Value of Politically Connected Independent Directors: Evidence from the Anti-Corruption Campaign in China *

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Abstract

A new regulation issued in the end of 2013 as part of the anti-corruption campaign in China leads to a wave of resignation of politically connected independent directors (PCID). I find while firms with PCIDs have negative cumulative abnormal return (CAR) around release of the new regulation, they have even larger positive CAR around announcement of PCID resignations, especially for non-SOEs. This is because firms with PCIDs have higher political risk after release of the regulation, but their political risk decreases after PCIDs resign and they are complied with the regulation. I also show operating performance does not change after PCID resignations, casting doubt on the "helping hand" theory of political connections. Moreover, corporate governance improves after firms replace PCIDs, especially for SOEs, suggesting the anti-corruption campaign is authentic.

JEL classification: G32, G34, G38
Keywords: Political connections; Independent directors; Firm value; Corporate governance

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1. Introduction

Political connections are widely considered as valuable resources to firms, especially in emerging markets. Previous studies find that political connected firms have easier access to debt financing (Khwaja and Mian, 2005; Sapienza, 2004) and equity financing (Claessens, Feijen, and Laeven, 2008), preferential regulatory treatment (Faccio, 2006; Johnson and Mitton, 2003), and lower tax rates (Faccio, 2010). Therefore, political connections improve firm performance and firm value (Fisman, 2001; Goldman, Rocholl, and So, 2008). However, some studies also show that political connections can destroy firm value because connected firms may have higher political risk and thus higher required rate of return from investors (Liu, Shu, and Wei, 2017; Pástor and Veronesi, 2013). Connected firms are also associated with worse corporate governance. Specifically, controlling shareholders expropriate more on minority shareholders (Tu, Lin, and Liu, 2013; Wang, 2015); managers are more entrenched (Cao, Pan, Qian, and Tian, 2017); and boards of directors have less industry experts (Fan, Wong, and Zhang, 2007). The recent study of Akcigit, Baslandze, and Lotti (2018) find that although politically connected firms have a higher rate of survival, as well as growth in employment and revenue, they are much less likely to innovate and have lower productivity. Several studies also find that while political connections are valuable to firms, the rent-seeking behavior distorts the allocation of economic resources and therefore brings about costs to the society overall (Claessens et al., 2008; Khwaja and Mian, 2005). Therefore, evidence on the overall effect of political connections is still mixing.

Although previous studies have investigated various effects of political connections, most of them focus on connections from blockholders and executives instead of independent directors, possibly because most connections are built by top insiders. However, it was prevalent for Chinese firms to appoint politicians as independent directors to build political connections. Appointing politically connected independent director (PCID) may help firms to build connections and thus increase firm value, but it may also distort the original role that independent directors should play in firm's governance and thus destroy firm value. Therefore, this study tries to extend existing research by focusing on PCIDs and shed more light on the overall effect of political connections.

In early 2013, Chinese government started a massive anti-corruption campaign after President Xi Jinping came to power. During this campaign, a new regulation known as Regulation No.18 was issued by the Organization Department of the CPC Central Committee on October 19, 2013. The new regulation prohibits all levels of government officials, who are currently in an official position or retried within 3 years, from taking any part-time position in firms and getting any kind of payment from firms. Many government officials had to resign from firms because of the regulation. Independent director is the largest group affected by this regulation given the prevalence of Chinese firms offering these positions to officials. Since officials are not required to resign immediately, we witnessed a wave of resignation of PCIDs in the following two years. Using this regulation as a shock, I examine the effect of losing PCIDs on Chinese listed firms in this study.

