

An Empirical Study of Hong Kong's "Collusion Between Government and Business"

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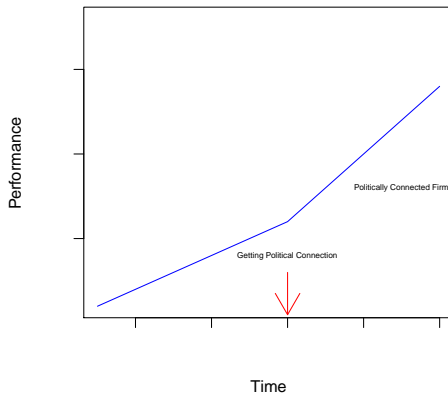
Definition

- ▶ "Collusion" is defined as secret and wrongful exchanges between individuals
- ▶ Direct evidence is often difficult to observe
- ▶ Must rely on indirect evidence, e.g. firm performance
- ▶ Empirical implication: politically connected firms perform better than politically unconnected firms

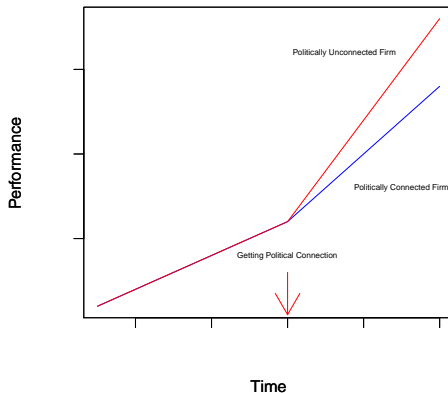
Challenges of the Empirical Study

- ▶ Political connection \Rightarrow Firm performance or
- ▶ Political connection \Leftarrow Firm performance?

Challenges of the Empirical Study



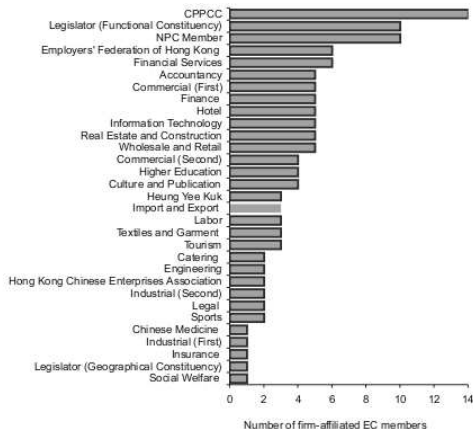
What if the situation is like this?



Empirical Strategy

- ▶ Difference-in-difference: comparison across groups and across time periods
- ▶ "Groups" = politically connected firms and politically unconnected firms
- ▶ "Political Connections" = firms with shareholders or directors serving in the Election Committee

Distribution of Firm Affiliations by Subsectors of 2000 Election Committee



Trends of Political Connections

Year	Number of Politically Connected Shareholders	Number of Politically Connected Directors	Number of Firms with Politically Connected Shareholders	Number of Firms with Politically Connected Directors	Total Listed Firms
2003	156	103	71	75	864
2004	171	132	74	97	898
2005	185	143	77	107	919
2006	208	150	87	111	969
2007	181	166	92	127	1047
2008	173	171	85	129	1093

Improve Business Performance?

- ▶ **Sample:** All firms listed in the Hong Kong Stock Exchange
- ▶ **Unit of Observation:** Firm-quarter / firm year
- ▶ **Period:** 1993 - 2000
- ▶ **Dependent Variables:** Return on Equity, Market-to-Book Ratio, Earnings-per-Share
- ▶ **Variable of Interest:** EC dummy X 1997 dummy
- ▶ **Estimation Strategy:** Difference-in-Difference
- ▶ **Controls:** Market value, market share, number of employees, industry fixed effects, etc.

