Do Political Ties Increase Firms’ Foreign Expansion? —Evidence from Private Chinese Firms

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Abstract: Political ties that a firm maintains shape its foreign expansion. This study posits that politically connected firms are better able to enter foreign markets than non-connected firms are as the former are better able to take advantage of economic, symbolic, and political resources accessed through those connections. Moreover, the impact of political ties is contingent on the internal resources and capability of politically connected firms. An investigation of the political ties maintained by Chinese private firms offers a robust support for these proposed effects. These findings have implications for research on foreign market entry, corporate political strategy, and the internationalization strategy of emerging economy firms.

JEL Classifications: M10, M13, M16

Keywords: Political ties, Foreign expansion, Technological capability, Financial leverage, Emerging economy
1. Introduction

The vast majority of international management research suggests that international expansion by firms is a process fraught with risks and uncertainty due to the differences in geography, politics, economics, and culture between home countries and host countries (Dunning, 1993). However, relatively less attention has been directed at a firm’s social networks in its home country as a source of competitive advantage, despite the prodigious amount of evidence on the influence of social networks on firm strategy and performance (Coleman, 1990; Burt, 1992; Gulati, Nohria, and Zaheer, 2000). A few recent studies have indicated that firms’ business ties (e.g., ties with buyers and suppliers) and institutional ties (e.g., ties with government and universities) affect their foreign expansion activities (Guillén, 2002; Yiu, Lau, and Bruton, 2007; Guler and Guillén, 2010), but they have regarded different types of network ties as generic conduits for information and resource exchanges between focal firms and external institutions. To the extent that different types of network ties are characterized by distinct content (McEvily and Marcus, 2005; Mahmood, Zhu and Zajac, 2011), binding different types of ties together might mask their inherently distinct ways of shaping internationalization.

To tackle this research gap, this study examines how an important but understudied type of social network ties—namely, a firm’s political ties to the government and its agencies—shapes the firm’s propensity to expand abroad. Building on the theory of foreign expansion and its emphasis on firm-specific advantages developed in a firm’s home country (Hymer, 1976; Dunning 1980), this study seeks to demonstrate how the incorporation of literature on corporate political strategy can offer a comprehensive and insightful analysis of the impact of a firm’s social networks in a home country on its foreign expansion. Our analysis focuses on political ties and foreign market entries of firms in emerging economies. Political ties play a particularly salient role in shaping firm strategy in emerging economies primarily because of the underdeveloped market infrastructure and the intense involvement of the government in economy (Khanna and Palepu, 1997; Ledeneva, 1998; Khwaja and Mian, 2005). Firms resort to political ties to acquire the desired information and resources that otherwise would be difficult or impossible to secure from external markets (Peng and Luo, 2000; Siegel, 2007). To the extent that foreign market entry requires access to a set of tangible and intangible resources, political ties are likely to influence firms’ propensity to expand abroad. By examining firms in emerging economies to contextualize our theoretical and empirical analysis, our study offers an ideal setting in which to study the importance of political factors in firms’ pursuit of international opportunities. It also sheds light on how the “institutional components” specific to emerging economies shape the internationalization of firms—an understudied subject in prior foreign expansion research focusing on internally generated assets and capabilities (Dunning, 1995; Wright, et al., 2005).

This study develops a framework that specifies whether and how political ties maintained by a firm’s CEO can affect the firm’s ability to leverage and exploit resources required for foreign expansion, develop a competitive advantage, and enter foreign markets successfully. Following prior research on the importance of top managers’ political networking to firm performance (Fan, Wang, and Zhang, 2007), this study measures a CEO’s political ties by assessing his or her current and former affiliations with the government and its agencies. This study argues that the benefits derived from a firm’s political ties in its home country can affect its propensity to enter foreign markets. Moreover, this study proposes that the impact of political ties on foreign expansion is contingent on firms’ internal resources and capabilities. In essence, our study suggests that firm-specific advantages arising from political ties determine foreign expansion, both individually and in combination with advantages that firms develop within their boundaries.

