

# **The Trinity Effect of Corporate-Political-GOB relationship over Debt Structure: Evidence from India**

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# Agenda

1. Introduction
2. Objective
3. Data and Research design
4. Results and Extensions
5. Conclusion
6. Forthcoming Research

# Introduction

- The present Work tests the genesis of TBS crisis through a detailed analysis of corporate-political connections and their debt structure.
- The Economic Survey of India (2017-18) indicates an unprecedented rise in the corporate loan defaults and IBC proceedings in India ever since the start of the banking crisis in 2016.
- The mid-2000s investment boom is expected behind this unprecedented situation.
- GAP: 1. Static Analysis of Khwaja and Mian (2005) for PCFs of Pakistan.  
2. Srinivasan and Thumpy (2017) reports the significant role of corporate-banking relationship.

# Objectives

- Role of corporate-political connections in explaining the debt structure of Indian firms.
- Different categories of these connections (weak or strong; persisting or dynamic) help explain the role of banks in providing easy loans to PCFs.
- Whether banks provide long-term credit to the firms without any cherry-picking on their political connections?
- Corporate-Political-GOB trinity may help decipher the underlying reasons for high corporate loan defaults and the TBS problem in the country.
- Understanding the sector specific trinity effect. Do some sectors outperform the default as compared to others?

# Data and Research Design

- Sample: S&P BSE 500 (excluding financial firms)
- Time period: 2003 to 2016.
- Data regarding firms' financial indicators are taken from the Thomson Reuters DataStream database and for their banking relationship we use the CMIE Prowess.
- Data regarding campaign contributions to National Political Parties (BJP, INC) are taken from ECI website.

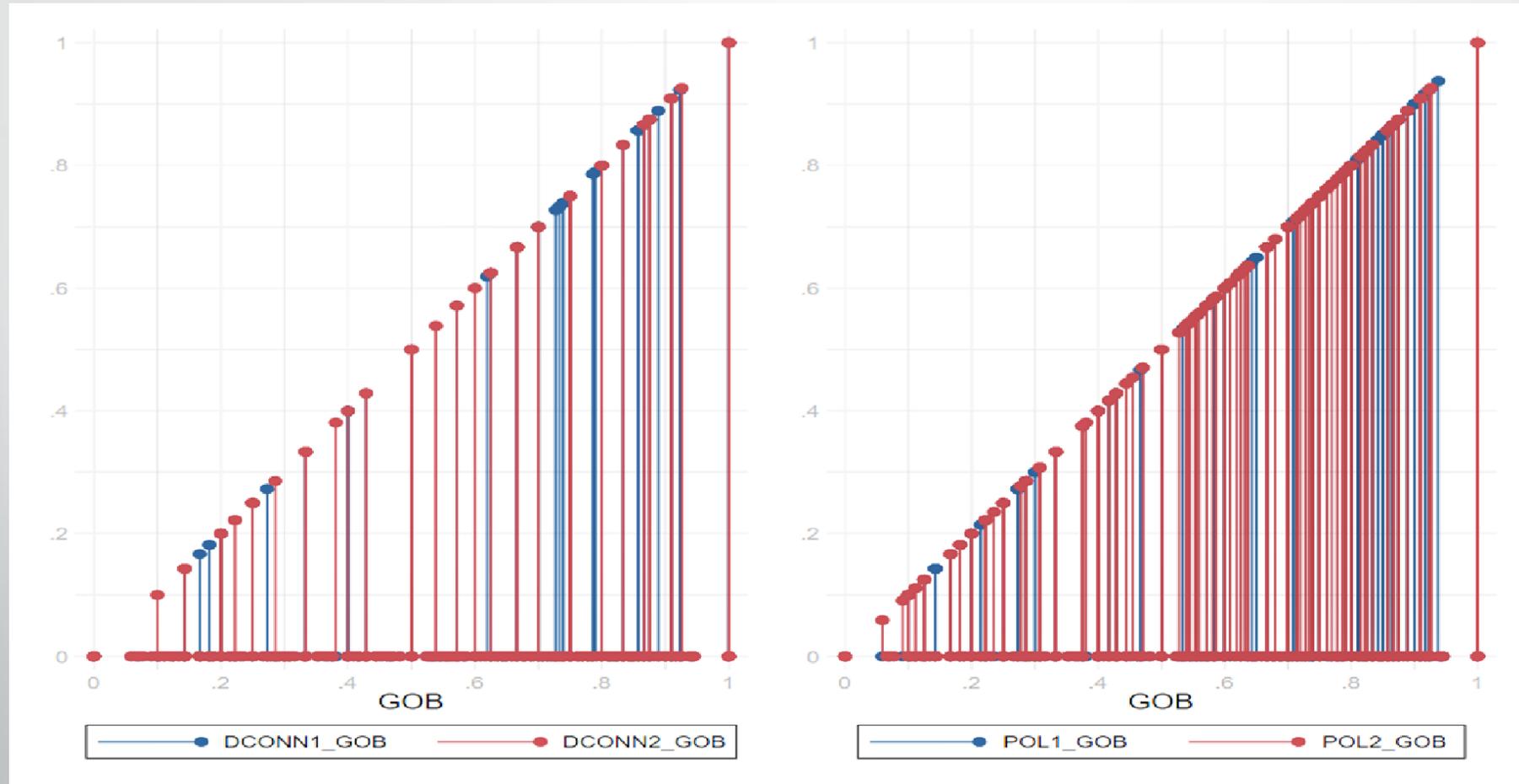
# Data and Research Design cont...

