

Does it Pay for Entertaining Your Stakeholders?

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Definition

- Business Entertainment Expenditure (BEE) includes all kinds of expenses to entertain **external stakeholders** in different forms:
 - Such as business lunches, concert shows, sport events
 - Therefore, BEE does not include any expenses used only for insiders like employees and shareholders

Motivation

- First, business entertainment is a **longstanding** and **prevalent** corporate activity
 - For instance, in the U.S., BEE is officially tax deductible since the inception of the nation's revenue laws in 1906
 - Currently, the tax deductible rate ranges from 50% to 100% in major countries:
 - U.S., Canada, 50%; Germany, 70%; Brazil, 50%; Russia, 100% if BEE < 4% of total annual pay-roll expenses; China, 60% if BEE < 0.5% of sales
 - **India, ??**
 - These practices suggest that BEE is generally considered as necessary operating costs and tax deductible

Motivation

- Second, the economic magnitude of BEE is **considerable**
 - In Korea, Chaebul.com, reported that BEE accounts for 0.19% of combined sales in 2012, based on 3.6 million Korea firms
 - In China, BEE accounts for 0.23% of combined sales, 4.5% of combined net income, 2004 – 2014.
 - The equal-weighted average of BEE as of net income is as high as 12.3%
 - In Japan, a report by Reuters in 1985, estimated that BEE probably amounts to 20% of the total costs for small firms
 - In U.K., the corporate hospitality market is about 0.82% of its GDP in 2011

Motivation

- Although this activity is **longstanding**, **prevalent** and **economically significant**, we still know very little about
 - **Why** do firms entertain their stakeholders?
 - **How** does this activity affect firm performance and through which channels?
 - **Whether** investors fully understand the info embedded in BEE?
- Taking advantage of unique disclosure practices in China, we investigate these questions using a manually constructed dataset for Chinese public firms from 2004 to 2014
 - Data is not available in other countries

Position in the literature

- To our best effort, there is only one related paper, Cai, Fang and Xu (2011JLE)
- Two major differences
 - Survey data (World Bank) vs. real data (listed firms)
 - ETC=Entertainment Costs (BEE) + Travel Costs
 - The nature of two items are different. Travel costs is incurred by **insiders**, while BEE is used to entertain **outsiders**. **Meaningless to add them up.**
- Opposite findings
 - Cai et al. (2011) find ETC has **negative** effect on firm performance, interpreting ETC as a proxy for corruption
 - Within the same industry, the higher travel costs, the more difficult to do business?
 - We find BEE has **positive** effect on firm performance

BEE and Firm Performance

- Agency theory implies that BEE can reduce firm performance
 - The higher BEE, the more agency problem
- Transaction cost theory and public choice theory suggest that BEE can improve firm performance by helping firms
 - Transaction cost theory
 - mitigate transaction costs involved in **market-based transactions**
 - Public choice theory
 - achieve favorable outcomes from **non-market-based transactions**

Transaction Cost Theory

- Transaction costs refer to the costs involved in **market exchange** (Coase, 1960)
 - Including the costs of discovering market prices, writing and enforcing contracts.
- Dahlman (1979) further points out that **the root of the existence of transaction costs is the lack of information**

Market-based Transactions

- Entertaining business partners can facilitate communication and information sharing between firms and their business partners. Therefore, this activity can
 - reduce transaction costs by mitigating information problem
 - secure some profitable business opportunities that might be otherwise impeded by the high transaction costs
- **Two predictions:**
 - Firms facing higher transaction costs tend to have higher BEE
 - Entertaining activities can improve outcomes in market-based transactions, and the improvement is stronger for firms facing higher transaction costs

