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Bank Political Connections and Performance in China[1]

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Abstract

We examine the effects of bank's political connection on bank performance and risk in China. We use hand-collected information on CEOs' professional background to identify their political affiliations, and find that banks whose CEOs have former government experiences have higher return on assets, lower default risk, and lower credit risk. Additionally, politically connected banks have disproportionally higher performance when the CEOs previous worked in the same city where the current bank's headquarter locates, had past banking experiences, spend more on entertainment and travel costs, and have higher previous administrative rankings (e.g., at the provincial or state level). These results suggest that politically connected banks have better access to lending to politically connected firms, which are high yield assets and more likely to be bailed out when in distress. Our results offer a mechanism of political rent seeking, consistent with the institutional environment of China's banking and political system.

Keywords: Political connection, Bank performance, Anti-corruption shock, China

JEL Classification: G21 G28 G34

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1. Introduction

It has been widely acknowledged in the literature that political connections add value to firms (Fisman, 2001; Johnson and Mitton, 2003; Li et al., 2008; Goldman et al., 2009). One of the benefits of firm's political connections is obtaining preferential accesses to lending from the government or politically connected banks (Khwaia and Mian, 2005). However, these studies have mainly focused on the borrowers' perspectives, and it is unclear whether connections with the government can add value to the banks that lend loans to these politically connected firms. It is surprising that there exists scarce empirical findings on the impact of political connections on the lenders. In this paper, we contribute to the literature by focusing on the impact of political connections on bank performance.

Khwaja and Mian (2005) show that politically powerful firms can obtain rents from government banks by threatening bank officers with job transfers and removals, or rewarding them with appointments and promotions. In what follows, these politically connected firms will benefit from these politically connected loans, while banks will suffer. Additionally, governments are also incentivized to prioritize creditors rather than bank shareholders to ensure bank safety (Onali et al., 2016). Consequently, instead of aiming to maximize shareholder value, the boards of politically connected banks may act in the interest of the government due to pressure from the authorities. Such agency problems can also arise in the form of policy loans or cronyism for political purposes, which would be detrimental to bank performance (Berger, Hasan, and Zhou, 2009; Gul, 2006). Hence, strong ties with the government may mean less focus on shareholder value maximization and lower performance.

On the other hand, Faccio, Masulis, and McConnell (2006) argue that lenders may willingly lend to those politically connected firms, who are more likely to be bailed out

than their non-connected peers when they encounter economic distress. In addition to the lending behavior, it is plausible that politically connected banks may have better access to the source of funding, timely liquidity support from either the central bank, counter parties or other connected banks, and if possible, face less pressure from legislative compliances such as receiving favorable deadline extensions or having easier pass on regulatory scrutiny. A politically connected bank can also utilize the connections to exchange favors to achieve organizational purposes (Gu et al., 2008), and thus improve bank performance. Furthermore, it is important for banks to balance the demands from the government to satisfy other non-economic motives without sacrificing the economic motive. Compared with a bank without political connection, a politically connected bank is more able to detect and interpret relevant political signals, to speak the 'right' diplomatic language, and in response, to take appropriate actions, hence achieving better performance. Based on these arguments, a politically connected bank may also benefit from the government ties.

It is possible that both positive and negative impacts of political connections on bank performance are at work, which requires a robust empirical analysis to determine the net effect. To answer this question, we examine the relationship between bank CEOs' political connections and bank performance and risk over the period of 2007 to 2014, with a focus on the 70 largest commercial banks operating in China. We use the CEO's political connection, defined as having former government working experience, as a measure for the bank's political connection. Due to the unique influence of the CEO in a bank, the CEO's political affiliation provides a suitable proxy for the bank's ties with the government.

We find that banks whose CEOs have former government experiences (our political connection measure) have higher return on assets (*ROA*), lower default risk (log Z-

score), and lower credit risk (the ratio of loan loss provisions to total loans). The results are highly significant, both economically and statistically. For instance, return on assets for banks with politically connected CEOs is 0.148% higher, which indicates a 13.21% increase relative to the sample average *ROA* of 1.12%. Similarly, banks whose CEOs have former government experiences are associated with a 20.97% increase in log Z-score (relative to the sample average log Z-score of 1.86) and a 44.23% decrease in loan loss provision ratio (relative to the sample average loan loss provision ratio of 1.16%).

To identify the causal impact of CEOs' political connections on bank performance, we exploit a quasi-natural experiment of the recent anti-corruption campaign launched by China's current president Xi Jinping since 2013 as an exogenous shock to the political connections between bank CEOs and the government. The unprecedented campaign has immensely cracked down on the unethical political connection network, which used to facilitate corrupt deals between businesses and the government, and led to the convictions of hundreds of thousands of corrupt officials (Economist, 2015; Lee, 2016).[4] Hence, Xi's anti-corruption campaign is plausibly exogenous at the level of Chinese banks, and allows us to establish the causal effect between CEOs' former government experiences and bank performance. To do so, we estimate a difference-in-differences (DID) regression, and the DID estimator compares changes in performance around the launch of the anti-corruption campaign between banks with and without politically connected CEOs. Since the anti-corruption campaign crushed the unethical political network, it is plausible that banks that rely more on their CEO's former government connections would suffer more during the post-anti-corruption period. Our

[4] Lee (2016) reports that more than 200,000 officials and Party members have been indicted for graft, with a 99% rate of conviction since 2013.

results confirm this conjecture, and our findings hold when we use the instrumental variable (IV) approach as an alternative identification method.

The finding that political connections improve bank performance is robust to the following several factors. First, we analyze whether bank ownership structure may affect our findings. We follow Jiang, Liu, and Molyneux (2017) and construct four ownership measures. We then reexamine the effect of CEOs' political connections on bank performance and risk after controlling for these ownership variables. We find that all of the results hold. Second, we analyze whether the main finding reflects that banks with politically connected CEOs can have better access to high-yield assets. To test this possibility, we examine the impact of CEOs' political connections on the ratio of interest income to total loans. The result supports this conjecture. Third, we analyze how a bank's performance reacts after replacing its non-politically connected CEO with a politically connected one. The results further confirm our previous finding that politically connected bank CEOs do improve bank performance.

We perform several additional tests to explore the heterogeneity in CEO characteristics and variations in CEOs' past government experiences on bank performance and risk. First, we expect that the positive association between politically connected CEOs and bank performance would be more pronounced when the city the bank CEO previously worked is the same as the bank's headquarter. Second, it is likely that politically connected CEOs would benefit from their past banking experiences, which strengthen their influence on bank performance. Third, we follow Lin et al. (2016) and use a CEO's entertainment and travel costs (ETC) as a proxy for the CEO's investment in the political connection with bureaucrats. We then examine whether politically connected CEOs with higher ETC spending have a more positive impact on bank performance and risk. Fourth, we expect the influence of CEOs' political

connections on bank performance and risk to be stronger for CEOs with higher previous administrative rankings (e.g., at the provincial or state level). Our findings are consistent with these expectations.

Our results are consistent with the institutional environment of China's banking and political system. It lends support to the argument of Faccio, Masulis, and McConnell (2006) that lenders willingly lend to politically connected firms who, despite being more inefficient and risky, are more likely to receive government bailouts than those non-connected counterparts in the event of financial distress, thus resulting in the higher profitability and lower credit risk for the lender.[5]

We contribute to several strands of the literature. First, this paper broadly relates to the empirical research on the effects of political connections on firm performance. Cao et al. (2009) investigate the monetary and political incentives of government appointed CEOs and find that both are positively related to firm performance. Lin et al. (2011) examine the influence of CEOs' professional background on firms' innovation activities and show that firms' innovation efforts are positively associated with CEOs' political connection. Fan et al. (2007) argue that firms with politically connected CEOs underperform those led by non-connected CEOs due to the government intervention. Our study contributes to this literature by exploring a different mechanism through which politically connected banks may be able to use political influence to compete for lending opportunities for politically connected firms (mostly state-owned), which receive implicit government bailout guarantees.

