

# Empirical Analysis on the Political Connection and the Selection of M&A Strategies

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**Abstract.** This paper analyzes the relationship between political connections and the M&A strategies of corporate. It can also guides companies to choose M&A strategies or to choose a direction to develop political connections. Based on the data of Chinese listed companies that implemented M&A from 2011 to 2014 by using SPSS analysis software as tools and combined with descriptive analysis, correlation analysis and other methods, we can draw conclusions about relationship between political connections and M&A strategies.

## 1. Introduction

As a kind of enterprise resource, political connection can bring many obvious benefits to enterprises when they implement mergers and acquisitions, such as providing preferential financing for enterprises, reducing industry barriers to help enterprises diversify, and enabling enterprises to get government subsidies to survive the crisis caused by mergers and acquisitions. Therefore, the political connection is not only valued by both parties, but also a craze for discussion and research in the academic world.

## 2. Literature Review

Existing research shows that the issue of political connections is a global one. But in the world, the research of political connection has a history of more than 20 years. Whether it is the breadth of research directions or the comprehensiveness of research conclusions, foreign countries are obviously ahead of domestic ones. Referring to many literatures, a considerable number of foreign scholars regard political connections as an important resource, and believe that political connections can bring many benefits to the development of enterprises, that is, the "hand of support" theory. Faccio (2006), Fan (2006), and so on believe that political connections can bring more financing opportunities, provide financing convenience, and enable enterprises to obtain more loans, get lower loan interest rates and longer term loans. At the same time, when Khwaja and Mian (2005) studied Pakistani enterprises, they found that political linkages brought more chances for enterprises to borrow, and enabled enterprises to enjoy general preferential interest rates and obtain special loans from state-owned banks. Faccio (2006) also found that political linkages made it easier for enterprises to get help from the government in their plight. Goldman (2008) analyzed American listed companies and found that government officials would help political affiliated enterprises to obtain more benefits in the period of strong political party power; Faccio (2006) also believed that political affiliation could help enterprises to gain higher market share and enhance corporate value.

Similar to foreign research conclusions, domestic experts and scholars also found that politically related enterprises can get more benefits when financing. For example, Luo Dang-lun and Yu Minggui (2008) found that politically related enterprises get larger loans, lower interest rates and longer loan duration. Wu Wenfeng, Wu Chongfeng (2009) and Tian Lihui (2013) believe that political connections can have a positive impact on the value of private enterprises. Pan Yue and Dai Yiyi (2009) found that political affiliated enterprises were more likely to get government assistance, and more likely to get government protection in case of financial crisis. Chen Yunsen and Zhu Song

(2009) found that increasing the degree of political connection could enhance the investment efficiency of enterprises capital. According to the research results of political connection and M&A, the political connection discovered by Pan Hongbo (2008) helps to improve the M&A performance of enterprises.

Based on the research results of scholars at home and abroad, we can see that the research field of political connection is very broad, and different research samples or research methods will draw different conclusions. However, it can be seen that in the above studies, there are few discussions on the issues of political connections and mergers and acquisitions, and most of them focus on the performance of mergers and acquisitions.

### 3. Research Design

#### 3.1. Research Hypothesis

Based on the literature analysis above, this paper presents the following research hypothesis:

Hypothesis 1: The degree of political relevance of the company is high, and it tends to be unrelated mergers and acquisitions (mixed mergers and acquisitions)

Hypothesis 2: The degree of political relevance of companies is low, and they tend to be related mergers and acquisitions (including horizontal mergers and mergers and acquisitions).

Research hypothesis on the relationship between political connections and M&A performance:

Hypothesis 3: In the non-related M&A events, the degree of political connections is positively correlated with M&A performance

Hypothesis 4: In the related M&A events, the degree of political connections is negatively correlated with M&A performance.