Difference-in-Difference Regression Results

	Connected Through Shareholders			Connected Through Directors		
Dep. Var.	ROE	MTB	EPS	ROE	MTB	EPS
$D_{1997} \times EC$	0.572 (2.205)	0.993*** (0.219)	0.772 (1.704)	4.864*** (1.883)	0.708*** (0.187)	2.12 (1.451)
R^2	0.522	0.351	0.799	0.523	0.35	0.8
N	3794	3794	3884	3884	998	998

Notes: * <0.10 , ** <0.05 , *** <0.01 .

What Kinds of Firms Are Likely to Have Political Connections?

- ▶ **Sample:** All firms listed in the HKSE
- ▶ **Period:** 1997 and 2000
- ▶ **Dependent Variable:** A dummy of EC membership
- ▶ **Variables of Interest:** Market Share, Market Value, Employees, Firm's First Listing Year
- ▶ **Estimation Strategy:** Logistic regression

Logistic Regression Results

	1997 Sample				2000 Sample			
	(1S)	(1D)	(2S)	(2D)	(3S)	(3D)	(4S)	(4D)
Listing Year	-0.068* (0.035)	-0.061* (0.032)	-0.067* (0.038)	-0.072** (0.035)	-0.054 (0.036)	-0.055** (0.028)	-0.08* (0.042)	-0.063** (0.031)
Market Value (HKD mil)	0.010 (0.008)	0.013 (0.009)	0.009 (0.010)	0.016 (0.011)	0.000 (0.006)	0.005 (0.005)	0.006 (0.008)	0.004 (0.007)
Employees ('000)	-0.062* (0.035)	-0.066** (0.028)	-0.066* (0.038)	-0.077** (0.034)	-0.014 (0.030)	-0.029 (0.025)	-0.03 (0.035)	-0.031 (0.028)
Market Share	2.566 (3.968)	-4.737 (4.16)	7.029 (8.499)	-8.137 (6.832)	7.719* (4.367)	1.169 (4.014)	2.645 (6.586)	1.881 (6.045)
HSI Constituent	-0.867 (0.927)	0.414 (0.828)	-1.202 (1.012)	0.883 (0.934)	-0.400 (0.998)	0.765 (0.715)	-0.083 (1.126)	0.786 (0.757)
Leverage	1.808 (1.135)	0.834 (1.045)	2.152* (1.209)	1.204 (1.110)	-1.548 (1.430)	-1.28 (1.172)	-1.599 (1.843)	-1.240 (1.207)
Growth Rate of Market Value (3-Yr Avg)	-0.068 (0.276)	-0.084 (0.257)	-0.105 (0.291)	-0.1 (0.242)	-0.41 (0.35)	-1.83** (0.825)	-0.078 (0.51)	-1.846** (0.853)
Constant	132.81* (69.347)	121.232* (63.086)	115.873 (3956.899)	127.192 (2400.552)	104.815 (71.944)	108.575* (56.071)	141.148 (4580.415)	106.929 (3351.947)
N	146	146	146	146	197	198	197	198
Industry FE	No	No	Yes	Yes	No	No	Yes	Yes

Major Families & Major Groups (Not a complete list)