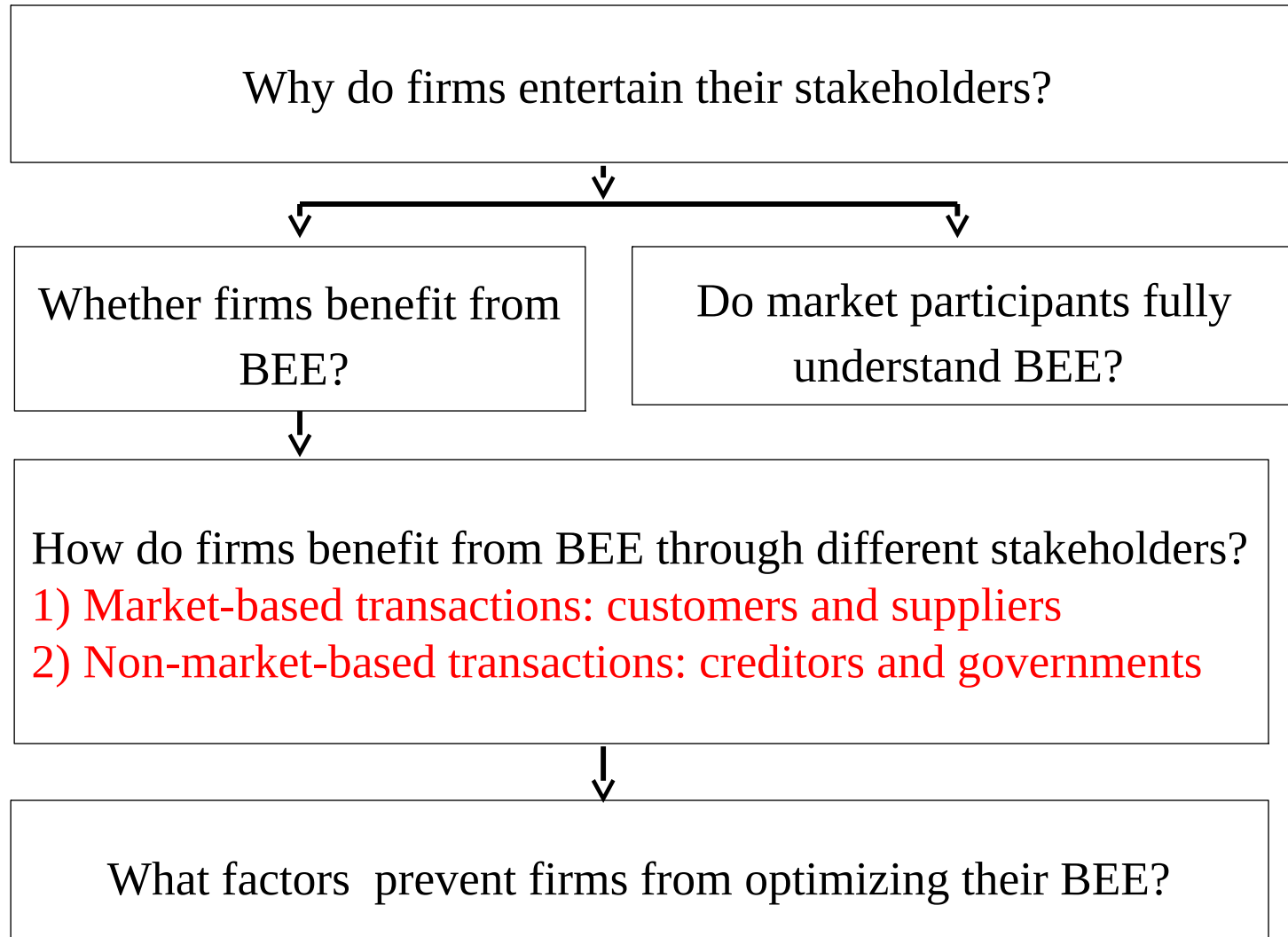
Non-market-based Transactions

- Public choice theory
 - Decisions or outcomes in public sectors are **not** completely determined by objective rules or procedures, **but also shaped by the lobbying or other activities (like business entertainment)** of interest groups or powerful economic actors (Bernstein, 1955)
 - The effectiveness of lobbying or other activities depends on **the degree of influence** that interest groups/individual actors can exercise over the decision-making of bureaucrats

Non-market-based Transactions

- The **degree of influence** depends on
 - The ability of lobbying groups to gain access to bureaucrats (Culhane, 1981)
 - The information sharing between lobbying groups and bureaucrats (e.g. Abeny and Lauth, 1986; Brudney and Hebert, 1987)
 - The perceived power or favorability of the lobbying groups versus their competitors in the eyes of bureaucrats (Khwaja and Mian, 2005)
- **Prediction:**
 - Politically favored firms could spend more or less on BEE.
 - Entertaining activities can generate benefit for firms from non-market-based transactions. The effect could be either stronger or weaker for politically favored firms.