## Variable Construction

- **Corporate-Political Connections:**
  - **Dynamic Connections:** A firm or any of its subsidiary monetarily contributes to any of the national political parties (BJP or INC) in a particular year.
  - **Persisting Connections:** At least once the firm or any of its subsidiary contributes to a national party (BJP or INC).
  - **Strength Effect:** On the lines of Cooper et al. (2010) firms contributing to a single party are weakly connected whereas those contributing to multiple parties are strongly connected.
- **Corporate-Banking Relationship:** Generate a score variable for each firm's banking relationship for each year. Figure below shows a higher preference of strong PCFs for GOBs.
- **Debt Structure:** Following Huang and Shang (2019) constructs two forms of debt variables i.e. book & market.

# Data and Research Design cont...

Interaction of Dynamic and Persisting Connections with GOBs (Fig. 1)



# Data and Research Design cont...

## Empirical Strategy

- $DEBT_{it} = \gamma_0 + \beta_0 DEBT_{it-1} + \beta_1 POL + \beta_0 Firm\_Factors + \beta_3 COUNTRY\_FACTORS + \alpha_k + \alpha_t + \varepsilon_{ijt}$

Further includes the strength and POL-GOB relationship in the specification.

- Beside the OLS technique study also uses the two-step robust GMM approach.

# Results & Extensions

GMM results of Corporate-Political connections and GOBs

VARIABLES	LTD_BV	LTD_MV	LTD_BV	LTD_MV
GOB	-0.651 (1.223)	-0.294 (1.085)	-0.0447 (0.571)	-0.514 (0.802)
DCONN_ONE	0.404 (0.822)	0.339 (0.853)		
DCONN_BOTH	-1.522# (0.966)	-1.635* (0.959)		
DCONN1_GOB	-0.820 (0.958)	-0.583 (1.077)		
DCONN2_GOB	2.380* (1.365)	2.422* (1.364)		
POL_ONE			0.172 (0.617)	0.528 (0.519)
POL_BOTH			0.842 (0.550)	0.440 (0.550)
POL1_GOB			1.372 (1.143)	0.602 (0.807)
POL2_GOB			2.346**	1.306#

# Results & Extensions Cont...

## Summarized

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	Effect on LTD (BV and MV)	Effect on LTD (BV and MV)
<b>Dynamic WPCs</b>	INSGF	INSGF
<b>Dynamic SPCs</b>	Pos. SGF	Neg. SGF
<b>Persisting WPCs</b>	INSGF	INSGF
<b>Persisting SPCs</b>	Pos. SGF	INSGF
<b>Dynamic WPC*GOB</b>		INSGF
<b>Dynamic SPC*GOB</b>		Pos. SGF
<b>Persisting WPC*GOB</b>		INSGF
<b>Persisting SPC*GOB</b>		Pos. SGF