Head	Representative Companies	Major Family	Major Group
Li Ka-Shing	Cheung Kong (HK0001), HK Electric (HK0006), Hutchison Whampoa (HK0013)	Yes	Yes
Swire	Cathay Pacific (HK0293), Swire 'A' (HK0019)	Yes	Yes
Lee Sau-Kee	Henderson Land (HK0012), HK Ferry (HK0050), HK Gas (HK0003)	Yes	Yes
Lo Yuk-Shui	Century City (HK0355), Pallburg (HK0073), Regal Hotel (HK0078)	Yes	Yes
Lau Luen-Hung	Chinese Estate (HK0127)	Yes	Yes
Ng Teng-Fong	Sino Land (HK0083)	Yes	Yes
Shaw Run-Run	Shaw Brothers (HK0080), Television Broadcast (HK0511)	Yes	Yes
Karl C. L. Kwok	Wing On (HK0289)	Yes	Yes
Deacon T.K. Chiu	Far East Consort. (HK0035), Far East Holdings (HK0036)	Yes	Yes
Y. K. Pao	Wharf (HK0004), Wheelock Properties (HK0049)	Yes	Yes
Kadoorie	China Light (HK0002), HK & Shanghai Hotel (HK0045)	Yes	Yes
Kwok Tak-Shing	KMB (HK0062), Sun Hung Kai Properties (HK0016)	Yes	Yes
Cheng Yu-Tung	New World Development (HK0017), Melbourne (HK0158)	Yes	Yes
Chen Tseng-Tao	Hang Lung Group (HK0001), Hang Lung Properties (HK0101)	Yes	Yes
Cha Chi Ming	Mingly Corporation (HK0478), HKR International (HK0480)	No	Yes
Stanley Ho Hung Sung	Melco (HK0200), Shun Tak (HK0242)	No	Yes
Tony Fung Wing Cheung	Tian An (HK0028), Sun Hung Kai & Co. (HK0086)	No	Yes
Chan Sui Kau	Yangtzekiang (HK0294), YGM Trading (HK0375)	No	Yes
Lim Por Yen	Crocodile Garments (HK0122), Lai Sun Development (HK0488)	No	Yes
Cheong Hooi Hong	Associated International Hotels (HK0105), Tian Teck (HK0266)	No	Yes
Wee Cho Yaw	Haw Par Brothers (HK0162), United Overseas Bank (HK0274)	No	Yes
Stephen Tjondro Riady	Lippo (HK0226), HKCB Bank (HK0655)	No	Yes
Liu Lit Mo	Liu Chong Hing Investment (HK0194), Liu Chong Hing Bank (HK1111)	No	Yes
Chow Yei Ching	Chevalier International Holdings (HK0025), Chevalier Development (HK0064)	No	Yes
Tai Tak Fung	Yaohan Food (HK0060), Four Seas Mercantile (HK0374)	No	Yes
Stephen			

Conclusions

What kinds of firms are more likely to have political connections?

- ▶ Firms with long history and relatively small employment size, not necessarily good performance

Do political connections improve firms' performance?

- ▶ Return on equity and Market-to-book ratio: Yes
- ▶ Earnings per share: No

Conclusions

Implication

- ▶ Functional constituencies: defending sectors' interests or connected firms' interests?

Caveats

- ▶ Election Committee is not a regular policy-making government body
- ▶ Only examined publicly accessible data

Within-EC Variations in the Directors Sample

Est. Strategy	OLS			LSDV		
Dep. Var.	ROE	MTB	EPS	ROE	MTB	EPS
$D_{1997} \times EC_2$	0.652 (3.101)	0.837** (0.401)	0.744 (0.807)	-0.075 (2.626)	0.719** (0.34)	0.829 (0.86)
$D_{1997} \times EC_3$	-2.387 (5.2)	0.39 (0.672)	-0.348 (1.334)	2.003 (4.687)	0.906 (0.608)	-0.913 (1.505)
$D_{1997} \times EC_4$	-0.439 (9.657)	-2.728** (1.251)	0.69 (2.274)	1.996 (7.757)	-2.749*** (1.006)	0.614 (2.318)
$D_{1997} \times EC_5$	-9.213**	-0.905*	0.124	-1.818	-0.108	0.408
R^2	0.236	0.156	0.3	0.534	0.483	0.413
N	1534	1542	394	1534	1542	394

Notes: EC_1 , EC_2 , EC_3 , and EC_4 are dummy variables denoting, respectively, "the Political," "Industry, Commerce, and Finance," "Professionals," and "Labor, Grassroot, and Religion," the four constituencies of the Election Committee in 1997. EC_1 is the baseline group. * <0.10 , ** <0.05 , *** <0.01 .