Second, the paper adds to the literature on China's '*guanxi*' that explores firm executives' personal relationship with the government and its role in explaining firm

[5] Khwaja and Mian (2005) argue an adverse effect for government banks by politically powerful borrowers that threaten bank officers with job transfers or removals, or lure officers with job appointments and promotions. Consequently, the affected lenders would have lower profitability and higher credit risk.

performance. For example, Xin and Pearce (1996) explore the importance of executives' *guanxi* with government officials to the business success of private companies, Park and Luo (2001) study the integrative framework of *guanxi* utilization and examine its impacts on firm growth and internal operation, and Gu et al. (2008) examine *guanxi*'s direct effects on market competence and performance in China. Our work focuses on the banking setting and highlights the value of *guanxi* in helping Chinese bank CEOs with political background to improve bank performance.

Third, our paper is also related to the corporate governance literature on CEO characteristics, which investigates the relation between firm performance and risk-taking, and various mechanisms of CEO characteristics, such as CEO compensation (Brick, Palmon, and Wald, 2006), CEO education (King, Srivastav, and Williams, 2016), CEO power (Adams, Almeida, and Ferreira, 2005; Pathan, 2009; Mollah and Liljeblom, 2016; Onali et al., 2016), and CEO execution (Kaplan, Klebanov, and Sorensen, 2012).

The rest of the paper proceeds as follows. Section 2 provides background information on the Chinese banking system and the role of bank CEOs in China, as well as their *guanxi* with the government. Section 3 describes the data and construction of variables. Section 4 sets out our identification strategies and reports the results. Section 5 presents the mechanisms behind our results. Section 6 concludes.

2. Institutional background and bank political connections in China

The banking system in China, which used to be state-owned and monopolistic, has gone through substantial structural changes in the past decades. The sector has changed from a mono-banking model to a profit-driven and multi-tiered banking system (Lin and Zhang, 2009). Meanwhile, the sector has made huge efforts to transform the

corporate governance mechanism into one similar to the western "Anglo-American System" (Liang et al., 2013). The transformations include ownership diversification, the introduction of a board of directors and a board of supervisors, and more autonomy in the senior management's decision-making process.

The establishment of the China Banking Regulatory Commission (CBRC) in 2003 is the landmark in the series of reforms. The CBRC enforces various laws to standardize operations of bank boards and enhance the efficiency of bank governance. In a process of financial liberalization following the banking reform in 2003, many former regional credit cooperatives have been restructured and consolidated into city commercial banks. Despite new governance mechanisms being put into place during the restructuring process, many CEOs of these newly formed banks were directly appointed by the local government and had former work experiences at various levels of government departments (Martin, 2012). The close political connections between these senior bank officers and the government have serious implications for the performance of the banks, and may even lead to corrupt deals.

The 2016 report on China's financial sector by the Communist Party's Central Commission for Discipline Inspection (CCDI) raised serious concerns on corruption across China's financial industry. According to the report, wasting public money on extravagant meals and overseas travel, taking bribes for handing out loans, and illegally pocketing off-the-book gains were some of the ways corruption had spread in the financial industry. The phenomenon of corruption is rooted in the long-standing political ties between bank executives and the government, who has the power to nominate senior bank executives.

In this context, one crucial nature of the economic system in China is that personal relationships, so-called *guanxi* in Chinese, play an important role in conducting

business.[6] In an environment where the government controls key resources, political connections may hold the key to the prosperity of banks in China. As political rent-seeking activities are prevalent in the Chinese society, politically connected senior executives of banks often utilize personal ties with government officials to secure preferential treatments such as capital injection (Faccio et al., 2006), and easy deposit collections (Nys et al., 2015). The role of the bank chief executive officer (CEO), in particular, is pivotal during this process.

In China, a bank CEO is often called a president (Stent, 2016). The bank president serves as the executive director of the board and is responsible for the overall direction and administration of programs, products, and services provided by the bank, including the bank's financial performance, credit quality, business development, operations, regulatory compliance, and risk management. Therefore, the president, much like bank CEOs in western countries, ensures that all aspects of the bank's activities operate in a safe and sound manner, and is indeed the most powerful position in a bank. Given their paramount roles, in this paper, we use the CEO's political connection as a proxy for bank political connection and aim to reveal insights into its impact on bank performance.

Political connections can have positive and negative effects on businesses. Most studies view the appointment of top executives with former government experiences as a special political resource that helps firms gain competitive advantages such as easier access to capital market (Francis et al., 2009), favorable tax and bank loans

[6] *Guanxi* plays a crucial role in Chinese businesses. As Hope (2014) notes, "having good '*guanxi*' – a wide network of mutually beneficial relationships developed outside the formal work setting, for instance at evening meals or over drinks – is often the secret to securing a business deal." It is culturally deep-rooted and extends into every corner of the Chinese society, including government officials. However, as pointed out by Lin et al. (2016), *guanxi* has, to some extent, become a form of corruption in China in recent years. Business leaders within the political *guanxi* network make unethical reciprocal deals with the government. Government officials favor these companies by wielding their influence over investment approval, regulatory favor, resources allocation, and the like.

(Charumilind et al., 2006; Faccio, 2006; Claessens et al., 2008), and government bailouts (Faccio et al., 2006), which ultimately increases firm value and performance (Fisman, 2001; Johnson and Mitton, 2003; Li et al., 2008; Goldman et al., 2009). Specifically, corporate senior executives in China with former government affiliations can invest in their established personal relationships or connections with bureaucrats in exchange for preferential treatment for their companies (Lin et al., 2016). This phenomenon is particularly prominent in the Chinese banking industry, as banks in China are not fully open to market competition, and top bank managers may have to devote more resources to sustain connections with government officials in order to cope with environmental uncertainty (Park and Luo, 2001). Since bank governance still lacks effectiveness and relationship-based systems dominate in Chinese society, political *guanxi* remains a vital part for bank CEOs in China.

3. Data, sample selection and variables

3.1. Data and sample selection

Our sample is comprised of 70 major domestic banks, including the "big four" state-owned commercial banks, 12 joint-equity banks, and 54 city commercial banks over the period 2007 to 2014.[7] These banks are the 70 largest banks based on total assets at the end of 2014 and account for 88% of the total assets of the Chinese banking sector.[8][9]

[7] The "big four" are the four largest state-owned banks, which dominate China's banking industry and are majorly owned by the government. Joint-equity banks are national-level commercial banks with a mixture of owners, including the state, state-owned enterprises (SOEs), private enterprises, and foreign entities. City commercial banks are municipal level joint-equity banks.

[8] We obtain the total assets of the whole Chinese banking sector from the website of the China Banking Regulatory Commission (CBRC).

[9] There are several takeover transactions happening over our sample period. To mitigate the bias of our results, we treat any bank after the acquisition as a new bank.

We hand-collect bank CEOs' prior professional experiences as well as age, gender, education background, and tenure from their biographies publicized on official websites. Whenever this information is not provided on banks' websites, we use news releases and annual reports of individual banks when available. Lastly, we retrieve bank financial information from the Bankscope database. Our final sample consists of 298 bank-year observations.

3.2. Variables

We define a CEO as having political connection if he or she is an ex-government official. That is, the dummy variable *CEO's political connection* is defined as one if the CEO served in the government before joining the bank.