This study conducts our empirical analysis using a novel dataset involving 236 cases of private firms in China in 2005. Private Chinese firms, which are characterized by great embeddedness in
political networks and substantial variation in internationalization activities, provide a particularly appropriate setting in which to explore our research questions. Our results support the prediction that political ties facilitate foreign market entry, and the positive effects of political ties are enhanced by technological capability and financial leverage. Our results are robust to the tests using alternative methods and specifications.

Our study makes important contributions to the theory of corporate political strategy. Specifically, this study enriches prior research on foreign expansion by highlighting the importance of firms’ interplay with the government—an important external institution that shapes the institutional context in which firms are embedded. Political ties and other internally generated assets and capabilities collectively shape the opportunities and constraints that firms in emerging economies face. In so doing, this study responds to the call from scholars such as Child and Rodrigues (2005) for research on how firms’ networking with external bodies affects their internationalization process, especially in the context of emerging economies. This study also contributes to the emerging literature about the efficacy of political capital in shaping firm strategies by investigating the role of political ties in foreign market entry. It shows that the home country’s specific advantages originating from firms’ political networks can be transferred to foreign locations, thereby creating a competitive advantage overseas.

In the next section, Section 2 reviews the literature and develops a set of hypotheses. Section 3 discusses the sample selection process and data measurement. Section 4 describes the research models and analyzes the empirical results. Section 5 presents our conclusions.

2. Literature Review and Hypotheses Development

Transnational entrepreneurs rely on economic, social, and cultural resources to navigate multiple institutional environments (i.e., social networks, power relations) when making strategic decisions about internationalization (Terjesen and Elam 2009). International exposure from informal (geographically proximate firms) and formal (international customers and alliance partners) social network relationships positively impacts new venture internationalization (Fernhaber and Li 2013; Khavul, Perez-Nordtvedt, and Wood 2010). Among the social network ties examined in prior studies focused on foreign expansion, political ties are an important but understudied type of ties whose effects are shaped to a large extent by the institutional environment. Political ties are a special type of institutional connection in which the major actors to be connected are the government and its agencies—key players in many emerging economies in the current global competition, such as China, in terms of exerting strategic resource allocation and regulatory controls on firms. Although recent theoretical development highlights the particular importance of institutional ties to firms from emerging economies in their coping with local institutional inefficiency and deficiencies, the differentiated role of political ties is underexplored (Yiu et al., 2007).

In emerging economies, top managers’ personal linkages with the government serve as a critical channel of business–government interplay. These political ties bear implications for the survival and profitability of firms to the extent that they shape firms’ access to information, resources, and preferential treatments (e.g., Backman, 2001; Khwaja and Mian, 2005; Faccio, Masulis, and McConnell, 2006) and affect their legitimacy (e.g., Peng, 2003; Siegel, 2007). The importance of political ties in emerging economies is primarily attributed to the prevalent institutional voids in economic and legal systems (Khanna and Palepu, 1997). The underdeveloped market infrastructures and weak enforcement of contracts make transaction costs in emerging economies extremely high. Consequently, firms draw upon political ties as a venue through which to acquire desirable information and resources with much lower levels of uncertainty and opportunism as such ties provide
informal institutions, such as trust, reciprocity, and obligations, as substitutes to the underdeveloped formal institutions (Nee and Su, 1996; Xin and Pearce, 1996).