#### 3.2. Variable Design

##### 3.2.1. Political Connection

**Table 1.** Political positions and corresponding scores

Political connection score	Government official position	NPC and CPPCC position
5	National government official	National People's Congress, CPPCC
4	Provincial and ministerial government officials	Provincial People's Congress, CPPCC
3	Department level government officials	Municipal people's congress, CPPCC
2	County level government official	County-level people's congress, CPPCC
1	Township government officials	Township-level people's congress, CPPCC
0	Non-government official	Non-people's congress, non-CPPCC

This paper mainly uses the assignment method to measure the degree of political connections of enterprises. And comprehensive consideration of the depth of political connections and the breadth of political connections, that is, consider the level of corporate executives, politically related positions. The specific operations are as follows: (1) Screen and assign a score to the positions of corporate executives. Corporate executives include the chairman and general manager, each with a score of 2 and 1. (2) Grading government positions. The positions are mainly government officials or NPC deputies, CPPCC members. The same level of deputies and CPPCC members are assigned the same score. Generally speaking, government officials are the actual controllers of political rights, while NPC deputies and CPPCC members are used as a link to connect enterprises and governments. In theory, NPC deputies have greater rights than government rights. Generally speaking, government officials are the actual controllers of political rights, while NPC deputies and

CPPCC members are used as a link to connect enterprises and governments. In theory, NPC deputies have greater rights than government officials' rights. Simplified here, the same level of government officials, NPC deputies and CPPCC members will be assigned the same score. As shown in Table 1 below. (3) Let the political connection be the variable Gov, and  $Gov = \sum(\text{Executive position corresponding score} \times \text{Political position})$ . Gov is the final score of political connection, the higher the score the higher the political connection of the company.

### 3.2.2. M&A Strategy

M&A strategies are divided into related M&A and non-related M&A.

### 3.2.3. M&A Performance

This paper mainly uses the simplified accounting rate of return method to evaluate the performance of corporate mergers and acquisitions. The accounting rate of return method considers the company's profitability, operational ability, solvency and other indicators, while the DuPont analysis principle is a comprehensive application of corporate financial indicators, reflecting the comprehensive capabilities of enterprises. Therefore, this paper uses DuPont analysis method to analyze the specific financial indicators, the specific indicators used are weighted ROE. Let M&A performance be a continuous variable MAP (Mergers and Acquisition Performance).

$$MAP = \Delta ROE = (\text{ROEL} + 3 + \text{ROEL} + 2 + \text{ROEL} + 1) / 3 - (\text{ROEL} + \text{ROEL} - 1 + \text{ROEL} - 2) / 3$$

ROEL represents the weighted return on equity of the merger company in the year in which the M&A event occurred, the higher the MAP value the better the performance of M&A; conversely, the smaller the MAP value the worse the performance of M&A.

## 3.3. Sample Selection

The data in this paper come from Guotai Jun'an database, PEdaily's merger and acquisition event database and other data websites. Because the accounting rate of return method has a long period, it can accurately describe the performance of M&A events by collecting data for at least several years. Therefore, the data of three years before and after the occurrence of M&A events are taken as performance indicators. The specific operation is as follows: Based on the latest announcement date, the data of merger and acquisition companies with completed events from January 1, 2011 to December 31, 2014 are collected. The data of financial ratio are the annual report data of the first three years and the last three years of the merger and acquisition year.

(1) To study the M&A strategy, M&A performance is meaningful only when the M&A event has to be completed. Therefore, only the data of the company whose "transaction progress" status is "completed" are selected.

(2) This paper mainly studies the domestic M&A activities. The selected M&A events exclude cross-border M&A, including mergers and acquisitions or at least one of the mergers and acquisitions is foreign enterprises.

(3) Considering the availability of company data, the mergers and acquisitions selected in the sample are excluded from listed companies.

(4) In order to make the research results more obvious, the samples chosen are the M&A activities that have a significant impact on the enterprise, so the selection conditions are set as follows: the acquisition of equity by the merger party exceeds 50% (including 50%).

(5) If both related and non-related mergers and acquisitions occur at the same time for the same acquirer, the event with larger transaction amount will be retained.

(6) Senior managers' positions and their political identities are screened out by their resumes, and their political connections are determined according to the above-mentioned criteria for measuring political connections.

(7) When judging the degree of political connections, if the senior executive has or has held multiple positions, the highest position is selected as his final position.

