

A Study of Influence Mechanism of Political Connection on Enterprise Performance—Based on the Perspective of Social Network Theory

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Received 9 July 2016; accepted 30 July 2016; published 2 August 2016

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Abstract

By using the three theories of social network theory: the strong and weak tie theory, the structural hole theory and the social capital theory, analyzing the influence mechanism of political connection on enterprise performance, the study found that, regardless of whether enterprise is in a dense or a sparse relationship zone, the political connection can help enterprise to obtain more resources. The influence mechanism of political connection on enterprise performance is mainly to help enterprises to obtain the heterogeneity resources and to broaden the enterprises' channels to obtain resources. In addition, the political connection is mainly related to the acquisition of resources, but when the tie between the enterprise and the government continues to strengthen, the political connection will affect resources allocation of enterprise. The paper provides explanation for the diversified conclusion of the research about the influence of political connection on the enterprise performance in a certain degree.

Keywords

Political Connection, Enterprise Performance, Social Network, Strong and Weak Tie, Social Capital, Structural Hole

1. Introduction

In recent years, China's comprehensive strength continues to rise; the politics, economy, culture, institution and other environments are also changing. Today, China is in the economic transition period; whether enterprise that

is economic entity of a country can adapt to the changes of environment not only is related to development of enterprise but also has an important influence on economy of country. There are scholars who believe that the political connection can be used as an alternative mechanism to provide a good external protection for the development of enterprises [1]. Therefore, political connection is an important tool for enterprises to adapt to institution environment and its influence cannot be ignored for the development of enterprises. There are a great many of studies on influence of political connection on enterprise performance. By combing the existing literature we found that research about the influence of political connection on the performance of enterprises can be seen as hundred schools. The conclusion of the influence of political connection on firm performance mainly includes the positive effect, negative effect, an inverted U-shaped relationship, and no influence. The existing researches mostly explore the relationship between political connections and enterprise performance by the empirical methods; the different conclusions may be caused by different measurement methods for the political connection and enterprise performance as well as the difference of sample selection. The different conclusions will cause some obstacles to practice guidance for enterprises. The study by the related theory to analyze the general influence mechanism of political connection on enterprise performance is still relatively less, and this kind of research not only can explain the variation in the existing research on the relationship of political connection and enterprise performance, but also could fill the gaps in the theoretical research, and is also very beneficial to explain the influence mechanism of political connection on enterprise performance and then to guide enterprises.

2. Political Connection

Although the political connection has been widely concerned by the academic circles, but the definition of the political connection has not reached a consensus. The political connections had ever been seen as a close relationship between the company's shareholders or executives and the heads of government or political groups. Fan, Wong and Zhang (2007) believe that if the company's president has the work experience in government or military, then the company has a political connection [2]. Yu Guiming and Pan Hongbo believe that if the chairman or general manager of company has had the experience in government, or served as NPC deputies or CPPCC members, then the company has a political connection [3]. Dang Li, Yang Ruilong and Yang Jidong pointed out that the political connection refers to that the enterprise maintain good relationship with government [4]. To sum up, the political connection refers to that the personnel in the high level of enterprise have served in the government (including the incumbent and former) or NPC deputies or CPPCC members. There are also great differences in the measurement of political connection. Some scholars measure the political connection by the proportion of the number of directors with political background in the number of directors of board [5]. Faccio measures the political connection through that whether executive or major shareholder serves as (including ever serve) government officials, senator etc. [6]. Du Xingqiang, Guo Jian Hua, Lei Yu measure political connection through making corresponding assignment to political connections of different levels, such as from the provincial and ministerial level, the vice ministerial level to bureau level, correspondingly give 10, 9, 8 point [7].

3. The Influence of Political Connection on Enterprise Performance

At present, there is no unified conclusion about the influence of political connection on enterprise performance, including the positive impact, negative impact, inverted U relationship, and no influence.

