

**Political Incentives to Suppress Negative Financial Information:  
Evidence from State-controlled Chinese Firms**

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## **Political Incentives to Suppress Negative Financial Information: Evidence from State-controlled Chinese Firms**

### **Abstract**

This paper examines the impact that political forces have on the flow of negative financial information into stock prices. Using a unique sample of listed Chinese firms ultimately controlled by local and/or provincial government entities, we test the proposition that the incentives of politicians and the local government shape financial reporting practices, especially with respect to the release of information about bad outcomes. We examine the flow of negative information around three visible political events: The National Congress of the Chinese Communist Party, provincial-level promotions, and the revelation of provincial-level corruption investigations. We find that state-controlled firms are significantly less likely to experience negative stock price crashes in the years of the National Congress of the CCP and in advance of political promotion decisions. Further analyses reveal that the suppression of negative information around National Congress meetings is a country-level phenomenon, while political promotion events produce local incentives to suppress negative information. These promotion effects are strongest in those regions where (a) meaningful capital market development, (b) strong performance expectations and (c) high levels of foreign investment raise the political and reputation costs of reporting financial performance. Overall, our results highlight the important role that political forces play in shaping financial reporting incentives of state-controlled entities.

## 1. Introduction

This paper examines the impact that political forces have on flow of negative financial information into stock prices. Using a unique sample of listed Chinese firms ultimately controlled by local and/or provincial government entities, we test the proposition that the incentives of politicians and the local government shape financial reporting practices, especially with respect to the release of negative financial information around key political events. Given the increased opportunity for foreign investors to purchase shares in state-controlled enterprises in both China and around the world, understanding the impact of political incentives on the underlying financial reporting environment is a first-order concern for participants in these markets.

Prior research shows that as the likelihood of government intervention increases, non-state-owned firms have an incentive to reduce transparency and to tilt reported valuations to minimize these political costs (e.g., Bushman, Piotroski and Smith (2004), Bushman and Piotroski (2006) and Leuz and Oberholzer (2007)). Yet despite the growing evidence that state intervention and political forces shape the financial reporting incentives of non-state-owned firms, there exists little evidence on the information environment of state-controlled entities. For state-controlled entities, the supply of timely information about the firm's performance is likely to be influenced by the ultimate objectives of the local politicians, regional public policies, and the net cost / benefit of releasing this news.

Local politicians and the managers of state-controlled entities face unique tradeoffs with respect to corporate transparency. In terms of overall economic development, transparency would benefit the economy by increasing the ability of both the State and outside investors to monitor local politicians and firm managers, by reducing information gathering costs, by improving the efficiency of capital allocation and investment decisions, by lowering the firm's / country's cost of capital and raising market valuations, and, ultimately, by increasing economic productivity and GDP.

The economic benefits of transparency, however, come at a cost to politicians and the firm's managers. Greater transparency about the operating performance will highlight inefficiencies, political agendas and economic disparities. Transparency will limit the ability of politicians' and managers' to consume their private benefits of control by exposing poor governance and highlighting

investment and asset management-related inefficiencies. Given that state-controlled entities frequently suffer from severe governance problems (see Shleifer and Vishny, 1997; Rajan and Zingales, 2003), managers and politicians will have an incentive for opaque reporting practices to hide these governance-related inefficiencies. Additionally, the revelation of poor performance resulting from these operating inefficiencies and governance conflicts will impose a personal reputation or political cost upon the manager and local politician. As such, these individuals may have an incentive to bias reported financial performance statistics to minimize the expected political cost of reporting adverse news.

To test these arguments, we examine the impact that three visible political events - the National Congress of the Chinese Communist Party, provincial-level promotions and the revelation of provincial-level corruption investigations - have on the incentive to release adverse financial information. We propose that these visible political events increase the costs for both managers and local politicians to release bad news, resulting in fewer stock price crashes during these event windows. Additional tests examine the impact of these political events conditional on regional and firm-specific attributes, such as the degree of market development, regional economic performance and policies, the presence of executive-level political connections, a Hong Kong-listing and the presence of a decentralized ownership structure, that are expected to either increase or decrease the relative cost of releasing bad news during these event periods.

We find that state-controlled firms are significantly less likely to experience negative stock price crashes around the years of the National Congress of the Chinese Communist Party and in advance of political promotion decisions relative to non-event years. Further analyses reveal that the suppression of negative information around National Congress meetings is a country-level phenomenon, with these meetings producing a broad, country-wide incentive that affects firms across all regions, regardless of the presence or absence of a politically-connected CEO or Chairman, and even influences the reporting behavior of family-owned firms. Interestingly, Hong Kong-listed Chinese firms, arguably the most visible Chinese firms and bell-weather indicators about the Chinese economy, experience a greater reduction in frequency of stock price crashes around National Congress events than non-HK listed Chinese firms, consistent with release of negative information

by these high profile firms during a National Congress being very costly for both regional and national politicians.

We also find that political promotion events produce local incentives to suppress negative information. These effects are strongest in those regions with (a) meaningful capital market development, (b) strong performance expectations and (c) strong foreign investment levels and investor interest. Additionally, firms with politically connected executives display longer periods of information suppression than non-connected firms around these promotion events. Together, this cross-sectional and cross-regional evidence is consistent with the suppression of negative information being strongest in those settings where the expected political and personal reputation cost of releasing adverse news is the greatest. These results highlight the important role that political factors play in shaping the financial reporting incentives of state-controlled entities.

The rest of the paper is organized as follows. Section 2 provides background on China and the expected impact of political forces on reporting behavior. Section 3 describes our research design and sample. Section 4 presents our empirical results for our sample of state-controlled Chinese firms, while section 5 presents empirical extensions and robustness tests. Section 6 concludes.

## **2. Background and motivation**

It is well documented that legal, political, financial and cultural institutions exert strong pressures on economic agents and their behavior. In finance and economics, a vast body of literature discusses and documents how primitive institutions influence the form of the economy and the resultant impact the equilibrium set of institutions have on investor protections, financial development, investment behavior and, ultimately, economic growth and wealth. As a key institution that aids in the allocation of capital within an economy, financial accounting standards, and the resultant financial reporting practices, are shaped by these same primitive forces.

In general, institutions associated with strong investor protections and economic outcomes are typically associated with more favorable financial reporting practices and better information environments. For example, corporate transparency is positively associated with stronger legal

protections and inversely related to state involvement in the economy (Bushman, Piotroski and Smith, 2004), earnings management is found to be less prevalent in economies with greater investor protection of minority shareholders and less concentrated ownership (Leuz, Nanda and Wysocki, 2003), timely loss recognition practices are stronger in countries with greater investor protections and institutions supporting contract usage (Ball, Robin and Kothari, 2000; Ball, Robin and Wu, 2003; Ball, 2001; Bushman and Piotroski, 2006), earnings informativeness is higher in the presence of less concentrated ownership (Fan and Wong, 2002) and stronger investor protections (DeFond, Hung and Trezevant, 2007), and the use of a high quality auditor is more likely in the presence of strong institutions (Francis, Khurana and Pereira, 2003).

Unfortunately, many developing economies lack the institutional structure that creates incentives for good governance and high quality financial reporting practices. One institutional arrangement that can give rise to adverse incentives is the state's ownership of economic assets. Lindbeck (1976), North (1990) and Olson (1993), among others, argue that the economic policies of the State frequently reflect the desire of the politicians to consolidate power and accumulate wealth. As a result, state-controlled firms are oriented towards maximizing neither social welfare nor their operating cash flows; instead, governments use their control to compensate their supporters with employment at above-market wages, with nepotism, with subsidies, through related party transactions and other indirect means (e.g., Shleifer and Vishny, 1993; LaPorta et al., 2002; Rajan and Zingales, 2003). The incentive to maximize these private benefits results in weak corporate governance and enormous inefficiencies among state firms (Shleifer and Vishny, 1997; OECD, 2005; Wurgler, 2000). Moreover, in the case of publicly listed firms, serious agency conflicts arise as the State (the controlling shareholder) attempts to expropriate the cash flows and capital of the minority shareholders (Shleifer and Vishny, 1993; LaPorta et al., 2002). In light of these inefficiencies, shareholder conflicts and weak corporate governance practices, the natural question is whether these same political forces create adverse financial reporting incentives among state-controlled entities.

Prior research shows that expected and actual government intervention in an economy influences financial reporting practices. In their seminal paper, Watts and Zimmerman (1978) argue that accounting choices are influenced by the expected political costs associated with given financial

reporting outcomes. These political costs can range from heightened tax burdens (e.g., windfall profits tax) to the outright expropriation of the firms' productive assets, and also include a host of indirect taxes such as heightened regulation or the threat of greater government intervention into the firm's business activities. As the likelihood of government intervention increases, non-state-owned firms have an incentive to reduce transparency and to tilt reported valuations to minimize these political costs. Consistent with these arguments, Bushman, Piotroski and Smith (2004) show the presence of strong state ownership in an economy creates incentives for opaque reporting practices among non-state-owned publicly traded firm. This opacity arises as firms attempt to limit information about the composition, value and profitability of their productive assets. Similarly, Bushman and Piotroski (2006) show that greater state involvement in the economy influences the timely recognition of losses into reported income. They show that the financial reporting incentives created are a function of the state's underlying incentives – whether the intervention is likely to involve the direct expropriation of valuable assets (by so-called “grabbing hand” governments) or will involve alternative “benevolent” forms of intervention (e.g., nationalization / regulation of underperforming assets). Leuz and Oberholzer (2007) examine the relations between political connections and corporate transparency in the context of Indonesia, and find that firms with strong political ties have lower corporate transparency.

Despite existing evidence that the financial reporting practices of non-state-controlled firms are shaped by the likelihood of government intervention and political connections, there exists only limited evidence on the financial reporting practices of state-controlled entities. Most of the papers in this area, including Wang, Wong and Xia (2008), Gul (2006) and Guedhami, Pittman and Saffar (2007), examine the impact of political forces on financial reporting practices around privatization events. These papers find that corporate transparency and the use of a high quality auditor after privatization are inversely related to the portion of the firm control retained by the State and positively related to the extent of foreign ownership in these firms.

In this paper, we examine one facet of the financial reporting process that is likely to be shaped by political forces: the willingness of managers and local politicians to release adverse financial news. Our analysis is designed to test the proposition that politicians and managers of state-

controlled firms have an incentive to suppress information about bad outcomes around specific political events and conditional on the underlying attributes of the firm. Unlike prior studies focusing on disclosure behavior, earnings management or audit choice, we examine an incentive to systematically insert a particular directional bias into reported financial performance, thereby shedding light on one dimension by which financial reporting transparency is limited among state-controlled firms.

### ***2.1 Background: State-controlled firms and corporate governance in China***

We focus on listed, state-controlled Chinese firms for several reasons. First, China is a natural laboratory to investigate the impact of political forces on reporting incentives; the vast majority of domestic firms listed on either the Shanghai or Shenzhen Stock Exchange are state-controlled entities.<sup>1</sup>

Second, all of the firms operate within a common institutional framework (i.e., the People's Republic of China), yet there exists considerable variation in market development, investor protections, investor interest and political objectives across China's provinces. For example, there are significant differences in economic policies and performance (value maximization versus full employment policy objectives), differences in the level of foreign investor interest (varying degrees of FDI and foreign ownership), differences in ownership structure (decentralized pyramidal arrangements versus direct control), differences in the type of shares issues (A shares; H shares; overseas listings) and differences in the degree of political connectivity (presence or absence of a politically-connected CEO or Chairman). These differences are expected to give rise to meaningful variation in the political incentives to suppress the timely release of financial information about poor economic outcomes.

Third, China is the world's largest 'emerging' economy and, in absolute terms, is a material component of the global economy.<sup>2</sup> Because significant levels of foreign investment are flowing into

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<sup>1</sup> For example, at the end of 2006, state-controlled enterprises accounted for approximately 70 percent of listed Chinese firms on these two exchanges.

<sup>2</sup> As of the end of 2006, China had the fourth largest economy, and expected growth in GDP for 2007 is 10.5%. Actual foreign investment during 2006 was \$60 billion (US), with commitments exceeding \$180 billion (US).

this economy each year, understanding the impact that political forces have on financial reporting practices should be a first-order concern for global investors and corporate managers alike. Moreover, China's recent adoption of International Financial Reporting Standards highlights the importance of understanding how local forces will shape reporting practices within the confines of the new standards.

Fourth, there exist several identifiable political events that are expected to impact the reporting incentives of local politicians and firm managers. These events include the National Congress of the Communist Chinese party, provincial-level promotion events and the revelation of provincial-level corruption cases. To the extent that the personal costs of reporting adverse news are greater around these political events, we expect the incentive to suppress negative news to be heightened around in these periods.

Finally, Chinese firms suffer from numerous governance conflicts and inefficient investment behavior that create both a supply of bad outcomes and a demand for timely information about these adverse realizations. As discussed early, the conflicting incentives of controlling and minority shareholders can lead to significant inefficiencies inside the firm (Shleifer and Vishny, 1993; Rajan and Zingales, 2003). Additionally, the decentralized pyramidal ownership arrangement that characterizes the majority of listed, state-controlled firms creates information asymmetry between local politicians and managers; this information friction exacerbates traditional investment-related agency problems, as managers of the firm invest in negative NPV project and/or fail to divest underperforming assets.

Consistent with the presence of these types of governance problems in China, Allen, Qian and Qian (2005), among others, show China's formal sector (consisting of state-controlled firms) underperforms the 'informal sector' of non-state-owned firms. Jian and Wang (2008) and Jiang, Yue and Lee (2005) both document the use of related party transactions and inter-company loans to facilitate the tunneling of resources in state-controlled firms, even though these transactions are economically inefficient for the firm as a whole. Finally, Fan, Wong and Zhang (2007) document the positive impact that severing the link between politicians and the managers of the state-controlled entity through decentralization has on investment efficiency and productivity. It is in this weak

corporate governance environment that politicians and firm managers will have both the motive and opportunity to suppress information about negative financial outcomes.