Road Map



Dataset Description

Panel A. Summary statistics of BEE by year

year	#Firm-year with BEE	%Disclosure rate	% BEE/TA			% BEE/Sales			% BEE/Operating Profit		
			Mean	Median	S.D.	Mean	Median	S.D.	Mean	Median	S.D.
2004	437	36.06	0.23	0.17	0.22	0.46	0.27	0.56	10.17	4.30	21.53
2005	441	36.63	0.24	0.18	0.22	0.46	0.28	0.55	12.72	5.27	25.30
2006	498	39.81	0.24	0.19	0.23	0.43	0.28	0.49	10.98	4.32	20.76
2007	570	43.35	0.25	0.18	0.24	0.45	0.27	0.61	9.38	3.39	24.12
2008	560	43.34	0.26	0.19	0.26	0.49	0.29	0.65	10.98	4.22	24.25
2009	836	76.84	0.25	0.17	0.26	0.52	0.32	0.64	11.17	4.03	23.63
2010	1,409	79.16	0.26	0.18	0.26	0.54	0.33	0.65	9.07	3.67	19.15
2011	1,667	79.99	0.28	0.19	0.27	0.57	0.34	0.70	10.38	4.00	22.10
2012	1,834	80.37	0.28	0.19	0.27	0.59	0.36	0.69	11.21	4.53	22.66
2013	1,819	78.61	0.26	0.17	0.27	0.56	0.33	0.69	12.31	4.49	25.42
2014	1,648	76.62	0.22	0.14	0.25	0.52	0.28	0.72	11.09	3.86	24.42
Total	11,719	65.20	0.26	0.18	0.26	0.53	0.32	0.67	10.87	4.12	23.06

Dataset Description

Panel B. Summary statistics of BEE by industry

Industry	#Firm-year with BEE	%Disclosure rate	% BEE/TA			% BEE/Sales			% BEE/Operating Profit		
			Mean	Median	S.D.	Mean	Median	S.D.	Mean	Median	S.D.
Information Technology	942	70.93	0.51	0.39	0.40	1.10	0.80	1.00	17.87	7.75	29.73
Pharmaceutical Products	805	67.82	0.35	0.26	0.31	0.69	0.45	0.74	11.35	4.20	23.76
Communication & Culture	152	76.00	0.31	0.23	0.25	0.64	0.45	0.57	9.40	3.30	22.40
Machinery	2,411	70.09	0.29	0.22	0.25	0.60	0.41	0.61	12.68	5.30	24.50
Retail & Wholesale	562	61.29	0.22	0.20	0.15	0.30	0.17	0.53	9.08	4.50	16.06
Other Manufacturing	127	63.82	0.34	0.19	0.36	0.60	0.30	0.77	12.13	4.67	23.55
Electronic	618	62.93	0.26	0.18	0.26	0.52	0.33	0.57	10.48	4.18	22.21
Agriculture	286	72.59	0.22	0.17	0.16	0.59	0.37	0.79	16.14	6.07	31.29
Food	475	63.50	0.24	0.17	0.22	0.37	0.27	0.36	9.02	3.09	23.66
Construction	251	62.28	0.19	0.17	0.13	0.30	0.24	0.24	8.91	5.38	11.72
Social Services	273	58.21	0.24	0.16	0.25	0.68	0.41	0.85	7.63	3.26	19.56
Apparel	446	62.03	0.20	0.15	0.17	0.37	0.23	0.48	9.76	3.74	20.20
Gas and Chemistry	1,399	69.29	0.21	0.15	0.19	0.35	0.22	0.50	9.06	3.71	20.55
Furniture	53	69.74	0.20	0.14	0.16	0.30	0.25	0.18	8.60	4.35	12.03
Printing	215	61.96	0.22	0.14	0.22	0.41	0.27	0.44	8.65	4.12	16.05
Metal	1,015	63.36	0.18	0.13	0.18	0.35	0.20	0.54	12.49	3.63	27.98
Transportation	257	57.75	0.19	0.13	0.24	0.51	0.40	0.49	7.46	2.91	18.84
Conglomerate	315	50.32	0.20	0.13	0.21	0.65	0.37	0.75	12.13	3.90	27.09
Mining	311	67.32	0.16	0.11	0.17	0.33	0.19	0.39	4.58	1.44	12.95
Real Estate	444	57.07	0.13	0.08	0.17	0.63	0.34	0.85	5.28	1.99	13.42
Utilities	362	57.28	0.10	0.07	0.10	0.31	0.19	0.34	5.01	1.98	12.81

Why do firms entertain their stakeholders?

- 8 variables to capture the transaction costs faced by firms in **market-based transactions**
 - Customer-base concentration (top 5)
 - Supplier-base concentration (top 5)
 - Reserves of account receivables, scaled by total assets
 - Related party transactions, scaled by total assets
 - PCM, firms' competitiveness, $(\text{sales} - \text{COGS} - \text{SGA}) / \text{sales}$
 - Litigation risk, a dummy variable, one if a firm experienced more lawsuits than its industrial median in the past three years
 - Leverage, Williamson (1988) predicts that firms with lower transaction costs tend to rely more on debt financing
 - Firm age

Why do firms entertain their stakeholders?