We use three measures of bank performance: return on assets (*ROA*), logarithm of Z-score (e.g., Boyd and Nicolo, 2005), and loan loss provisions ratio (*LLP*/*loans*). *ROA* is calculated as net income over total assets. Z-score is computed as the ratio of *ROA* plus the capital-asset ratio to the standard deviation of *ROA*.[10] Z-score is commonly used to reflect a bank's probability of insolvency, with a higher value indicating that the bank has lower risks and is more stable. Due to its highly-skewed characteristics, we use the natural logarithm of Z-score in our analysis. *LLP*/*loans* measures the fragility of bank assets, whereby an increase in this ratio indicates an anticipated increase in the non-performing loans (NPLs) in a bank's loan portfolio. This measure is particularly applicable to China's banking sector. Given the large amount of policy loans and the internal control weakness, non-performing loans have been a serious

[10] We use three-year rolling window for estimating the standard deviation of *ROA*. Therefore, the standard deviation of *ROA* is time-varying.

concern for Chinese banks (Lin and Zhang, 2009; Berger et al., 2009). As such, we use *LLP*/*loans* as a performance measure to investigate asset qualities across Chinese banks.

We use two sets of control variables: (1) bank CEOs' characteristics, including a CEO's age, gender, MBA qualification, education, and tenure, and (2) bank financial characteristics, all of which have been shown to have significant influences on bank performance (e.g., see Adams and Ferreira, 2009; King et al, 2016; Lin and Zhang, 2009; Berger et al., 2009; Liang et al., 2013; Mergaerts and Vennet, 2016). One important bank characteristic is size (calculated as *log total assets*). We also include size squared in the regression to capture the non-linear relationship between size and performance. Other financial characteristic variables include bank *Equity to total assets* (capital ratio), *Noninterest income*/*income*, *Cost to income* (managerial efficiency), and *Total loans*/*assets*. Previous research shows that better capitalized banks and banks with more diversified income sources are associated with higher return on assets and greater risk reduction (Chan-Lau et al., 2015; Berger and Bouwman, 2013; Demirgüç-Kunt and Huizinga, 2010). Additionally, bank cost to income ratio, perceived as managerial efficiency, indicates a bank's running costs and is supposed to be negatively correlated with bank performance (Goddard et al., 2010). Following Lin and Zhang (2009), we further use loan-to-asset ratio to control for loan portfolio orientation.

3.3. Summary statistics

We present summary statistics for all the variables in Panel A of Table 1.[11] The mean value of *CEO's political connection* indicates that 37.9% of the observations on bank CEOs have former government experiences. Most of the CEOs in the Chinese banking sector are male, and in over one quarter of the bank-year observations, the

[11] Table A1 in the appendix gives variable definitions.

CEOs do not have a bachelor's degree. Most of the CEOs are also newly appointed, with fewer than one quarter of the observations showing that the CEOs have been in their current bank for more than four years.

Panel B of Table 1 shows the characteristics of banks with politically connected CEOs and banks with non-connected CEOs. As shown in the table, banks with politically connected CEOs have significantly higher return on assets (*ROA*) and lower default risk (higher log Z-score) and credit risk (as proxied by *LLP*/*loans*). In terms of CEO characteristics, politically connected bank CEOs are more likely to be male, older, holders of an MBA degree, have higher education background and longer tenure. We also find that banks with politically connected CEOs are larger in asset size, which corresponds to the common observation that larger banks in China are more likely to have close ties with the government and have senior executives from the government.

Panel C of Table 1 reports the mean values of CEOs' characteristics each year in the sample. The percentage of politically connected CEOs exhibits swings over the sample period. Noticeably, however, starting from 2013, when the anti-corruption campaign began, the percentage of CEOs with former government experiences diminishes markedly.

[Insert Table 1 here]

Table A2 presents the correlations among the explanatory variables we use for the analyses and shows that most of the variables have modest correlations with each other.

4. Results

4.1. The effect of CEOs' political connections on bank performance

We begin our analysis by examining the effect of CEOs' former government experiences (i.e., political connections) on bank performance. Specifically, our baseline regression model is as follows:

$$\begin{aligned} Bank\ Performance_{i,t} = {} & \alpha + \beta * CEO's\ Political\ Connection \\ & + \gamma * CEO's\ Controls_{i,t} + \delta * Bank\ Controls_{i,t-1} \\ & + Bank\ Fixed\ Effects + Year\ Fixed\ Effects + \varepsilon_{i,t} \end{aligned} \quad (1)$$

where *i* denotes the bank, *t* denotes the year, the indicator variable *CEO's Political Connection* equals one if the CEO has former government experiences and zero otherwise, and $CEO's\ Controls_{i,t}$, $Bank\ Controls_{i,t-1}$ are a group of control variables representing CEOs' characteristics and lagged bank financial characteristics that include *Age*, *Gender*, *MBA*, *Education*, *Tenure*, *Log total assets*, *Log total assets square*, *Equity to total assets*, *Non-interest income*/*income*, *Cost to income*, and *Total loans*/*assets*. We control for bank and year fixed effects to eliminate unobserved time-invariant and bank-invariant effects. The coefficient of interest is β. Throughout this paper, we cluster standard errors at the bank level to account for heteroscedasticity and serial correlation of error term.

The results reported in Table 2 indicate that a bank with a CEO who has former government experiences has higher profitability, lower probability of insolvency, and lower fragility of loans. The coefficient estimates indicate that the economic impact of CEOs' former government experiences on bank performance is economically large. For instance, the point estimate for *CEO's Political Connection* dummy on *ROA* implies that return on assets for banks with politically connected CEOs is 0.148% higher, which indicates a 13.21% increase relative to the sample average *ROA* of 1.12%. Similarly, for the other two performance measures, banks with CEOs having former government experiences are associated with a 20.97% increase in log Z-score (relative

to the sample average log Z-score of 1.86) and a 44.23% decrease in loan loss provision ratio (relative to the sample average loan loss provision ratio of 1.16%).

We also find that banks with CEOs that have higher education levels are associated with better operating performance and lower risk, while banks with longtime CEOs fare worse. The significant coefficients on *Equity to total assets* and *Cost to income* indicate that better capitalized banks, and banks with higher managerial efficiency, are associated with higher return on assets and more risk reduction, which is consistent with our predictions. Note that the coefficient on *log total assets square* in column (3) is positive and significant, indicating a convex relationship between bank size and loan loss provisions. This confirms the previous literature that larger banks tend to have better risk management, while whopping banks enjoy "too big to fail" benefits and are more risk-taking, thereby incurring more non-performing loans (Laeven et al., 2016; Minton et al., 2014). It also reflects the conditions of the largest Chinese banks, who are mainly controlled by the government, and suffer more from the problem of NPLs due to more policy intervention.

[Insert Table 2 here]

4.2. The effect of CEOs' political connections on bank performance under the anti-corruption shock

One concern on our baseline analysis is that the appointment of politically connected CEOs is endogenous to bank performance and risk. The government, if having controlling ownership, may directly appoint their preferred CEO to that bank. A well performing bank may also have incentives to build up strong relationships with the government and hence, is more inclined to hire a former government officer as its CEO.

We are also concerned about the confounding factors that may affect CEO appointment and bank performance simultaneously. To address these issues, we employ several identification strategies.

We first use the natural experiment of the anti-corruption campaign that has exogenously affected the political connections between firm CEOs and the government. The advantage of this approach is that this policy event creates a shock to bank CEOs' political connections that is orthogonal to alternative factors that may drive the positive relationship between bank political connections and performance.[12] We begin with some background about the anti-corruption efforts and then compare the performance changes of politically connected banks versus non-connected counterparts around the campaign launch.