One would expect firms with PCIDs decrease in firm value after the release of Regulation No.18, because they may lose the various benefits from political connections, which leads to worse operating performance or less cash flows (cash flow explanation). However, since PCIDs do not necessarily resign right after the release of the regulation, firms with PCIDs may have higher political risk than other firms before their PCIDs actually leave, which leads to higher discount rate by investors and thus decrease in firm value (political risk explanation). To explore these two explanations, I further test the value effect when firms announce the actual resignation of their PCIDs. If the cash flow explanation holds, firm value should not change around announcement of PCID resignation since the loss of political connection is already expected by the market when Regulation No.18 is released. Moreover, firms should have worse operating performance after losing PCIDs. On the contrary, if the political risk explanation holds, firms should gain in firm value around PCID resignation because of lower political risk after announcing the actual leave of PCIDs. Furthermore, since previous studies find political connections may be costly in terms of corporate governance, especially if the connection is built by independent directors who play an important role in governance, I propose firms improve in corporate governance after losing PCIDs. Specifically, monitoring efficiency of board of directors increases; management entrenchment decreases; expropriation from controlling shareholders decreases; and entertainment and travel costs decrease.

I use two methods to identify PCID in this study. First, I check the reasons of independent director resignations from their resignation reports. If a firm reports its independent director resigns in order to comply with Regulation No.18, I identify the independent director as being politically connected. Second, for the other resigning independent directors, I use the most popular definition of political official in the literature: directors who are current or former (1) government officials, (2) members of the People's Congress (CPC), or (3) members of the People's Consultative Conference (CPPCC) (Chen, Li, Su, and Sun, 2011; Fan et al., 2007; Li, Meng, Wang, and Zhou, 2008). My final sample includes 418 treated firms that have PCID resignations and 418 controlled firms matched with the treatment group using propensity score matching. The sample period is from 2011 to 2016. I have three event dates (year) in this study. The first one is the issuance date of Regulation No.18 and the second one is the announcement date of PCID resignation, which is different across firms. Since the resignation of an independent director cannot take effect if the fraction of independent directors is less than one third until the firm appoints a new director, the third one is the actual leaving date (year) of the resigning PCID.

This study has four main findings. First, the treatment group has significantly negative cumulative abnormal return (CAR) around release of Regulation No.18, especially in the longer event windows. This is consistent with the first hypothesis that firms with PCIDs decrease in firm value because of the new regulation. Second, treated firms have large and significantly positive CAR around announcement of PCID resignations, providing support to the political risk explanation. However, the cross-sectional regression of CAR shows that the value effect is significant for non-SOEs but not significant for SOEs. Third, using a difference-in-difference regression model, I find that firms' operating performance does not change after their PCIDs resign. This suggests that political connections built by PCIDs may not be so valuable for firm performance in China and casts doubt on the "helping hand" theory of political connections. On the contrary, political risk decreases significantly after PCIDs resign, providing further support to the political risk explanation. The sum-sample analysis shows that while non-SOEs decrease significantly in firm risk, SOEs' firm risk does not change, which is consistent with results from CAR analysis. One possible explanation for the different results is that SOEs have more other political connections than non-SOEs because of their special relation with the government. Even their PCIDs leave, they still have other connections and thus the same political risk. Fourth, corporate governance improves significantly after PCIDs resign. The improvement is more prominent for SOEs, possibly because SOEs have more serious governance problem before replacing PCIDs and one of the aims of the anti-corruption campaign is to curb corruption in SOEs.

This study contributes to the literature in three ways. First, the results cast doubt on the "helping hand" theory of political connections. Although connections may bring benefits to firms and increase firm value, it can also increase firm risk and thus decrease firm value. The results also suggest that political risk is priced by investors in China. Second, I show that the effect of losing PCIDs is different for SOEs and non-SOEs, suggesting that the effect of political connections in contingent on firm's ownership structure. Third, I provide further evidence that politically connected firms are associated with poor corporate governance, especially in SOEs. The improvement in governance after PCID resignations also suggests that the anti-corruption campaign is authentic. This study is also different from existing studies on the anti-corruption campaign in China (e.g., Ding, Fang, Lin, and Shi, 2017; Lin, Morck, Yeung, and Zhao, 2016; Liu, Lin, and Wu, 2018; Griffin, Liu, and Shu, 2018). Specifically, Ding et al. (2017) use the inspection of provincial government as the event and examine the value effect of corruption on firms, while I use Regulation No.18 to test the value effect of political connections. Similarly, Lin et al. (2016) and Griffin et al. (2018) also examine the consequences of corruption on firms. Although Liu et al. (2018) use Regulation No.18

to test the value effect of political connections, they only focus on the value effect around release of the regulation and do not explore the potential mechanisms. While they argue firms have negative CAR around release of Regulation No.18 because they are expected to lose benefits from political connections, my results suggest that the negative CAR is because of higher political risk.