- 2 dummy variables to capture firms' incentive to engage in entertainment activities for obtaining favorable outcomes in **non-market-based transactions** with stakeholders such as governments and state-owned banks
 - SOE
 - set at one if a firm is controlled by a government agency, or a state-owned entity.
 - political connection
 - set at one if the CEO or board chair of a firm is or was a government bureaucrat.

Why do firms entertain their stakeholders?

- Control variables
 - A batch of **governance indicators** to capture the role of corporate governance in determining BEE
 - A set of **ownership structure** characteristics to capture the interest alignment of various corporate decision makers
 - Size, B2M, cash availability, marketization index
 - Industry-year fixed effect

Model Specifications

- Disclosure Decision

- Self-selection bias
- Three dummy variables are further introduced to meet exclusion restriction in Heckman two-stage model:
 - Shanghai Stock Exchange, GEM market at Shenzhen Stock Exchange, Early listers

$$P(\text{Disclosure}_{i,t}) = f(\text{Explanatory Vars}_{i,t}, \text{Additional Vars}_{i,t})$$

- Determinants of BEE

- Scaled by total assets, as entertainment with non-market-based stakeholders like governments and creditors will not directly generate sales

$$BEE_{i,t+1} = \alpha + \beta' * \text{Explanatory Vars}_{i,t} + \gamma * IMR_{i,t} + \varepsilon_{i,t}$$

Table 2. Determinants of BEE

Key Explanatory Variables				
	Determinants of BEE			
		(2)		(3)
Customer-base concentration	-0.145***	(-7.511)	-0.077***	(-3.538)
Supplier-base concentration	-0.083***	(-4.389)	-0.018	(-1.284)
Reserve of receivables	0.025***	(6.663)	0.008**	(2.466)
RPT/TA	-0.013	(-1.402)	-0.004	(-0.558)
Litigation risk	0.011	(1.229)	0.012*	(1.791)
SOE	0.007	(0.613)	-0.008	(-0.488)
Political connectedness	0.012	(1.341)	0.011*	(1.822)
Leverage	-0.083***	(-2.934)	0.019	(0.722)
Firm age	-0.025**	(-2.002)	-0.006	(-0.173)
Price-cost margin	-0.036	(-1.381)	-0.003	(-0.160)
Industry-year FE		Yes		Yes
Firm FE		No		Yes

Table 2. Determinants of BEE

Control Variables				
	Determinants of BEE			
		(2)		(3)
Fraction of outside directors	0.010	(0.455)	-0.051***	(-3.002)
Duality	0.011	(0.938)	0.013	(1.388)
Board size	0.042*	(1.727)	0.004	(0.131)
Largest shareholder's ownership	-0.116***	(-3.779)	-0.065	(-1.464)
Managerial ownership	0.026	(0.797)	0.074*	(1.708)
Mutual funds' ownership	0.115*	(1.663)	-0.026	(-0.538)
Herfindahl index (2-10)	-0.115	(-0.664)	-0.023	(-0.097)
Remuneration	0.385***	(3.160)	0.127**	(1.987)
Incentive scheme	0.023	(1.548)	0.015*	(1.728)
Firm size	-0.029***	(-3.779)	-0.052***	(-5.951)
lnB2M	-0.016**	(-2.445)	-0.001	(-0.283)
Cash holding	0.059**	(1.966)	-0.030	(-1.306)
Marketization index	0.009***	(3.358)	0.014	(1.360)
IMR	0.048	(1.082)	0.034	(1.103)
Constant	0.737***	(5.010)	1.269***	(5.547)
Industry-year FE		Yes		Yes
Firm FE		No		Yes

The Effect of BEE on Future Firm Performance

- Identification Strategy

- Endogeneity

- Omitted variables

- Time-invariant, industry-year and firm fixed effects

- Time-variant, IV

- Reverse causality (IV)

- Instrumental Variable

- Cai et al. (2011) use the average ETC of other firms within the same city and industry as an instrument for a firm's ETC.

- Nevo (2001), use other regional average prices as an instrument for the city-level price as both of them respond to the product's common marginal costs.