This study argues that politically connected firms are more likely to enter foreign markets than their non-connected counterparts because of their favorable access to resources and information, administrative privileges, enhanced legitimacy, and superior political capabilities. First, political ties might provide access to scarce and valuable resources that are conducive to foreign expansion. Compared to non-connected firms, politically connected firms can get more bank loans from government banks (Johnson and Mitton, 2003; Khwaja and Mian, 2005; Leuz and Oberholzer-Gee, 2006), enabling them to make large capital investments overseas. The government can also provide human resources to connected firms using its jurisdiction over research institutes and universities, promoting the development of technological and managerial assets of firms. Political ties also serve as conduits for information about economic policies and regulations, such as policies regarding foreign exchange rates, interest rates, and the relative importance of domestic versus foreign markets—all of which bear important implications for firms’ internationalization strategies. Given the information asymmetry and constantly changing policies in emerging economies, such information is particularly valuable for firms to make strategic decisions, such as whether to enter a foreign market (Keister, 1998; Khanna and Palepu, 1999). Previous studies in the context of China have shown that firms are able to acquire critical information and resources, such as financial capital and technology, which are difficult to obtain through arm’s-length relationships through political ties (Xin and Pearce, 1996; Li and Atuahene-Gima, 2001; Li and Zhang, 2007).

Second, politically connected firms enjoy favors and administrative privileges provided by the government that facilitate their foreign expansion. They might easily get permits to invest abroad and approval for overseas projects (Buckley et al., 2007). When the government intends to promote the export or global market share of certain industries (e.g., agricultural products in China; consumer electronics in South Korea), politically connected firms are likely to obtain more government support, such as substantial subsidies and greater tax reduction. Thus, new venture international entry is in part an imitative response to the internationalization of other firms in the venture’s home country industry (Fernhaber and Li 2010).

Third, political ties enhance the legitimacy of firms and consequently reduce their liability of foreignness in foreign markets. When entering a new foreign market, firms might lack the legitimacy that is critical for operating in the new market because local actors do not know how reliable and trustworthy the entering firms are (Zaheer, 1995). Political ties might mitigate these concerns because they are a strong signal to the foreign market, suggesting that the government of the home country backs the entering firms. When firms develop ties to the government, which is a highly legitimate institution, these firms’ legitimacy and status increase because the ties imply their conformance to taken-for-granted institutional prescriptions (Meyer and Rowan, 1977; Baum and Oliver, 1991). The enhanced legitimacy and desirability in turn facilitate firms’ attempts to acquire key resources abroad, foster trust with local buyers and suppliers, and thus enable firms to compete effectively with local rivals.

Finally, politically connected firms are able to employ superior political capability in foreign countries and reduce political risks in their host countries. International research has indicated that multinational enterprises are exposed to a variety of political risks when operating in foreign countries, including government instability, political violence, discriminative policies against foreign firms, expropriation, and corruption (Kobrin, 1979; Henisz, 2000; Henisz and Delios, 2001). Firms with the capacity to deploy or leverage their political resources to initiate or maintain favorable government policies in host countries are able to reduce their political risk substantially (Henisz and Zelner, 2005). Compared to non-connected counterparts, politically connected firms are likely to have such superior political capability due to their rich experience accumulated through intense
interactions with the government in their home countries (Holburn and Zelner, 2010). As a result, they are more able to identify the key politicians and preferences in the host countries they enter, establish good relationships with them, and subsequently exert sufficient pressure on them to remove discriminative policies. In line with the discussion thus far, this study proposes the following hypothesis:

**Hypothesis 1:** *The more political ties a firm has, the greater its rate of foreign market entry.*

After articulating the overarching relationship between political ties and rate of foreign expansion, this study argues that such a relationship is likely to vary across firms depending on their internal assets and capabilities. To enter new foreign markets, firms need to employ large amounts of resources, including both internally accumulated ones and those derived externally from political ties. Firms with distinct internal resource profiles are thus likely to benefit from political ties to different degrees, depending on the extent to which the internally generated assets and capabilities complement those acquired through political ties. Specifically, this study examines how the efficacy of political ties on foreign market entry varies across firms with different levels of technological capabilities and financial leverage—two of the most fundamental sources of competitive advantages.