China's political corruption has long been a thorny issue since the economic reforms in the 1980s. The types of corruption usually involve extravagant bribes in exchange for political favor, such as firms trying to secure profitable investments (Svensson, 2005). The network of political connections, at this point, often plays an active role and facilitates corrupt deals between the business and the government (Fan, 2002). As corruption was becoming a canker, an unprecedented anti-corruption campaign was launched shortly after China's current president, Xi Jinping, came to power at the end of 2012. Several potent measures, including the announcement of the Eight-point Regulation and the initiation of sending inspection teams nationwide, were immediately taken to intensify the anti-graft efforts.[13] Since then hundreds of thousands of officials have been convicted of corruption, including some top-level government officials and

[12] One may argue that it is the government stake in banks that makes these banks favored. As the background detailed in Section 4.2, the quasi-natural experiment from the anti-corruption campaign excludes such possibility and many other alternatives that could affect bank performance.

[13] For "Eight-point Regulation", see http://cpcchina.chinadaily.com.cn/2012-12/05/content_15991171.htm. For "inspection teams", see https://en.wikipedia.org/wiki/Central_Leading_Group_for_Inspection_Work.

senior executives at state-owned enterprises (SOEs). The banking sector is also not exempt from the campaign. For example, the former CEO of China Minsheng Banking Corp, Xiaofeng Mao, was investigated for bribery in early 2015. His political connection with former top official Ling Jihua was believed to be the main reason for the detainment (Flannery, 2015).

The unexampled campaign against corruption has led to much anxiety among businessmen with close ties to government officials (Economist, 2015). Previously, corporate senior managers who invested in official connections could grease the wheels of the government and enable their firms to "get things done" (Lin et al., 2016). However, the anti-corruption campaign has halted this kind of unscrupulous utilization of political connections. Fearful of being indicted for corruption, government officials and businessmen are reluctant to make reciprocal deals.

The announcement of the Eight-point Regulation in December 2012 marked the beginning of the anti-corruption campaign. We therefore define the post-policy period as 2013 and the years afterwards. Since market competition is still weak in the Chinese banking industry, banks, relative to other non-banking firms, are more susceptible to political influence due to the environmental uncertainty. As such, we conjecture that the campaign severely sways the roles of bank CEOs with former government experiences and affects the performance of these politically connected banks thereafter.

We run the following difference-in-differences (DID) regression over the full sample period to examine our hypothesis:

$$\begin{aligned} Bank\ Performance_{i,t} = {} & \alpha + \beta_1 * CEO's\ Political\ Connection \\ & + \beta_2 * Anti\text{-}corruption\ Campaign \\ & + \beta_3 * CEO's\ Political\ Connection * Anti\text{-}corruption\ Campaign \\ & + \gamma * CEO's\ Controls_{i,t} + \delta * Bank\ Controls_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (2)$$

where the dummy variable *Anti-corruption Campaign* is defined as one for the time period after 2013 (including 2013). The coefficient of interest is β_3, which captures the extent to which the performance of banks whose CEOs are former government officials is more affected than that of banks whose CEOs are not, following the launch of the anti-corruption campaign. We thus expect β_3 to be negative and significant if the dependent variables are *ROA* and log Z-score, and to be positive and significant if the dependent variable is *LLP*/*loans*.

Table 3 reports the results. In columns (1) through (3), we test the effect of CEOs' former government experiences on bank performance under the anti-corruption shock without using fixed effects, while in columns (4) through (6) we repeat the regression after including bank and year fixed effects to control for unobserved heterogeneity across banks and years. The dummy variable *Anti-corruption Campaign* is dropped from the regression because of the inclusion of year fixed effects. As shown in the table, the coefficient on the interaction term β_3 is negative and significant when the dependent variables are *ROA* and log Z-score, and is positive and significant when using *LLP*/*loans* as another measure of bank performance. These findings indicate that the anti-corruption shock is associated with lower levels of bank performance for politically connected bank CEOs relative to their non-connected counterparts, which supports our argument.

[Insert Table 3 here]

Overall, by exploiting the anti-corruption shock in China as a natural experiment, we use the DID estimation to confirm the causal relationship of Chinese bank CEOs' former government experiences on bank performance. Since the anti-corruption campaign crushed the unethical political network, banks with politically connected

CEOs experience significant performance deterioration during the post-anti-corruption period.

4.3. Placebo tests

A possible concern with our results in Table 3 is that we use a single event, namely, the anti-corruption campaign, as an exogenous shock to identify the impact of CEOs' former government experiences on bank performance. If there are differential trends across banks in performance before the anti-corruption campaign, we may incorrectly attribute these trends to the anti-corruption shock. To investigate whether our results are driven by differential trends prior to the anti-corruption shock, we conduct placebo (falsification) tests. We replicate specification (2), but shift the start of the post-policy period to 2012 (one year ahead).

Table 4 shows that there is no evidence of pre-existing differential trends in performance between banks with politically connected CEOs and those with non-connected CEOs for the placebo shock year, as shown by the insignificant coefficients on the interaction term. Therefore, by examining the period that is not accompanied by the anti-corruption shock, we alleviate the concern that unobserved variations other than the anti-corruption campaign trigger sharp contrasts in the post-policy period between banks whose CEOs have former government experiences and those whose CEOs do not.

[Insert Table 4 here]

4.4. Instrumental variable regressions

We next use an alternative instrumental variable (IV) approach to further enrich our identification for the causal effect of CEOs' political connections on bank performance. Specifically, we need an instrumental variable that is correlated with *CEO's Political Connection*, but does not directly affect the dependent variable *Bank Performance* in equation (1). Thus, we construct such an instrument in the following way. For each bank in each year, we focus on the proportion of CEOs with former government experiences among all other banks (i.e., excluding the bank itself) in the size decile to which the bank itself belongs in that year. We refer to this variable as *proportion of politically connected CEOs in comparable banks*. We use it as an instrument for the bank's *CEO's Political Connection*.

Note that we depend on commonalities in size while defining our instrumental variable. The motivation for this comes from the wisdom that banks of a similar size share common behaviors (Sapienza, 2004). Thus, the characteristics of a bank CEO are correlated with those of CEOs in peer banks that are comparable in size. The instrument also meets the exclusion restriction because CEOs in other banks cannot plausibly have direct influence on the examined bank.

Table 5 reports the IV results using two-stage least squares (2SLS). For brevity, we do not report the coefficients on the control variables.[14] We find strong explanatory power from the instrument for the endogenous variable *CEO's Political Connection* with the highly significant coefficient on the instrument in the first-stage regressions. Moreover, the *F*-statistic in the first regression is above 30, which suggests that the instrument is powerful and unlikely to be biased towards the OLS estimates based on the cut-off threshold of Staiger and Stock (1997).[15]

[Insert Table 5 here]

[14] The omitted coefficients on the control variables are available upon request.
[15] If there is one endogenous variable, the minimum value of the first-stage *F*-statistic, which Staiger and Stock (1997) suggest should be greater than 10.

The results of the IV regressions are qualitatively similar to our baseline results. The findings confirm the argument that politically connected CEOs can lift profitability and lower default and credit risk in Chinese banks. As described in Section 4.1, the OLS results in Table 2 may suffer from the inherent selection bias associated with the decision to appoint a CEO. The IV approach as well as the above DID regression address this concern and provide further robustness evidence.

4.5. Robustness checks

We perform several robustness checks for our main findings. To streamline the presentation, we report only the key variables of interests. Table 6 reports the results of these tests.