- Following them, we use the median BEE of other firms within the same industry at two-digit level in a given year as the IV

The Effect of BEE on Firm Future Performance

- **Underlying logic:** firms within the same industry share some common but unmeasurable factors that affect BEE, such as specific product attributes and industry regulations
 - **Relevance Criteria**, this IV is related to a firm's BEE
 - **Validity Criteria**, this IV less likely affects a firm's other outcomes **directly**, except **indirectly** through BEE
- A strong IV: the industry median BEE of other firms alone can explain about 12.05% of the BEE variation, which is more than 48% of the total explained variation in BEE in Table 2

The Effect of BEE on Firm Future Performance

- Model Specification

$$Outcomes_{i,t+1} = \alpha + \beta * BEE_{i,t} + \gamma' * Controls_{i,t} + \varepsilon_{i,t}$$

- Controls = explanatory variables, IMR, year, industry and firm dummies
- We use the total assets **at year t** as the deflator when the outcome is scaled by total assets
- An advantage of this specification is that we can interpret the coefficient of BEE as **one dollar increase in BEE will lead to β dollar increase in the outcome of interest**

Table 3. BEE, Firm Performance and Valuation

Panel A. Asset Turnover								
	OLS						IV	
	(1)		(2)		(3)		(4)	
BEE	0.363***	(7.737)	0.167***	(5.733)	0.350***	(5.299)	0.161**	(2.301)
Asset Turnover (t)			0.653***	(28.887)	0.206***	(8.803)	0.654***	(29.181)
Other controls	Yes		Yes		Yes		Yes	
Industry-year FE	Yes		Yes		Yes		Yes	
Firm FE	No		No		Yes		No	
Observations	10,054		10,054		10,054		10,054	
Adjusted R ²	0.248		0.606		0.754		0.606	

Panel B. ROA								
	OLS						IV	
	(1)		(2)		(3)		(4)	
BEE	0.025***	(5.901)	0.021***	(5.436)	0.033***	(4.228)	0.033***	(3.777)
ROA(t)			0.265***	(16.751)	0.104***	(6.165)	0.262***	(16.743)
Other controls	Yes		Yes		Yes		Yes	
Industry-year FE	Yes		Yes		Yes		Yes	
Firm FE	No		No		Yes		No	
Observations	10,054		10,054		10,054		10,054	
Adjusted R ²	0.332		0.376		0.500		0.374	

Table 3. BEE, Firm Performance and Valuation

Panel C. Tobin's Q								
	OLS						IV	
	(1)		(2)		(3)		(4)	
BEE	0.431***	(3.378)	0.366***	(4.025)	0.896***	(5.695)	0.449**	(2.390)
Tobin' Q (t-1)			0.438***	(30.261)	0.173***	(13.906)	0.438***	(30.623)
Industry-year FE	Yes		Yes		Yes		Yes	
Other controls	Yes		Yes		Yes		Yes	
Firm FE	No		No		Yes		No	
Observations	10,054		10,054		10,054		10,054	
Adjusted R ²	0.513		0.619		0.737		0.619	

- Economic significance – **surprisingly huge!!**
 - 1 dollar increase in BEE improves sales by 16.7 dollars
 - 1 dollar increase in BEE improves net profits by 2.1 dollars
 - 1 dollar increase in BEE is associated with 36.6 dollars more in firm valuation

A quasi-natural experiment

- The anti-corruption campaign initiated by the Xi Administration at the end of 2012
- On Dec 4, 2012, the Political Bureau of the Communist Party of China passed an Eight-provision regulation on how government employees and leaders of SOEs should improve their work style in eight aspects, focusing on rejecting extravagance and bureaucratic visits, meetings and empty talks.
- Therefore, this exogenous shock would lead to a reduction in BEE, especially for SOEs.
- SOEs (treatment group) vs Non-SOEs (control group) , propensity score matching

Table 4. A quasi-natural experiment

Panel A. Univariate test						
	(1)		(2)		(3)	
	SOEs (After - Before)		Matched mon-SOEs (After - Before)		DiD	
BEE	-0.068***	(-9.764)	-0.036***	(-4.197)	-0.031***	(-3.025)
Asset Turnover	-0.118***	(-6.850)	-0.079***	(-4.002)	-0.039*	(-1.833)
ROA	-0.014***	(-3.801)	-0.014***	(-4.111)	-0.000	(-0.677)
Tobin's Q	0.390***	(3.008)	1.041***	(5.953)	-0.651***	(-3.196)
Panel B. DiD regressions						
<i>Dependent Variable</i>	Asset Turnover		ROA		Tobin's Q	
SOE	0.114**	(2.329)	-0.014*	(-1.652)	-0.036	(-0.279)
SOE × After	-0.030**	(-1.972)	-0.006**	(-2.142)	-0.601***	(-9.237)
BEE	0.350***	(5.293)	0.033***	(4.223)	0.894***	(5.633)
Other controls	Yes		Yes		Yes	
Firm, Industry-year FE	Yes		Yes		Yes	
Observations	10,054		10,054		10,054	
Adjusted R ²	0.752		0.497		0.739	