Firms with superior technological capability are better able to leverage this competitive advantage in foreign markets so as to outperform indigenous firms and enhance profitability (Hymer, 1976; Dunning, 1980). When politically connected firms are technologically advanced, they are more likely to pursue international opportunities successfully by taking advantage of the various tangible and intangible resources derived from political ties. With sufficient financial and human resource investment in R&D activities, innovative firms are more able to generate new products customized for foreign markets through numerous trials under the guidance of technological knowledge. They are also more able to ally with highly innovative indigenous firms in host countries and share technological resources with less innovative local firms in exchange for their superior country-specific resources, thanks to their enhanced legitimacy. Furthermore, firms with superior technologies might have greater opportunities to interact with host countries’ government officials, thereby being better able to deploy their political capability to create a favorable political environment for their foreign operations. Accordingly, this study hypothesizes the following:

**Hypothesis 2:** *The technological capability of a firm will positively enhance the effect of political ties on its rate of foreign market entry.*

The financial leverage of a firm indicates its dependence on external financial resources (Pfeffer and Salancik, 1978). Highly leveraged firms are more dependent on external financial resources relative to their counterparts with low debt ratios. In emerging economies where the financial market is generally underdeveloped (Khanna and Palepu, 1997), political ties serve as an important channel through which firms can acquire financial resources. Faccio (2006) finds that politically connected firms have easier access to debt financing and enjoy lower taxation. Khwaja and Mian (2005) demonstrate that politically linked firms borrowed twice as much as non-connected firms from government banks in Pakistan. Johnson and Mitton (2003) show that firms connected to powerful politicians received substantial government subsidies in Malaysia. As highly leveraged firms are more reliant on external financial capital, political ties to the government and its agencies that control financial resources are more valuable to highly leveraged firms than to lower leveraged ones.

To the extent that foreign expansion requires sufficient financial capital to establish operations, construct supply chains and marketing channels, and overcome the liability of foreignness arising from a limited knowledge of local rules and practices, firms can benefit more from political ties.
when they are highly leveraged than when they are less leveraged. This study therefore proposes the following:

Hypothesis 3: The financial leverage of a firm will positively enhance the effect of political ties on its rate of foreign market entry.

3. Sample Selection and Data Measurement

Our conceptual framework specifies how a CEO’s political ties will affect the firm’s rate of foreign expansion and how the effect will be contingent on the firm’s technological capability and financial leverage. To test the proposed hypotheses, data on a firm’s foreign expansion, its resource profile, and its CEO’s political ties are needed. As no database currently exists that integrates the types of information needed, a unique database, integrating data from multiple sources is compiled.

The sample for this study consists of 236 Chinese private firms listed on either Shanghai or Shenzhen stock exchanges as of the end of 2005. Data on firms’ basic information were obtained from the China Stock Market and Accounting Research (CSMAR) database, which is a comprehensive and reliable data source for Chinese listed firms that has been widely used in previous studies (e.g., Fan, Wong, and Zhang, 2007). The data on political ties were collected from the yearbooks of Chinese People’s Congress (CPC), the yearbooks of Chinese People’s Political Consultative Conference (CPPCC), and the official websites of these two institutions. This study also traced the CEOs’ work experience in the government and the military as well as their leadership history in industry associations from the profile of senior managers, provided by CSMAR. Data on the foreign expansion of firms were manually collected from companies’ annual reports, companies’ websites, and the Chinese Statistic Bureau. Patent data were collected from the State Intellectual Property Office of P.R.C. (http://www.sipo.gov.cn/zljs/). The final dataset consists of 236 firm-year observations with annual financial data in 2005. Of the 236 firms, 31 firms entered new foreign markets during 2005.

Our focus on private firms provides an appropriate research setting for examining the impact of political ties on foreign expansion. Unlike state-owned firms that naturally receive support and protection from the government, private firms have to engage in political activities so as to influence government policies and create a favorable political environment. Thus, political ties are crucial for private firms as a substitute for formal institutional support endowed exclusively to state-owned firms by the government (Peng and Luo, 2000; Li and Zhang, 2007). Furthermore, substantial variation exists across private firms in China regarding their technological capability and financial leverage, thus enabling us to examine how the relationship between political ties and foreign expansion is contingent on these two characteristics of firms.