3.1. Positive Influence

Many researches have found that political connection has a positive effect on firm performance. For example, The study of Niessen and Ruenzi that take the German companies as samples found that enterprise that have political connection have higher performance than the enterprise that have no political connection [8]. Faccio through the study on more than 20202 listing corporations from a number of countries found that the degree of company's political connection improve the cumulative rate of return on the stock [6]. Khwaja and Mian through the study on the Pakistan enterprises found that the enterprises that have political connection often have better performance than those who do not have political connection. Mitton and Johnson [9] found that after Malaysia government implemented capital controls in September 1998, companies those had political association with President Mahathir obtained maximum benefit, after the implementation of the capital controls the market value of these companies get a substantial increase, amplitude reached about 32% [10]. Wong and Opper

found that in the private sector, entrepreneurs who have party membership will actively promote business performance [11]. Slinko *et al.* found that in Russia, if the company has the relatively larger political influence then its performance is relatively better [12]. There are also researches that carry on the related demonstration from the opposite side. For example, Ramalho studied the impeachment of Collor who was president of Brazil case and found that after the open of the news about the impeachment of the president, the market value of enterprises that associated with his family mehad a significant loss, the average loss was 2% - 9% [13]. In China, some related researches also found that the political connection of chairman will have a positive impact on company's performance [14]. Gao Bing and Wang Yanzhang found that political connections of different levels have different impacts on enterprise performance, compared to the provincial and municipal level political connection, central political connection has greater promotion to enterprise performance [15]. Some scholars pay attention to distinguishing the individual political connection from organization political connection (The individual political connection is the social connection between entrepreneur and political government officials or government, and its center is entrepreneur. The organization political connection is social connection between enterprise and government officials or government, and its center is organization. The differences between them are that the organization political connection is caused by enterprise organization and will disappear with the disappearance of organization and the individual political connection is caused by individual and will disappear with the disappearance of individual, and individuals tend to erode organizationa political connection) and found that individual political connection has a positive impact on enterprise short-term performance, organization political connection has positive effects on enterprise long-term performance [16].

3.2. Negative Influence

Many current researches has found that political connection has negative impact on enterprise performance. Vishny and Shleifer through establishing the game model about administrative officials and business managers found that political relations can also play the role of "predatory hand" [17]. In order to achieve its political objectives, government will produce negative impact of "predatory hand" on enterprise, which greatly damage the value of the enterprise. Ni Changhong and Zou Guoqing found that the executive team that has a political connection will damage the performance of enterprises [18]. Bertrand, Ramarz and Schoar made the relevant research by taking French companies as the sample, the results show that the political connection will do harm to enterprise performance [19]. Aggarwal, Meschke and Wang also support the above conclusions [20]. Boubakri measures the operating performance of enterprise by using the rate of return on net asset, the rate of return on total asset and the rate of return on sales, and found that enterprises which have not political connection had better operating performance than those which have political connection. Deng Jianping and Zeng Yong found that for private enterprises, the political connection will actually damage the efficiency of business [21]. Hu Shimin and Du Bin taking electric power, gas and water listed companies as the object, studied the relationship between political connection of state-owned enterprise executives and enterprise performance. The results of the study showed that generally speaking, political connection of state-owned enterprise executives have negative impact on enterprise performance [22]. There is also study found that unlike the chairman of the board, the political connection of general manager will have a negative impact on the performance of the company [14].

3.3. Inverted U-Shaped Relationship

Research has also found that the relationship between political connection and enterprise performance is not simple positive or negative but an inverted U-shaped, that is to say, with the increase of the degree of political connection, enterprise performance rising, after the degree reaching a certain value, corporate performance will decrease gradually with the further increase of the degree of political connection. For example, Wang Chan and Cao Lihui studied private listing Corporation from 2006 to 2009 and found that the relationship between the degree of political connection and enterprise performance is inverted U-shaped relationship [23]. As the same, Li Weian, Qiu Aichao, Gu Zhihui, Ren Guangqian and Wang Minda made the study by taking the Chinese listed companies as sample and had come to the same conclusion [24] [25].

3.4. No Influence

At the same time, some studies have found that there is no obvious relationship between enterprise political connection and enterprise performance. Fisman and Erker, for example, have found that political connection

have no significant effect on firm performance [26]. Amore and Bennedsen found that in the context of little occurrence of corruption, the political connection does not have an impact on corporate performance [27]. Some other researches also show that there is no significant relationship between political connection and performance. Wu Wenfeng, Wu Chongfeng and Liu Xiaowei through studying private listing corporation of A shares found that managers who whether have government background have not overall impact on the company's value [28]. And such as Wang Qingwen and Wu Shinong through investigating the political influence index of the listing Corporation found that the political connection has no significant impact on enterprise performance [29].