The rest of this paper is organized as follows. Section 2 introduces Chinese institutional background and Regulation No.18. I develop my hypothesis in Section 3. Section 4 describes the data and variables. Section 5 presents empirical results and Section 6 concludes.

2. Institutional Background

First introduced in 1990 with only eight firms listed, China's stock market has become the second largest in the world by 2012. 3052 companies are listed in SHSE and SZSE with market capitalization of about 50 trillion CNY (7.4 trillion USD) as of 2016.[1] However, corporate governance in Chinese listed firms has always been a looming issue because many firms are controlled by the government and legal structures of most firms are complicated. In order to improve corporate governance, on August 16, 2001, China Securities Regulatory Commission (CSRC) issued the *Guideline for the Establishment of the Independent Director System in Listed Firms* (Guideline). The Guideline requires that all firms listed on Chinese stock exchanges should have at least one third of board members as independent directors by June 30, 2003. As in Clarke (2006), the independent director system in China was meant to be a "legal transplant" from the U.S. corporate governance law and practice, but the definition of "independence" is even stricter. A director affiliated with or representing a non-insider block holder who holds more than 1% of shares outstanding is not considered independent in China, while the common ownership threshold for insider classification is 10% in the United States (Jiang, Wan, and Zhao, 2015).

Although the definition of independence is stricter, monitoring from independent directors

[1] Source: The Annual Report of the CSRC.

can be weak in China since many of them are government officials instead of industry experts. Studies have shown that although PCID may bring valuable political resources to firms, it may also distort the original role that independent directors should play in firm's governance. Some Chinese SOEs appoint politicians as independent directors in order to occupy more board seats and achieve political and social objectives (Wang, 2015). For non-SOEs, building good relationship with the government is even more important as the government has large control over resources and Chinese culture values interpersonal connections in business (or *Guanxi* in Chinese). Appointing PCIDs is an easy way to build such a relationship with the government. As a result, appointing PCID was prevalent in Chinese listed firms.

However, this situation has changed from 2013. In early 2013, Chinese government started a massive anti-corruption campaign after President Xi Jinping came to power. During this campaign, the Organization Department of the CPC Central Committee issued a new regulation known as Regulation No.18 on October 19, 2013.[2] This regulation prohibits all levels of government officials, who are currently in an official position or retried within 3 years, from taking any part-time position in firms and getting any kind of payment from firms. Independent director is the largest group affected by this regulation because it was common for firms to appoint PCIDs. Most PCIDs resigned after the release of this regulation. However, since this regulation gives some time for government officials to resign in order to maintain the normal operation of boards, we witnessed a wave of independent director resignations over the next two years. According to the Guideline of CSRC, all listed firms must have at least one third board members as independent. Therefore, the resignation of an independent director cannot take effect if the fraction of independent directors is less than one third until the firm appoints a new director in a shareholder meeting. Some PCID stayed in the board after announcing resignation until they are replaced.

Regulation No.18 is an exogenous shock to the market because it is difficult to anticipate

[2]See Organization Department of the CPC Central Committee, *Guanyu jinyibu guifan dangzheng lingdao ganbu zai qiye jianzhi (renzhi) wenti de yijian (Guidance on the Regulation of Party and Government Leaders Taking Office in Companies)*, issued on October 19, 2013. The original document is available on http://hdtz.buct.edu.cn/docs/20141103161920781696.pdf.

the release of such a regulation. Even though firms could anticipate that their political connections could be affected by the anti-corruption campaign, it is unlikely for them to know to what extent officials would be regulated or the exact time of a new regulation. Moreover, this regulation applies to officials who resigned or retired from the government within 3 years, which means officials could not choose to leave the government and stay in firms. Therefore, some firms unexpectedly lost political connections, especially some privately controlled firms.