First, we analyze whether various ownership types of banks may affect our findings. This is because some studies show that the impact of political connections may depend on a firm's ownership structure (e.g., Wu, Wu, and Rui, 2012). To this end, we adopt the hand-collected ownership data of Chinese banks from Jiang, Liu, and Molyneux (2017), and follow their method to define the measures reflecting ownership types. Specifically, we classify banks into four mutually exclusive groups based on ownership types: *State owned*, *Private*, *Foreign*, and *Widely-held*.[16] Importantly, our ownership measures allow for changes in a bank's ownership type since a bank's top ten owners and their stakes may vary over time. We then incorporate these ownership variables into our baseline model (1), in which the variable item *Bank Control* contains the set of control variables defined earlier. Columns (1) to (3) in Table 6 report the results, and show that the inclusion of bank ownership types does not change the pattern of results

[16] Detailed definitions of ownership variables are given in Table A1 in the appendix.

reported in Table 2. We also find that state owned banks are associated with higher *ROA* and lower Log Z-score, indicating higher bank performance and higher risk.

[Insert Table 6 here]

Second, we consider whether the positive association between political connections and bank performance is because banks with politically connected CEOs can do "cream-skimming", i.e., they have better access to high-yield assets and get more (implicit) public guarantees. This consideration reflects our hypothesis that banks with better political connections are more able to secure lending to politically connected firms. In general, these lending deals are high-yield loans and are more likely to be repaid by the government in the event of a default. To test this possibility, we examine the impact of CEOs' political connections on the ratio of interest income to total loans. If politically connected banks stand a better position to lend to politically connected borrowers, we would expect a positive relationship between CEOs' political connections and this ratio. Column (4) in Table 6 reports the results. The positive and significant coefficient on *CEO's political connection* shows that politically connected banks have higher interest income ratios over total loans compared with non-connected counterparts. The finding supports our conjecture that these banks have better access to high-yield assets.

Third, we consider how a bank's performance reacts after replacing its non-politically connected CEO with a politically connected one. We define a dummy variable *CEO replacement* as one after the bank experienced a CEO turnover where its non-politically connected CEO was replaced by a politically connected one. We then examine the effect of *CEO replacement* on different performance measures.[17] The coefficient on *CEO replacement* dummy essentially captures the differential effects of

[17] We only select those banks without any politically connected CEOs within our sample period as the control group.

non-politically connected CEO turnover on bank performance and risk. In order to avoid the adverse impact of the anti-corruption campaign starting from 2013 on politically connected CEOs, we restrict the sample period to between 2007 and 2012. The results are reported in columns (5) to (7) in Table 6. The significant coefficients on *CEO replacement* indicate that banks, after replacing their CEOs without political connections by those with such connections, have an increase in return on assets (*ROA*) and log Z-score, and a decrease in loan loss provision ratio, relative to those banks without such a replacement. These results further confirm our previous findings that politically connected bank CEOs do improve bank performance.

5. Bank CEOs' characteristics and political connections

The results thus far suggest that CEOs' political connections have a positive effect on bank performance. To better understand the mechanisms behind our results, we further explore the heterogeneity in CEO characteristics and examine variations in the CEOs' former government experiences on bank performance.

First, if a CEO, before joining their current bank, worked in a city the same as where the bank's headquarter locates, he or she may have already established a dense network of interpersonal obligations in that city. This geographical advantage should enable the CEO to divert personal connection more efficiently into the current bank following the appointment. Therefore, we expect that the political impact will be much stronger for CEOs from the same city of the headquarters of the current bank.

To examine the local political connection effect, we define the dummy variable *Local Experience* as one if the CEO worked in the same city immediately before being appointed by their current bank. Note that our definition does not require that *Local Experience* is one only if the CEO is from local government. For example, *Local*

Experience is also equal to one if the CEO worked for a technology company right before joining the current bank within the same city. We include this dummy variable into our regression and estimate the following specification:

$$\begin{aligned} Bank\ Performance_{i,t} = {} & \alpha + \beta_1 * CEO's\ Political\ Connection \\ & + \beta_2 * CEO's\ Political\ Connection * CEO\ Characteristics \\ & + \beta_3 * CEO\ Characteristics \\ & + \gamma * CEO's\ Controls_{i,t} + \delta * Bank\ Controls_{i,t-1} \\ & + Bank\ Fixed\ Effects + Year\ Fixed\ Effects + \varepsilon_{i,t} \end{aligned}$$

(3)

where we replace the general term *CEO Characteristics* by the variable *Local Experience*. The results are reported in columns (1) through (3) in Table 7. We find that the coefficient on the interaction term *CEO's Political Connection * Local Experience* is positive and significant for both dependent variables *ROA* and log Z-score, and is negatively significant for the dependent variable *LLP*/*loans*. These findings show that the positive impact of political connections on bank performance is intensified for CEOs who worked in the local city, a result that is consistent with our prediction.

[Insert Table 7 here]

Second, previous literature shows that a CEO who has previously worked in the relevant industry can exploit their experience to introduce strategic changes, improve governance efficiency, and thus maximize firm performance (Greiner and Bhambri, 1989; Acharya et al., 2011). Thus, we expect that prior banking experiences can help politically connected CEOs further strengthen their positive impact.

To evaluate this conjecture, we re-estimate the regression model in equation (3) by using another CEO characteristic *Banking Experience*, which is an indicator variable defined as one if the CEO has previously worked for banks. The results are presented in columns (4) through (6) in Table 7. As indicated by the significant coefficients on the

interaction term, the positive impact of political connections on bank performance is stronger for CEOs who also used to work for banks. Our findings are consistent with the development in the banking industry that privatization and enhanced market competition resulting from the recent banking reforms in China have deepened the need for managerial expertise. As such, the banking experiences of senior management become increasingly important for these more market-oriented banks.

Third, different bank CEOs may invest differently in their connections with the government to sustain political influence. Lin et al. (2016) use firm executives' entertainment and travel costs (ETCs) as a proxy for firms' investment in political connections. They argue that higher ETCs are associated with stronger political connections, which can be utilized by firms to "get things done". We therefore expect that the positive association between CEOs' political connections and bank performance is more pronounced for CEOs with high ETC spending.

In this vein, we use bank CEOs' ETCs from the WIND database and define the dummy variable *High ETC Bank* as one if the CEO's ETC is in the top quartile among all listed banks at the end of 2012. As the ETC data are only available for listed companies, we use the subsample of listed banks to re-estimate model (3) and replace *Banking Experience* with *High ETC Bank*.

As shown in columns (7) through (9) in Table 7, the significant coefficients on the interaction term suggest that the high spending on ETC is associated with a more positive impact on bank performance for CEOs with former government experiences. The result is in line with our expectation that, with more resources devoted to sustaining connections with the government, politically connected banks may be better able to overcome institutional barriers and instability in the face of market uncertainty.

Fourth, politically connected CEOs may have different previous administrative hierarchies. Francis, Hasan, and Sun (2009) argue that firms with high-ranking ex-government officials on their boards could be characterized by stronger political connections. We thus expect the impact of CEOs' political connections on bank performance to be stronger for CEOs with higher previous administrative rankings (e.g., at the provincial or state level). Specifically, we use the dummy variable *High Administrative Ranking* to distinguish between CEOs who are from government departments above the city level and those from the government at or below the city level. We then examine the effect of *High Administrative Ranking* on bank performance. Our results are shown in columns (10) through (12) in Table 7. The finding confirms our prediction.

6. Conclusion

In this paper, we examine the relation between banks' political connections and the performance and risk using a sample of the top 70 banks from 2007 to 2014. We use hand-collected information on CEOs' professional background to identify their political affiliations. We then analyze their effects on bank performance in China after controlling for other CEO and bank characteristics, and we find that banks led by politically connected CEOs outperform their non-connected counterparts.

We employ several identification strategies to pin down the causal effect of CEOs' political connections to address inherent selection biases associated with the decision to appoint a CEO. We first use Xi's anti-corruption campaign as an exogenous shock to the political connections between CEOs and the government. By using a difference-in-differences framework, we find that banks whose CEOs have former government experience undergo significant performance deterioration during the post-anti-

corruption period. We also use another IV approach to confirm the causal interpretation of the positive effect of CEOs' political connections on bank performance. Our findings are not driven by the confounding factors that affect bank performance and CEO appointment simultaneously.