## ***2.2 Incentives to suppress negative financial information in China***

Prior research suggests that China's financial markets and listed firms are associated with a poor information environment. This weak environment is characterized by firm-level returns that are highly synchronized with general market movements (Morck, Yeung and Yu (2000)) and with returns that are significantly left skewed and subject to a greater frequency of crashes and lower levels of disclosure and corporate transparency (Jin and Myers, 2006). In terms of financial reporting practices, Jian and Wong (2008) document the prevalence of propping activities through related party transactions among China's state-controlled firms. These earnings management effects were most pronounced in those provinces characterized by weak legal institutions and less deregulation of the marketplace. Closely related to our study, Ball, Robin and Wu (2001) show that despite the introduction and adoption of international (western) accounting standards among listed firms on the Shanghai and Shenzhen exchanges, timely loss recognition (TLR) practices still lag the reporting practices of common law countries during the period 1992 to 1998. The authors conclude that the general lack of investor protections and well-developed legal institutions attenuated both the supply and demand for conservative accounting practices.

Numerous theoretical and empirical papers argue that greater corporate transparency and stricter disclosure standards will improve corporate governance by improving monitoring and limiting the consumption of private benefits by controlling shareholders (e.g., Rajan and Zingales, 2003; Stulz, 1999; Doidge, 2004; Doidge, Karolyi, and Stulz, 2004). An increased commitment towards better disclosure practices will therefore aid China's economic development through greater levels of foreign investment, lower costs of capital and higher market valuations (e.g., Gelos and Wei, 2005). Moreover, as foreign capital flows into the economy, foreign and minority shareholders will demand information in order to monitor both managers and controlling shareholders.

However, local politicians and managers of state-controlled firms have countervailing incentives to suppress information about poor financial performance. These incentives arise through

several channels. First, individual managers and local politicians will incur a personal reputation / political cost by reporting poor firm-level performance. For example, Chen, Li and Zhou (2005) and Li and Zhou (2005) find that provincial leaders' promotions and demotions are significantly associated with the change in economic performance of the province under their control. This cost is expected to be largest when a key government promotion looms in the province. Similarly, the cost is expected to be large in those settings where, *ex ante*, the State and local politicians anticipate the firm to produce strong performance results. Such settings include operating in provinces with market-oriented policies (i.e., minimal regulation), a history of strong growth and profitability, or if the firm operates in a region attracting foreign investment.

Second, the suppression of bad news allows politicians and politically astute managers to hide inefficiencies in project selection and asset management, to hide expropriation-related activities from minority shareholders, to mask the inefficient allocation of resources in order to achieve certain political objectives and to hide the diversion of resources as a result of political cronyism and corruption. This incentive to suppress or hide inefficiencies is likely to be strongest when local politicians are being investigated for corruption by the central government. Additionally, the incentive to suppress these inefficiencies is likely to be strongest among "politically connected" managers. Finally, if the value of retaining control is larger in "wealthy" provinces, we would expect the desire to suppress bad news to be strongest in those provinces with strong investment inflows and strong average performance.

Third, the cost of reporting poor outcomes is expected to be larger in those settings where any bad news will have a material impact on foreign investment activity, foreigner's perceptions or market values. For example, reporting poor performance in a high profile industry or province will result in a greater "loss of face" for both local politicians and the central government than if a similar outcome is reported in a neglected or under-performing province. Additionally, if foreign investors have a preference for certain provinces or industries, any negative financial news (even if infrequent) has the potential to undermine investor confidence and interest, potentially adversely affecting the future levels of foreign direct investment. Given these concerns, central and local politicians may

have an incentive to delay the release of bad news around highly visible political events, such as the National Congress of the Communist Chinese Party.

There exists considerable anecdotal evidence that Chinese politicians suppress negative information. In the context of environmental and health-related issues, commentators argue that China was slow to release information about the existence and spread of both the SARS virus in 2003 and bird flu virus in 2005. Similarly, information about the existence and ramifications of environmental accidents is frequently suppressed by local politicians to prevent further economic losses. “Even in a China that is more capitalist than ever, the instinctive response to bad news is to suppress it with all the force available to the nominally communist state” (Forbes, July 3, 2007) and “[the] suppression of bad news remains an unedifying habit that dies hard on the Mainland” (South China Morning Post, June 2007). More recently, firms and local politicians appear to have suppressed negative information during the 2008 Summer Olympic Games, held in Beijing. For example, local politicians in the city of Shijiazhuang suppressed a company report from Sanlu Group identifying the existence and pervasiveness of contaminated milk products in the marketplace for more than one month, until the completion of the Olympic Games, to avoid “creating a negative influence in society.”

In the realm of economic statistics, there is considerable evidence that local politicians masked the true economic impact of the Asian Financial Crisis on provincial level GDP statistics. “The Chinese government ... systematically falsified its gross domestic product data to hide an economic downturn that took place in 1998 and 1999” (Rawski, 2001). This skeptical view - that China’s economic growth temporarily stagnated while the State publicly reported double digit growth statistics - has been subsequently endorsed by numerous domestic and foreign investors (Forbes, 2003). Given that local politicians appear to succumb to political incentives to suppress adverse information, a natural question is whether these same incentives systematically influence the financial reporting practices of state-controlled listed firms.

### **3. Research design, sample construction and data sources**

#### ***3.1 Data***

We utilize a sample of publicly listed Chinese firms that were ultimately controlled by the local government in the respective fiscal year. In order to be included in the sample, we require the firm to have sufficient accounting and stock price data available in the China Security Market and Accounting Research (CSMAR) dataset to estimate our empirical models. Due to data constraints, our sample is limited between fiscal years 1993 and 2003. Our final sample consists of 801 unique state-controlled firms and 3,752 firm-year observations.

### **3.2 Research Design**

#### *3.2.1 Measure of stock price crash frequency*

To measure firm level variation in the flow of negative information into stock prices, we utilize three “crash statistics” that reflect the presence of large, negative stock price movements. The first statistic, NCSKEW, is taken directly from Jin and Myers (2006) and Chen, Hong and Stein (2001), and is measured as the third moment of each stock’s daily residual return, divided by the cubed standard deviation of daily residual returns, times negative one. By putting the negative sign in front of the standardized third moment, an increase in NCSKEW corresponds to greater left skewness in the distribution of daily excess returns and is interpreted as the firm being more crash prone.

The second statistic, DUVOL, is taken from Chen, Hong and Stein (2001), and is designed to capture the “down-to-up volatility” of the individual stock. DUVOL is measured as the log of the ratio of the standard deviation of residual returns on “down” days to the log of standard deviation of residual returns on “up” days. Down and up days are defined relative to the firm’s mean daily residual return realization over the measurement period. Firms with higher level of DUVOL are interpreted as being more crash prone.

The third statistic, FRACTION, represents the number of weeks that the firm experiences a large, negative stock price drop during the fiscal year. We define a large negative stock price drop as a negative weekly excess return of greater than -10% (i.e., at least a ten percent decline in the market value of equity). Firms with a higher level of FRACTION are interpreted as being more crash prone.

Our analyses test whether the prevalence of stock price crashes is influenced by the incentives facing these listed firms around specific political events. In these tests, we equate the presence of a large, stock price crash as indicative of the release of material negative information about the firm's financial performance. A decline in the frequency of stock price crashes during an event window is interpreted as a reduction in the flow of negative information about these firms, consistent with the transitory suppression of negative financial information during these political event windows.

### *3.2.2 Research design: Political events creating an incentive to suppress negative financial information*

Our research design focuses on three political events that are expected to influence the financial reporting practices of state-controlled entities: The National Congress of the Chinese Communist Party, provincial-level political promotions and the revelation of provincial-level political corruption investigations. We hypothesize that these highly visible political events heighten the costs of releasing adverse news for the local politicians and politically-connected managers. To the extent that these events exert an incentive to suppress negative information, we would expect to observe a decrease in negative skewness, down-side volatilities and significant negative return periods during these event windows relative to non-event periods. These three events are discussed in detail below.

***National Congress of the Chinese Communist Party:*** The National Congress of the CCP is held once every five years, and represents the most significant central government meeting in China. The congress was held in 1997 and 2002 during our sample period. These meetings outline central government policy, identify party leaders, highlight key developments and set key party objectives for the next five years. Releasing negative information during these congress years inherently contradicts an objective of these meetings and would be expected to impose a high political cost on the local politician.

***Political promotion:*** Our measure of a political promotion event reflects the turnover of local governors during our sample period. The turnover event is defined as a promotion when the

local governor moves to a more senior position than his original one, which includes: 1) promotion within the same province (e.g., promotion to party secretary), 2) promotion to another province (e.g., governor or party secretary of a larger province), and 3) promotion to the minister level of the central government. Given the nature of the political promotion process in China, these promotion events are highly visible within the political party. Candidates for a higher post are aware of their candidacy and effectively compete over a period of eighteen to twenty-four months for the available position. As such, we define our event window as the two-year period preceding and the year containing the promotion event (years -2 to 0). Prior research shows that political promotions in China are influenced by the recent performance of the region (Chen, Li and Zhou, 2005; Li and Zhou, 2005); as such, it is beneficial for local politicians to suppress the release of negative financial information in advance of the appointment. Firms that operate in the same region as the local governor are considered to be those affected by political turnover.

***Revelation of political corruption:*** Our measure of corruption events reflects the exposure of political corruption cases involving politicians at or above the bureau level. Firms operating in the same region in the years surrounding the announcement of the corruption cases are considered to be those firms affected by the politician's corruption. In the context of China, these corruption investigations rarely extend for more than one year before the cases are exposed. As such, we examine information flows over the year preceding and including the revelation of the corruption case (i.e., years -1 and 0).<sup>3</sup> We hypothesize that it is extremely costly for local politicians to release negative financial information that could highlight inefficiencies and draw attention to suspicious decisions during these investigation periods.

### *3.2.3 Research design: Empirical model*

Our primary tests search for an association between our crash measures and events that capture the heightened political incentives to suppress negative information. Because fundamental factors other than the flow of information will also influence the shape of a firm's return distribution,

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<sup>3</sup> In China, both the revelation of a corruption case, and the preceding investigation itself, is not an exogenous event. Instead, corruption cases themselves are an endogenous outcome of the regional institutions and political forces at the regional and central party level.

our tests control for cross-sectional differences in firm attributes. Specifically, we estimate variations of the following cross-sectional models:

$$\begin{aligned} \text{NSCKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{LOGSIZE}_{i,t} + \beta_3 \text{GROWTH}_{i,t} + \beta_4 \text{SIGMA}_{i,t} \\ & + \beta_5 \text{TURNOVER}_{i,t} + \beta_6 \text{TURNOVER}_{i,t-1} + \beta_7 \text{BETA}_{i,t} + \beta_8 \text{RET}_{i,t} + \beta_9 \text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (1)$$

In these models, the indicator variable *POLITICAL* is equal to one if the firm-year falls within the time window where the specific political event is expected to produce heightened incentives to suppress negative financial information, zero otherwise. The control variables are drawn from prior research examining the determinants of stock return skewness (Chen, Hong and Stein, 2001; Harvey and Siddique, 2000) or represent additional firm characteristics that could plausibly induce a stock return crash independent of the historical suppression of financial information (such as the firm's riskiness or contemporaneous performance). These explanatory variables are defined in Appendix A.

### ***3.3 Research design: Regional incentives to suppress negative information around political events***

Our within-country analysis around specific political events is designed to exploit both time-series and cross-sectional variation in the political cost of reporting negative information. However, as noted earlier, there also exists considerable differences in institutions, market development, economic performance and economic policies across China's regions. The cost of reporting adverse financial information is likely to vary by these attributes, resulting in systematically different financial reporting incentives across regions in response to these political events. The link between these regional attributes and the reporting incentives of local politicians are outlined below.

#### ***3.3.1 Influence of market deregulation and foreign investment activity***

Prior cross-country research shows that the level of investor interest, market valuations and economic wealth are positively related to the level of investor protections found in the economy. More importantly, absent significant political forces, regions characterized by greater investor protections tend to be positively associated with greater corporate transparency, less earnings management and better governance practices. However, in China, these institutions may interact with political forces when shaping corporate behavior around politically-charged events. For

example, the cost to the local politician and the State of a poor outcome is expected to be larger in those settings where any bad news will have a material impact on foreign investment activity or foreigner's perceptions of market values; as such, we expect the relative political incentive to suppress bad news to be positively related to the degree of market development and level of foreign investment.

We use three regional level variables as a proxy for these institutional pressures. The first variable is a marketization index, which captures the overall level of market development, including degrees of market competition and government intervention (Fan and Wang, 2001). The second variable is an index of deregulation constructed by Demurger et al. (2002) which captures the amount of preferential policies granted to a region by the central government. Higher value in the deregulation index suggests more deregulation in the region's markets. The third variable is Fixed Assets Investment: FDI / SOE, which is measured as the ratio of fixed asset investment financed by foreign capital to that financed by state-owned enterprises. We expect the incentive of the local politician to suppress negative information around political events to be increasing in all three variables.

### *3.3.2 Influence of regional conditions and government-level policy objectives*

In China, the incentives of a state-controlled entity's executives are expected to be shaped by the local government's economic policies. When the local government is faced with poor economic conditions, policy objectives are tilted towards the achievement of social welfare objectives, such as full employment targets, instead of profit maximization. To the extent that managers and local politicians are being evaluated against objectives other than market development activities or value creation, the political penalties associated with reporting poor financial performance are likely to be smaller. Moreover, to the extent that the reporting of adverse news could be used as a mechanism to extract additional resources from the central government in these settings, local politicians might face fewer incentives to actively suppress this information around political events.

We employ two regional-level variables as proxies for the local government's economic policy. The first variable is the unemployment rate of the region under the jurisdiction of the local

government. The second variable is the average percentage of non-operating assets for the state-owned firms under the jurisdiction of the local government. Consistent with prior research, we assume that regions facing poor performance are less likely to focus on profit maximization-oriented policies. Given that assumption, the expected political cost of releasing bad news should be decreasing in these two measures; as such, we expect to incentive of the local politician to suppress negative information around these political events to be decreasing in these measures of poor regional performance.

### 3.3.3 Empirical model incorporating regional institutions

To estimate the impact that these regional differences have on the flow of negative financial information around our political events, we estimate variations of the following cross-sectional model:

$$\begin{aligned} \text{NSCKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{INSTITUTION}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{INSTITUTION}_{i,t} \\ & + \beta_4 \text{LOGSIZE}_{i,t} + \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{SIGMA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{TURNOVER}_{i,t-1} \\ & + \beta_9 \text{BETA}_{i,t} + \beta_{10} \text{RET}_{i,t} + \beta_{11} \text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (2)$$

In these estimations, the variable  $\text{INSTITUTION}_{i,t}$  captures the realization of one of the regions' economic or institutional attributes. The inclusion of these regional variables will also help mitigate concerns that our  $\text{POLITICAL}$  indicator variable merely captures differences in regional attributes. All other variables are as defined in Appendix A.

