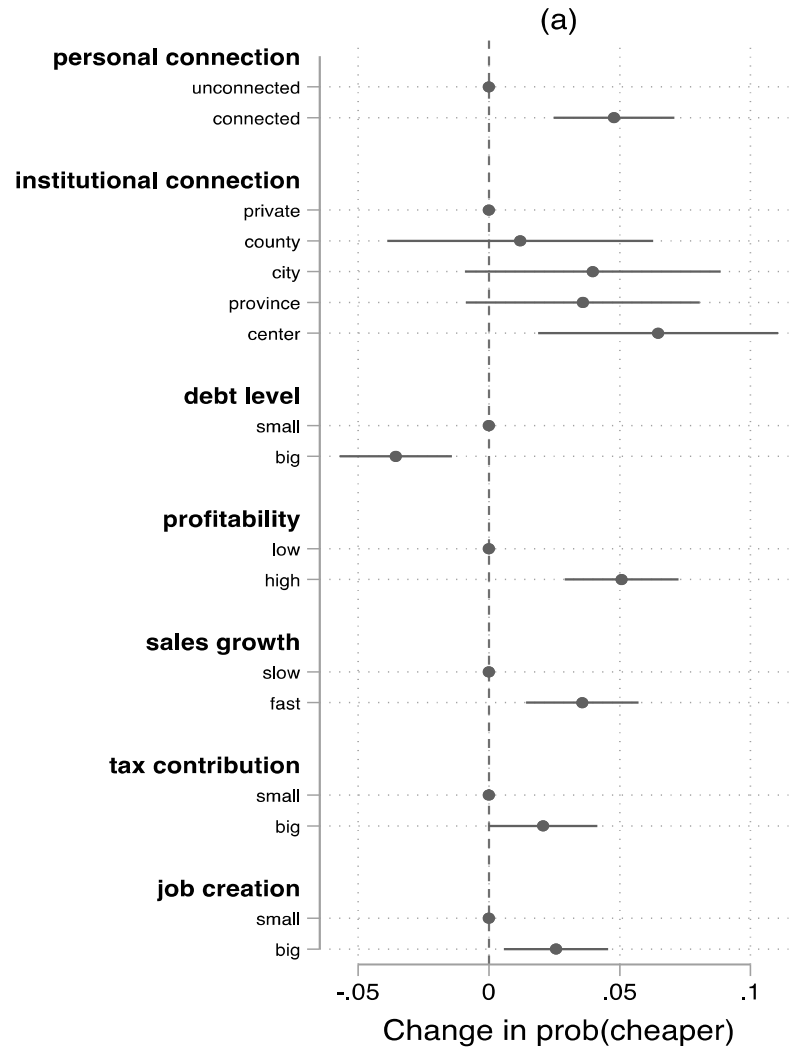
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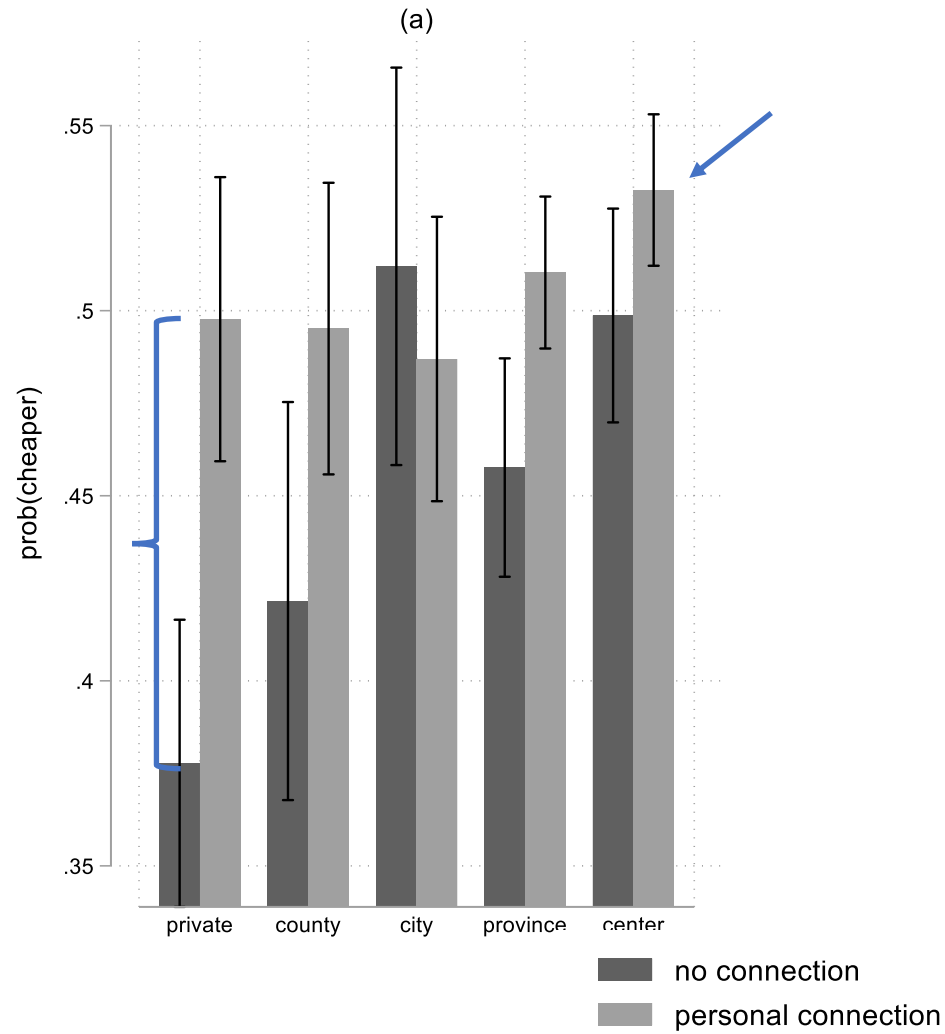