Table 4. A quasi-natural experiment

Panel C. The impact of the reduction in BEE on firm performance						
<i>Dependent Variable</i>	Asset Turnover		ROA		Tobin's Q	
SOE	0.023	(1.290)	-0.004	(-1.462)	-0.125*	(-1.918)
More reduction in BEE	-0.165***	(-4.973)	-0.015***	(-4.146)	-0.564***	(-5.344)
BEE	0.067*	(1.836)	0.017***	(2.994)	0.120	(0.920)
Other controls	Yes		Yes		Yes	
Industry-year FE	Yes		Yes		Yes	
Observations	3,421		3,421		3,421	
Adjusted R ²	0.614		0.387		0.710	

- More reduction in BEE = 1 if a firm experience more than 20% reduction in BEE in a given year
- Sample period: post anti-corruption period (2013 – 2014)

The Predictability of BEE on Future Stock Returns

- Firms are sorted into quintile portfolios by BEE for each industry at two-digit level in each year at the end of April in year t and hold for the next 12 months.
- Compare alphas across portfolios derived from CAPM, Fama-French (1993) three-factor, Carhart (1997) four-factor models.

Table 5. Can BEE Predict Future Stock Returns?

Panel A. Equal-weighted (%)							
	1 (Lowest)	2	3	4	5 (Highest)	5 - 1	Annualized
CAPM alpha	0.922*	1.105**	1.045**	1.219**	1.507***	0.585***	7.254%
	(1.830)	(2.202)	(2.047)	(2.420)	(2.834)	(3.380)	
Three-factor alpha	-0.071	0.084	-0.027	0.182	0.386	0.457***	5.624%
	(-0.216)	(0.273)	(-0.092)	(0.639)	(1.302)	(2.760)	
Four-Factor alpha	-0.201	-0.014	-0.140	0.074	0.290	0.491***	6.051%
	(-0.659)	(-0.047)	(-0.506)	(0.278)	(1.026)	(2.890)	
Panel B. Value-weighted (% by tradable market capitalization)							
	1 (Lowest)	2	3	4	5 (Highest)	5 - 1	Annualized
CAPM alpha	0.247	0.416	0.562	0.616	1.353***	1.107***	14.122%
	(0.677)	(1.024)	(1.310)	(1.454)	(2.870)	(3.970)	
Three-factor alpha	-0.258	-0.241	-0.209	-0.088	0.524*	0.782***	9.795%
	(-0.843)	(-0.758)	(-0.715)	(-0.302)	(1.725)	(3.280)	
Four-Factor alpha	-0.349	-0.331	-0.308	-0.168	0.461	0.810***	10.163%
	(-1.182)	(-1.072)	(-1.112)	(-0.590)	(1.540)	(3.390)	
Panel C. Fama-MacBeth regression							
R_BEE	R_lnMKV	R_lnB2M	R_MOM	R_Leverage	R_SDRet	Constant	R ²
0.056**	-0.361***	0.007	-0.088	-0.004	-0.257***	3.983***	0.072
(2.100)	(-3.613)	(0.110)	(-0.759)	(-0.066)	(-3.287)	(3.569)	

The Predictability of BEE on Unexpected Future Earnings

- Following Mayew and Venkatachalam (2012), we relate BEE to unexpected future earnings to investigate whether BEE contains novel information about earnings that has not been realized by analysts.
- Unexpected future earnings = $(EPS_{i, t+1} - \text{forecasted } EPS_{i, t+1}) / \text{stock price two days prior to the earnings announcement}$.

Table 6. BEE and Unexpected Future Earnings

	OLS		IV	
	(1)		(2)	
BEE	0.297***	(4.234)	0.274***	(2.843)
SD_FEPS	-4.276***	(-16.134)	-4.275***	(-16.471)
Industry-year FE	Yes		Yes	
Observations	5,696		5,696	
Adjusted R ²	0.209		0.209	

- SD_FEPS is the standard deviation of forecasted earnings per share from -12 months to two days prior to the earnings announcement

How do firms benefit from market-based transactions?