We also document that CEOs' political connections affect bank performance through a series of mechanisms that are related to the heterogeneity in CEOs' characteristics and former government experiences. These results suggest that politically connected banks have better access to lending to politically connected firms, which are high yield assets and more likely to be bailed out when in distress. Our results offer a mechanism of political rent seeking consistent with the institutional environment of China's banking and political system.

Appendix

Table A1
Definition of Variables

Variable Name	Definition
Bank Performance	
ROA%	The ratio of net income to total assets
Log Z-score	The natural logarithm of Z-score. Z-score is an accounting-based bank-level indicator of financial stability. It is measured by the sum of ROA and equity ratio over the standard deviation of ROA. Standard deviation of ROA is calculated on a three-year rolling window basis. A high Z-score indicates a high level of stability
LLP/total loans%	The ratio of loan loss provisions to total loans
CEOs' Characteristics	
CEO's political connection	A dummy variable equal to one if the CEO served in the government before joining the current bank
Age	The age of the CEO
Gender	A dummy variable equal to one if the CEO is male
MBA	A dummy variable equal to one if the CEO holds an MBA
Education	A discrete variable that ranges from zero to three. This variable is equal to one if the CEO has acquired a Bachelor's qualification, equal to two if the CEO has acquired a Master's qualification; equal to three if the CEO has acquired a doctoral qualification; and 0 otherwise
Tenure	A discrete variable that records the number of years that the CEO has worked in the current bank
CEO replacement	A dummy variable equal to one after a bank replaced its non-politically connected CEO with a connected one, and zero otherwise
Local Experience	A dummy variable equal to one if the CEO's previous work experience was in the same city
Banking Experience	A dummy variable equal to one if the CEO has worked in the banking industry
High ETC Banks	A dummy variable equal to one if the CEO's personal entertainment and travel costs are in the top quarter among all listed banks
High Administrative Ranking	A dummy variable equal to one if the CEO's previous administrative hierarchy is above the city level
Bank Financial Characteristics	
Total assets	The total assets of each bank
Log total assets	The natural logarithm of total assets
Equity to total assets%	The ratio of total equity to total assets
Noninterest income/income%	The ratio of noninterest income to total operating income
Cost to income%	The ratio of total cost to total income
Total Loans/assets%	The ratio of total loans to total assets
Interest income/total loans%	The ratio of interest income to total loans

(*Continued*)

Table A1
Continued

Variable Name	Definition
Bank Ownership Variables	
State owned	A dummy variable equal to one if a bank satisfies both of the following criteria: (1) the sum of the stock of the top ten largest stockholders (CR10) is greater than 50%; and (2) state owners collectively are the largest stockholder group with at least 25% of total outstanding shares
Private	A dummy variable equal to one if a bank satisfies both of the following criteria: (1) CR10 is greater than 50%; and (2) private owners collectively are the largest stockholder group with at least 25% of total outstanding shares
Foreign	A dummy variable equal to one if a bank satisfies both of the following criteria: (1) CR10 is greater than 50%; and (2) foreign owners collectively are the largest stockholder group with at least 25% of total outstanding shares
Widely-held	A dummy variable equal to one if a bank belongs to none of the above groups

Table A2
Correlation Matrix
This table reports the correlation matrix. * denotes the 5% significance level. All variables are defined in Table A1 in the Appendix.

	CEO's political connection	Age	Gender	MBA	Education	Tenure	Log total assets	Equity to total asset%	Noninterest income/income%	Cost to income%	Total loans/assets%
CEO's political connection	1										
Age	0.1096*	1									
Gender	0.2691*	-0.1922*	1								
MBA	0.1290*	0.0472*	0.0522*	1							
Education	0.3886*	-0.3369*	0.3497*	-0.1055	1						
Tenure	0.1408*	0.0756*	-0.0217	-0.0515*	-0.0322	1					
Log total assets	0.2329*	0.1076*	0.2352*	-0.0855*	0.4625*	-0.0917*	1				
Equity to total assets%	0.0262	0.0038	-0.1846*	0.0795*	-0.1462*	-0.1196*	-0.3035*	1			
Noninterest income/income%	0.0487*	0.0233	-0.0650*	-0.1034*	0.0973*	-0.0378	0.0408*	0.2581*	1		
Cost to income%	-0.0466*	-0.1056*	0.1093*	0.0596*	0.0548*	0.1219*	-0.0394*	-0.1316*	0.1208*	1	
Total loans/assets%	0.0891*	-0.0082	-0.1239*	0.1035*	-0.0628*	0.2200*	-0.1376*	0.0054	-0.1169*	-0.0710*	1

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Table 1
Summary Statistics

Panel A reports the summary statistics for the sample of Chinese banks in the period of 2007-2014. Panel B compares banks that have politically connected CEOs with banks that have non-connected CEOs. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively. Panel C reports a year-wise distribution of the mean values of CEOs' characteristics. All variables are defined in Table A1 in the Appendix.

Panel A

Variable	N	Mean	Standard Deviation	Min	p25	Median	p75	Max
Bank Performance								
ROA%	298	1.123	0.440	-0.970	0.900	1.130	1.400	2.580
Log Z-score	298	1.855	1.040	-1.470	1.223	1.865	2.600	4.497
LLP/loans%	298	1.162	2.728	0.000	0.300	0.750	1.160	38.220
CEOs' Characteristics								
CEO's political connection	298	0.379	0.486	0.000	0.000	0.000	1.000	1.000
Age	298	51.852	4.595	37.000	49.000	53.000	55.000	64.000
Gender	298	0.789	0.409	0.000	1.000	1.000	1.000	1.000
MBA	298	0.010	0.100	0.000	0.000	0.000	0.000	1.000
Education	298	0.762	0.730	0.000	0.000	1.000	1.000	3.000
Tenure	298	2.909	1.783	1.000	1.000	2.000	4.000	7.000
Bank Financial Characteristics								
Total assets (CNY billion)	298	855.894	10422.050	0.010	0.061	0.123	0.325	20151.032
Log total assets	298	12.120	1.736	9.762	11.020	11.719	12.692	19.431
Equity to total assets%	298	6.770	2.034	2.200	5.440	6.510	7.870	14.180
Noninterest income/income%	298	8.041	6.529	-1.692	3.383	6.026	10.966	29.518
Cost to income%	298	60.459	10.903	0.000	56.061	61.611	66.856	77.561
Total Loans/assets%	298	47.223	10.328	21.691	40.588	48.769	55.638	64.277

Panel B: Comparison of banks with politically connected CEOs and banks without

	CEO's political connection = 1		CEO's political connection = 0		Difference
	N	Mean	*N*	Mean	
Bank Performance					
ROA%	111	1.192	187	1.018	0.174***
Log Z-score	111	1.982	187	1.636	0.122***
LLP/loans%	111	0.972	187	1.322	-0.336**
CEOs' Characteristics					
Age	111	52.496	187	51.497	0.998*
Gender	111	0.929	187	0.706	0.223***
MBA	111	0.027	187	0.000	0.026**
Education	111	1.124	187	0.535	0.589***
Tenure	111	3.239	187	2.690	0.549***
Bank Financial Characteristics					
Total assets	111	1270.211	187	1.073	1270.234*
Log total assets	111	12.636	187	11.804	0.832***
Equity to total assets%	111	6.838	187	6.739	0.099
Noninterest income/income%	111	8.447	187	7.739	0.708
Cost to income%	111	59.809	187	60.801	-0.992
Total Loans/assets%	111	48.399	187	46.316	2.083