4. The Main Influence Mechanism of Political Connection on Enterprise Performance

From the above we can see that the influence of political connection on corporate performance is not yet conclusive, analysing the specific mechanism of the impact of political connection on corporate performance is a powerful way to explain the different results. Most of the existing researches focus on the direct influence of political connection on corporate performance, but the study of internal mechanism is not enough. And political connection as a non market factor, its influence on the enterprise performance must be indirect. Political connection reflects the interaction effect of enterprise and system environment, which forms a dominant or recessive link between the enterprise and the government. Through this link, the enterprise can obtain facilities from financing, taxation, market access and so on from the government, thus political connection produces the influence on the enterprise operating performance and market value [30]. The influence of political connections on corporate performance in the industry of policy leading is more obvious, by political connections, the enterprise can inform policy orientation before the open of policy, and some can even guide policies to make the policy implementation direction is more conducive to enterprise [31]. These studies have indicated that the influence of political connection on enterprise performance is indirect. Through combing the relevant literatures, it is found that the political connection influence enterprise performance mainly by the following aspects: financing, taxation, access regulation industry.

4.1. Financing

Most of the studies considered the political connection has a positive effect on enterprise financing, scholars took Pakistani companies as the research sample of related research, and found that firms with political connection than non political connection enterprises have loan amount of more than 45% [32]. There are scholars have shown that as a substitute informal institution in the Chinese political association can help enterprises obtain more credit resources under the imperfect institutional environment, so as to alleviate the financing problems of enterprises [33]. Faccio (2001) made relevant study by taking enterprises from a number of countries as sample of research and found that compared to enterprises with no political connection, enterprises with political connection had higher asset liability ratio. Financing also is reflected by government aid, Faccio took a number of enterprises from many countries as the sample and made research. The results show that in the face of financial distress enterprises that have political connection than non political connection enterprises could obtain higher proportion of government rescue, between 1997 and 2002, the former get the proportion of government rescue is 11.3% but the latter is only 4.4% [34]. Political connection can also help enterprises to reduce financing costs, for example, to reduce the credit constraints, the direct cost of financing and to strengthen the government's rescue efforts, etc. [35]. Some scholars believe that the political connection can help enterprises to overcome the barriers of financing and the barriers of entering the industry thus producing a positive impact on business performance [3]. At the same time, Hu Xuyang taking the top 100 private enterprises in Zhejiang Province as the research sample confirmed political connection can not only reduce the barriers of private enterprises enter the financial industry, but also be directly advantageous to corporate financing, and then to promote the performance of development of private enterprises [36]. In addition, for private enterprises, it can influence the bank's lending decisions by building political connection with government to get more loan financing [37], and improve the business performance.

4.2. Tax

Adhikari, Erashid and Zhang took Malaysian companies as the research object, using empirical methods to study the relationship between political connection and corporate tax, found enterprises with political connections are

more likely to get preferential tax, enterprise's actual tax rate is also lower [38]. Wang Zhongwei studied private listed companies from 2008 to 2013 and found that political connection and preferential tax correlated positively, in the region with poor institutional environment, enterprises are more likely to get preferential tax through the political connections [39]. Tao Baoshan, Li Yaping examined the relationship between the political connection and preferential tax by taking private listing corporation as sample, the results show that the political connection can help enterprises to obtain a lower actual income tax rates [40]. Li Weian, Xu Yekun found that political identity can help enterprises avoid tax, the government's financial pressure is greater, the corporate tax avoidance effect is more obvious, and found that the political status is higher, the tax avoidance effect is more obvious [41].

4.3. Access Regulation Industry

The unique resources of the government are which many enterprises can not touch but very need, such as mine, energy industry access, etc. Under the background of China's imperfect legal system environment and high market access barriers, the private enterprises will get the care of the government through the political connection [42], and will get some unique resources. In many cases, companies want to enter the industry which have high policy barriers, but the political connection can help enterprises to overcome those barriers, so as to get access to the industry [43] [44]. "Relationship" not only enable enterprises to obtain the desired resources but also to take less procedures, saving a large number of additional costs to meet the policy. Based on the resource based view, the obtain of enterprise competitive advantage is based on the heterogeneity of resources. Entering the regulated industries can enable the enterprise to get the unique resources other companies do not have, so political connection, to a certain extent, enables enterprises to have more advantages relative to other enterprises. According to institution based view, the development of enterprise is subject to the limitation and restriction of system. Because Political personnels are people who are charge in maintenance and implementation of system, through the political connections, enterprises will integrated better with institutions and has more advantages to enter regulated industries under the constraint of system. It would be great to the development of enterprises.