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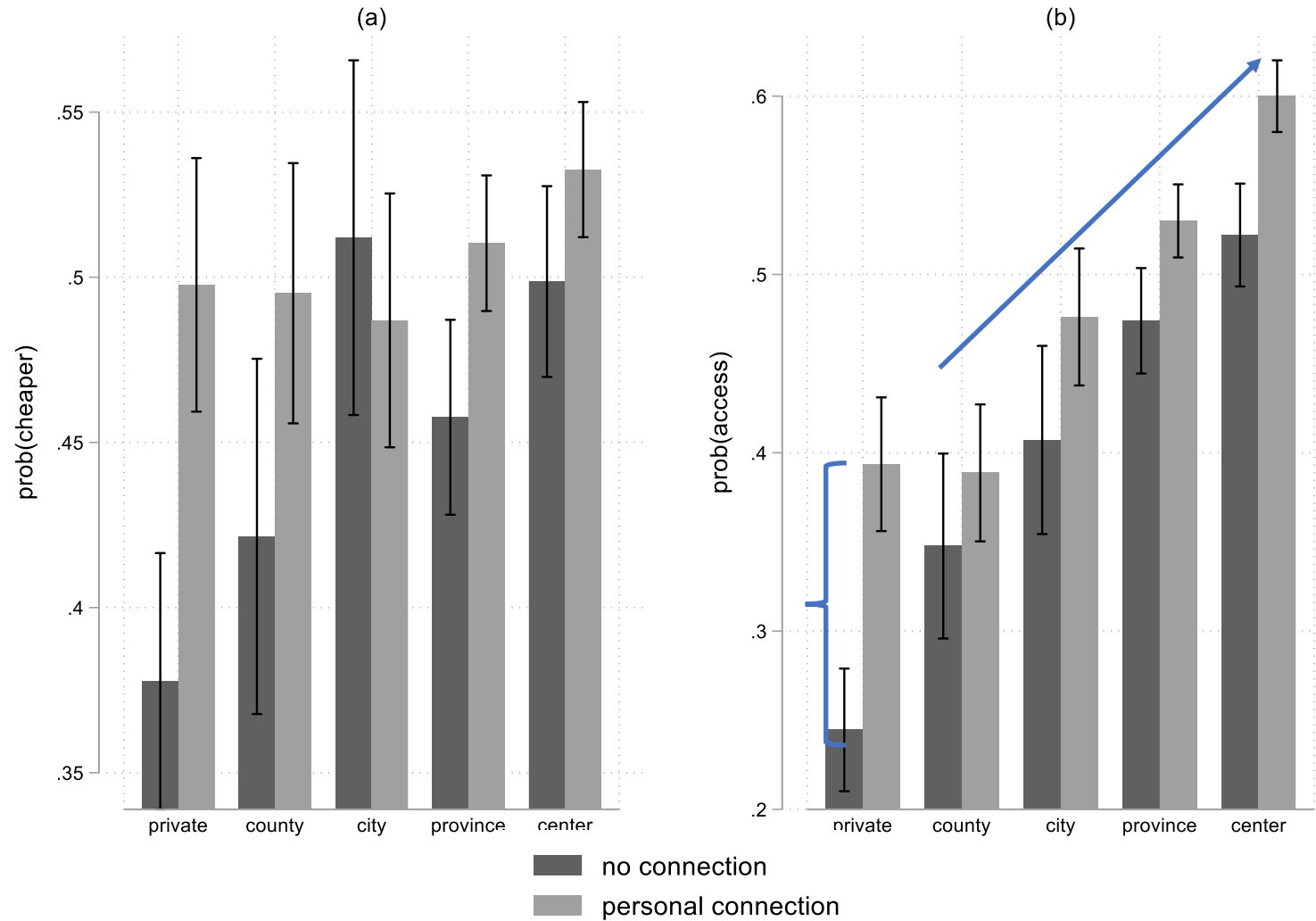
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3. Findings