- Private sector: market-based transactions
 - Litigation incidence (with all other firms)
 - The dependent variable is a dummy variable, which is set at one if a firm experiences any litigation dispute with other firms in the next year, and zero otherwise.
 - Customers: the quality of account receivables
 - Reserve ratio of AR, defined as the ratio of provision for bad AR to total AR at year $t+1$.
 - Suppliers: trade credit from them (account payables)
 - Trade credit from suppliers, defined as the ratio of account payables AP at $t+1$ divided by total assets at t

How do firms benefit from non-market-based transactions?

- Public sector: non-market-based transactions
 - Government: subsidy
- Hybrid sector
 - Creditor: collateral requirement on bank borrowings
 - Voluntarily disclosed, data is available since 2006
 - $Var = \frac{\text{collateralized loans}}{\text{total loans}}$ at year $t+1$

Table 8. Securing Benefits from Stakeholders in Public Sectors – Government Subsidy

Panel A. All sample and subsamples by political environment						
	All sample		National turnover years		City heads' tenure	
			Yes	No	Early	Late
	OLS	IV	OLS			
	(1)	(2)	(3)	(4)	(5)	(6)
BEE	0.425***	0.509***	0.530***	0.121	0.431**	-0.070
	(4.143)	(3.221)	(3.203)	(0.923)	(2.507)	(-0.422)
<i>Equal coefficient?</i>			-0.409**		-0.502***	
Observations	10,054	10,054	4,774	5,280	3,213	1,925
Adjusted R ²	0.517	0.138	0.576	0.540	0.571	0.636
Panel B. Subsamples by ownership, political connectedness, and firm size						
	SOE		Political connectedness		Firm size	
	Yes	No	Yes	No	Large	Small
	(1)	(2)	(3)	(4)	(5)	(6)
BEE	0.241*	0.419***	0.309**	0.478***	0.377**	0.496***
	(1.796)	(3.093)	(2.155)	(3.633)	(2.555)	(3.152)
<i>Equal coefficient?</i>	0.178*		0.169*		0.119	
Observations	4,864	5,190	3,021	7,033	3,348	3,348
Adjusted R ²	0.499	0.564	0.630	0.499	0.682	0.448

Table 9. Reducing Transaction Costs and Securing Benefits in Hybrid Sectors – Collateral Requirement

Panel A. All sample and subsamples by financial constraint						
	All sample		Z-score		Dividend payout	
			High	Low	Early	Late
	OLS	IV	OLS			
	(1)	(2)	(3)	(4)	(5)	(6)
BEE	-0.054**	-0.144***	0.019	-0.137***	-0.027	-0.106**
	(-1.966)	(-3.471)	(0.450)	(-2.699)	(-0.785)	(-2.472)
<i>Equal coefficient?</i>			-0.155***		-0.079**	
Observations	6,199	6,199	2,069	2,069	3,968	2,231
Adjusted R ²	0.276	0.273	0.233	0.365	0.244	0.331
Panel B. Subsamples by ownership, political connectedness, and firm size						
	SOE				Political connectedness	
	Yes	No			Yes	No
	(1)	(2)			(3)	(4)
BEE	-0.136***	-0.014			-0.109**	-0.032
	(-3.310)	(-0.377)			(-2.325)	(-0.921)
<i>Equal coefficient?</i>	0.122***				0.077**	
Observations	2,992	3,207			1,905	4,294
Adjusted R ²	0.264	0.240			0.288	0.279

What Factors Prevent Firms from Spending more BEE?

- We have documented positively marginal effect of BEE on firm performance. A natural question is that: Why firms don't spend more on BEE to improve firm value?
- Two possible factors:
 - The accessibility to key decision makers of stakeholders
 - Political connectedness
 - Firm size

 - The existence of managerial agency problem
 - Managerial incentive scheme
 - Managerial shareholding