Table 1 on the next page presents information on the organizational characteristics and foreign expansion activities of the sample firms. The first row shows that 179 of the 236 sample firms (about 76%) had political ties. Compared to non-connected firms, politically connected firms are younger, larger, higher leveraged, and more inclined to enter foreign markets. However, they demonstrate no significant differences in their innovativeness, number of subsidiaries, or number of foreign countries entered.

A dummy variable for the foreign expansion is created and used as the dependent variable. It is coded as 1 if the firm had opened at least one operation in foreign countries during 2005 and 0 otherwise. This study focus on three independent variables: political ties, patents, and debt ratio. This study traced each CEO’s political ties by examining whether he or she was (1) a member of the Chinese People’s Congress at the national, provincial, or municipal level; (2) a member of the Chinese People’s Political Consultative Conference (CPPCC) at the national, provincial, or municipal
level; (3) currently or formerly a government officer; and (4) currently or formerly a leader of industry associations. This study used the sum of these four types of political ties as the measure of a CEO’s political ties. The patents measure captures a firm’s technological capability as it denotes the total number of patents granted to the firm. The debt ratio measure reflects a firm’s financial leverage; it is calculated as the ratio of liability to total assets of the firm.

### Table 1. Organizational Characteristics and Foreign Expansion of Sample Firms

<table>
<thead>
<tr>
<th></th>
<th>Total sample</th>
<th>Politically connected firms</th>
<th>Non-connected firms</th>
<th>Difference in mean</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Number of firms</td>
<td>236</td>
<td>179</td>
<td>57</td>
<td>N/A</td>
</tr>
<tr>
<td>2. Firm age</td>
<td>9.69</td>
<td>9.48</td>
<td>10.33</td>
<td>-0.85*</td>
</tr>
<tr>
<td>3. Firm assets (in millions of Chinese Yuan)</td>
<td>1,680</td>
<td>1,880</td>
<td>1,060</td>
<td>816***</td>
</tr>
<tr>
<td>4. Number of employees</td>
<td>2,086</td>
<td>2,451</td>
<td>918</td>
<td>1,533***</td>
</tr>
<tr>
<td>5. Patents</td>
<td>6.10</td>
<td>6.36</td>
<td>5.26</td>
<td>1.10</td>
</tr>
<tr>
<td>6. Debt ratio</td>
<td>0.64</td>
<td>0.68</td>
<td>0.52</td>
<td>0.15**</td>
</tr>
<tr>
<td>7. Foreign expansion dummy</td>
<td>0.13</td>
<td>0.15</td>
<td>0.07</td>
<td>0.08**</td>
</tr>
<tr>
<td>8. Number of internationalized firms that entered foreign markets in 2005</td>
<td>31</td>
<td>27</td>
<td>4</td>
<td>N/A</td>
</tr>
<tr>
<td>9. Number of foreign subsidiaries of internationalized firms</td>
<td>55</td>
<td>47</td>
<td>8</td>
<td>N/A</td>
</tr>
<tr>
<td>10. Average number of foreign subsidiaries of internationalized firms</td>
<td>1.8</td>
<td>1.8</td>
<td>2</td>
<td>-0.20</td>
</tr>
<tr>
<td>11. Average assets of foreign subsidiaries (in millions of U.S. dollars)</td>
<td>1.48</td>
<td>1.48</td>
<td>1.40</td>
<td>0.08</td>
</tr>
<tr>
<td>12. Number of foreign countries entered by internationalized firms</td>
<td>44</td>
<td>36</td>
<td>8</td>
<td>N/A</td>
</tr>
</tbody>
</table>

**Notes to Table 1:** Two tailed tests for all variables.

Asterisks *, **, and *** indicate significant levels at 10%, 5%, and 1%, respectively.