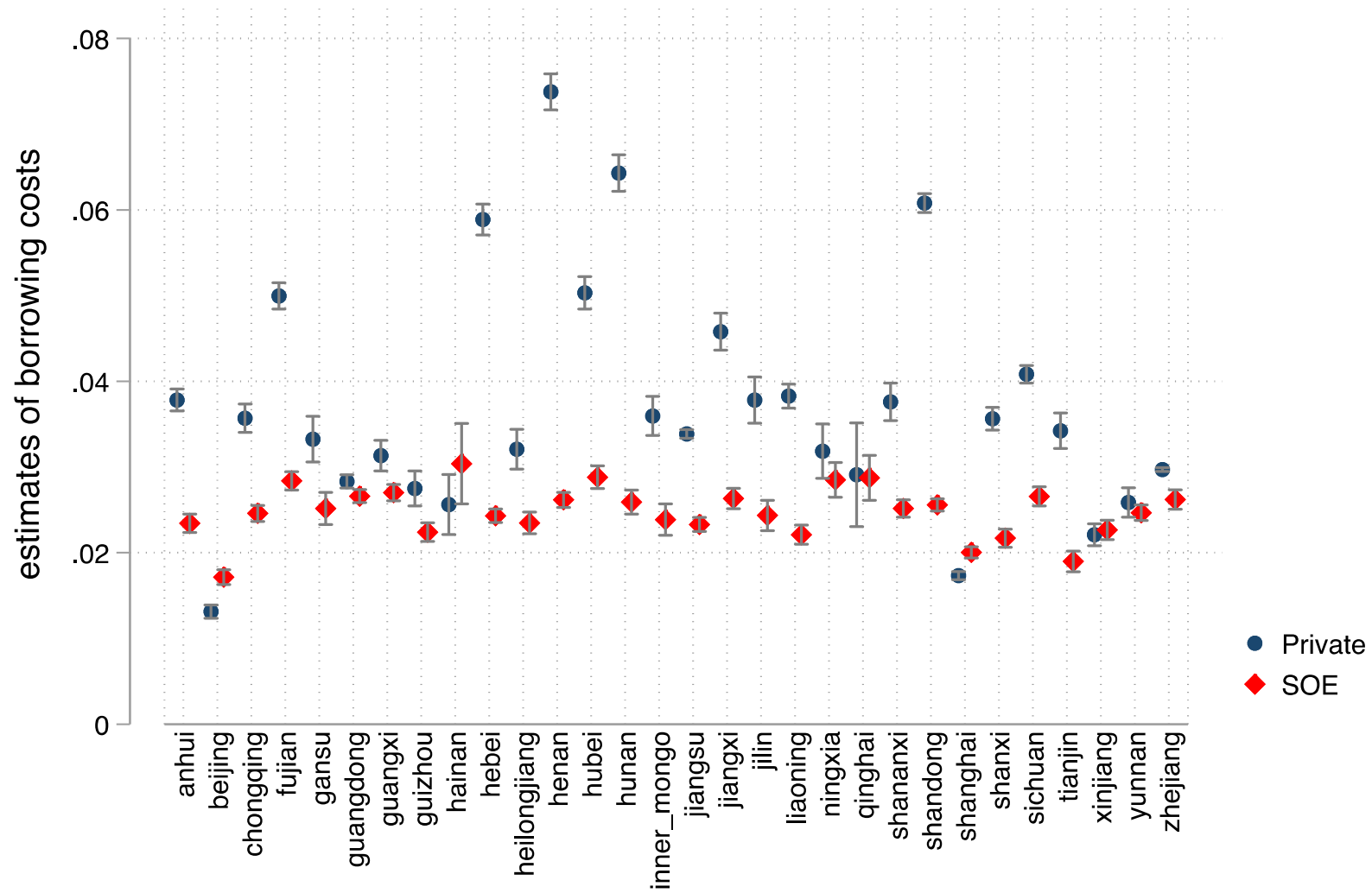


Conclusion

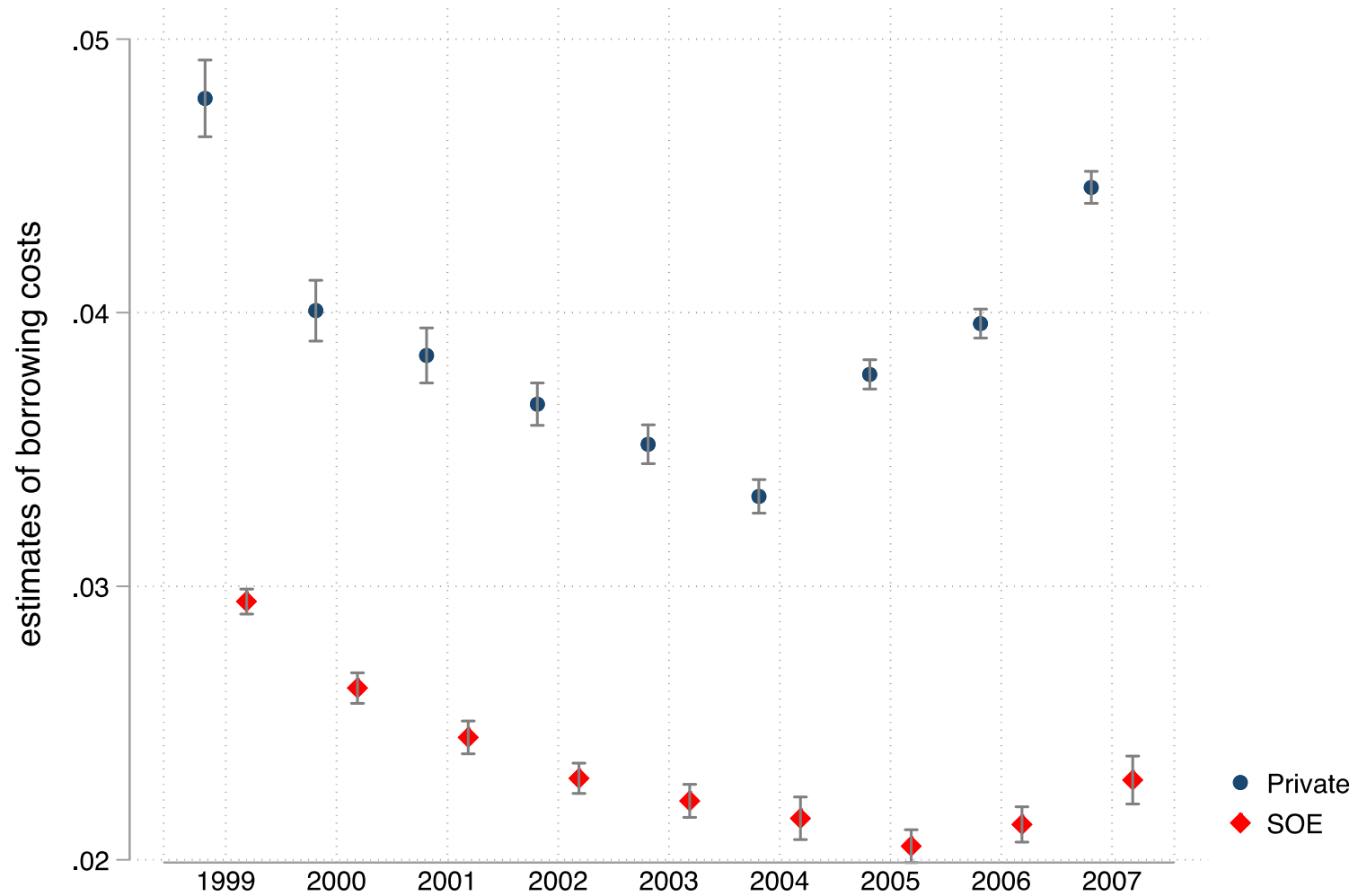
- Experimentally tease out the causal effects of political connections
- Institutional connection vs personal connection
- Microscopic view of how grassroots economic resource allocators in China deliberate