### 3.4 Research design: Impact of political connections on the incentive to suppress negative financial information

Through their direct relationships with local government officials, politically-connected executives are likely to be more scrutinized than executives without political connections. This relationship, and the political benefits and repercussions it can bring, raises the relative cost of releasing bad news for these executives. Moreover, these relationships create an easier conduit by which local or national party officials can exert influence over the reporting practices of state-controlled entities. Utilizing firm-level data on the political connections of each state-controlled

firm's CEO and Chairman, we examine whether politically connected firms experience fewer stock price crashes around these political events. We expect a negative relation between the likelihood of a stock price crash and the presence of a connected CEO or Chairman around these political events.

To test for these relations, we estimate the following cross-sectional model for those firm-years with data on political connections:

$$\begin{aligned} \text{NSCKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{CONNECT}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{CONNECT}_{i,t} + \beta_4 \text{LOGSIZE}_{i,t} \\ & + \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{SIGMA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{TURNOVER}_{i,t-1} + \beta_9 \text{BETA}_{i,t} \\ & + \beta_{10} \text{RET}_{i,t} + \beta_{11} \text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (3)$$

where the variable CONNECT is an indicator variable equal to one if the firm's CEO or Chairman has past work experience in the government or has a current political position, as identified from the company's annual report.

### ***3.5 Descriptive statistics***

Table 1 presents evidence on the distribution of our firm-year observations. The number of observations increases dramatically over our eleven-year period, as a greater number of state-owned enterprises were listed onto Chinese (and foreign) exchanges over this timeframe. Geographically, the firms are drawn from 31 different provinces, with 16.4% and 13.6% of the observations concentrated in Shanghai and Guongdong, respectively.

Table 2, panel A presents descriptive statistics on our sample of state-controlled firms. Not surprisingly, these firms tend to be large entities. However, despite their fairly uniform size, these firms display considerable variation in terms of financial performance (RET), sales growth (GROWTH), investor interest (TURNOVER) and risk (BETA and SIGMA).<sup>4</sup> Given the variation in these underlying firm characteristics, it will be important to control for the impact of these attributes in our crash tests. These descriptive statistics also highlight substantial variation in our crash

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<sup>4</sup> In terms of ownership structure, nearly 85% of these firm-year observations represent firms that were controlled through some form of a pyramidal arrangement (i.e., more than one ownership layer). However, fewer than 19% of these pyramidal arrangements involved more than two layers, suggesting that a binary variable reflecting the presence of more than one layer is likely to be sufficient to capture meaningful variation in ownership structure. These descriptive statistics are consistent with the evidence in Fan, Wong and Zhang (2007).

measures across these firm-year observations. Finally, Appendix B documents substantial variation in regional market development, foreign ownership and regional performance.

Table 2, panels B, C and D, presents evidence on the political connections of these firms and the provincial-level political events present during our sample period. In terms of political connections, 22.5% of available firm-year observations are associated with the presence of a politically connected CEO, while 45.4% of available firm-years are associated with a politically connected Chairman. In terms of political events over our sample time period, there exist 35 unique instances of disclosed political corruption cases in 19 provinces and 30 political promotion events in 21 provinces. Neither of these events is clustered within the sample time period.

Table 3 presents a correlation matrix for our firms' crash statistics, firms' financial characteristics, regional institutional variables and our political event indicators. Several interesting relations emerge. First, consistent with prior research, regional institutions and attributes are highly correlated, with regions possessing stronger institutions displaying stronger economic performance and attracting greater levels of foreign direct investment. Second, our crash statistics (NCSKEW and DUVOL) display significant relations with numerous firm-level characteristics, highlighting the importance of explicitly controlling for attributes such as firm size, liquidity and risk in our tests.

Lastly, our crash statistics are negatively related to our institutional measures of market development and regional performance. These cross-sectional relations indicate that stronger, market-oriented institutions produce more transparent reporting in the form of fewer incidences of large stock price crashes, on average, in these regions. This inverse relation across all available firm years is consistent with prior research on the average impact that information suppression has on the distribution of returns in an economy (Jin and Myers, 2006; Bris, Goetzmann and Zhu, 2007).<sup>5</sup>

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<sup>5</sup> In a non-event setting, the presence of large, negative stock price crashes indicates the prior likely suppression of information, or constrained flow of information, about bad outcomes. Jin and Myers (2006), building on the analysis in Chen, Hong and Stein (2001), argue that negative skewness in returns, and the resultant crash measures, are influenced by the release of current and previously suppressed negative financial information at one time. Essentially, as opposed to the alternative return distribution where negative news is released in a timely and sequential manner, the deferral of individual bad news events leads to larger negative price shocks and greater negative skewness in returns when the combined news is eventually released. Thus, greater skewness, *ceteris paribus*, is indicative of a greater likelihood that earlier negative news was withheld. Consistent with this interpretation, Jin and Myers show that their country-level crash measures are significantly correlated with measures of firm disclosure and corporate opacity, as well as stock return synchronicity. Similarly, Bris, Goetzmann and Zhu

## 4. Empirical Results

This section presents the primary analysis and results of our paper. Section 4.1 presents our baseline estimations around our three political events. Section 4.2 extends the analysis to examine the impact of different regional incentives on reporting behavior around these political events, while section 4.3 discusses our analysis of political connections.

### *4.1 Impact of political events on the suppression of negative financial news*

Our primary empirical tests examine the frequency and severity with which state-controlled entities in China experience negative stock return crashes in the time period surrounding political events. As discussed in the preceding section, each of these political events is expected to increase the cost of reporting negative financial news, thus lowering the likelihood of observing extreme negative stock price realizations during these event windows.

Table 4 presents univariate evidence on the distribution of excess weekly returns around political events. For parsimony, this table only presents the left-tail of the distribution of excess weekly returns for our event and non-event periods, because it is these observations that map more directly into our hypotheses with respect to the suppression of negative information. Interestingly, median returns for our event and non-event periods are comparable; for both time periods, the median return is -0.002, consistent with the median week conveying only minimal firm-specific news. However, for those weekly return observations less than the median, we observe that negative weekly returns realizations during our three event windows are systematically less extreme (i.e., more right skewed) than the weekly return realizations associated with the corresponding non-event period. Although the statistical significance of these differences in the returns distribution have not been assessed, this descriptive distributional evidence is consistent with the prediction that these

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(2007) show that downside volatility is significantly larger when short-selling is constrained, consistent with the prior build up (i.e., artificial suppression) and subsequent simultaneous pricing of negative financial information in those settings with downside trading frictions. Finally, recent research by Hutton, Marcus and Tehranian (2007) and Kothari, Shu and Wysocki (2007) support this interpretation of crash statistics among the broad cross-section of firms in a non-event setting.

political event periods are associated with a reduced frequency of extreme negative price movements. The remainder of the paper examines these patterns more formally.

Table 5 present coefficients (and t-statistics using clustered standard errors) from various pooled cross-sectional estimations of equation (1) for our complete sample of state-controlled firms for each of these particular event periods. Each panel presents coefficients from an estimation of the model that incorporates an indicator variable representing the presence of one unique political event. The first set of columns present coefficients from estimations where NCSKEW is the dependent variable, while the second set of columns present coefficients from estimations where DUVOL is the dependent variable. If these political events increase the incentive to suppress negative information, we would expect a negative coefficient on the indicator variable POLITICAL in these estimations.

Panel A presents coefficients from estimations that include an indicator variable denoting whether or not the firm-year corresponds to the meeting of the National Congress of the Chinese Communist Party. These estimations reveal that state-controlled firms are significantly less likely to experience a negative stock price crashes during congress years relative to non-congress years. This negative effect is consistent with the heightened costs of the releasing negative news around this highly visible political event.

Panel B presents coefficients from estimations that include an indicator variable denoting a political promotion in the province. Consistent with arguments that politicians will suppress negative news in advance of promotion decisions, we find that state-controlled firms are significantly less likely to experience a negative stock price crash in the three year period preceding and including these promotion events. This reduced crash frequency is consistent with local politicians suppressing bad news to minimize their personal cost of reporting bad news during this evaluation period. Interestingly, the rate of bad news dissemination reverts back to normal levels once the promotion announcements have been made, as denoted by the insignificant effect documented in the post-promotion window (years +1 and +2).<sup>6</sup>

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<sup>6</sup> For completeness, we also examined political demotions in a region. These estimations are unable to detect a change in reporting incentives around these events. The lack of a significant effect in this setting may (a) reflect a lack of forewarning about these demotions, or (b) be an artifact of the endogenous nature of these events. For example, our sample demotions only contains events where the local governor was actually demoted, which likely

Panel C presents coefficients from estimations that include an indicator variable denoting the revelation of a corruption case in the region. These estimations reveal significantly fewer stock prices crashes during these periods relative to non-corruption periods. Similar to political promotions, local politicians are aware of corruption investigations in their regions before they are publicly revealed, and appear to respond by suppressing the flow of adverse news during the course of these investigations. This result, however, is only robust to the use of NCSKEW as our measure of information flow.

Together, the results from these estimations imply that managers and/or local politicians respond to the incentives created by these political events by suppressing the flow of negative information to the marketplace. The next two sections will examine these relations conditional on factors that are expected to heighten or attenuate the incentives to suppress information around these political events.

#### ***4.2 Impact of local government institutions on the incentive to suppress negative financial information***

Differences in economic conditions, institutions and policies across China's regions are expected to influence the relative incentives of local politicians and managers to suppress negative financial information around political events. Specifically, the relative cost of reporting bad news is expected to be higher in regions with significant levels of market deregulation, greater levels of foreign direct investment, a profit maximization orientation and strong economic performance.

Table 6 presents select coefficients from our estimations of equation (3) around our three key political events. Each column presents coefficients from an estimation of the model that incorporates one unique provincial-level institutional attribute expected to influence the cost of reporting bad news. For parsimony, only the coefficients on the political and institutional variables are tabulated from these estimations.

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consist of those instances where performance was the poorest or the information about poor performance was already publicly available. In contrast, those politicians who may have prevented turnover (at least partially) by suppressing negative information are not captured in our sample.

The first panel presents coefficients from our estimations around the meetings of the National Congress of the CCP. First, the negative relation between our crash statistics and this political event indicator is robust to the inclusion of these provincial-level attributes. Second, our crash statistics are positively related to the level of provincial market development and negatively related to economic performance; that is, provinces characterized by greater market development, greater foreign direct investment and strong economic performance (i.e., value maximization versus full employment agenda) are, on average, more likely to experience stock price crashes. Lastly, the interaction terms between our political event indicator variable and our measures of provincial institutions are insignificant in all estimations. These insignificant coefficients suggest that the incentive to suppress negative financial news around this national political event is a country-level phenomenon.

Panel B presents coefficients from our estimations around regional political promotion events. In contrast to the meeting of the National Congress, regional factors influence the intensity with which negative financial information is suppressed in advance of political promotion decisions. Specifically, these estimations reveal that suppression is significantly stronger in provinces with substantial levels of market development and foreign direct investment and weaker in provinces facing weak economic conditions. Essentially, politicians with significant autonomy and focused on profit maximization and market development activities incur the greatest cost for releasing bad news, while politicians in weak regions face smaller penalties for reporting losses because full employment, not profit maximization, is likely to be the state's primary objective. Similarly, local politicians and managers operating in a province with strong economic performance, and therefore strong expected performance, face a greater personal reputation cost of reporting adverse news; the adverse news will likely have a larger negative effect on their careers in these settings.

Finally, Panel C presents coefficients from our estimations around the revelation of political corruption investigations. Unlike the preceding analyses, the impact of a corruption investigation on reporting incentives appears to be subsumed by the underlying institutional environment in which these investigations are taking place. In all estimations, the previously documented negative relation between our crash statistics and our corruption event indicator variable is subsumed by the inclusion of the regional variables. Given the endogenous relation between the existence of corruption, the

likelihood of a corruption investigation occurring and underlying regional attributes, these estimations should be interpreted with caution.

#### ***4.3 Impact of political connections on the incentive to suppress negative financial information around political events***

To further our understanding of how political factors shape these firms' information environments, we examine the extent to which firms with political connection are more likely to suppress the release of negative financial information around these political events. Table 7 presents select coefficients from our estimations of equation (4) around our three key political events. Each column presents coefficients from an estimation of the model that incorporates one unique political events. For parsimony, only the coefficients on the political and institutional variables are tabulated from these estimations. Due to data limitations on the political connections of firm-level executives, our sample size is reduced by approximately one-third for these tests.

Panel A presents our estimations for politically connected CEOs, while panel B presents our estimations for politically connected Chairmen. These estimations reveal several interesting observations. First, politically connected firms are more likely to experience stock price crashes, on average, over the sample period. To the extent that politically connected firms are more likely to suffer from governance conflicts and poor investment decisions, this result could be a manifestation of these firms experiencing more frequent losses as a result of these inefficiencies. This evidence is also consistent with these politically connected firms responding more sharply to political pressures to delay, on average, the release of negative information, similar to the cross-country evidence presented in Jin and Myers (2006) and Bris et al (2007).

Second, we observe that for meetings of the National Congress of the CCP, politically connected firms and non-connected firms respond similarly around this event. Specifically, the insignificant coefficient on the interaction term POLITICAL\*CONNECT in these models reinforces the interpretation that these national meetings produce wide-ranging incentives to suppress negative information around these events.

Lastly, these estimations show that, on average, politically connected firms respond as sharply to the incentives created by a political promotion as non-connected firms. However, whereas non-connected firms experience an increased likelihood of releasing negative news following the promotion decision (i.e., the firm releases the previously suppressed information), connected firms experience a much smaller reversal of information flow. In other words, these politically connected firms appear to continue to suppress negative information in the period immediately following the promotion announcement relative to non-connected firms.