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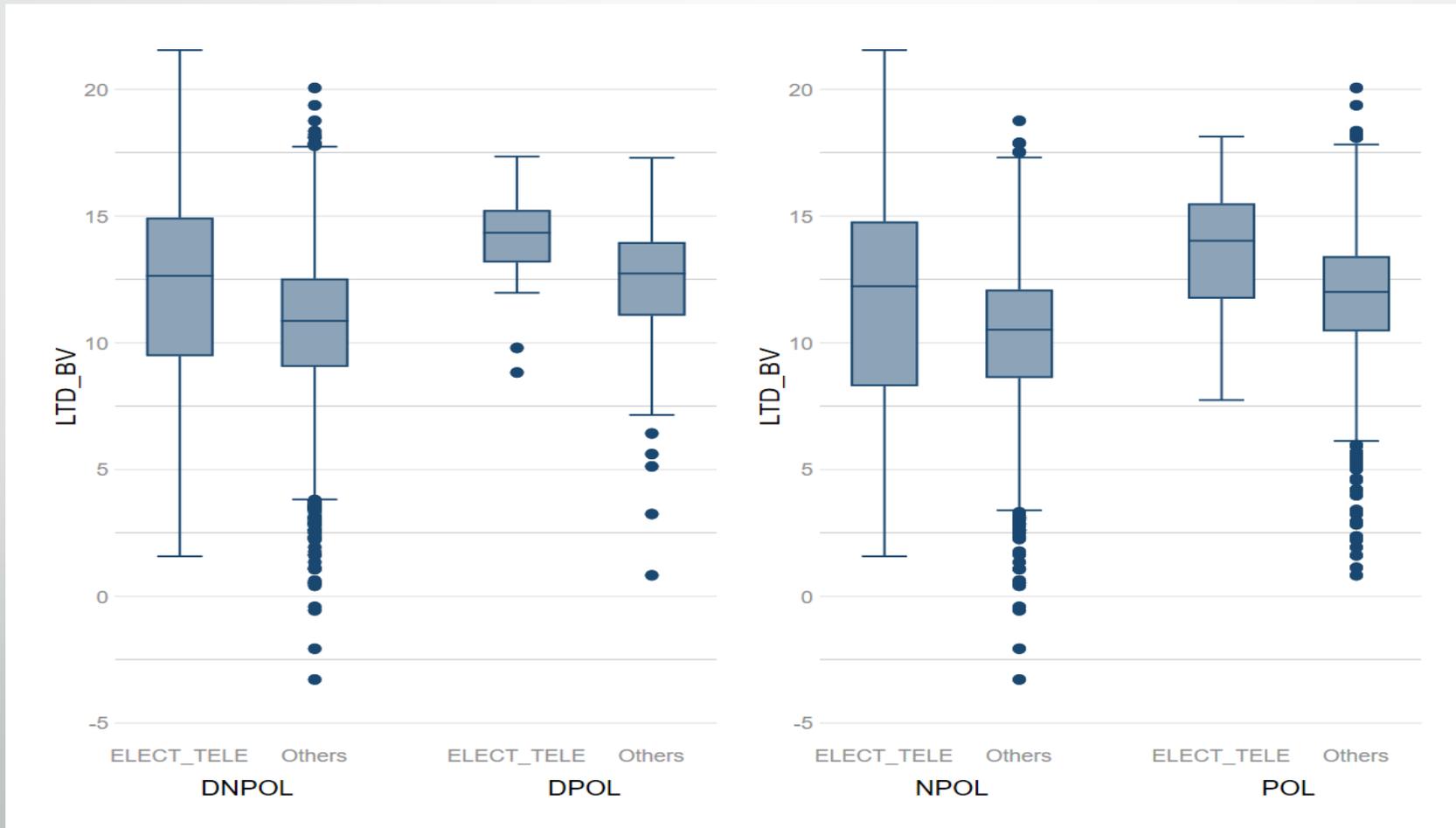
# Results & Extensions cont...

## Competency Analysis of GOBs

VARIABLES	INT_EXP	RLD	PRV_BD
DCONN_ONE	0.119 (0.442)	-0.536 (0.581)	-0.884 (0.641)
DCONN_BOTH	0.511*** (0.193)	1.448*** (0.479)	0.541* (0.307)
GOB	-0.0145 (0.127)	0.501** (0.251)	-0.246 (0.190)
DCONN1_GOB	-0.500 (0.722)	1.291 (0.837)	0.488 (1.050)
DCONN2_GOB	-1.014**	-2.207***	-0.659

# Results & Extensions cont...

## Electronic and Telecommunication sector



# Conclusions

- Only strong political connections have a significant effect with higher returns for persisting connections in comparison to dynamic ones.
- The efficiency of GOBs is significantly affected by their favouritism towards PCFs.
- Further, find a support to the inefficiency of GOBs particularly for the Electronics and Telecommunication sectors.

# Forthcoming Research

- We are developing a fraud risk mitigation mechanism.
- The study will discover the relationship between firms political connections and their financial reporting standards (FRS).

# References

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Thank You for your attention !!