Thank you!

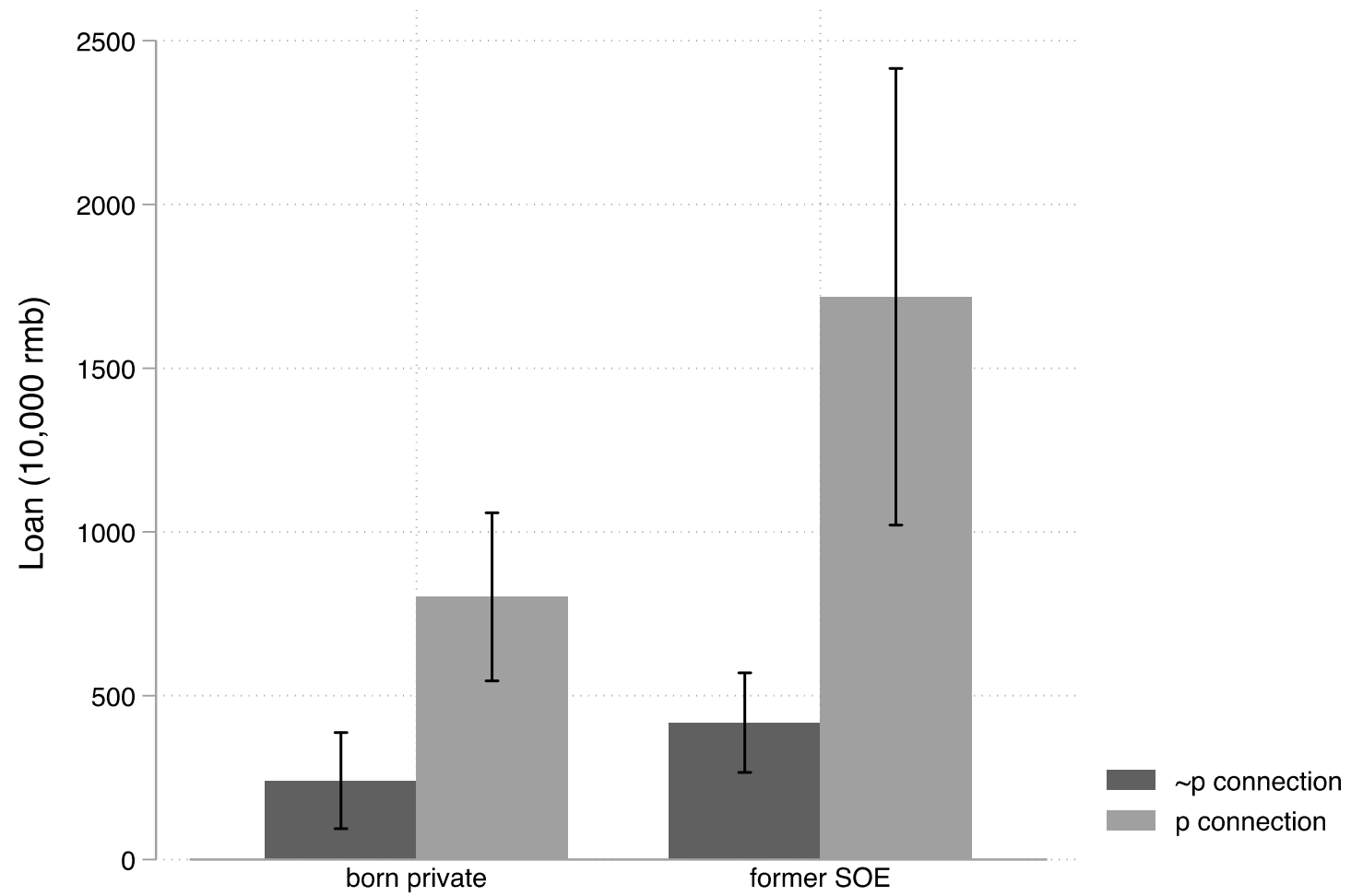
Spatial variations in firms' estimated borrowing costs