The dependent variable Foreign expansion dummy is coded as 1 if the firm had at least one operation in foreign countries and 0 otherwise. We define three independent variables: political ties, patents, and debt ratio. We traced a CEO’s political ties by examining whether he/she was (1) a member of the Chinese People’s Congress of either the national, provincial, or municipal level; (2) a member of the Chinese People’s Political Consultative Conference (CPPCC) of either the national, provincial, or municipal level; (3) currently or formerly a government officer; and (4) currently or formerly a leader of industry associations. The sum of these four types of political ties is the measure of a CEO’s political ties. The measure of a CEO’s political ties for politically connected firms is at least 1; and the measure of a CEO’s political ties for non-connected firms is 0. The Patents measure is defined as total number of patents granted to the firm. The Debt ratio measure is defined as the ratio of liability to total assets of the firm. Firm age is the number of years since the firm was established.

Following previous studies (Guillén, 2002; Yiu, Lau and Bruton, 2007), a set of firm characteristics that might also affect the internationalization of the firm are controlled for. Firm Size is measured by the natural logarithm of a firm’s total assets. It is predicted that larger firms tend to have more resources for internationalization. Firm age is the number of years since the firm was established. It is also predicted that older firms are risk averse and less likely to engage in expansion abroad. Previous expansion is a dummy variable that is equal to 1 if a firm entered foreign markets before January 1, 2005 and 0 otherwise. Firms with experience in foreign expansion tend to enter more foreign markets. In addition, nine industry dummies representing ten industries were also included in the analysis.

The Cox proportional hazard model is used to estimate the effect of political ties and covariates on the rate of foreign expansion. Hazard rates of foreign expansion were modeled as a function
of the baseline hazard \( (h_0) \) at time \( t \) and the effects of covariates of interest. The baseline model estimated is as follows:

\[
h(t) = h_0(t) \exp (b_1 \text{Politicaltie} + b_2 \text{Politicaltie} \times \text{Patent} + b_3 \text{Politicaltie} \times \text{Debt ratio} + X)
\]

where \( h(t) \) is the likelihood at time \( t \); \( h_0(t) \) is the baseline hazard at time \( t \); and \( X \) is the vector of control variables. H1 predicts \( b_1 > 0 \), and H2 and H3 predict \( b_2 > 0 \) and \( b_3 > 0 \), respectively.

4. Empirical Analysis

Table 2 reports the summary statistics and correlations among variables. It shows significant heterogeneity in whether a firm expanded abroad during 2005, with a standard deviation (0.34) almost three times higher than the mean (0.13). It also shows significant variation in political ties, which has a mean of 1.23 and a standard deviation of 0.86.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>S.D.</th>
<th>Min.</th>
<th>Max.</th>
<th>1.</th>
<th>2.</th>
<th>3.</th>
<th>4.</th>
<th>5.</th>
<th>6.</th>
<th>7.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Foreign expansion dummy</td>
<td>0.13</td>
<td>0.34</td>
<td>0</td>
<td>1</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Political tie</td>
<td>1.23</td>
<td>0.86</td>
<td>0</td>
<td>4</td>
<td>0.14*</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Previous expansion</td>
<td>0.05</td>
<td>0.22</td>
<td>0</td>
<td>1</td>
<td>0.55*</td>
<td>0.10</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Patent</td>
<td>6.12</td>
<td>17.06</td>
<td>0</td>
<td>161</td>
<td>0.10</td>
<td>0.04</td>
<td>0.04</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Debt ratio</td>
<td>0.64</td>
<td>0.50</td>
<td>0.07</td>
<td>7.51</td>
<td>-0.07</td>
<td>-0.11</td>
<td>-0.04</td>
<td>-0.04</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Firm size (^a)</td>
<td>7.05</td>
<td>0.86</td>
<td>4.51</td>
<td>9.37</td>
<td>0.21*</td>
<td>0.25*</td>
<td>0.22*</td>
<td>0.19*</td>
<td>-0.12</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>7. Firm age</td>
<td>9.69</td>
<td>4.17</td>
<td>4.00</td>
<td>25.00</td>
<td>-0.08</td>
<td>-0.07</td>
<td>0.04</td>
<td>-0.16*</td>
<td>0.17*</td>
<td>0.10</td>
<td>1.00</td>
</tr>
</tbody>
</table>

Notes: * indicates \( p < 0.05 \).