(8) Samples with insufficient data were excluded, including 265 listed companies in more than 20 industries, such as Internet, new energy, real estate, new materials, food processing, IT, application software, chain and retail, agriculture, forestry, animal husbandry and fishery, chemical raw

materials, electricity, etc.

#### 4. Empirical Test and Analysis

##### 4.1. Descriptive Statistics of M&A Types

Frequency analysis of the M&A types of the whole sample shows that the results are as follows:

**Table 2.** Frequency Analysis Table of M&A Types

	frequency	Percentage
Non-related M&A	40	15.1
related M&A	225	84.9
total	265	100

The table 2 shows that there are 265 effective M&A enterprises in the sample, of which 40 are non-related M&A, accounting for 15.1% of the total, while 225 enterprises implement related M&A, accounting for 84.9% of the total.

The experimental data show that mergers and acquisitions in the market are the mainstream of mergers and acquisitions decision-making, and the vast majority of mergers and acquisitions are related mergers and acquisitions.

##### 4.2. Descriptive Statistics of Political Connections

A frequency analysis of the degree of political connection of the full samples, the results are shown in the following table:

**Table 3.** Descriptive Analysis for the Political Connection Gov

	N	Minimum	maximum	Mean	Standard deviation
Gov	265	0	12	1.38	2.333
Valid N (list state)	265				

**Table 4.** Gov Frequency Analysis of Political Connection

		frequency	Percentage	Effective percentage	Cumulative percentage
valid	0	154	58.1	58.1	58.1
	1	25	9.4	9.4	67.5
	2	32	12.1	12.1	79.6
	3	20	7.5	7.5	87.2
	4	10	3.8	3.8	90.9
	5	5	1.9	1.9	92.8
	6	7	2.6	2.6	95.5
	7	5	1.9	1.9	97.4
	10	3	1.1	1.1	98.5
	11	2	0.8	0.8	99.2
	12	2	0.8	0.8	100.0
	total	265	100.0	100.0	

From Table 3 and Table 4, we can conclude that 58.1% of the mergers and acquisitions enterprises have no political connections, while 41.9% of the mergers and acquisitions enterprises have political connections, which indicates that most enterprises do not have political connections. Among the politically connected enterprises, the enterprises with the degree of political connection of 2 are the most, accounting for 12.1% of the total sample and 28.8% of the total political connection, followed by the enterprises with the degree of political connection of 1 and 3. Specific analysis found that most of the politically connection enterprise executives have county-level cadres

or county-level people's Congress Political Consultative positions, a small number of municipal level and township-level officials, and less government officials or people's Congress Political Consultative positions at the provincial level or above. In addition, the higher the degree of political connection, the smaller the number of mergers and acquisitions, indicating that in reality, for a number of reasons, after a certain degree of political connection, it is quite difficult for enterprises to upgrade.

### 4.3. Descriptive Statistics of Political Connections and Types of Mergers and Acquisitions

The purpose of descriptive and statistical analysis of Gov and M&A types is to find the relationship between them. The analysis process and results are as follows:

We can see that the degree of political connection of the relevant M&A group is mainly concentrated at “0”, while the degree of political connection of the non-related M&A group is mainly concentrated near “2”. Using table 5 and table 6 to test the mean values of related and non-related M&A groups, further analysis shows that the P value of T-test is 0.000 (approximate to 0), indicating that the Gov mean values of related M&A groups are significantly different from those of non-related M&A groups. The mean value of political connection of the non-related M&A group was 3.23, which was higher than 1.06 of the related M&A group. It can be concluded that non-related mergers and acquisitions generally have a higher degree of political connection, which is consistent with hypothesis 1 and hypothesis 2.