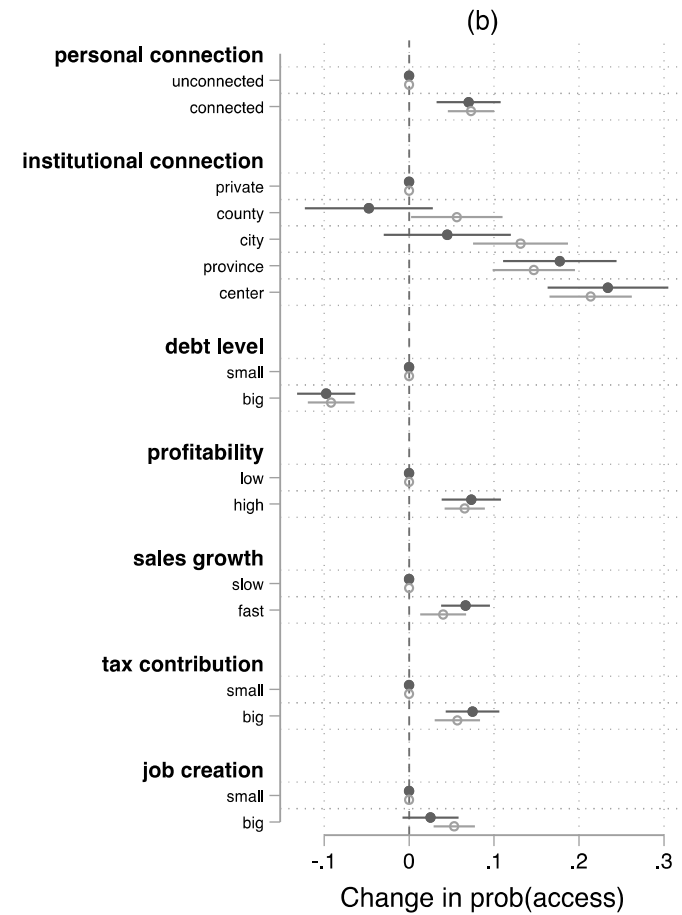
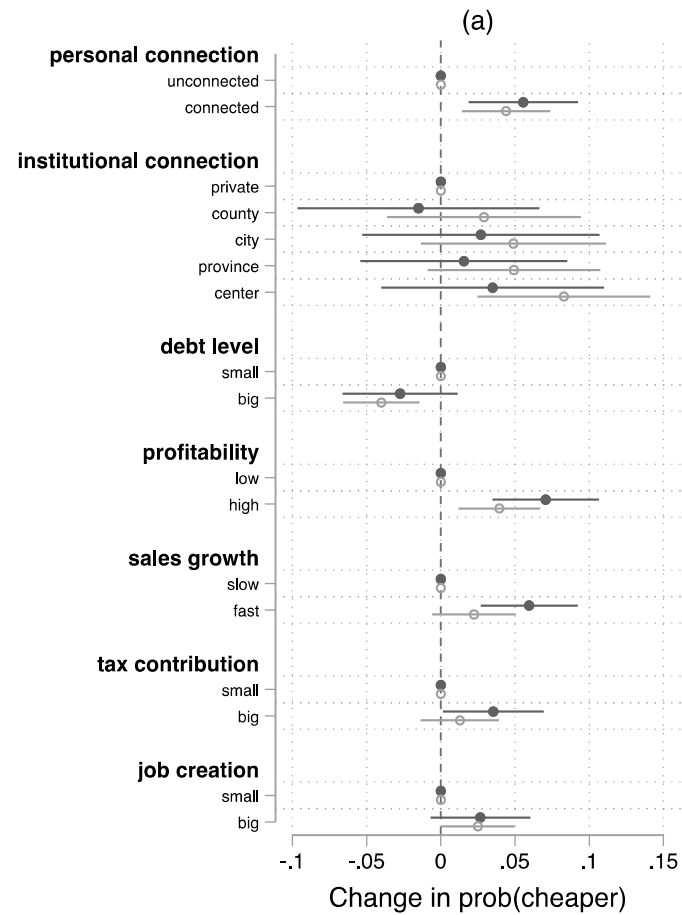
Temporal variations in firms' estimated borrowing costs