## 5. Robustness tests and extensions

### 5.1 Evidence from the frequency of crash weeks

The preceding evidence on the incidences of stock price crashes relies upon two dependent variables, NCSKEW and DUVOL, that reflect the higher moments of each firm's daily return distribution. An alternative approach to measure the release of negative financial information is to examine the frequency that the firm experiences a material negative weekly stock return. To verify the robustness of our preceding inferences, we re-examined stock price behavior around our events using the fraction of calendar weeks in a year that experienced a greater than a ten percent decline in stock price (FRACTION) as our proxy for stock market crashes.

First, univariate evidence using this measure can be found in Figures 1 through 3. As seen in these figures, the frequency of a crash being reported around each of these events is systematically lower, as reflected by greater periods of no crash activity (i.e., lack of bars) and lower crash frequencies (i.e., smaller bars) during the event windows. Although simply descriptive in nature, these figures clearly highlight the material decline in the frequency of stock price crashes around each of these three events.

Second, we estimate the following multivariate models for each of these three political events:

$$\begin{aligned} \text{Log}(1+\text{FRACTION}) = & \alpha + \beta_1\text{POLITICAL}_{i,t} + \beta_2\text{LOGSIZE}_{i,t} + \beta_3\text{GROWTH}_{i,t} + \beta_4\text{SIGMA}_{i,t} \\ & + \beta_5\text{TURNOVER}_{i,t-1} + \beta_6\text{MTB}_{i,t} + \beta_9\text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (4)$$

$$\begin{aligned} \text{Log}(1+\text{FRACTION}) = & \alpha + \beta_1\text{POLITICAL}_{i,t} + \beta_2\text{INSTITUTION}_{i,t} + \beta_3\text{POLITICAL}_{i,t} * \text{INSTITUTION}_{i,t} \\ & + \beta_4\text{LOGSIZE}_{i,t} + \beta_5\text{GROWTH}_{i,t} + \beta_6\text{SIGMA}_{i,t} + \beta_7\text{TURNOVER}_{i,t-1} + \beta_8\text{MTB}_{i,t} + \beta_9\text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned} \quad (5)$$

All variables are defined in Appendix A. Select coefficients from these estimations are presented in Table 8.

Our estimations using FRACTION as the dependent variable confirm the basic inferences gleaned from Tables 4 and 5. Specifically, we continue to document the country-level suppression of negative information in the year of the meeting of the National Congress of the CCP, with minimal evidence of variation in this incentive across regions. Additionally, after controlling for the level of market development and foreign direct investment, we continue to observe a decline in crash frequency in advance of political promotions, with the effect strongest in those regions with the *ex ante* largest cost to reporting bad news around these events. Lastly, we are again unable to document a statistically reliable negative effect around the revelation of corruption investigations.

## 5.2 Stock return synchronicity

Prior research by Morck, Yeung and Yu (2000) shows that stock price movements are highly synchronous in China. One explanation for this return behavior is due to the limited flow of firm specific information into prices in this marketplace. Building on this interpretation of stock return synchronicity, we examine whether the flow of information into prices, as proxied by stock return synchronicity, is affected by these political events. Specifically, we estimate variations of the following cross-sectional models around our three political events:

$$\begin{aligned} \text{SYNCH}_{i,t} = & \alpha + \beta_1\text{POLITICAL}_{i,t} + \beta_2\text{LOGSIZE}_{i,t} + \beta_3\text{GROWTH}_{i,t} + \beta_4\text{STD\_ROA}_{i,t} \\ & + \beta_5\text{TURNOVER}_{i,t} + \beta_6\text{REGULATED}_{i,t-1} + \beta_7\text{IND\_NUM}_{i,t} + \beta_8\text{IND\_SIZE}_{i,t} + \varepsilon_{i,t} \end{aligned} \quad (6)$$

In these estimations, SYNCH is measured as the log ( $R^2/(1+R^2)$ ), where  $R^2$  is from an estimation of the market model of firm weekly returns against current and lagged domestic market and US market returns in year  $t$ . The control variables are drawn from prior research and defined in Appendix A. To the extent that these political events are correlated with a general reduction in the amount of

information influencing security prices, we would expect a positive association between POLITICAL and SYNCH.

Coefficients from various estimations of this model are presented in Table 9. These estimations reveal that both the National Congress of the CCP and corruption investigation periods are associated with a significant increase in stock return synchronicity, consistent with a general decline in the amount of firm specific information being released about state-controlled firms during these periods. After controlling for regional institutions, the positive impact of the National Congress of the CCP remains, while the political corruption effect is once again subsumed by inclusion of local institutions. Finally, we are unable to document any change in stock return synchronicity around political promotion events. One explanation for this lack of relation with SYNCH may be the result of local politicians simultaneously suppressing bad news while releasing a greater amount of good news during the promotion evaluation period.

### ***5.3 Impact of decentralization on incentives to suppress negative financial information***

Fan, Wong and Zhang (2007) provide evidence that corporate pyramids allow for the credible decentralization of decision rights from a controlling owner to a manager. The intermediate layers of the pyramid create an informational friction between the owner and manager, making it difficult for the owner to intervene in the manager's decisions. To the extent that this decentralization is credible, decentralization has the potential to reduce the likelihood of direct government reprisal, thus lowering the expected political costs associated with the reporting of adverse financial news. If true, we would expect a positive relation between pyramidal ownership arrangements and stock price crashes during these political event periods. However, to the extent that the central or local government can pierce this structure, the incentive to suppress will remain unchanged despite a decentralized organizational structure. Untabulated results are unable to document a significant relation between the use of these pyramidal arrangements and our crash statistics.

### ***5.4 Influence of foreign listing choice on the reporting practices of state-controlled firms***

Prior research shows that firms cross-listing onto exchanges characterized by strong investor protections experience an improvement in corporate governance and financial reporting practices. These bonding-related effects yield a lower cost of capital and heightened valuations for the cross-listed firms. In the case of China, state-controlled firms also have the opportunity to list their shares overseas. The most direct route to access “foreign” markets would be via an H-share listing in Hong Kong.

If Hong Kong institutions create credible incentives, these listings should exert a positive influence on the financial reporting practices of these state-controlled firms. However, there is considerable debate about whether these host institutions are binding. First, in the case of an H-share listing, are the legal protections afforded in Hong Kong substantially different than those available in mainland China? Second, are foreign exchanges and regulators able to credibly punish state-owned firms that violate host country requirements? Lastly, there is criticism that local regulators (e.g., the U.S.’s SEC) do not take action against foreign firms that list their shares in the U.S. and that very few lawsuits brought against foreign firms are successful (Licht, 2003; Siegel, 2005). A recent paper by Hung, Wong and Zhang (2007) find that while Chinese state-owned firms’ overseas listing decisions are primarily determined by politicians’ agendas, there are bonding effects even in the Hong Kong markets due to the increase in analyst following. This bonding would create an incentive for transparency reporting regardless of presence of these political events.

Conversely, state-controlled firms listed on foreign exchanges are the most prominent and visible Chinese firms, and are frequently viewed as “bell weather” firms for the entire Chinese economy. The release of bad news by these firms during one of our political event windows is expected to impose a large cost on the local politician and central government, especially in terms of “loss of face” and a reduction in foreign investment flows. As such, the visibility of these firms is expected to create a countervailing incentive to suppress the release of bad news during visible, politically charged event periods.

Table 10 presents coefficients from an estimation of model that includes an indicator variable for the presence of a Hong-Kong listing for our sample of state-controlled firms. These estimations reveal that the suppression of bad news around meetings of the National Congress of the CCP is

greater for these Hong Kong listed companies. This heightened level of suppression for these Hong Kong listed firms supports the argument that unfavorable news about high profile firms is very costly to both local and national politicians during visible events such as the National Congress. In contrast, Hong Kong listed firms are no more or less likely to suppress negative information around promotion and corruption events than local firms only listed on domestic exchanges; the lack of a Hong Kong effect around these events further support the notion that central government concerns (versus provincial government concerns) drive the observed Hong Kong effect around the National Congress meetings. Moreover, the impact of central government-related political incentives on these Hong Kong-listed firms casts further doubt on the strength of any bonding-related effects associated with a Hong Kong listing for politically connected firms (e.g., Hung, Wong and Zhang, 2007).

### ***5.5 Influence of political events on the reporting incentives of family-owned Chinese firms.***

As a means of calibrating our results for state-controlled firms, we re-estimate our primary tests on a sample of family-owned firms in China. Due to the prevalence of state ownership in the Chinese economy, the sample size for these tests consists of 617 firm-year observations. Results from these estimations are presented in Table 11.

Despite a limited amount of data on family-owned firms in China, we find strong evidence that these firms also suppress negative information in the year of a National Congress, consistent with central role these meetings have on shaping the Chinese environment among politicians, firm executives and leading families. In contrast, none of the other political events have an impact of the behavior of these family-owned firms. The lack of a result around these political events is expected, given that local politicians are able to exert less influence over the practices of these family firms, and because promotion decisions and corruption investigations are principally focused on the activities of the firms directly under control of local officials.

## **6. Conclusions**

This paper examines the impact that political forces have on the flow of negative information into stock prices. Using a unique sample of listed Chinese firms ultimately controlled by local and/or

provincial government entities, we test the proposition that the incentives of politicians and the local government shape financial reporting practices, especially with respect to the release of information about bad outcomes around key political events. Our tests focus on three visible political events over the time period 1993 to 2003: National Congresses of the Chinese Communist Party, provincial-level promotions, and the revelation of provincial-level corruption investigations.

We find that state-controlled firms in China temporarily suppress the release of negative news around the years of the National Congresses of the Chinese Communist Party and in advance of political promotion decisions relative to non-event years. Further analyses reveal that the suppression of negative information around National Congress meetings is a country-level phenomenon, with these meetings producing a broad, country-wide incentive that affects firms across all regions, regardless of the presence or absence of a politically-connected CEO or Chairman, and even influences the reporting behavior of family-owned firms. Moreover, Hong Kong-listed Chinese firms, arguably the most visible Chinese firms and bell-weather indicators about the Chinese economy, experience a greater reduction in stock price crashes around National Congress events, consistent with release of negative information by these high profile firms during a National Congress being very costly for both regional and national politicians.

Additional analyses show that regional events, such as political promotions, produce localized incentives to suppress negative information. These incentives are strongest in those settings where (a) the presence of meaningful capital market development raises the cost of releasing bad news, (b) strong performance expectations raise the expected political / reputation cost to a manager and/or local politician of reporting an economic loss, and (c) strong foreign investment increases the likelihood of loss of face or adverse reputation consequences. Additionally, the political connections of the executives of the state-controlled firms also appears to shape the response to local promotions, with these connected firms displaying longer periods of information suppression than non-connected firms. Overall, the systematic impact of these political events and the incentives they create on the flow of negative financial information from state-controlled entities highlight the important role that political forces play in shaping financial reporting incentives.



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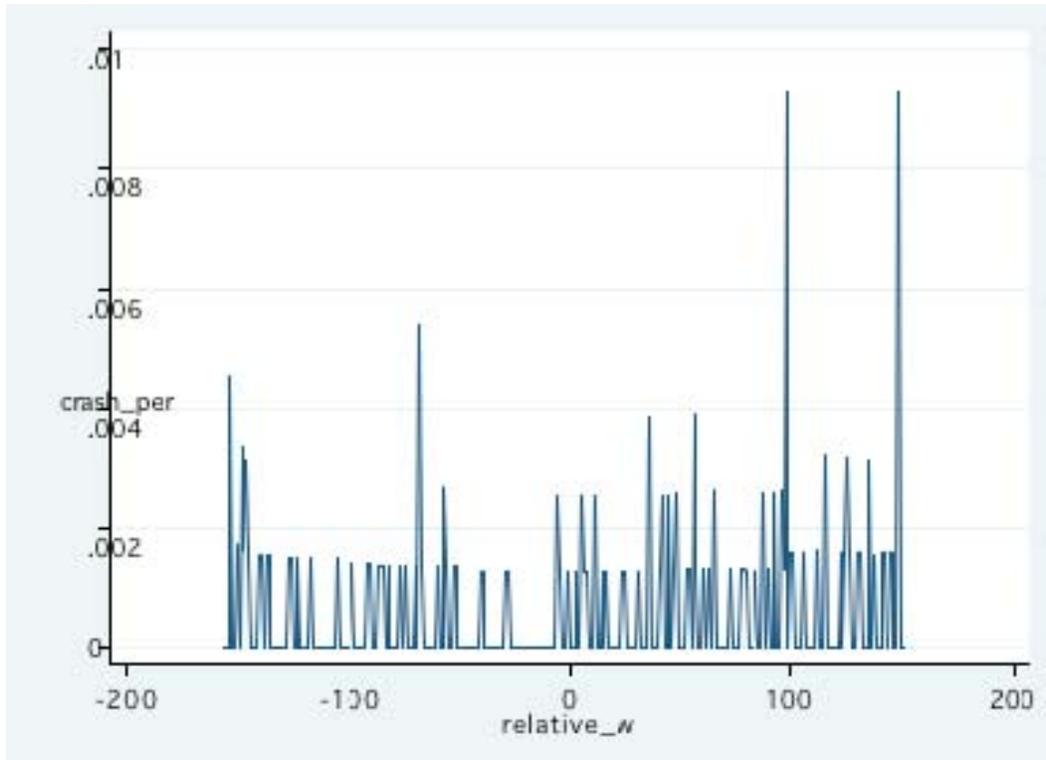
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Figure 1: Frequency of Significant Negative Stock Price Movements (excess returns < -20%) around the Announcement of Corruption Investigation

Crash weeks



Crash Month (if there is a crash week in the month)