3. Hypothesis Development

Previous studies find that political connections are valuable because connected firms have easier access to debt financing (Khwaja and Mian, 2005; Sapienza, 2004) and equity financing (Boubakri, Guedhami, Mishra, and Saffar, 2012; Claessens et al., 2008), preferential regulatory treatment (Faccio, 2006; Johnson and Mitton, 2003), and lower tax rates (Faccio, 2010). These are also summarized as "helping hand" of political connections in the literature. As a result, connected firms have better operating performance and higher firm value than other firms (Fisman, 2001), especially in China where government has large control over resources. After the release of Regulation No.18, some firms are expected to lose political connections as PCIDs are forced to resign. Therefore, I postulate the following:

Hypothesis 1: Firms with PCIDs decrease in firm value following the release of Regulation No.18.

While firms may decrease in firm value, the underlying mechanism is not obvious. First, after the release of Regulation No.18, firms with PCID may lose various benefits associated with political connections, which potentially leads to worse operating performance or less future cash flow. This is summarized as the cash flow explanation. Second, beside the benefits, connected firms may also have higher political risk as predicted by the theory of political uncertainty (Pástor and Veronesi, 2013). Liu et al. (2017) find strong evidence for the existence of priced political risk using the Bo scandal in China. They show that firms connected with Bo suffer great loss in firm value following the scandal. Since Regulation No.18 gives some time for government officials to resign in order to maintain the normal operation of boards, most PCIDs resign during 2014 to 2015. Therefore, firms may have higher political risk before the actual leave of PCIDs, especially during the anti-corruption campaign when connected firms are more likely to be investigated by the government (e.g., Griffin et al., 2018). This leads to higher risk premium by investors and thus decrease in firm value. This is summarized as the political risk explanation.

To explore these two explanations, I further test the value effect when firms announce the actual resignation of their PCIDs. If the cash flow explanation holds, firm value should not change around announcement of PCID resignation since the loss of political connection is already expected by the market when Regulation No.18 is released. Moreover, firms should have worse operating performance as a result of losing political connections. Therefore, I postulate the following:

Hypothesis 2a: Firms value does not change around the announcement of PCID resignation.

Hypothesis 2b: Firms have worse operating performance after replacing PCIDs.

On the contrary, if the political risk explanation holds, firm value should increase around announcement of PCID resignation as firms have lower political risk and thus lower overall firm risk after announcing the actual leave of PCIDs and complying with the regulation. Therefore, I postulate the following:

Hypothesis 3a: Firms value increases around the announcement of PCID resignation.

Hypothesis 3b: Firms have lower risk after replacing PCIDs.

Previous studies find political connections are costly in terms of corporate governance, especially if the connection is built by independent directors who play an important role in governance. The first potential governance problem is weaker monitoring from board of directors, as board characteristics of politically connected firms tend to be different from non-connected firms. Fan et al. (2007) document that politically connected firms in China have fewer directors with business experience from unaffiliated firms, fewer academicians and women serving as directors, and older directors on average. Second, they also find that when the CEO of the firm is politically connected, his or her allies are highly likely to sit on the board. As a result, PCIDs are more likely to be captured by the management. Furthermore, since most PICDs are lack of professional knowledge and experience, they are less likely to prevent executives from entrenchment. For example, Wang (2015) find that SOEs in China with a large fraction of PCIDs have more severe over-investment problems. Third, firms with political connections have more conflicts between controlling and minority shareholders. Wang (2015) argues that some Chinese SOEs appoint politicians as independent directors in order to occupy more board seats and achieve political and social objectives. Therefore, PCIDs tend to behave in the best interest of the State rather than minority shareholders. Politicians sitting on boards of non-SOEs are also highly likely to collude with controlling shareholders for private benefits, such as financial support for future political promotion and financial kickbacks from business transactions. Last, studies find that politically connected firms spend more on establishing and maintaining the connection, which has a significantly negative effect on firm productivity. Cai, Fang, and Xu (2011) show that firm-level "entertainment and travel costs (ETC)" can proxy for firm's expenses on connections. Moreover, as in Lin et al. (2016), ETC also includes executive's spending on their own entertainment and travel. Thus, it may also proxy for self-serving management's spending on private benefits. Therefore, I postulate the following:

Hypothesis 4a: Monitoring efficiency of board of directors increases after replacing PCIDs.

Hypothesis 4b: Management entrenchment decreases after replacing PCIDs.

Hypothesis 4c: Expropriation from controlling shareholders decreases after replacing PCIDs.

Hypothesis 4d: Entertainment and travel costs decrease after replacing PCIDs.

4. Data and Variables

4.1. Data Sources and Identification Strategy

I use two methods to identify PCID in this study. First, I check the reasons of independent director resignations from their resignation reports. CSRC requires listed firms to make public announcements for all major issues, including independent director resignations. A resignation report normally states why an independent director resigns and when the resignation is effective. I collect all independent director resignation reports during the period of January 2013 to May 2017 from the official website of SHSE (www.sse.com.cn) and SZSE (www.szse.cn). Based on the resignation reports, I identify 2342 independent directors resigning from 1477 firms, in which 2217 independent directors from 1433 firms resign after the release of Regulation No.18. If a firm reports its independent director resigns in order to comply with Regulation No.18, I identify the independent director as being politically connected. Second, for the other resigning independent directors, I use the most popular definition of political official in the literature: directors who are current or former (1) government officials, (2) members of the People's Congress (CPC), or (3) members of the People's Consultative Conference (CPPCC) (Chen et al., 2011; Fan et al., 2007; Li et al., 2008). Using the two methods, I identify 741 PCIDs resigning from 562 firms. Then I exclude financial firms and firms whose PCIDs resign after December 2016. Since I use 2010 as the matching year for propensity score matching, I also exclude firms listed after 2010. Finally, I am left with 418 firms, which comprise my treatment group. The sample period is from 2011 to 2016 for the empirical analysis. The firm-level data are from CSMAR database maintained by GTA Information Technology Company Ltd. The background information of independent directors are collected from firm's annual reports. I collect release date of 55 regulatory documents of CSRC from their official website during 2011 to 2016 (www.csrc.gov.cn).

Figure 1 plots the number of independent director resignations during January 2013 to May 2017. The solid line shows that the total number of independent director resignations increase dramatically after the release of Regulation No.18 and goes back to normal level from the beginning of 2016. At the end of 2014 and 2015, there are two peaks when more than 200 independent directors resign within a month. This is probably because they tend to resign in the end of the financial year in order to take full compensation. The dashed line shows that the first resignation of PCID takes place in January 2014 and the last one in June 2016. The distribution of PCID resignations shows the same pattern as that of independent director resignation. Figure 2 plots the actual leaving dates of the resigning PCIDs following the release of Regulation No.18. The first effective resignation takes place in January 2014. Since many Chinese listed firms hold their annual shareholder meetings in April and May, we witness three peaks of effective PCID resignation around May 2014, 2015, and 2016.

I have three event dates (year) in this study. The first one is the release date of Regulation No.18. Since the regulation is issued on Saturday, I use the following Monday (October 21, 2013) as the event date. The second one is the announcement date of PCID resignation, which is different across firms. I use this event date to examine the value effect of PCID resignation. Third, since some of the resignations cannot take effect if the fraction of independent director is less than one third until a new director is appointed in a shareholder meeting, I use the effective date of the resignation as the actual leaving date of the PCID. Since listed firms are also required to make public announcements after each shareholder meeting, it is possible to identify the appointing date of the new director or the actual leaving date of the resigning director. I use this event date (year) to test the change of operating performance, firm risk, and corporate governance. For firms that have more than one independent director resignation, I use the date when the firm loses its first PCID as the event date.

