



Political Connections and Stock crash risk—Empirical evidence from A-share companies in China

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ABSTRACT

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Based on the sample data of 2010-2014 A-share companies in China, This thesis empirically tested the influence of political connections on stock price crash risk in the future. The results showed that both of political connections and political connections strength were remarkable negative correlation with the listed company's share price crash risk in the future. Research conclusion of this thesis has an important theoretical and practical significance both for overall understanding the economic consequences of political connections and how to guard against crash risk.

I. Introduction

The collapse in stock prices is refers to the phenomenon that company's share price bubble due to hiding the bad news, and when the accumulated bad news are all released into the market in an instant, stock price drops sharply (Jin and Myers, 2006; Nianhang Xu, etc., 2012). This kind of phenomenon will not only destroy the investors' confidence in the financial markets, affect the national financial stability, but also could lead to a mismatch of scarce capital, eventually endanger the normal operation of the real economy, even cause the economic crisis (Guojin Chen, etc., 2008). So how to prevent and reduce the crash risk of the listed company is both a topic of common interest for supervision department and investors, and is also a hot issue discussed by current companies in the financial field.

This research aims to examine whether the stock price crash risk is affected by the political connections of listed companies and the variations in the influences of a variety of political connections on the stock price crash risk. Two types of opposite opinions are reflected in the influence mechanism of political connections, i.e. government intervention and interactive relationship, respectively. From above two opinions, the political connections of the companies may affect the stock price crash risk theoretically, however, in fact, whether the political connections really affect the stock price crash risk of the companies? Whether the various influences on the stock price crash risk are generated due to various advantages of relations and intensity of government intervention?

II. methods

A hypothesis

The price collapses is also known as share price slumping, it means that in the absence of any warning, the market index or individual stocks price suddenly sharply slump (Guojin Chen, etc., 2008). The share price collapses is caused by information management behavior of company the management and other matters result in information opaque and information asymmetry, the specific formation mechanism is that the company management generally tend to not disclose or delay to disclose bad news, as operating cycle of hidden bad news continues to gradually accumulate to a limitation, the hidden bad news are instantaneously concentrated to release into the stock market, and then cause great negative impact on the company stock prices and eventually collapse (Jin and Myers, 2006, Nianhang Xu, 2012). This thesis holds that political connections will affect the crash risk of company stock price from multiple aspects.

Firstly, the main purpose for the enterprises to establish political connections is to consider the political connections as an important strategic resource, take advantage of all kinds of scarce resources and preferential policy obtained from the government (Peng and Luo, 2000, Jianping Deng and Yong Zeng, 2009). Secondly, under background of the special system in China, the executives with political connections often play the dual role of "both of officer and businessman", when these executives (especially state-owned enterprise executives) are making business decisions, they need to do difficult trade-off between the economic interests of enterprises and political outlook of individuals. Thirdly, in addition to demand enterprises with political connections to bear policy burdens, the more general patterns of manifestation that government intervene enterprise business through political connections is the supervision and guidance for enterprises to perform and comply with the relevant supervisory policies and laws and regulations. Based on the above theoretical analysis, this thesis holds that enterprises with political connections tend to be more active in disclosing bad news, thus reducing stock price crash risk caused by instantly releasing the accumulated bad news, hereby put forward the first research hypothesis of this thesis.

Hypothesis H: compare with enterprises without political connections, the future crash risk of enterprises with political connections is lower.

V. REFERENCES

Based on the relevant data of political connection of 2010-2014 A-share main board listed companies in China, This thesis researched the influence of political connections on stock price crash risk of listed companies in the future. The research results showed that both of political connections and its strength are remarkable negative correlation with the listed company's share price crash risk in the future. It shows that political connections reduced the risk of the listed company's share price crash risk, political connections, especially connections between government officials is an important factor of the listed company share price crash risk. Under the background of special system in China, In order to maintain a good relationship with the government (especially local governments), help the government avoid the dramatic ups and downs of economic development and at the same time also in order to obtain more tax deduction and exemption, governmental subsidy and other policy benefits from the government department, and avoid the risk of judicial investigation due to share prices fell sharply, companies with political connection, especially the connection with government officials tend to strictly implement the information disclosure rules of security supervision department, timely and timely reveal bad news rather than hiding company's bad news to improve information disclosure quality, thus to a certain extent, it could alleviate the excessive accumulation of bad news and negative impact on the company's share price caused by sudden disclosure, eventually reduce the crash risk of the company's share price in the future.

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