From the above summary, it can be known that political connections can influence the enterprise performance through the ways of financing, taxation and access regulation industry. But the ways can't be just these. At the same time, because the external resources of enterprises, include all external factors that could promote enterprise [45], so these ways can be seen as external resources. How to obtain these resources by political connection is rarely involved in the study. The social network is the channel to obtain the resources, and the social network provides an important way to analyze the growth of enterprises and the obtain of resources [46]. Here, we will not exhaust every kind of specific resources, but from the perspective of social network theory to reveal the mechanism that companies join variety of resources by political connection to promote the development of performance.

5. Social Network Theory

In the fifty's or sixty's of last century, social network theory began to appear [47]. Social network is a association network which formed by individual or organization as nodes through mutual or direct or indirect links. Along with the continuous development of the theory, node in the network has changed, from the original individual has been developed into including both individual and group or organization, including personal social relations and including the relations between groups or organizations. The main theories of social network theory are the strong and weak tie theory, the social capital theory, the structural hole theory.

5.1. Strong Tie and Weak Tie

The strong and weak tie theory is one of the most important theories in the social network theory. The tie is the basic unit of social network analysis, which refers to all kinds of social relations, including colleagues, relatives, friends, classmates and so on. In the social network, because various relationships lead to the complexity, the tie includes direct and indirect tie. American scholar Granovetter's research on tie is typical, he divided tie into Strong Tie and Weak Tie. Strong Tie forms by social contact through that individual keep close contact with the other individual with similar social characteristics. Weak Tie forms by social contact through which individual keep estranged contact with the other individual with different social characteristics. Here, the social character-

ristics refers to the age, gender, educational background, income and the nature of work and so on. According to Granovetter's viewpoint, the transfer of new resources are very limited between homogeneity nodes, therefore, weak tie compared to strong tie has stronger ability of transferring effective information and resources. Because strong tie represents the transfer of information and resources among similar individuals thus resources are often redundant. Weak tie represents the transfer of information and resources among individuals with different background, once the flow channels of information and resource among weak tie established, more valuable information and resources could be obtained. Of course, strong tie is the foundation of weak tie to produce influence, weak tie getting resources and information is based on closely social contact established by strong ties, the effect of weak tie needs close social contact from strong tie to consolidate and maintain.

5.2. Social Capital Theory

In 1970s, French scholar Bourdieu firstly proposed the concept of social capital. It is believed that social capital is the ability to obtain scarce resources through the tie of social networks [48]. Coleman and James believe that social capital refers to the capital property presenting by social structure resources [49]. According to these views, social capital refers to the ability that individual or organization obtains the capital property presenting by social structure resources in the process of contact with the outside world. Therefore, if there are more connections among individual or organization and the outside world, then there are more channels to get resources. For an organization, mastering social capital indicates that it has a variety of contacts with the outside world, these contacts may form a interwoven network and organizations through the network will continue to acquire new resources. When organization found that it can successfully obtaine the required resources by the network, it often will summarize the process of network formation, including characteristics of various contact in the network, and then repeat the process to expand the network to acquire more resources, that is, forming the path dependence. At the same time, the social capital theory thinks that the quantity of social capital of organization or individual determines its position in the network structure. The relationship distribution of the network is not uniform, and some places are crowded, and some places are sparse. In general, a place with intensive relationship is more conducive to obtain resources for enterprise.

5.3. Structural Hole Theory

Structural hole theory was proposed by American scholar Burt [50]. Structure hole theory believed that the sparse zone among the dense relationship zones of social network relationship is structural hole, and structural holes can bring the enterprise competitive advantage. Although the structural hole represents the lack of resources, enterprises in the structure hole can get adequate resources by connecting dense relationship zones to make the resources flow through the structural hole. Because of the existence of the above mechanism, enterprises in the network will continue to get the resources through the development of structural hole, as a result, the network structure changes.

As can be seen from the above statement, there is a strong relationship between the structural hole theory and the strong and weak tie theory. In the structural hole, it's weak tie that connects two dense relationship zones together, so Burt's point of view can be seen as a further development of the Granovetter's viewpoint [51].