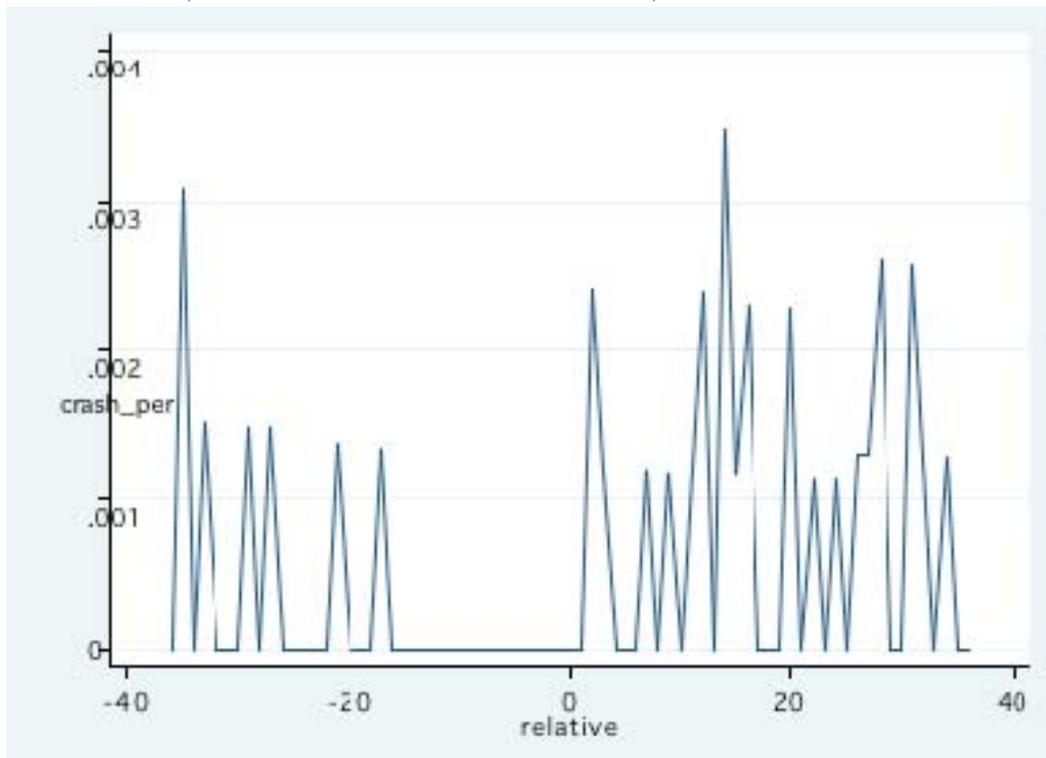
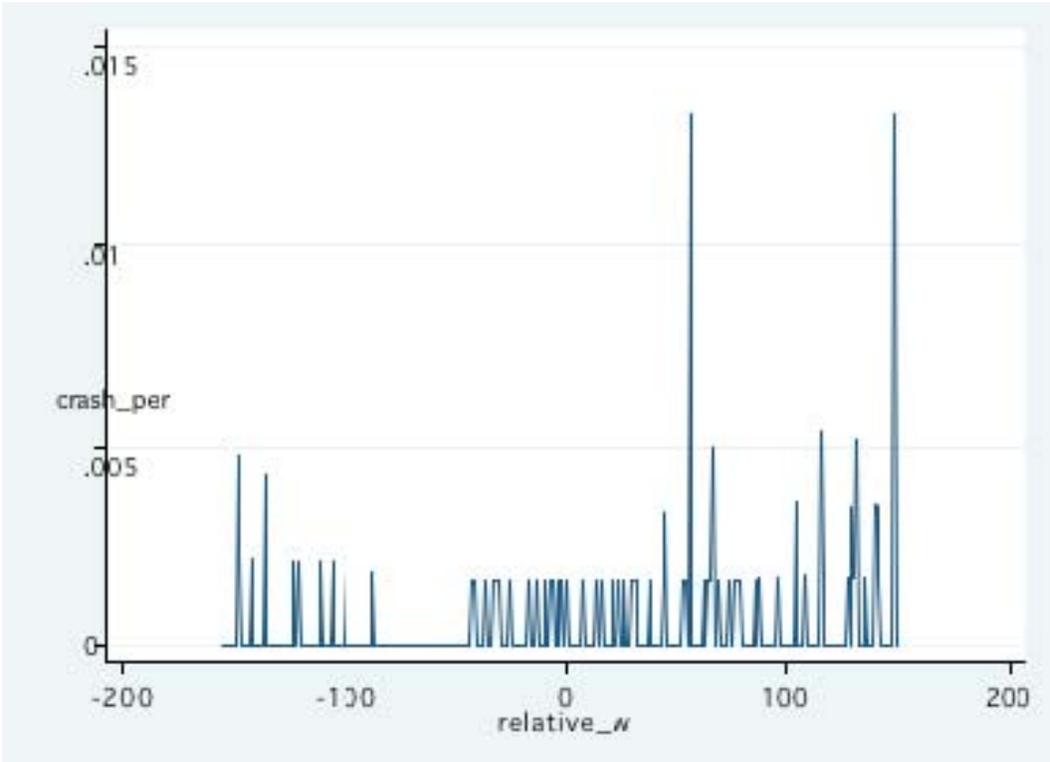


Figure 2: Frequency of Significant Negative Stock Price Movements (excess returns < -20%) around provincial-level political promotions

Crash weeks



Crash Month (if there is a crash week in the month)

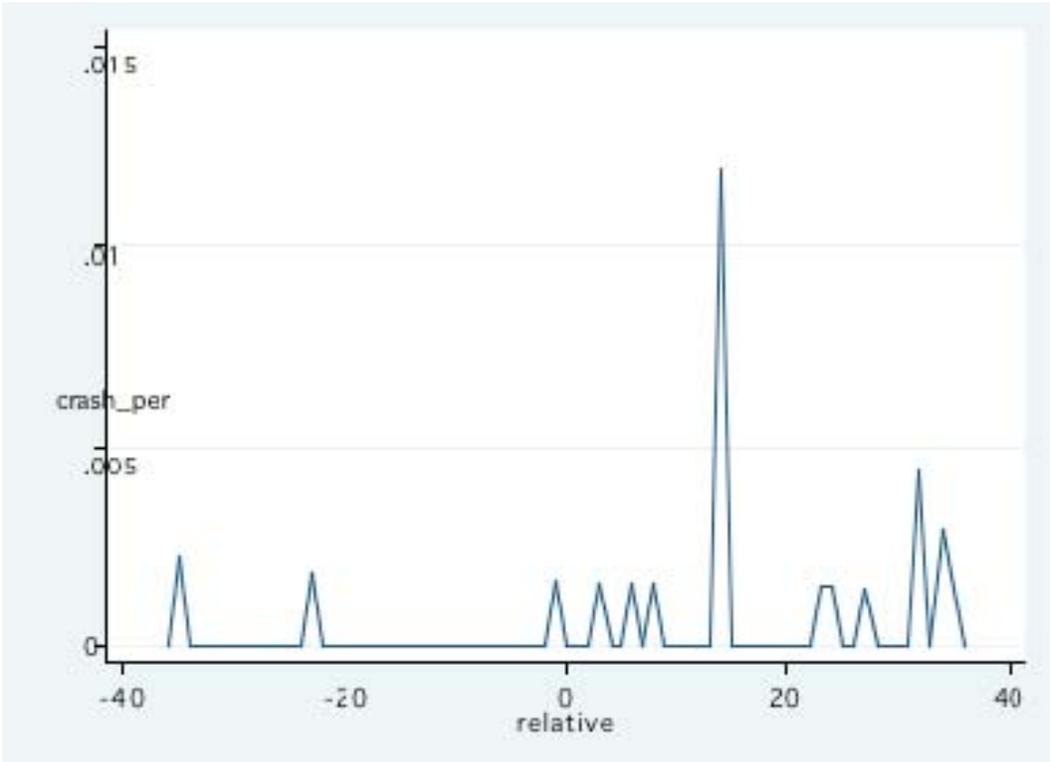
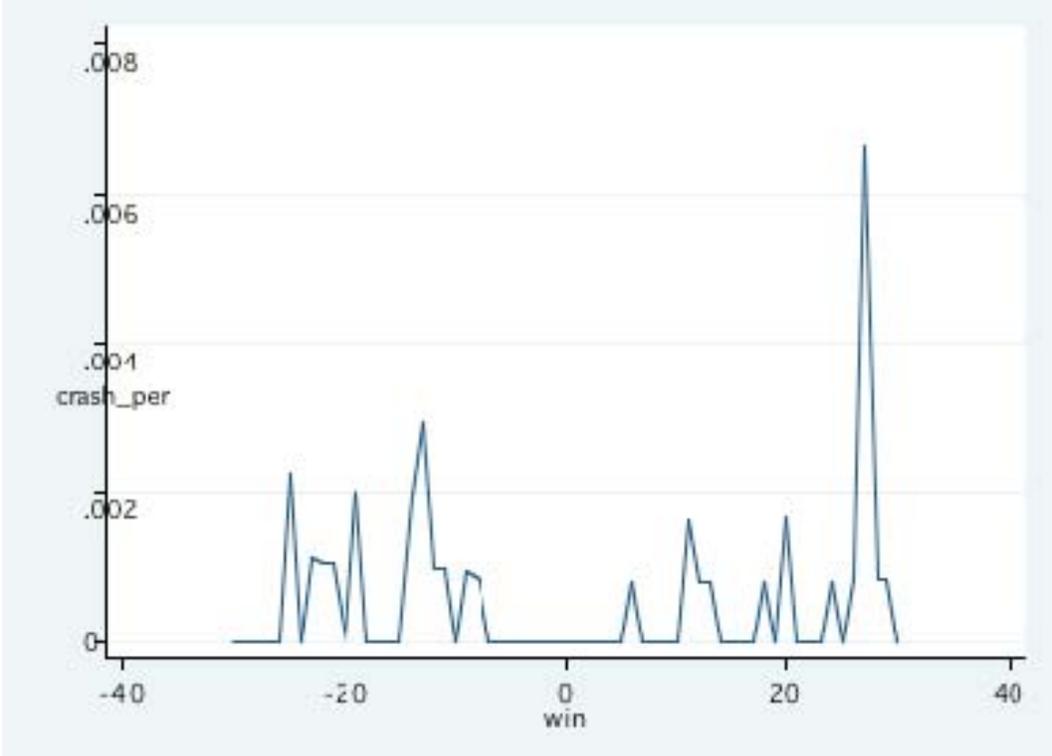


Figure 3: Frequency of Significant Negative Stock Price Movements (excess returns < -20%) around the National Congress of the CCP

Crash Month



## Appendix A

### Variable definitions

Variable	Description	Sources
NCSKEW	This is the negative coefficient of skewness of daily excess return. It is defined as the negative of third moments of daily excess return scaled by cubed standard deviation of daily excess return in the year.	CSMAR
DUVOL	This is the log of ratio standard deviation of return in the down days to that of up days in the year.	CSMAR
SYNCH	This is the synchronicity of the daily stock return with daily market return. It's defined as the $\log(R^2/(1-R^2))$ , where $R^2$ is from the market model of firms daily return against current and one week lagged domestic weekly market return and US weekly market return.	CSMAR
Congress	It is the year of the National Congress of the Chinese Communist Party, which was held once every five years. The congress was held in 1997 and 2002 during our sample period.	
Politician Promotion	This variable captures the turnover of local governors. The turnover is defined as a promotion when he moves to a more senior position than his original one, which includes: 1) promotion within the same province (e.g. promotion to party secretary), 2) promotion to another province (e.g. governor or party secretary position of a larger province), and 3) promotion to the minister level of the central government. Firms that operate in the same region surrounding the turnover years are considered to be those that are affected by politician turnover.	
Politician Demotion	This variable captures the turnover of local governors. The turnover is defined as demotion if the politician moves to a more junior position or loses his current position in the government. The demotion includes the following situations: 1) explicit demotion, 2) lateral movement, 3) retirement, 4) demotion due to health problem, 5) jailed, and 6) demotion to a junior position in the central government. Firms that operate in the same region surrounding the turnover years are considered to be those that are affected by politician turnover.	
Corruption	These are corruption cases involving politicians at or above the bureau level. Firms operating in the same region surrounding the years when the corruption cases are announced are considered to be those that are affected by politicians' corruption.	China Newspaper Database; The Law Yearbook; Xinhua News.
Political Connection	This variable is to capture the political connection of the firm. The firm is defined to be politically connected when its CEO or Chairman has past work experience in the government or current political positions, such as the People's Representative or Member of Chinese People's Political Consultative Conference..	Annual report of company
Marketization Index	This is a comprehensive index that captures the following aspects of regional market development: (1) relationship between government and market, including the role of market in allocating resources and firms' policy burden in addition to taxes; (2) development of non-state business in terms of the ratio of industrial output by private sector to total industrial output; (3) development of product markets in terms of the degree of regional trade barriers; (4) development of factor markets captured by foreign direct investment and labor mobility; and (5) development of market intermediaries and legal environment. These various components of the index are constructed based on prior research such as Beck and Levine (2002), Brandt and Li (2003), Javorcik (2004), Johnson, McMillan, and Woodruff (2002), LaPorta et al. (1999, 2002), and Wurgler (2000). We use the average of the 1999 and 2000 indexes in our analyses.	Fan and Wang (2001)
Market Deregulation Index	The amount of preferential treatments granted to a region by the central government to set up special economic zones during 1978 to 1998.	Demruger et al. (2002)

Fixed assets investment: FDI/SOE	The average ratio of fixed assets investment financed by foreign capital to that financed by state owned enterprises between 1996 and 2003.	China Statistical Yearbook
Non-performing assets	The percentage of non-performing assets out of total equity in SOE in the region between 1997 and 2003	China Information Bank
Unemployment rate	The unemployment rate officially reported for each province, autonomous region, and municipality. The data are available annually.	China Bureau of Statistics
LOG(SIZE)	Log of total market value of equity at the end of the fiscal year.	CSMAR
SIGMA	Standard deviation of daily excess return in the year.	CSMAR
TURNOVER	Average of weekly turnover, which is defined as the total value traded of tradable shares scaled by total value of tradable shares at the end of the week	CSMAR
RET	Annual market-adjusted stock return.	CSMAR
GROWTH	Sales growth, defined as the $\log(\text{sale}_t/\text{sale}_{t-1})$	CSMAR
STD_ROA	The standard deviation of ROA in the past five years including current year with availability of at least three years data.	CSMAR
REGULATED	This is an indicator variable for companies operating in regulated industry.	CSMAR
IND_NUM	The log of total number of listed companies in the two-digit SIC industry at the fiscal year end.	CSMAR
IND_SIZE	The log of total assets of all listed companies in the two-digit SIC industry at the fiscal year end.	CSMAR