Panel C

		Mean value of CEOs' characteristics					
Year	Number of CEOs	CEO's political connection	Age	Gender	MBA	Education	Tenure
2007	9	0.286	51.714	0.857	0.000	0.571	2.714
2008	18	0.333	52.333	0.750	0.000	0.667	2.250
2009	21	0.429	52.143	0.714	0.000	0.714	2.238
2010	38	0.342	51.711	0.763	0.000	0.658	2.184
2011	47	0.362	51.319	0.787	0.000	0.745	2.702
2012	55	0.400	51.691	0.818	0.018	0.818	3.018
2013	58	0.362	52.155	0.793	0.017	0.810	3.345
2014	52	0.349	52.651	0.721	0.023	0.721	3.674

Table 2

The effect of CEOs' political connections: Baseline results

This table reports the OLS results of the impact of bank CEOs' political connections on bank performance and risk for Chinese banks in the sample period of 2007-2014. All variables are defined in Table A1 in the Appendix. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

Dependent Variable	ROA%	Log Z-score	LLP/loans%
	(1)	(2)	(3)
CEO's political connection	0.148**	0.389*	-0.514**
	(2.15)	(1.97)	(-2.11)
Age	0.013	0.027	-0.079**
	(1.08)	(0.63)	(-2.66)
Gender	0.251**	1.449***	-0.023
	(2.10)	(3.46)	(-0.06)
MBA	-0.241**	0.179	1.220***
	(-2.54)	(0.42)	(6.46)
Education	0.201***	0.470***	-0.049
	(8.22)	(4.32)	(-0.53)
Tenure	-0.014**	-0.077***	0.024
	(-2.44)	(-2.75)	(0.54)
Log total assets	0.199*	0.863	1.188
	(1.88)	(1.61)	(1.19)
Log total asset square	0.023	0.005	0.015**
	(1.60)	(0.27)	(2.35)
Equity to total assets%	0.010***	0.199***	-0.104***
	(2.60)	(2.77)	(-3.28)
Noninterest income/income%	0.000	0.000**	-0.005
	(0.22)	(2.62)	(-0.56)
Cost to income%	-0.027***	-0.088***	0.028**
	(-5.43)	(-5.29)	(2.60)
Total loans/assets%	-0.010*	-0.037*	0.036
	(-1.73)	(-1.71)	(1.58)
Constant	-0.407	2.908	-5.956
	(-0.27)	(0.37)	(-0.98)
Bank Fixed Effects	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes
N	298	298	298
adj. R-sq	0.3969	0.3597	0.2080

Table 3
The effect of CEOs' political connections: The Anti-Corruption Campaign as a natural experiment of political connection

This table reports the difference-in-differences (DID) regression results of banks' performance and risk on bank CEOs' political connections for Chinese banks in the sample period of 2007-2014. *Anti-corruption Campaign* is a dummy variable, which equals one if the year is later than 2012. All other variables are defined in Table A1 in the Appendix. Columns (1) to (3) show the results of the effect of bank CEOs' political connections on bank performance around the anti-corruption campaign using the standard DID regression. Columns (4) to (6) show the DID results after controlling for bank and year fixed effects. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

Dependent Variable	ROA%	Log Z-score	LLP/loans%	ROA%	Log Z-score	LLP/loans%
	(1)	(2)	(3)	(4)	(5)	(6)
CEO's political connection	0.146	0.644**	-0.303*	0.086***	0.088**	-0.553**
	(1.33)	(2.59)	(-1.94)	(2.92)	(2.49)	(-2.27)
CEO's political connection* Anti-Corruption Campaign	-0.256**	-0.669***	0.561***	-0.229**	-0.645*	0.409**
	(-2.28)	(-2.71)	(3.27)	(-2.02)	(-1.88)	(2.00)
Anti-Corruption Campaign	0.133*	0.268	-0.161			
	(1.76)	(1.35)	(-0.80)			
Age	0.013*	-0.015	-0.020	-0.010	0.065	-0.075***
	(1.83)	(-0.92)	(-1.40)	(-0.15)	(0.25)	(-2.68)
Gender	-0.101	-0.341***	-0.480***	0.007	-0.015	-0.047
	(-1.61)	(-2.93)	(-2.97)	(1.15)	(-0.92)	(-0.13)
MBA	-0.847**	-0.884***	2.010***	-0.148**	-0.320***	0.893***
	(-2.46)	(-4.23)	(6.99)	(-2.34)	(-2.66)	(2.83)
Education	0.145***	0.144**	0.158	0.763**	2.027***	-0.110
	(2.84)	(2.61)	(1.07)	(2.23)	(4.48)	(-1.32)
Tenure	-0.035**	-0.086***	0.038	-0.134**	-0.141**	0.009
	(-2.03)	(-2.94)	(1.00)	(-2.25)	(-2.39)	(0.20)
Log total assets	-0.309	0.444	0.052	-0.038**	-0.088***	1.462
	(-1.62)	(1.36)	(0.16)	(-2.17)	(-3.07)	(1.39)
Log total asset square	0.009	-0.012	-0.003	-0.202	0.384	-0.027
	(1.34)	(-1.10)	(-0.32)	(-1.12)	(1.25)	(-0.60)
Equity to total assets%	-0.002	0.037	-0.047	0.006*	-0.010	-0.110***
	(-0.09)	(0.96)	(-1.25)	(1.86)	(-0.97)	(-3.36)
Noninterest income/income%	0.003	0.001	0.000	-0.000	0.032	-0.004
	(0.77)	(0.05)	(0.03)	(-0.02)	(0.85)	(-0.43)
Cost to income%	-0.003	-0.034***	0.020***	0.003	0.000	0.030***
	(-0.64)	(-4.44)	(3.28)	(0.81)	(0.02)	(2.80)
Total loans/assets%	-0.001	-0.009	0.016***	-0.005	-0.033***	0.033
	(-0.46)	(-1.53)	(2.60)	(-0.85)	(-4.35)	(1.47)
Constant	-0.010	12.386**	4.017*	-0.002	-0.009	-4.005
	(-0.01)	(2.20)	(1.77)	(-0.90)	(-1.47)	(-0.18)
Bank Fixed Effects	No	No	No	Yes	Yes	Yes
Year Fixed Effects	No	No	No	Yes	Yes	Yes
N	298	298	298	298	298	298
adj. R-sq	0.5178	0.3856	0.2011	0.5101	0.1658	0.4112

Table 4

The effect of CEOs' political connections: Placebo test for Anti-Corruption Campaign

This table reports the difference-in-differences regression results of banks' performance and risk on bank CEOs' political connections for Chinese banks in the sample period of 2007-2014. Columns (1) to (3) show the results of the effect of bank CEOs' political connections on bank performance around one year before the anti-corruption campaign. Columns (4) to (6) show the results after controlling for bank and year fixed effects. All variables are defined in Table A1 in the Appendix. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