Private Firm's Bank Borrowing, 2006

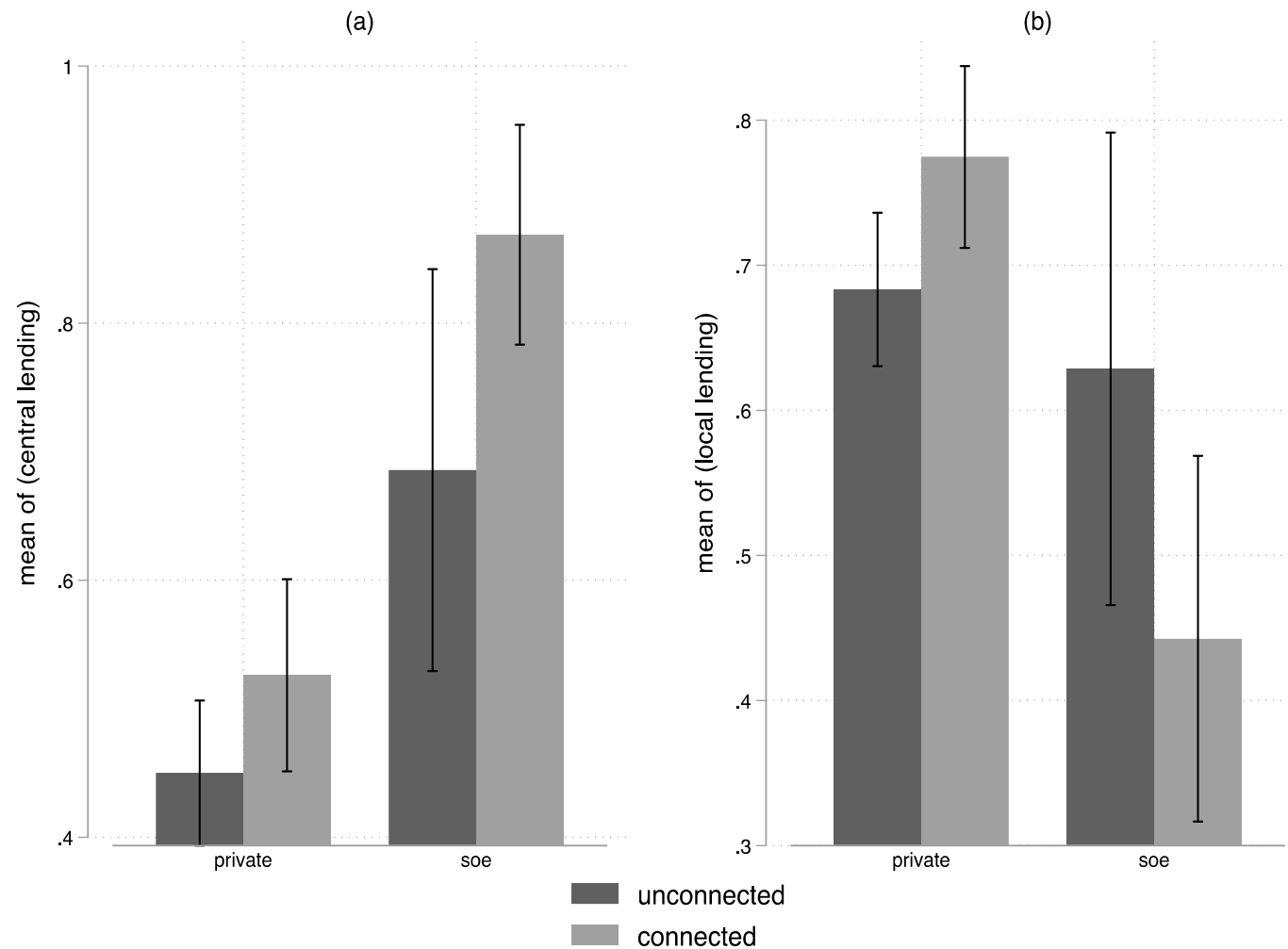


Central State Banks vs. Local State Banks

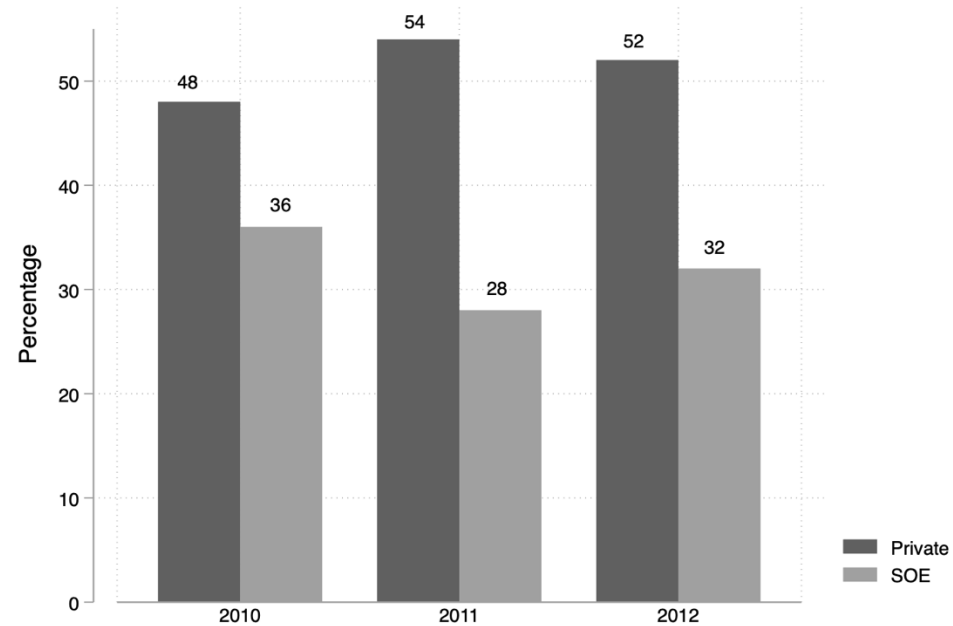


- central state banks
- local state banks