6. The Social Network Theory Explanation of the General Mechanism of the Influence of Political Connection on Enterprise Performance

6.1. Obtain Heterogeneous Resources

Corporate political connection is the connection between organizations with different social characteristics, namely, enterprise and government. The association between them can not be close due to policy, institutional and other reasons. According to the strong and weak tie theory, the tie between the two belongs to weak tie. So from the role of strong and weak tie, through the political connection, the enterprise can obtain the resources that are different from the resources enterprise get from other enterprise, thus increasing its competitive advantage. And association between the enterprise and the longitudinal enterprise tend to belong to the strong tie, such as the connection with the upstream and downstream enterprises, resources of these enterprises are mostly redundant. As the connection with horizontal enterprises, due to the existence of competition between the two sides, both sides are very familiar with each other, horizontal enterprises will take a conservative attitude to some re-

sources. At the same time, the enterprise's acquisition of resources is generally through the exchange with resource owners by some kind of transaction, that is, enterprises pay a certain cost directly for exchanging the resources. The political connection gives the enterprise a new way to obtain resources. According to the structural hole theory, the relationship network whose center is government represents the dense zone of relationship network, companies are in a sparse region, on the one hand, through the political connections, on the other hand, through weak ties with other dense zone, the enterprise could obtain heterogeneity resource as media of transporting resources between two dense zones (as shown in **Figure 1**), these heterogeneity resources include information resources refer to policy and project bidding, knowledge resources etc. [52]. Other dense zone here can refer to the relationship network whose core is government or another enterprise. In this process, the way that enterprise obtains resources is not directly exchanged with the resource owner, but by the process of active transport. The resources flowing in this process may be necessary and difficult to obtain for enterprise and also difficult to obtain for other non political connection enterprises. It can be seen that one of the main ways to obtain the heterogeneous resources for enterprise is the political connection and the acquisition of the heterogeneous resources lays a solid foundation for the growth of the enterprise performance.

But if the relationship between enterprise and government develops continuously and exceeds a certain close degree, then the connection between the enterprise and the government will transform gradually from the weak tie to strong tie. According to the strong and weak tie theory, at this time, the resources government provided tend to be redundant, and the political connection cost will gradually exceed the value of acquired resource, thus damaging the corporate performance. At the same time, the connection between the enterprise and the government transforming gradually from the weak tie to strong ties makes the government have the opportunity to implement more intervention to enterprise. After all, the government is likely to take enterprise as a tool to achieve political goals [53], which leads to inefficient of enterprise's resource allocation [34], and then create the adverse effect to the enterprise performance. This is also a reasonable explanation for the inverted U-shaped relationship between the political connection and enterprise performance.

6.2. Obtain More Resource Channels

Enterprises have direct or indirect contact with the outside world and are in a large social network. Social capital can effectively promote the enterprise performance [54], whether can make full use of social capital to provide the necessary resources for enterprise concerns enterprise's rise and fall.

According to the social capital theory, if the enterprise as an organization can build more contact with the outside world, its channels to access resources will increase. Government as a node in the network society, due to its own particularity usually is the center of resource intersection. The relationship network whose center is government is dense and its position in the network structure inevitable also live in the center attracting other

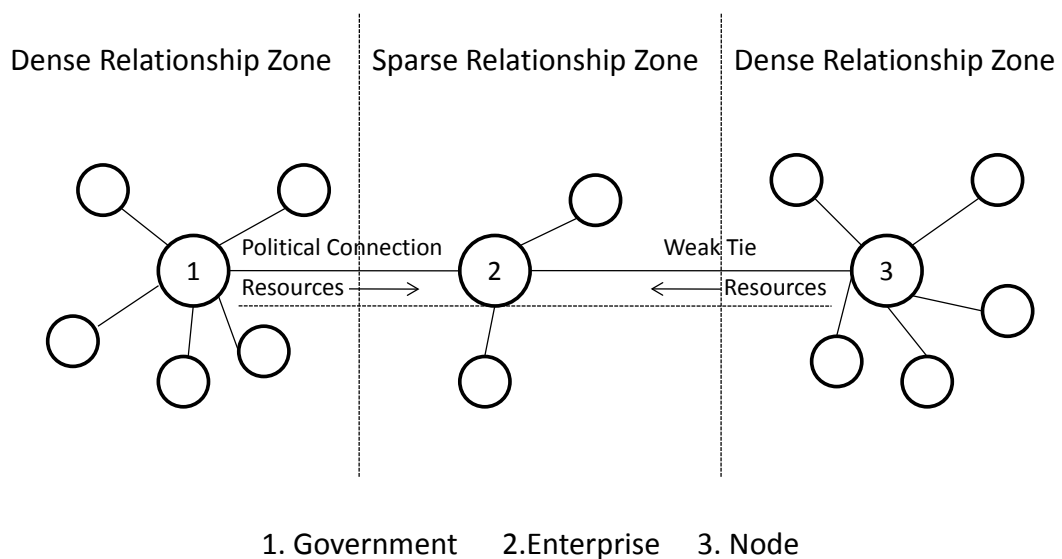


Figure 1. Enterprise transports resources through connecting two dense relationship zones.