4.2. Variables

I calculate cumulative abnormal return (CAR) around the event dates to measure the value effect of Regulation No.18 and PCID resignation. Following the literature, I use return on equity (ROE) and cash flow from operation (CFO) to measure firm's operating performance. I also use operating profit to total assets (OPOA) and total cash flow (CF) in the robustness tests. It is difficult to measure firm's political risk and isolate political risk from firm's overall risk. Therefore, following Liu et al. (2017), I use stock return volatility to measure firm risk in this study. Volatility is defined as the annual standard deviation of daily stock return multiplied by 100. I also construct a policy sensitivity measure is the spirit of Liu et al. (2017). Specifically, I calculate the firm's CAR from market model over the three-day window around announcements of the new regulatory documents issued by CSRC each year. Then I sum the absolute value of these CAR in the year and use it to proxy firm's policy sensitivity. I use four variables to measure different aspects of corporate governance. First, since Fich and Shivdasani (2006) document that busy boards are not effective monitors, I use independent director busyness to measure monitoring efficiency of board of directors. It is defined as the average number of directorship the firm's independent director hold. Second, previous studies find that higher executive compensation is associated with more entrenchment (e.g., Borokhovich, Brunarski, and Parrino, 1997; Coles, Daniel, and Naveen, 2014). Therefore, I use top three executives' compensation to measure management entrenchment. Third, following the literature (e.g., Wang, 2015), I use related party transactions (RPT) to measure expropriation from controlling shareholders. Fourth, following Cai et al. (2011) and Lin et al. (2016), I calculate "entertainment and travel costs" (ETC) based on information disclosed in annual report notes to measure firm's expenses on political connections and self-serving management's spending on private benefits. All variables used in this study are summarized in Appendix A.

4.3. Propensity Score Matching

In order to use difference-in-difference (DID) regression in empirical analysis, firms in the treatment and control group need to be comparable before release of the new regulation. Therefore, I implement propensity score matching as a resampling technique. Since the regression analysis uses data from 2011 to 2016, I use 2010 as the matching year to make the treatment and control groups comparable throughout the pre-event period. I first estimate the following cross-sectional logit regression in 2010 for all non-financial listed firms in China to estimate an ex-ante probability of being treated, i.e., the propensity score:

$$\begin{aligned} PCID_i = \alpha &+ \beta_1 Size_i + \beta_2 Leverage_i + \beta_3 B/M_i + \beta_4 Growth_i \\ &+ \beta_5 Top1_i + \beta_6 Independence_i + \beta_7 Board\ size_i + \epsilon_i, \end{aligned} \tag{1}$$

where $PCID_i$ is a dummy variable which is equal to 1 if firm i is in the treatment group and 0 otherwise. The regression results are reported in Table B1 of Appendix B. Then for each treated firm, I use one-to-one matching without replacement to identify a controlled firm with the closest propensity score as well as the same industry and ownership structure (SOE or non-SOE). The propensity score density of the treatment group and control group is plotted in Figure B1 of Appendix B. It shows that the two groups have similar propensity score distributions, suggesting that they have similar ex-ante probability of being treated. Table B2 reports summary statistics of firm characteristics for the matched sample, which includes 418 treated firms and 418 controlled firms. I compare firm characteristics of treated firms and controlled firms in all three pre-event years. It shows that the treatment and control groups are not significantly different in firm characteristics, suggesting the propensity score matching succeeds in finding comparable controlled firms.