Firm Managers' Self-Report on Main Sources of Bank Borrowing (2017)



Local state banks are now a crucial pillar of local economy Private sector development



Lardy 2014

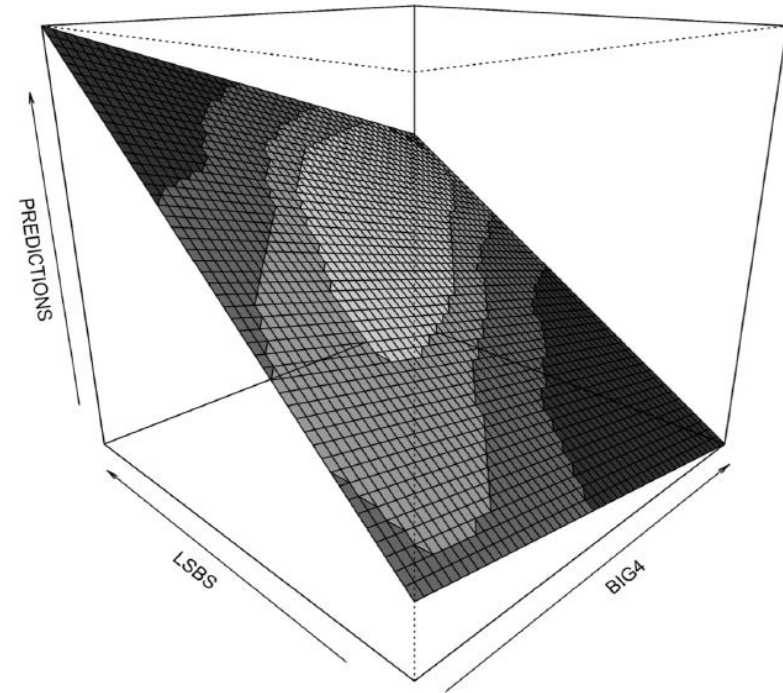


Figure 4-9 LSBs, Big 4 and Private Investment

