

## 2019-2020 AFAANZ Research Grant Outcome report

### (1) Recipients:

Dr Zhaohua Li, Senior Lecturer at Lincoln University, New Zealand. [Zhaohua.li@lincoln.ac.nz](mailto:Zhaohua.li@lincoln.ac.nz)

Dr Xiaofei Pan, Senior Lecturer at University of Wollongong, Australia. [xpan@uow.edu.au](mailto:xpan@uow.edu.au)

(2) Project title: How do firms respond to corruption in China? Evidence from firm's spending on building political connection.

(3) Updated Project summary: Using Chinese corruption convictions to measure the level of political corruption at the province level, we find that firms located in more corrupt provinces invest more in building connections and hold more cash than firms located in less corrupt provinces. These results are robust to the instrumental variable approach, adjacent province matching and propensity score matching. We also show that the effect of political corruption is more pronounced in privately controlled firms, smaller firms, firms with financial constraints and firms without political connections. Overall, the evidence from China is consistent with the view that firms respond to political corruption by maintaining adequate liquidity to purchase political favors, which contrasts with the evidence from the US.

(4) Funds granted: A\$4000

(5) Expenditure of Funds:

Description	Amount	Transaction Date	Reference	Period
Research project	4,363.48	21/10/2019	157251-Receipt of grant	10/2019
FOREX FEES D108486 13/11	-113.72	30/11/2019	GS161-Currency translation fee	11/2019
Noosuwan Chutarat	-529.85	10/12/2020	Research assistant	10/2020
Noosuwan Chutarat	-51.02	12/07/2020	Research assistant	7/2020
Noosuwan Chutarat	-637.78	12/07/2020	Research assistant	7/2020
Noosuwan Chutarat	-27.47	31/05/2020	Research assistant	5/2020
Noosuwan Chutarat	-343.42	31/05/2020	Research assistant	5/2020
ZHAOHUA LI	-1,326.46	10/02/2020	WOLLONGONG2	2/2020
ZHAOHUA LI	-173.04	18/11/2019	CARTRIDGE	1/2019
ZHAOHUA LI	-600.00	17/02/2020	COPY EDITING	2/2020
ZHAOHUA LI	-151.26	01/10/2020	JOURNALPAPER SUBMISSION	10/2020
Sum	409.46		Pass to the Faculty's research funds pool	10/2020

(6) Outcomes: This paper with a slightly different title “political corruption and relationship investment in China” was presented at research seminars at Lincoln University, university of Wollongong and Griffith University. We incorporated the comments received at seminars and submitted to Journal of Corporate Finance on 27 October 2020.

(7) Future intention: We hope to receive comments from JCF. Then we will revise the paper based on comments.

(8) Summary of outcomes and benefits:

This study used entertainment and travel cost (ETC) to proxy for the relationship building between corporate and politicians. The finding of this paper will have implications for auditors, policy makers and managers/entrepreneurs. For auditors of Chinese firms, they can pay special attention to the ETC accounts by comparing a firm's ETC to industry average. Abnormal ETC in highly corrupted areas could raise a red flag to auditors. For the public policy makers, it can help them to make China's anti-corruption campaign more effective by targeting firms that have abnormally high ETC expenses and tracing the ETC transactions to individuals. For managers and entrepreneurs, the corruption map produced in this study will help them to decide where the corporation should be registered. A district with low corruption conviction cases can be more attractive to managers/entrepreneurs who have no political resources.