nodes that want to get more new resources to approach. Therefore, enterprises can expand the scope of contact with the outside world through political connection and continuously expand its network formed by contacting with outside world by the use of special status of government. Here, enterprise through the political connections not only connects with the government directly and obtains resources from the government, but also can connects indirectly with other nodes of connection network where government is the center to obtain more extensive resources. It is clear that this indirect connection is a weak tie, and is different from the indirect connection without government as a “middleman”. According to Coleman’s view, the social capital of network can enhance the loyalty and responsibility of the individual or enterprise to the relationship of network so as to reduce the uncertainty in the process of transaction and improve the efficiency of cooperation. Because of the existence of government, the connection between the enterprise and other nodes becomes subtle. Firstly, because of the government’s “guarantee”, the problem of trust among business and other nodes can be solved well, which will greatly reduce the two sides’ trust obstacles in flow of resources. Secondly, enterprises can better understand the nodes’ situation of resources through the government, and according to the resources of each node to select the appropriate connection mode to build a more robust distribution channels of resources. Generally speaking, the enterprise through the political connection is equivalent to make itself transfer from the sparse relationship zone to the dense relationship zone making itself have more channel of obtaining resources, as shown in **Figure 2**. After successfully obtaining resources, companies are likely to replicate such a model to guarantee the maximize inflow of resources, for example, companies’ branch company in one regional succeed in obtaining resources through political connection, headquarters is likely to require branch company in another region to do the same so that channels to obtain resources will continue to expand.

7. Conclusion

From the perspective of social network, it is found that the establishment of political connection is beneficial to the improvement of performance. Through the political connection, enterprises can obtain heterogeneity resources and broaden the channels of obtaining resource. Regardless of enterprises which are in dense zone or sparse zone of social network, political connection (weak tie between enterprise and government) can effectively help enterprises to actively acquire resources, so as to lay a good foundation for establishing competitive advantage, and provide sufficient power for the development of enterprise performance. At the same time, the study found that in the process of building political connection, enterprise will gradually transfer to the position of network which is conducive to itself, so as to obtain more resources. In addition, through the analysis, it is found that the direct result of enterprises building political connections mainly is to obtain more resources. But when the extent of political connection is constantly enhanced and to a certain value, political connection cost will exceed the value of resources obtained through political connection and political connection will make adverse

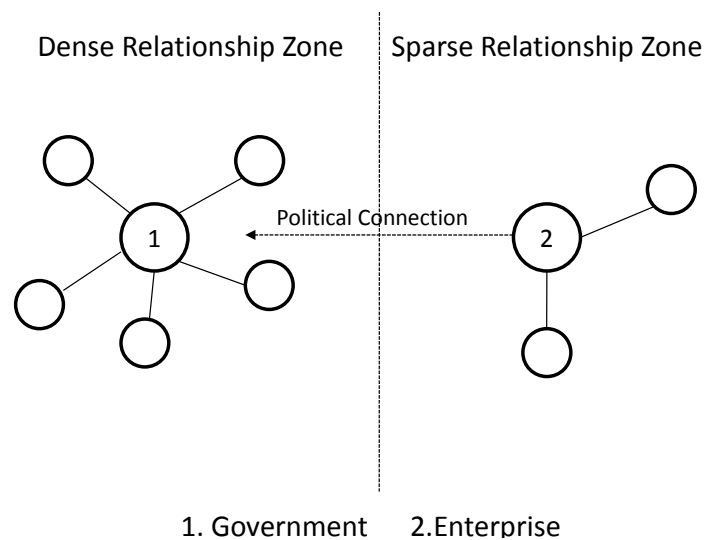


Figure 2. Enterprise transfers from the sparse relationship zone to the dense relationship zone through political connection.

effects on the enterprises' allocation of resources, and damage corporate performance, which provides an explanation for inverted U-shaped relationship between political connection and corporate performance. As to the conclusion that political connection will produce negative impact on corporate performance, as described in the previous section, when the strength of connection is in a certain scope, political connection is mainly to help enterprises acquire resources; the appearance of phenomenon that political connection is completely not conducive to enterprise performance is usually correlated with the too large strength of political connection and the enterprises' configuration of resources.

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