Dependent Variable	ROA%	Log Z-score	LLP/loans%	ROA%	Log Z-score	LLP/loans%
	(1)	(2)	(3)	(4)	(5)	(6)
CEO's political connection	0.194***	0.564***	-0.511**	0.235**	0.582***	-0.471**
	(2.66)	(2.96)	(-2.11)	(2.51)	(2.64)	(-2.18)
CEO's political connection* Falsified one year before Anti-Corruption Reforms	0.086	0.296	0.444	0.017	-0.188	0.008
	(0.86)	(1.13)	(1.50)	(0.26)	(-0.83)	(0.05)
Falsified one year before Anti-Corruption Reforms	-0.164*	-0.321	-0.247			
	(-1.66)	(-1.27)	(-1.37)			
Age	0.013**	0.003	-0.022	0.013*	0.001	-0.079**
	(2.07)	(0.19)	(-1.53)	(1.91)	(0.06)	(-2.62)
Gender	-0.081	-0.428***	-0.503***	-0.085	-0.439***	-0.020
	(-1.31)	(-4.15)	(-3.19)	(-1.34)	(-4.09)	(-0.06)
MBA	-0.887**	-2.262***	1.644***	-0.891**	-2.319***	1.214***
	(-2.43)	(-3.79)	(5.20)	(-2.44)	(-3.88)	(5.95)
Education	0.006	0.025	0.121	0.005	0.018	-0.048
	(0.11)	(0.20)	(0.87)	(0.09)	(0.15)	(-0.53)
Tenure	-0.009	-0.145***	0.004	-0.006	-0.138***	0.025
	(-0.57)	(-4.57)	(0.12)	(-0.45)	(-4.43)	(0.54)
Log total assets	-0.338*	0.534	0.055	-0.326*	0.571	1.199
	(-1.67)	(1.40)	(0.17)	(-1.69)	(1.64)	(1.21)
Log total asset square	0.010	-0.018	-0.005	0.010	-0.019	-0.016
	(1.38)	(-1.34)	(-0.46)	(1.41)	(-1.56)	(-0.37)
Equity to total assets%	-0.010	0.021	-0.060*	-0.010	0.022	-0.104***
	(-0.49)	(0.49)	(-1.72)	(-0.48)	(0.54)	(-3.30)
Noninterest income/income%	0.004	0.010	0.000	0.002	0.005	-0.005
	(0.97)	(0.86)	(0.03)	(0.57)	(0.45)	(-0.55)
Cost to income%	-0.004	0.006	0.020***	-0.003	0.011	0.028**
	(-0.73)	(0.75)	(3.11)	(-0.49)	(1.51)	(2.57)
Total loans/assets%	-0.000	-0.001	0.019***	0.000	0.001	0.036
	(-0.07)	(-0.14)	(3.43)	(0.15)	(0.08)	(1.59)
Constant	3.322***	-2.218	4.476*	3.078**	-2.850	-6.452
	(2.66)	(-0.86)	(1.91)	(2.54)	(-1.17)	(-1.09)
Bank Fixed Effects	No	No	No	Yes	Yes	Yes
Year Fixed Effects	No	No	No	Yes	Yes	Yes
N	298	298	298	298	298	298
adj. R-sq	0.1594	0.1861	0.207	0.2427	0.2178	0.4314

Table 5

The effect of CEOs' political connections: Evidence from the instrumental variable

This table reports the 2SLS results of banks' performance and risk on bank CEOs' political connections for Chinese banks in the sample period of 2007-2014. Column (1) shows the first stage results of instrumental variables. Columns (2) to (4) show the second stage regression results for the impact of bank CEOs' political connections on bank performance and risk. All variables are defined in Table A1 in the Appendix. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

	CEO's political connection	ROA%	Log Z-score	LLP/loans %
	(1)	(2)	(3)	(4)
Proportion of politically connected CEOs in comparable banks	0.985***			
	(15.88)			
CEO's political connection		0.151**	0.115**	-0.008***
		(2.25)	(2.60)	(-3.62)
Constant	-0.826***	2.878*	2.487	-14.207
	(-8.31)	(1.75)	(1.06)	(-1.39)
Bank Controls	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes	Yes
F-statistics	35.571			
N	298	298	298	298
adj. R-sq	0.3136	0.5136	0.5195	0.4613

Table 6

Robustness checks

This table reports robustness tests for links between CEOs' political connections and bank performance and risk for Chinese banks by using three different strategies. Columns (1) to (3) show the results after controlling for government ownership. Column (4) examines whether banks with politically connected CEOs have better access to high-yield assets. Columns (5) to (7) investigate how bank performance changes when its non-politically connected CEO is replaced by a politically connected CEO. *CEO replacement* is a dummy variable, which equals one for the time period after the bank changed a non-politically connected CEO to a politically connected one. Please note, we only select those banks without any politically connected CEO within our sample period as the control group. All other variables are defined in Table A1 in the Appendix. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

Dependent Variable	ROA%	Log Z-score	LLP/loans%	Interest income/ total loans%	ROA%	Log Z-score	LLP/loans%
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
CEO's political connection	0.213***	0.354***	-0.538***	0.142**			
	(4.87)	(4.32)	(-3.44)	(2.41)			
CEO replacement					0.191***	0.467***	-0.781***
					(3.94)	(5.22)	(-4.69)
State owned	0.318***	-0.423*	0.289				
	(3.89)	(-1.90)	(1.37)				
Private	-0.157	-0.129	0.681				
	(-1.39)	(-1.63)	(1.23)				
Foreign	-0.035	0.180	0.562				
	(-0.93)	(1.42)	(1.65)				
Widely-held	0.246	0.224	1.384				
	(1.33)	(0.43)	(0.95)				
Bank Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes
N	298	298	298	298	134	134	134
adj. R-sq	0.4524	0.5832	0.4419	0.6235	0.4568	0.4478	0.5437

Table 7

Bank CEOs' characteristics and political connections

This table reports the OLS results of banks' performance on bank CEOs' political connections with different CEOs' characteristics for Chinese banks in the sample period of 2007-2014. *Local Experience* is a dummy variable, which equals one if the CEO's previous work experience was in the same city. *Banking Experience* is a dummy variable, which equals one if the CEO has worked in the banking industry. *High ETC Banks* is a dummy variable, which equals one if the CEO's personal entertainment and travel costs are in the top quarter among all listed banks. *High Administrative Ranking* is a dummy variable, which equals one if the CEO's previous administrative hierarchy is above the city level. Columns (1) to (3) report the results for whether local CEOs have superior performance. Columns (4) to (6) report the results for whether experienced CEOs have superior performance. Columns (7) to (9) report the results for whether high ETC banks have superior performance. Columns (10) to (12) report the results for whether CEOs with previous higher administrative hierarchies in the government have superior performance. *t*-statistics are in parentheses. *, **, and *** denote the 10%, 5%, and 1% significance levels, respectively.

Dependent Variable	ROA%	Log Z-score	LLP/loans%	ROA%	Log Z-score	LLP/loans%	ROA%	Log Z-score	LLP/loans%	ROA%	Log Z-score	LLP/loans%
	Local experience			Banking experience			High ETC banks			High administrative ranking		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
CEO's political connection	0.150***	0.391**	-0.673**	0.532*	0.529**	-0.514**	0.228***	0.543	-0.493*			
	(2.90)	(2.16)	(-2.65)	(1.72)	(2.60)	(-2.11)	(3.05)	(1.17)	(-1.74)			
CEO's political connection *Local Experience	0.244***	0.169***	-0.481**									
	(3.32)	(2.90)	(-2.46)									
CEO's political connection *banking experience				0.158***	0.119**	-0.410**						
				(4.01)	(2.33)	(-2.67)						
CEO's political connection*High ETC banks							0.006***	0.299***	-0.014**			
							(3.00)	(2.68)	(-2.49)			
High Administrative Ranking										0.373***	0.972***	-0.413**
										(2.72)	(2.70)	(-2.07)
Local Experience	0.042*	0.006	-0.311									
	(1.71)	(1.07)	(-0.53)									
Banking Experience				0.529*	0.315***	0.113						
				(1.70)	(2.94)	(0.43)						
High ETC Banks							-0.003	0.219**	0.105			
							(-0.09)	(2.58)	(1.25)			
Bank Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
N	298	298	298	298	298	298	113	113	113	298	298	298
adj. R-sq	0.5141	0.5182	0.5445	0.5101	0.5161	0.0554	0.4953	0.2516	0.5221	0.5198	0.3998	0.3980