**Appendix B**  
**Descriptive statistics for regional institutional variables**

Region	Marketization Index	Deregulation Index	Fixed asset investment FDI/SOE	Non-performing assets (%)	Unemployment rate (%)
Beijing	5.56	0.67	0.37	21.16	0.83
Tianjin	6.65	1.43	0.38	40.86	2.47
Shanghai	6.71	1.76	0.46	21.16	3.45
Chongqi	6.27	-	0.15	74.04	3.70
Hebei	6.36	1.24	0.14	45.94	2.82
Shanxi	4.52	0.33	0.08	38.71	2.18
Neimenggu	4.70	0.67	0.02	47.29	3.50
Liaoning	6.24	1.24	0.23	79.41	4.18
Jilin	5.45	0.67	0.15	204.43	3.13
Heilongjiang	5.01	0.67	0.04	142.71	3.35
Jiangsu	7.85	1.43	0.39	33.66	2.93
Zhejiang	8.15	1.43	0.20	13.77	3.27
Anhui	6.37	0.62	0.12	54.49	3.42
Fujian	7.98	2.71	0.63	21.74	2.72
Jiangxi	5.38	0.33	0.10	99.34	2.64
Shandong	7.07	1.43	0.20	36.31	3.28
Henan	5.58	0.33	0.11	59.39	2.58
Hubei	5.53	0.62	0.15	80.43	3.51
Hunan	5.45	0.33	0.08	78.13	3.93
Guangdong	8.26	2.86	0.61	35.47	2.45
Guangxi	5.96	1.24	0.13	50.14	3.43
Hainan	6.40	1.57	0.35	54.31	3.36
Sichuan	5.62	0.62	0.08	43.57	3.88
Guizhou	4.54	0.33	0.04	101.14	4.20
Yunnan	4.81	0.67	0.05	37.84	2.94
Shannxi	4.08	0.33	0.04	89.23	3.65
Gansu	4.89	0.33	0.05	56.53	3.19
Qinghai	3.17	0.33	0.03	81.47	2.77
Ningxia	3.96	0.33	0.04	50.44	4.62
Xinjiang	2.75	0.67	0.03	68.87	3.77
Tibet	-	0.33	0.01	25.97	3.29

**Table 1**  
**Composition of Sample**

This table presents the distribution of sample firms by region and fiscal year. The sample consists of firms that are ultimately controlled by the local government at fiscal year end, with sufficient financial accounting and stock price data available in the China Security Market and Accounting Research (CSMAR) database.

Region	Year											Total
	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	
Beijing	0	1	2	4	4	4	10	16	18	22	26	107
Tianjin	0	0	2	3	4	6	7	7	9	10	12	60
Shanghai	5	21	49	70	69	70	65	69	64	65	67	614
Chongqi	0	0	3	5	5	8	10	10	14	15	16	86
Hebei	0	0	0	2	2	8	13	16	19	21	21	102
Shanxi	0	0	0	1	1	3	7	11	11	14	15	63
Neimenggu	0	0	0	1	1	5	9	10	11	14	15	66
Liaoning	0	1	5	7	8	14	22	26	26	30	31	170
Jilin	0	0	3	4	5	13	13	14	17	18	20	107
Heilongjiang	0	0	1	4	4	7	9	10	13	13	14	75
Jiangsu	0	0	3	7	7	14	20	21	28	32	36	168
Zhejiang	0	0	4	8	8	11	19	20	21	24	25	140
Anhui	0	0	2	3	3	8	12	17	18	22	24	109
Fujian	0	0	6	7	8	14	22	21	20	20	20	138
Jiangxi	0	0	1	1	1	5	9	8	9	11	11	56
Shandong	0	0	3	4	5	17	25	29	27	33	32	175
Henan	0	0	1	2	3	6	10	13	14	16	19	84
Hubei	0	1	4	5	5	13	20	22	23	28	28	149
Hunan	0	0	2	2	1	6	8	9	14	16	18	76
Guangdong	1	11	28	41	44	52	62	64	63	71	73	510
Guangxi	0	0	1	1	2	5	6	7	8	12	13	55
Hainan	0	2	2	3	3	4	6	7	8	10	10	55
Sichuan	0	0	8	13	19	24	30	37	36	36	36	239
Guizhou	0	0	0	1	1	2	5	5	5	6	8	33
Yunnan	0	0	1	3	3	6	8	10	12	14	12	69
Shannxi	0	0	1	4	4	5	9	11	12	14	14	74
Gansu	0	0	0	1	1	4	7	7	8	11	12	51
Qinghai	0	0	0	0	1	3	4	3	3	3	4	21
Ningxia	0	0	0	0	0	2	3	6	7	8	8	34
Xinjiang	0	0	0	0	0	3	4	4	6	9	11	37
Tibet	0	0	0	0	1	3	4	5	5	5	6	29
Total	6	37	132	207	223	345	458	515	549	623	657	3752

**Table 2**  
**Descriptive Statistics**

This table presents descriptive statistics on the sample of firms and political events included in our study. Panel A presents descriptive financial statistics on our sample of listed Chinese firms that are ultimately controlled by the local government. All financial accounting and stock price data are gathered from the China Security Market and Accounting Research (CSMAR) database. Panel B presents descriptive evidence on the extent of the political connections of the CEO and Chairman of the companies in our sample by fiscal year. Backgrounds on these executives are tracked through CSMAR, where available. Panel C presents the number of corresponding political events (corruption, promotion and demotion) in each region in our sample period. All variables and events are defined in Appendix A

**Panel A: Firm-level characteristics**

	Mean	Median	Std. Dev.	Minimum	Maximum	N
NCSKEW	-0.71	-0.70	0.81	-6.03	3.00	3752
DUVOL	-0.33	-0.35	0.25	-1.08	0.53	3752
FRACTION	0.01	0.00	0.02	0.00	0.10	3752
Log (1+FRACTION)	0.01	0.00	0.02	0.00	0.10	3752
SYNCH	-0.28	-0.26	0.83	-3.89	1.90	3390
LOG(SIZE)	14.60	14.56	0.77	12.26	17.90	3752
SIGMA	0.02	0.02	0.01	0.00	0.07	3752
TURNOVER	0.08	0.06	0.06	0.00	0.55	3752
RET	-0.03	-0.06	0.31	-1.29	1.64	3752
GROWTH	0.09	0.09	0.38	-1.46	1.59	3752
BETA	1.02	1.04	0.22	0.03	1.67	3752
IND_SIZE	8.36	9.14	1.25	4.84	9.51	3390
IND_NUM	5.32	6.11	1.25	1.79	6.47	3390
STD_ROA	0.04	0.02	0.04	0.00	0.39	3390
REGULATED	0.10	0.00	0.30	0.00	1.00	3390

**Panel B: Political connections**

Year	Politically-connected CEO			Politically-connected Chairman		
	NO	Yes	Total	NO	Yes	Total
1999	331	92	423	241	207	448
2000	361	111	472	265	236	501
2001	409	112	521	284	256	540
2002	460	133	593	343	273	616
2003	480	144	624	372	277	649
Total	2041	592	2633	1505	1249	2754

**Table 2 (continued)**  
**Descriptive Statistics**

**Panel C: Distribution of political corruption and turnover events across regions**

Region	Corruption	Promotion
Beijing	3	2
Tianjin	0	2
Shanghai	0	1
Chongqi	2	1
Hebei	3	0
Shanxi	0	1
Neimenggu	0	1
Liaoning	2	0
Jilin	0	1
Heilongjiang	1	2
Jiangsu	0	1
Zhejiang	2	1
Anhui	1	2
Fujian	1	1
Jiangxi	1	0
Shandong	1	1
Henan	0	2
Hubei	3	1
Hunan	0	3
Guangdong	3	0
Guangxi	3	0
Hainan	2	1
Sichuan	0	1
Guizhou	2	1
Yunnan	2	0
Shannxi	0	0
Gansu	1	2
Qinghai	0	2
Ningxia	1	0
Xinjiang	1	0
Tibet	0	0
Total	35	30

**Table 2 (continued)**  
**Descriptive Statistics**

**Panel D: Distribution of political corruption and turnover events over sample period**

Year	Corruption	Promotion
1995	1	-
1996	1	-
1997	2	-
1998	4	7
1999	3	6
2000	6	2
2001	3	4
2002	2	1
2003	6	10
2004	7	-
Total	35	30

**Table 3**  
**Correlation Matrices**

This table presents spearman correlations between the financial characteristics of our sample of state-controlled Chinese firms and provincial institutional characteristics. All financial accounting and stock price data are gathered from the China Security Market and Accounting Research (CSMAR) database. All variables are defined in Appendix A.

**Panel A: Correlation between firm-level crash statistics, financial characteristics, regional institutional characteristics and political event**

	NCSKEW	DUVOL	SYNCH	LOG(SIZE)	SIGMA	TURNOVER	RET	GROWTH	BETA
NCSKEW	1.00								
DUVOL	0.94	1.00							
SYNCH	-0.05	0.02	1.00						
LOG(SIZE)	-0.11	-0.14	-0.07	1.00					
SIGMA	-0.20	-0.29	-0.55	-0.15	1.00				
TURNOVER	-0.21	-0.32	-0.34	-0.09	0.84	1.00			
RET	-0.04	-0.08	-0.06	0.20	-0.07	-0.01	1.00		
GROWTH	-0.01	-0.02	0.01	0.13	-0.12	-0.06	0.20	1.00	
BETA	-0.08	-0.08	0.49	-0.12	-0.04	0.04	-0.08	-0.06	1.00
Marketization Index	-0.05	-0.05	0.03	0.10	0.08	0.09	-0.02	-0.02	-0.01
Market Deregulation Index	-0.08	-0.08	0.05	0.12	0.12	0.13	-0.02	-0.02	0.02
Fixed Assets Investment: FDI/SOE	-0.08	-0.08	0.06	0.13	0.10	0.12	-0.04	-0.02	0.02
Non-performing Assets	0.07	0.07	-0.04	-0.13	-0.06	-0.10	0.00	-0.03	0.04
Unemployment Rate	0.22	0.27	0.02	0.04	-0.40	-0.41	0.11	0.06	0.02
CCP Congress	0.05	0.06	0.43	-0.03	-0.23	-0.15	0.05	0.03	0.19
Regional Promotion	0.04	0.05	0.02	0.08	-0.14	-0.14	0.05	0.00	-0.01
Corruption	0.06	0.08	0.07	-0.05	-0.14	-0.15	0.01	0.00	0.06
Politically connected CEO	0.04	0.04	-0.01	0.01	-0.01	-0.01	-0.01	0.00	-0.03
Politically connected Chairman	0.02	0.01	0.01	0.05	0.00	0.01	0.00	0.00	-0.02

**Table 3 (continued)**  
**Correlation Matrices**

**Panel B: Correlation between regional institutional characteristics and political events**

	Marketization Index	Market Deregulation Index	Fixed Assets Investment: FDI/SOE	Non-performing Assets	Unemployment Rate	CCP Congress	Regional Promotion	Political Corruption
Marketization Index	1.00							
Market Deregulation Index	0.88	1.00						
Fixed Assets Investment: FDI/SOE	0.86	0.92	1.00					
Non-performing Assets	-0.67	-0.66	-0.65	1.00				
Unemployment Rate	-0.28	-0.32	-0.36	0.25	1.00			
CCP Congress	-0.01	-0.01	-0.01	0.00	0.16	1.00		
Regional Promotion	-0.16	-0.19	-0.15	0.01	0.14	0.05	1.00	
Corruption	0.21	0.17	0.12	0.14	0.01	0.09	-0.17	1.00
Politically connected CEO	0.00	-0.02	0.01	0.03	0.03	0.00	-0.07	-0.05
Politically connected Chairman	0.04	0.05	0.06	-0.02	-0.01	-0.01	0.00	-0.03

**Table 4**  
**Distribution of Weekly Excess Stock Returns around Political Event and Non-Event Periods**

This table presents descriptive statistics on excess weekly returns for our sample of state-controlled firms during event and non-event periods. For parsimony, only return realization less than the median observation (i.e., left-tail of the distribution) are tabulated.

**Panel A: National Congress of the Chinese Communist Party**

	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>1%</b>	<b>5%</b>	<b>10%</b>	<b>25%</b>	<b>Median</b>
Non-Congress Years	0.000	0.048	-1.234	-0.114	-0.068	-0.049	-0.024	-0.002
Congress Years	0.000	0.038	-0.521	-0.095	-0.056	-0.040	-0.019	-0.002
Difference (Congress– NonCongress)	0.000	0.010	0.731	0.019	0.012	0.009	0.005	0.000

**Panel B: Promotion Events**

	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>1%</b>	<b>5%</b>	<b>10%</b>	<b>25%</b>	<b>Median</b>
Non-Promotion Period Years	0.000	0.048	-1.234	-0.113	-0.067	-0.048	-0.023	-0.002
Promotion Event Period (t=-2,0)	0.000	0.039	-0.443	-0.096	-0.057	-0.041	-0.020	-0.002
Difference (Promotion-NonPromotion)	0.000	0.009	0.791	0.017	0.010	0.007	0.003	0.000

**Panel C: Revelation of Corruption Cases**

	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>1%</b>	<b>5%</b>	<b>10%</b>	<b>25%</b>	<b>Median</b>
Non-Corruption Period Years	0.000	0.047	-1.234	-0.111	-0.066	-0.048	-0.023	-0.002
Corruption Event Period (t=-1,0)	0.000	0.041	-0.774	-0.101	-0.060	-0.043	-0.021	-0.002
Difference (Corruption-NonCorruption)	0.000	0.006	0.460	0.010	0.006	0.005	0.002	0.000

**Table 5**  
**Influence of political events on the incentive to suppress negative financial information**

The following panels present coefficients from various pooled, cross-sectional estimations of the following model:

$$\text{NCSKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{LOGSIZE}_{i,t} + \beta_3 \text{GROWTH}_{i,t} + \beta_4 \text{SIGMA}_{i,t} \\ + \beta_5 \text{TURNOVER}_{i,t} + \beta_6 \text{TURNOVER}_{i,t-1} + \beta_7 \text{BETA}_{i,t} + \beta_8 \text{RET}_{i,t} + \beta_9 \text{RET}_{i,t-1} + \varepsilon_{i,t}$$

where NCSKEW is the firm's third moment of excess daily stock returns scaled by its cubed standard deviation times minus one and DUVOL is the log of the ratio of standard deviation of returns on down days to the standard deviation of returns on up days. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

**Panel A: National Congress of the Chinese Communist Party**

POLITICAL is an indicator variable equal to one for the years that the National Congress of the Chinese Communist Party was held, zero otherwise.