Table 10. The accessibility to key decision makers of stakeholders

	Political Connectedness				Firm Size			
	OLS		IV		OLS		IV	
	Yes	No	Yes	No	Big	Small	Big	Small
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Panel A. Asset Turnover</i>								
BEE	0.123	0.375***	0.134***	0.176***	0.185*	0.382***	-0.067	0.272**
	(1.274)	(4.467)	(3.148)	(3.713)	(1.672)	(4.023)	(-0.148)	(2.306)
<i>Equal coefficient?</i>	0.253**		0.042		0.197***		0.338***	
Observations	3,021	7,033	3,021	7,033	3,448	3,451	3,448	3,451
Adjusted R ²	0.842	0.748	0.640	0.591	0.874	0.639	0.693	0.469
<i>Panel B. ROA</i>								
BEE	0.005	0.039***	0.017	0.034***	0.015	0.042***	-0.102*	0.038**
	(0.353)	(3.958)	(1.463)	(2.884)	(1.079)	(2.970)	(-1.845)	(2.156)
<i>Equal coefficient?</i>	0.034**		0.017**		0.028***		0.140***	
Observations	3,021	7,033	3,021	7,033	3,448	3,451	3,448	3,451
Adjusted R ²	0.561	0.507	0.390	0.373	0.646	0.430	0.440	0.272
<i>Panel C. Tobin's Q</i>								
BEE	0.445	0.935***	0.264	1.068***	0.320	0.725***	0.073	0.691**
	(1.538)	(4.871)	(0.865)	(3.990)	(1.226)	(3.135)	(0.244)	(2.435)
<i>Equal coefficient?</i>	0.490*		0.804**		0.405**		0.617**	
Observations	3,021	7,033	3,021	7,033	3,448	3,451	3,448	3,451
Adjusted R ²	0.775	0.745	0.624	0.613	0.771	0.713	0.594	0.588

Table 11. The existence of managerial agency problem

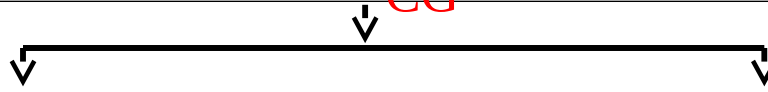
	Managerial Incentive Scheme				Managerial Shareholding			
	OLS		IV		OLS		IV	
	Yes	No	Yes	No	Big	Small	Big	Small
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Panel A. Asset Turnover</i>								
BEE	-0.085	0.403***	0.079	0.168**	0.104**	0.564***	0.043	0.327***
	(-0.799)	(5.368)	(1.250)	(2.122)	(2.309)	(3.866)	(1.257)	(3.875)
<i>Equal coefficient?</i>	0.488***		0.089		0.460***		0.284**	
Observations	1,249	8,805	1,249	8,805	3,354	3,414	3,354	3,414
Adjusted R ²	0.849	0.747	0.761	0.596	0.869	0.697	0.697	0.515
<i>Panel B. ROA</i>								
BEE	-0.016	0.041***	0.012	0.036***	0.007	0.055***	0.005	0.055***
	(-0.756)	(4.601)	(0.930)	(3.652)	(0.718)	(3.057)	(0.532)	(2.879)
<i>Equal coefficient?</i>	0.056***		0.024**		0.048***		0.050***	
Observations	1,249	8,805	1,249	8,805	3,354	3,414	3,354	3,414
Adjusted R ²	0.647	0.471	0.555	0.348	0.618	0.468	0.435	0.325
<i>Panel C. Tobin's Q</i>								
BEE	0.119	0.989***	-0.574	0.631***	0.831***	0.704**	0.396**	0.479*
	(0.262)	(5.563)	(-0.968)	(3.151)	(3.377)	(1.992)	(2.558)	(1.807)
<i>Equal coefficient?</i>	0.870***		1.205***		-0.127		0.082	
Observations	1,249	8,805	1,249	8,805	3,354	3,414	3,354	3,414
Adjusted R ²	0.806	0.728	0.685	0.603	0.752	0.738	0.610	0.610

Conclusion

Why do firms entertain their stakeholders?

1) reduce TC in market-based transactions; 2) secure favors in non-market-based transaction; 3) mixed evidence on the role of

CG



Whether firms benefit from BEE? **YES, sales/TA, ROA,**

Do market participants fully understand BEE? **No, return, UE**

Q

How do firms benefit from BEE through different stakeholders?
1) litigation incidence, customers (quality of AR), and suppliers (AP); stronger effect for firms facing higher TC
2) governments (subsidies) and creditors(collateral requirement on loans)

What factors prevent firms from optimizing their BEE?

1) Accessibility; 2) Managerial agency problem

Contributions

- The first study that systemically explores the reasons and benefits of entertaining business stakeholders.
- Also contribute to the young but growing literature on the importance of social networks in corporate finance
 - Prior studies have found that a firm's social networks can facilitate the various corporate activities such as investment performance (Hochberg et al., 2007) and bank borrowing (e.g., Engelberg et al., 2012a), **while our study focuses on the activities that build up the social networks.**
- A new dataset to measure transaction costs at firm level.

Thanks!