\(^a\) Natural logarithm of firm assets in millions of Chinese Yuan.

Variable definitions are shown in Table 1.

Table 3 on the next page reports the coefficient estimates and standard errors for five model specifications. Model 1 serves as a baseline model with all of the control variables, while subsequent models add variables to test the hypotheses. The results of Model 1 confirm the conventional wisdom that the rate of foreign expansion increases with a firm’s size, technological capability, and prior experience of internationalization.

Model 2 tested the effect of political ties on the rate of foreign expansion. The results demonstrate that political ties lead to significant increases in the rate of foreign expansion (\( P<0.01 \)). Therefore, H1, which proposes the positive effect of political ties, is supported.

Model 3 tested H2, which proposes complementarities between political ties and technological capability. Model 3 incorporates the interaction term between political ties and patents. Consistent with our expectation, the result shows that political ties are more conducive to foreign expansion when the firm is innovative (\( P<0.05 \)).

Hypothesis 3, predicting that higher levels of financial leverage enhance the positive effect of political ties on the rate of foreign expansion, receives support in Model 4. Model 4 indicates that political ties are more facilitative to foreign market entry when the firm is highly leveraged (\( P<0.05 \)). Model 5 includes all main and interaction terms, and indicates that the results in Model 1 to Model 4 are robust to the additional covariates.
Table 3. Political Ties and Foreign Expansion of Chinese Private Firms

<table>
<thead>
<tr>
<th>Variable</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
<th>Model 4</th>
<th>Model 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Political tie</td>
<td>0.74***</td>
<td>0.78***</td>
<td>0.70***</td>
<td>0.74***</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.23)</td>
<td>(0.25)</td>
<td>(0.24)</td>
<td>(0.25)</td>
<td></td>
</tr>
<tr>
<td>Political tie*Patent</td>
<td>0.41**</td>
<td>0.37**</td>
<td></td>
<td></td>
<td>0.55**</td>
</tr>
<tr>
<td></td>
<td>(0.20)</td>
<td>(0.16)</td>
<td></td>
<td></td>
<td>(0.26)</td>
</tr>
<tr>
<td>Political tie*Debt ratio</td>
<td></td>
<td></td>
<td>0.58**</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.26)</td>
<td></td>
<td>(0.27)</td>
</tr>
<tr>
<td>Patent</td>
<td>0.57**</td>
<td>0.60*</td>
<td>0.87**</td>
<td>0.69**</td>
<td>0.86**</td>
</tr>
<tr>
<td></td>
<td>(0.20)</td>
<td>(0.31)</td>
<td>(0.36)</td>
<td>(0.33)</td>
<td>(0.38)</td>
</tr>
<tr>
<td>Debt ratio</td>
<td>-1.18</td>
<td>-0.56</td>
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<td>-0.58</td>
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<tr>
<td></td>
<td>(1.23)</td>
<td>(1.13)</td>
<td>(1.14)</td>
<td>(1.02)</td>
<td>(1.05)</td>
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<tr>
<td>Firm size</td>
<td>0.49**</td>
<td>0.43*</td>
<td>0.51**</td>
<td>0.40**</td>
<td>0.46*</td>
</tr>
<tr>
<td></td>
<td>(0.24)</td>
<td>(0.24)</td>
<td>(0.24)</td>
<td>(0.20)</td>
<td>(0.25)</td>
</tr>
<tr>
<td>Firm age</td>
<td>-0.03</td>
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<td>-0.04</td>
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<td>(0.05)</td>
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<tr>
<td>Previous expansion</td>
<td>1.81***</td>
<td>1.69***</td>
<td>1.84***</td>
<td>1.80***</td>
<td>1.93***</td>
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<tr>
<td></td>
<td>(0.43)</td>
<td>(0.43)</td>
<td>(0.44)</td>
<td>(0.45)</td>
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<td>Industry fixed effect</td>
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<td>YES</td>
<td>YES</td>
<td>YES</td>
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<tr>
<td>Log-likelihood</td>
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<td>-142.01</td>
<td>-140.10</td>
<td>-140.22</td>
<td>-137.30</td>
</tr>
<tr>
<td>Model chi-square</td>
<td>49.01***</td>
<td>53.53***</td>
<td>57.35***</td>
<td>57.41***</td>
<td>60.32***</td>
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<td>Number of cases</td>
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<td>236</td>
<td>236</td>
<td>236</td>
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</tr>
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</table>