Dependent Variable:	NCSKEW	DUVOL
POLITICAL <sub>t</sub>	-0.590 (6.85)***	-0.339 (13.16)***
LOGSIZE <sub>t</sub>	-0.158 (4.16)***	-0.062 (5.54)***
GROWTH <sub>t</sub>	-0.039 (1.34)	-0.013 (1.85)*
SIGMA <sub>t</sub>	-23.859 (2.47)**	1.304 (0.67)
TURNOVER <sub>t</sub>	2.351 (2.75)***	0.119 (0.71)
TURNOVER <sub>t-1</sub>	1.094 (2.10)**	0.208 (1.48)
BETA <sub>t</sub>	-0.551 (10.48)***	-0.205 (16.61)***
RET <sub>t</sub>	-0.165 (4.46)***	-0.116 (9.87)***
RET <sub>t-1</sub>	0.058 (1.46)	0.028 (2.46)**
Constant	2.637 (3.92)***	0.877 (4.65)***
Observations	3752	3752
Adjusted R-squared	0.16	0.28

\*\*\*, \*\*, \* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 5 (continued)**  
**Influence of political events on the incentive to suppress negative financial information**

**Panel B: Political promotion in the region**

POLITICAL is an indicator variable equal to one for the years within the corresponding period around a promotion event (with year zero being the year of the promotion), zero otherwise.

Dependent Variable:	Pre-promotion period [ -2 , 0 ]		Post-promotion period [ 1 , 2 ]	
	NCSKEW	DUVOL	NCSKEW	DUVOL
POLITICAL <sub>t</sub>	-0.069 (2.12)**	-0.018 (2.16)**	0.020 (0.58)	0.004 (0.39)
LOGSIZE <sub>t</sub>	-0.154 (3.95)***	-0.061 (5.31)***	-0.156 (4.05)***	-0.061 (5.46)***
GROWTH <sub>t</sub>	-0.037 (1.22)	-0.012 (1.57)	-0.036 (1.20)	-0.012 (1.56)
SIGMA <sub>t</sub>	-23.779 (2.46)**	1.417 (0.73)	-23.439 (2.39)**	1.501 (0.75)
TURNOVER <sub>t</sub>	2.435 (2.95)***	0.158 (0.99)	2.412 (2.90)***	0.152 (0.94)
TURNOVER <sub>t-1</sub>	1.181 (2.14)**	0.244 (1.78)*	1.147 (2.12)**	0.235 (1.70)*
BETA <sub>t</sub>	-0.560 (10.56)***	-0.209 (16.47)***	-0.554 (10.38)***	-0.207 (16.36)***
RET <sub>t</sub>	-0.167 (4.34)***	-0.116 (9.61)***	-0.167 (4.41)***	-0.116 (9.79)***
RET <sub>t-1</sub>	0.043 (0.92)	0.020 (1.79)*	0.045 (0.98)	0.021 (1.85)*
Constant	2.176 (2.71)**	0.641 (3.07)***	2.202 (2.75)**	0.649 (3.12)***
Observations	3752	3752	3752	3752
Adjusted R-squared	0.16	0.28	0.16	0.28

\*\*\*,\*\*,\* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 5 (continued)**  
**Influence of political events on the incentive to suppress negative financial information**

**Panel C: Identification of political corruption**

POLITICAL is an indicator variable equal to one for the years within the corresponding period related to the unraveling of corruption, and zero otherwise.

Dependent Variable:	Pre-corruption period [-1,0]		Post-corruption period [1,2]	
	NCSKEW	DUVOL	NCSKEW	DUVOL
POLITICAL <sub>t</sub>	-0.060 (2.31)**	-0.007 (0.87)	0.050 (1.66)	0.011 (1.51)
LOGSIZE <sub>t</sub>	-0.159 (4.19)***	-0.062 (5.57)***	-0.157 (4.06)***	-0.061 (5.44)***
GROWTH <sub>t</sub>	-0.038 (1.26)	-0.012 (1.60)	-0.035 (1.16)	-0.012 (1.53)
SIGMA <sub>t</sub>	-23.635 (2.39)**	1.471 (0.74)	-23.684 (2.44)**	1.450 (0.74)
TURNOVER <sub>t</sub>	2.433 (2.94)***	0.155 (0.96)	2.438 (2.98)***	0.158 (0.99)
TURNOVER <sub>t-1</sub>	1.111 (2.04)*	0.230 (1.66)	1.133 (2.14)**	0.232 (1.70)*
BETA <sub>t</sub>	-0.551 (10.24)***	-0.207 (16.09)***	-0.560 (10.58)***	-0.208 (16.37)***
RET <sub>t</sub>	-0.167 (4.57)***	-0.116 (9.90)***	-0.167 (4.41)***	-0.116 (9.75)***
RET <sub>t-1</sub>	0.045 (1.00)	0.021 (1.85)*	0.046 (1.00)	0.021 (1.86)*
Constant	2.246 (2.79)***	0.656 (3.15)***	2.218 (2.80)***	0.652 (3.14)***
Observations	3752	3752	3752	3752
Adjusted R-squared	0.16	0.28	0.16	0.28

\*\*\*,\*\*,\* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 6**  
**Impact of regional institutions on political incentives to suppress negative financial information**

The following panels present select coefficients from pooled, cross-sectional estimations of the following model:

$$\begin{aligned} \text{NSCKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{INSTITUTION}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{INSTITUTION}_{i,t} \\ & + \beta_4 \text{LOGSIZE}_{i,t} + \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{SIGMA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{TURNOVER}_{i,t-1} + \beta_9 \text{BETA}_{i,t} \\ & + \beta_{10} \text{RET}_{i,t} + \beta_{11} \text{RET}_{i,t-1} + \epsilon_{i,t} \end{aligned}$$

where NCSKEW is the firm's third moment of excess daily stock returns scaled by its cubed standard deviation times minus one and DUVOL is the log of the ratio of standard deviation of returns on down days to the standard deviation of returns on up days. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

**Panel A: National congress of Chinese Communist Party**

POLITICAL is an indicator variable equal to one for years when national congress of Chinese Communist Party was held, zero otherwise.

Dependent Variable:	NCSKEW				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	-0.477 (2.23)**	-0.528 (3.91)***	-0.487 (3.11)***	-0.654 (8.68)***	-0.545 (2.96)***
INSTITUTION	0.030 (2.89)***	0.048 (2.64)**	0.230 (3.58)***	-0.001 (2.72)**	0.015 (0.90)
POLITICAL*INSTITUTION	-0.019 (0.75)	-0.050 (1.19)	-0.351 (1.67)	0.001 (1.19)	-0.013 (0.32)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.16	0.16	0.16	0.16	0.15

Dependent Variable:	DUVOL				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	-0.314 (5.20)***	-0.318 (8.43)***	-0.312 (6.91)***	-0.355 (17.44)***	-0.316 (6.02)***
INSTITUTION	0.010 (2.96)***	0.015 (2.41)**	0.072 (3.22)***	-0.000 (3.24)***	0.007 (1.30)
POLITICAL*INSTITUTION	-0.005 (0.64)	-0.014 (1.10)	-0.097 (1.58)	0.000 (1.07)	-0.007 (0.60)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.28	0.28	0.28	0.28	0.27

\*\*\* \*\* \* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 6 (continued)****Impact of regional institutions on political incentives to suppress negative financial information****Panel B: Political promotion in the region**

POLITICAL is an indicator variable equal one for years within the three years preceding and including the year of promotion, zero otherwise.

Dependent Variable:	NCSKEW				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	0.192 (1.31)	0.059 (1.31)	0.044 (1.14)	-0.186 (3.80)***	-0.094 (1.36)
INSTITUTION	0.032 (2.29)**	0.050 (1.92)*	0.231 (2.54)**	-0.001 (3.75)***	0.005 (0.31)
POLITICAL*INSTITUTION	-0.040 (1.72)*	-0.101 (2.81)***	-0.424 (3.35)***	0.002 (3.64)***	0.008 (0.32)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.16	0.16	0.16	0.16	0.15

Dependent Variable:	DUVOL				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	0.029 (0.63)	0.014 (1.03)	0.013 (1.26)	-0.048 (3.72)***	-0.039 (2.52)**
INSTITUTION	0.010 (2.26)**	0.015 (1.83)*	0.073 (2.36)**	-0.000 (4.03)***	0.001 (0.18)
POLITICAL*INSTITUTION	-0.007 (0.97)	-0.024 (2.42)**	-0.115 (3.09)***	0.001 (3.34)***	0.006 (1.14)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.28	0.28	0.28	0.28	0.28

\*\*\*, \*\*, \* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 6 (continued)****Impact of regional institutions on political incentives to suppress negative financial information****Panel C: Revelation of political corruption**

POLITICAL is indicator variable equal one for years within the period of two years preceding and including the year of unraveling of political corruption, zero otherwise.

Dependent Variable:	NCSKEW				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	-0.047 (0.29)	-0.082 (1.20)	-0.071 (1.37)	-0.069 (1.09)	-0.161 (1.35)
INSTITUTION	0.034 (2.61)**	0.050 (2.46)**	0.173 (2.01)*	-0.001 (2.96)***	-0.002 (0.07)
POLITICAL*INSTITUTION	-0.005 (0.22)	-0.001 (0.03)	0.005 (0.03)	0.000 (0.17)	0.029 (0.85)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.16	0.16	0.16	0.16	0.15

Dependent Variable:	DUVOL				
	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
POLITICAL	0.020 (0.44)	-0.007 (0.36)	-0.001 (0.10)	-0.009 (0.49)	-0.022 (0.63)
INSTITUTION	0.011 (3.36)***	0.016 (3.15)***	0.064 (3.30)***	-0.000 (4.00)***	0.002 (0.32)
POLITICAL*INSTITUTION	-0.005 (0.74)	-0.006 (0.48)	-0.028 (0.63)	0.000 (0.11)	0.004 (0.45)
Observations	3723	3666	3752	3752	3744
Adjusted R-squared	0.28	0.28	0.28	0.28	0.28

\*\*\*,\*\*,\* The estimated coefficient is significantly different than zero at the one, five and ten percent level (two-tailed test), respectively.

**Table 7**  
**Influence of political connections on the incentive to suppress negative financial information around political events**

The following panels present select coefficients from pooled, cross-sectional estimations of the following model:

$$\begin{aligned} \text{NCSKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{CONNECT}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{CONNECT}_{i,t} + \beta_4 \text{LOGSIZE}_{i,t} \\ & + \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{SIGMA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{TURNOVER}_{i,t-1} + \beta_9 \text{BETA}_{i,t} \\ & + \beta_{10} \text{RET}_{i,t} + \beta_{11} \text{RET}_{i,t-1} + \epsilon_{i,t} \end{aligned}$$

where NCSKEW is the firm's third moment of excess daily stock returns scaled by its cubed standard deviation times minus one and DUVOL is the log of the ratio of standard deviation of returns on down days to the standard deviation of returns on up days. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. CONNECT is an indicator variable equal to one if the firm's CEO (panel A) or Chairman (panel B) is politically-connected. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

**Panel A: Firms with a politically-connected CEO**

Dependent Variable:	NCSKEW				
	National Congress	Pre-Promotion	Post-Promotion	Pre-Corruption	Post-Corruption
POLITICAL <sub>t</sub>	-0.163 (2.21)**	-0.061 (1.71)*	0.084 (2.25)**	-0.062 (1.52)	0.048 (1.52)
CONNECT	0.091 (2.89)***	0.087 (2.56)**	0.169 (5.91)***	0.106 (3.43)***	0.117 (3.85)***
POLITICAL*CONNECT	0.130 (1.68)	0.106 (1.50)	-0.223 (3.92)***	0.046 (0.92)	0.031 (0.39)
Observations	2633	2633	2633	2633	2633
Adjusted R-squared	0.10	0.10	0.10	0.10	0.10

Dependent Variable:	DUVOL				
	National Congress	Pre-Promotion	Post-Promotion	Pre-Corruption	Post-Corruption
POLITICAL <sub>t</sub>	-0.020 (1.10)	-0.017 (1.83)*	0.024 (1.96)*	-0.006 (0.60)	0.012 (1.35)
CONNECT	0.022 (1.81)*	0.018 (1.34)	0.044 (4.07)***	0.026 (2.24)**	0.028 (2.36)**
POLITICAL*CONNECT	0.028 (1.30)	0.031 (1.19)	-0.070 (3.07)***	0.006 (0.37)	0.001 (0.06)
Observations	2633	2633	2633	2633	2633
Adjusted R-squared	0.24	0.24	0.24	0.24	0.24

**Table 7 (continued)****Influence of political connections on the incentive to suppress negative financial information around political events****Panel B: Firms with a politically-connected Chairman**

Dependent Variable:	NCSKEW				
	National Congress	Pre-Promotion	Post-Promotion	Pre-Corruption	Post-Corruption
POLITICAL <sub>t</sub>	-0.126 (1.50)	-0.099 (2.47)**	0.099 (2.54)**	-0.031 (0.70)	0.049 (0.86)
CONNECT	0.057 (2.18)**	0.026 (0.94)	0.081 (3.06)***	0.055 (1.84)*	0.049 (1.79)*
POLITICAL*CONNECT	-0.024 (0.35)	0.076 (1.73)*	-0.141 (2.72)**	-0.013 (0.29)	0.008 (0.10)
Observations	2754	2754	2754	2754	2754
Adjusted R-squared	0.10	0.10	0.10	0.10	0.10

Dependent Variable:	DUVOL				
	National Congress	Pre-Promotion	Post-Promotion	Pre-Corruption	Post-Corruption
POLITICAL <sub>t</sub>	-0.011 (0.49)	-0.027 (2.93)***	0.030 (2.67)**	0.008 (0.66)	0.009 (0.66)
CONNECT	0.017 (1.71)*	0.005 (0.50)	0.024 (2.45)**	0.018 (1.53)	0.011 (0.94)
POLITICAL*CONNECT	-0.015 (0.78)	0.024 (1.43)	-0.051 (2.57)**	-0.017 (0.97)	0.010 (0.40)
Observations	2754	2754	2754	2754	2754
Adjusted R-squared	0.25	0.25	0.25	0.25	0.25