**Table 5.** Descriptive Analysis of Political connection GOV and M&A Types

M&A Types		N	Minimum	maximum	mean	SD
Non-related M&A	Gov	40	0	12	3023	2.948
	N	40				
Related M&A	Gov	225	0	12	1.06	2.047
	N	225				

**Table 6.** Double Mean Comparison Test of Political connection GOV

	Levene test for variance equation		T-test of mean equation				
						95% confidence interval for difference	
	F	sig	t	df	Sig two- sides	Upper limit	Lower limit
GOV equal variance	7.347	0.007	-5.731	263	0.000	-2.912	-1.423
Non-equal variance			-4.462	45.910	0.000	-3.145	-1.190

### 4.4. Descriptive Statistical Analysis of the Impact of Political Connections on M&A Performance of Different M&A Decisions

Table 7 is the Descriptive analysis of GOV-MAP in non-related M&A groups. It can be seen from the table that in the non-related mergers and acquisitions, the M&A performance of enterprises with different degrees of political connection is different. As the degree of political relevance increases, the value of M&A performance MAP is -1.7873, 0.5167, 1.6522, 4.4688, -4.2544, respectively. However, it is not clear whether there is a relationship between GOV and MAP. Then, through further analysis of the GOV-MAP mean scatter plot, we can see that in the non-related M&A group, with the increase of the degree of political connection, the M&A performance MAP shows an upward trend, which is consistent with the assumption three above. That is, in the non-related M&A events, the degree of political connection is positively related to the M&A performance.

Table 8 is the Descriptive Analysis of GOV-MAP in Related M&A Groups. As can be seen from the table, in the process of increasing GOV from 0 to 12, the average MAP of M&A performance is -1.9916, -5.4448, -2.8709, -8.8236, -13.0657, -18.7867, -20.1225, -12.5067, -13.5467, -43.1100, respectively. In the relevant M&A group, the abnormal point is removed. As the GOV value

increases, the MAP mean value generally decreases, which is consistent with the hypothesis 4, that is, in the related mergers and acquisitions, the degree of political connection is negatively correlated with M&A performance.

**Table 7.** Descriptive analysis of GOV-MAP in non-related M&A groups

M&A types	Gov	N	Minimum	maximum	mean	SD
Non-related M&A	0 MAP	5	-8.98	4.34	-1.7873	4.98399
	1 MAP	6	-1.87	3.34	.5167	2.45695
	2 MAP	9	-6.40	9.66	1.6522	5.07442
	3 MAP	8	-6.67	12.12	4.4688	6.67226
	4 MAP	3	-19.32	5.45	-4.2544	13.22923
	5 MAP	2	-8.84	.87	-3.9833	6.86365
	6 MAP	3	5.76	10.11	7.9033	2.17569
	7 MAP	1	5.12	5.12	5.1200	.
	11 MAP	2	17.12	19.21	18.1650	1.47785
	12 MAP	1	21.22	21.22	21.2200	

**Table 8.** Descriptive Analysis of GOV-MAP in Related M&A Groups

M&A types	Gov	N	Minimum	maximum	mean	SD
related M&A	0 MAP	149	-43.12	56.00	-1.9916	14.33715
	1 MAP	19	-41.21	21.21	-5.4448	17.87580
	2 MAP	23	-34.54	13.31	-2.8709	11.69065
	3 MAP	12	-19.67	7.78	-8.8236	8.88949
	4 MAP	7	-23.11	1.45	-13.0657	9.69875
	5 MAP	3	-34.34	1.32	-18.7867	18.26085
	6 MAP	4	-34.32	3.50	-20.1225	17.38468
	7 MAP	4	-41.31	.31	-12.5067	19.72041
	11 MAP	3	-45.11	3.11	-13.5467	27.34865
	12 MAP	1	-43.11	-43.11	-43.1100	.

## 5. Conclusion

The following conclusions are drawn:

(1) Political connections affect the strategic choice of M&A. In the process of researching and analyzing the research results of foreign scholars, it is found that political connection will affect the M&A decision of enterprises. As an important enterprise resource, political connection brings many benefits to enterprises. Therefore, as the results of the study show, companies with a high degree of political relevance tend to choose non-related mergers and acquisitions; companies with low political connections tend to choose related mergers and acquisitions.

(2) Under different M&A strategies, political connections have different effects on M&A performance. While political connections have an impact on corporate M&A decisions, political connections also affect corporate M&A performance. Specifically, in the non-related M&A events, the degree of political relevance is positively correlated with M&A performance; in related M&A events, the degree of political relevance is negatively correlated with M&A performance.

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