Notes: Asterisks *, **, and *** indicate significant levels at 10%, 5%, and 1%, respectively; two-tailed tests for all variables. Variable definitions are shown in Table 1. Cell entries are coefficients estimates. Numbers in parentheses are standard errors.

A comparison of the full model (Model 5) to the baseline model (Model 1) yields a significant improvement in the overall model fit. This suggests that the baseline model containing economic control variables provides only a partial explanation of the process of foreign expansion of firms. Beyond economic variables, organizational linkages with external institutions, such as the government and its agencies, also shape the foreign expansion decision. Thus, analysis including both economic variables and political ties provides a more complete picture of the process of internationalization.

The evidence so far shows a strong association between political ties and foreign expansion among Chinese firms. However, this result should be interpreted with caution because it is possible that entry into foreign markets leads to the establishment of political connection. For instance, top managers might have a greater chance to be elected as CPC or CPPCC representatives due to the global presence of their firms. To address this causality issue, this study compared the emergence of political ties to firms’ foreign market entry and observed that CEOs’ affiliation with the government largely predates the foreign expansion of connected firms.

As distinct levels of government institutions differ in their political power, the efficacy of political ties in promoting foreign expansion might vary across political ties to national, provincial, and municipal governments. To examine the relative effects of political ties on distinct levels of government institutions, three types of political ties are separately examined: national political ties.

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1 The improvement in goodness of fit is 15.14 (two times the difference in log-likelihood), following a chi-square distribution with three degrees of freedom (p<0.01).
(including membership in national CPC, membership in national CPPCC, work experience at the central government), provincial political ties (including membership in provincial CPC, membership in provincial CPPCC, work experience at a provincial government), and municipal political ties (including membership in municipal CPC, membership in municipal CPPCC, work experience at a municipal government). The regressions in Table 3 are repeated using the three types of political ties as independent variables. The regression results show that the strongest positive effects arise from national political ties, followed by provincial political ties and municipal political ties, thereby implying that political ties to different levels of government with distinct political strength altered firms’ access to favorable government policies and resources and, as a result, their entry into foreign markets.

5. Conclusion

The role of political capital in firms’ international expansion activities is a neglected avenue of research. Our motivation is to focus on political ties maintained by firms and provide empirical evidence for their impacts on firm internationalization using a novel dataset of firms from China’s emerging economy. This study differentiates the political network from typical institutional and business networks that have primarily been addressed in previous literature. It also examines the interaction of political capital and firm capabilities as well as their financial capacity.

Our study contributes to this ongoing theoretical dialogue in the context of emerging economies by examining the role of political ties in firms’ entry into foreign markets. Our findings shed light on the role of corporate political strategy in internationalization by firms from emerging economies. This study provides strong support for the positive facilitation of political networks in firms’ internationalization activities. This is in line with the ownership advantage theory that relational capital helps strengthen firm-specific advantages in a firm’s home country over time, thereby enabling it to leverage the advantages in international expansion. In addition, the demonstrated enhancing effects of technological capabilities and financial leveraging on the political capital–foreign expansion relationship also manifest the capability-based view of internationalization theory. With high-level internal capabilities and financial assets needs, firms are more likely to be motivated by their political networks to go abroad as they are better able to explore the technological advantages of such action and raise capital in international financial markets.

References


~ 10 ~