**Table 8**  
**Influence of political events on the incentive to suppress negative financial information:**  
**Evidence from Frequency of Crash Weeks**

The following panels present select coefficients from pooled, cross-sectional estimations of the following model:

$$\text{Log}(1+\text{FRACTION}) = \alpha + \beta_1\text{POLITICAL}_{i,t} + \beta_2\text{INSTITUTION}_{i,t} + \beta_3\text{POLITICAL}_{i,t} * \text{INSTITUTION}_{i,t} \\ + \beta_4\text{LOGSIZE}_{i,t} + \beta_5\text{GROWTH}_{i,t} + \beta_6\text{SIGMA}_{i,t} + \beta_7\text{TURNOVER}_{i,t-1} + \beta_8\text{MTB}_{i,t} + \beta_9\text{RET}_{i,t-1} + \varepsilon_{i,t}$$

where FRACTION is the number of weeks experiencing a negative return greater than 10% scaled by the number of trading weeks in the fiscal year. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

	Baseline Model	Marketization Index	Market Deregulation Index	Fixed assets investment: FDI/SOE	Non-performing assets	Unemployment rate
<b>Panel A: National congress of Chinese Communist Party</b>						
POLITICAL <sub>t</sub>	-0.014 (4.94)***	-0.009 (3.01)***	-0.012 (4.98)***	-0.012 (5.56)***	-0.013 (4.45)***	-0.015 (3.80)***
INSTITUTION	-	0.000 (1.72)*	0.001 (1.49)	0.002 (1.54)	0.000 (0.75)	-0.000 (0.97)
POLITICAL*INSTITUTION	-	-0.001 (1.51)	-0.001 (2.05)**	-0.004 (1.34)	-0.000 (1.26)	0.000 (0.45)
Observations	3752	3723	3666	3752	3752	3744
Adjusted R-squared	0.45	0.46	0.46	0.45	0.45	0.46
<b>Panel B: Political promotion (pre-period)</b>						
POLITICAL	-0.000 (0.72)	0.003 (0.76)	0.001 (1.14)	0.002 (1.50)	-0.001 (0.75)	-0.002 (1.52)
INSTITUTION	-	0.000 (1.63)	0.001 (1.75)*	0.003 (2.58)**	-0.000 (0.09)	-0.001 (1.82)*
POLITICAL*INSTITUTION	-	-0.000 (0.90)	-0.002 (2.09)**	-0.008 (2.99)***	0.000 (0.37)	0.001 (1.21)
Observations	3752	3723	3666	3752	3752	3744
Adjusted R-squared	0.46	0.46	0.46	0.46	0.46	0.46
<b>Panel C: Revelation of political corruption (pre-period)</b>						
POLITICAL	-0.000 (0.91)	0.003 (1.13)	-0.000 (0.07)	-0.001 (0.69)	0.000 (0.42)	-0.000 (0.24)
INSTITUTION	-	0.000 (1.99)*	0.000 (0.88)	0.002 (1.02)	0.000 (0.81)	-0.000 (0.75)
POLITICAL*INSTITUTION	-	-0.001 (1.35)	-0.000 (0.36)	0.000 (0.04)	-0.000 (1.05)	-0.000 (0.02)
Observations	3752	3723	3666	3752	3752	3744
Adjusted R-squared	0.46	0.46	0.46	0.46	0.46	0.46

**Table 9**  
**Impact of political incentives on the incentive to release firm-specific information**

**Panel A: Impact of political incentives on stock return synchronicity**

This panel presents coefficients from various pooled, cross-sectional estimations of the following model:

$$\text{SYNCH}_{i,t} = \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{LOGSIZE}_{i,t} + \beta_3 \text{GROWTH}_{i,t} + \beta_4 \text{STD\_ROA}_{i,t} \\ + \beta_5 \text{TURNOVER}_{i,t} + \beta_6 \text{REGULATED}_{i,t-1} + \beta_7 \text{IND\_NUM}_{i,t} + \beta_8 \text{IND\_SIZE}_{i,t} + \varepsilon_{i,t}$$

where SYNCH is  $\log(R^2/(1-R^2))$ , where  $R^2$  is from estimation of market model of firm weekly return against current and one week lagged domestic market return and US market return. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

	CCP Congress	Pre- Promotion [-2,0]	Post- Promotion [1,2]	Pre- Corruption [-1,0]	Post- Corruption [1,2]
POLITICAL	0.581 (5.62)***	-0.006 (0.17)	-0.030 (0.96)	0.087 (2.26)**	0.031 (0.78)
SIZE	-0.081 (2.77)***	-0.081 (2.82)***	-0.082 (2.85)***	-0.077 (2.47)**	-0.080 (2.66)**
GROWTH	-0.056 (1.84)*	-0.056 (1.87)*	-0.056 (1.87)*	-0.058 (1.94)*	-0.056 (1.85)*
STD_ROA	-3.841 (11.20)***	-3.845 (11.62)***	-3.843 (11.43)***	-3.914 (12.34)***	-3.871 (11.46)***
TURNOVER	-6.437 (14.02)***	-6.438 (13.99)***	-6.462 (14.08)***	-6.377 (13.48)***	-6.424 (13.83)***
REGULATED	0.115 (1.72)*	0.115 (1.71)*	0.116 (1.74)*	0.120 (1.74)*	0.117 (1.75)*
IND_NUM	-2.064 (1.85)*	-2.048 (1.81)*	-2.052 (1.81)*	-1.838 (1.62)	-1.953 (1.70)*
IND_SIZE	2.053 (1.85)*	2.037 (1.80)*	2.042 (1.81)*	1.826 (1.61)	1.943 (1.70)*
Constant	-4.530 (1.29)	-4.987 (1.40)	-4.980 (1.41)	-4.436 (1.24)	-4.720 (1.32)
Observations	3390	3390	3390	3390	3390
Adjusted R-squared	0.51	0.51	0.51	0.51	0.51

**Table 9 (continued)****Impact of political incentives on the incentive to release firm-specific information****Panel B: Impact of political incentives conditional on regional institutions**

This panel presents coefficients from various pooled, cross-sectional estimations of the following model:

$$\begin{aligned} \text{SYNCH}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{INSTITUTION}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{INSTITUTION}_{i,t} + \beta_4 \text{LOGSIZE}_{i,t} \\ & + \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{STD\_ROA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{REGULATED}_{i,t-1} + \beta_9 \text{IND\_NUM}_{i,t} \\ & + \beta_9 \text{IND\_SIZE}_{i,t} + \varepsilon_{i,t} \end{aligned}$$

where SYNCH is  $\log(R^2/(1-R^2))$ , where  $R^2$  is from estimation of market model of firm weekly return against current and one week lagged domestic market return and US market return. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. INSITITUTIONS is marketization index. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

	CCP Congress	Pre-Politician's promotion [-2,0]	Post- Politician's Promotion [1,2]	Pre-Corruption Period [-1,0]	Post- Corruption Period [1,2]
POLITICAL	0.502 (3.95)***	0.060 (0.26)	0.001 (0.01)	-0.158 (0.94)	0.033 (0.22)
INSTITUTION	0.018 (1.49)	0.023 (1.89)*	0.020 (1.41)	0.005 (0.42)	0.021 (1.40)
POLITICAL*INSITUTION	0.010 (0.63)	-0.011 (0.28)	-0.004 (0.17)	0.035 (1.38)	-0.004 (0.21)
SIZE	-0.091 (3.10)***	-0.091 (3.16)***	-0.092 (3.16)***	-0.087 (2.81)***	-0.091 (3.02)***
GROWTH	-0.044 (1.60)	-0.044 (1.60)	-0.044 (1.60)	-0.046 (1.64)	-0.044 (1.58)
STD_ROA	-3.916 (13.09)***	-3.927 (13.61)***	-3.916 (13.16)***	-3.963 (13.35)***	-3.920 (13.03)***
TURNOVER	-6.502 (14.40)***	-6.504 (14.37)***	-6.521 (14.28)***	-6.490 (14.06)***	-6.501 (14.30)***
REGULATED	0.117 (1.74)*	0.118 (1.72)*	0.118 (1.76)*	0.119 (1.73)*	0.118 (1.76)*
IND_NUM	-2.059 (1.74)*	-2.011 (1.68)	-2.030 (1.70)	-1.815 (1.52)	-2.028 (1.72)*
IND_SIZE	2.049 (1.74)*	2.001 (1.67)	2.020 (1.69)	1.804 (1.51)	2.018 (1.72)*
Constant	-4.478 (1.20)	-4.867 (1.29)	-4.893 (1.30)	-4.243 (1.12)	-4.910 (1.33)
Observations	3361	3361	3361	3361	3361
Adjusted R-squared	0.52	0.52	0.52	0.52	0.52

**Table 10**  
**Influence of Hong Kong listing on the incentive to suppress negative financial information around political events**

The following panels present select coefficients from pooled, cross-sectional estimations of the following model:

$$\begin{aligned} \text{NCSKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = & \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{HKLIST}_{i,t} + \beta_3 \text{POLITICAL}_{i,t} * \text{HKLIST}_{i,t} + \beta_4 \text{LOGSIZE}_{i,t} + \\ & \beta_5 \text{GROWTH}_{i,t} + \beta_6 \text{SIGMA}_{i,t} + \beta_7 \text{TURNOVER}_{i,t} + \beta_8 \text{TURNOVER}_{i,t-1} + \beta_9 \text{BETA}_{i,t} \\ & + \beta_{10} \text{RET}_{i,t} + \beta_{11} \text{RET}_{i,t-1} + \varepsilon_{i,t} \end{aligned}$$

where NCSKEW is the firm's third moment of excess daily stock returns scaled by its cubed standard deviation times minus one and DUVOL is the log of the ratio of standard deviation of returns on down days to the standard deviation of returns on up days. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. HKLIST is an indicator variable equal to one if the firm's equity is traded as an H-share on the Hong Kong Stock Exchange. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

Dependent Variable:	NCSKEW			DUVOL		
	CCP Congress	Pre-promotion	Pre-Corruption	CCP Congress	Pre-promotion	Pre-Corruption
POLITICAL	-0.571 (7.00)***	-0.060 (1.82)*	-0.060 (2.28)**	-0.334 (13.99)***	-0.016 (1.87)*	-0.010 (1.01)
HKLIST	0.075 (1.05)	0.009 (0.09)	0.074 (0.82)	0.031 (1.27)	0.013 (0.40)	0.026 (0.79)
POLITICAL*HKLIST	-0.530 (3.31)***	-0.014 (0.12)	-0.303 (1.29)	-0.149 (3.81)***	0.011 (0.32)	-0.037 (0.60)
Observations	3752	3739	3739	3752	3739	3739
Adjusted R-squared	0.16	0.14	0.14	0.28	0.23	0.23

**Table 11**  
**Impact of political events on the incentive of family-owned Chinese firms to suppress financial information**

This table presents coefficients from various pooled, cross-sectional estimations of the following model in a sample of family firms:

$$\text{NCSKEW}_{i,t} \text{ or } \text{DUVOL}_{i,t} = \alpha + \beta_1 \text{POLITICAL}_{i,t} + \beta_2 \text{LOGSIZE}_{i,t} + \beta_3 \text{GROWTH}_{i,t} + \beta_4 \text{SIGMA}_{i,t} \\ + \beta_5 \text{TURNOVER}_{i,t} + \beta_6 \text{TURNOVER}_{i,t-1} + \beta_7 \text{BETA}_{i,t} + \beta_8 \text{RET}_{i,t} + \beta_9 \text{RET}_{i,t-1} + \varepsilon_{i,t}$$

where NCSKEW is the negative of the firm's third moment of daily stock returns scaled by its cubed standard deviation and DUVOL is the log of the ratio of standard deviation of returns on down days to the standard deviation of returns on up days. POLITICAL is an indicator variable equal to one if the firm-year relates to a specific political event. All other variables are defined in Appendix A. T-statistics derived using clustered standard errors by region are presented in parentheses. Models include annual fixed effects [coefficients not reported].

Dependent Variable:	NCSKEW			DUVOL		
	CCP Congress	Pre-promotion	Pre-Corruption	CCP Congress	Pre-promotion	Pre-Corruption
POLITICAL	-0.929 (6.36)***	0.036 (0.89)	-0.025 (0.56)	-0.400 (6.31)***	-0.003 (0.17)	0.013 (0.99)
LOGSIZE <sub>t</sub>	0.008 (0.18)	0.007 (0.16)	0.007 (0.16)	-0.029 (2.09)**	-0.029 (2.10)**	-0.030 (2.12)**
GROWTH <sub>t</sub>	-0.063 (1.23)	-0.064 (1.24)	-0.062 (1.20)	-0.001 (0.09)	-0.001 (0.08)	-0.001 (0.05)
SIGMA <sub>t</sub>	39.273 (2.59)**	39.304 (2.58)**	39.317 (2.58)**	11.199 (3.71)***	11.196 (3.71)***	11.126 (3.71)***
TURNOVER <sub>t</sub>	-0.223 (0.15)	-0.243 (0.16)	-0.226 (0.15)	-0.115 (0.29)	-0.114 (0.29)	-0.113 (0.28)
TURNOVER <sub>t-1</sub>	1.296 (2.46)**	1.263 (2.37)**	1.310 (2.47)**	0.394 (1.86)*	0.396 (1.87)*	0.385 (1.83)*
BETA <sub>t</sub>	-0.327 (1.96)*	-0.327 (1.97)*	-0.328 (1.97)*	-0.186 (4.82)***	-0.186 (4.80)***	-0.186 (4.83)***
RET <sub>t</sub>	-0.340 (4.64)***	-0.340 (4.58)***	-0.340 (4.58)***	-0.155 (8.36)***	-0.155 (8.34)***	-0.155 (8.42)***
RET <sub>t-1</sub>	-0.082 (1.39)	-0.080 (1.37)	-0.083 (1.42)	-0.031 (1.57)	-0.031 (1.58)	-0.031 (1.53)
Constant	0.205 (0.23)	-1.426 (1.49)	-1.460 (1.53)	0.240 (1.02)	-0.281 (1.14)	-0.273 (1.12)
Observations	617	617	617	617	617	617
Adjusted R-squared	0.21	0.21	0.21	0.31	0.31	0.31