5. Empirical Results

5.1. *Summary Statistics*

Table 1 reports summary statistics of variables used in this study. In Panel A, the initial sample includes all listed firms in China from 2011 to 2016. Then I exclude financial firms because their financial reports are complied under different accounting standards. All variables are winsorized at 1%-99% except dummy variables. $PCID$ has a mean of 0.204, suggesting that 20.4% A-share firms have PCIDs resignation after the release of Regulation

No.18. The sum of absolute CAR around issuance of regulatory documents by CSRC is 4.95%, suggesting that policy and regulation of CSRC has a large impact on market performance. Independent directors hold 2.144 directorship on average, suggesting that Chinese listed firms have busy board members and thus the monitoring from independent directors may be weak in China. Compensation of top three executives is around 0.07% of firm's total assets. However, the median of compensation is much smaller than the mean, which suggests that some executives receive very high compensation and are more entrenched. Similarly, the median of RPT and ETC are also smaller than the mean. This means that a small part of firms may have extremely poor governance. The largest shareholder hold 35.4% of A-share stocks (Top1), suggesting that ownership concentration is high in China. The high ownership concentration leads to potential expropriation from majority shareholders. The average board independence is 0.374, which is consistent with the regulation in China that at least one third board members should be independent. The statistics of other variables are comparable with other recent studies (e.g., Liu et al., 2017). Panel B shows the summary statistics of the matched sample used in the empirical analysis. Firm characteristics in the matched sample are similar to those of the full sample except the matched sample has more SOEs.

5.2. *Value Effect*

5.2.1. *Market Reaction to Release of Regulation No.18*

To investigate the value effect of Regulation No.18, I perform an event study to test the stock market reaction to the release of the regulation. To obtain CAR, I first estimate the following regression for stock i:

$$R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t} \tag{2}$$

where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized returns of stock i and market return on day τ. τ is equal to 0 on the event day (October 21, 2013). CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different windows. Since many Chinese listed firms have a large fraction of non-tradable shares, I use float value weighted market return when calculating CAR. I also use total value weighted market return for robustness tests.

Table 2 reports CAR of treated firms around release of Regulation No.18. The first column shows the results of full sample. Generally, treated firms have negative CAR in all five windows, although they are not significant in the short event windows. The CAR is -0.04% in the 3-day window and -0.543% in the 7-day window without significance. In the 12-day window, the negative CAR is very large in magnitude (-2.006%) and significant at 1% level. While it decreases to -1.729% and -0.933% in the 11-day and 22-day window, it is still significant. The non-significant CAR in short event windows is possibly because of inefficient information transmission. As in Liu et al. (2018), the new regulation was initially sent to certain government agencies and institutions concerned through the internal administrative system, which may have caused a delay in the dissemination of the message across the market. The next two columns show results for the SOEs and non-SOEs subsamples. Non-SOEs seems to be more affected by the new regulation than SOEs as evident by the slightly larger CAR. The CAR estimated using total value weighted market return are reported in Table IA1 and similar with the main results, although they are smaller in magnitude.

Next, to further build the causal effect of Regulation No.18 on firm value, I estimate the following cross-sectional regression:

$$CAR_i = \alpha + \beta_1 PCID_i + Controls + \omega_j + \epsilon_i, \tag{3}$$

where CAR_i is the CAR of firm i. I control for firm size, leverage ratio, book-to-market ratio, growth rate, ROE, ownership of the largest shareholder, idiosyncratic risk, and SOE status in the regression. I also include ω_j to control for industry fixed effect. Moreover, in order to avoid correlations in the error term due to unobserved heterogeneity, I adjust standard errors by clustering observations at industry level throughout the paper. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group.

The regression results are reported in Table 3. It shows that coefficients on the main interest variable, $PCID$, are all significantly negative. The coefficient is -0.342% in the 3-day window. It further decreases to -1.047%, -1.267%, and -1.437% in the 7-day, 12-day, and 17-day window, respectively. Although the coefficient is smaller in magnitude in the longest window, it is still significant at 1% level. The results suggest that the treated firms have significant lower CAR than controlled firms and thus the release of Regulation of No.18 has negative effect on firm value of treated firms. Regression results of CAR estimated using total value weighted market return are reported in Table IA2 of Internet Appendix. The results show similar pattern as those in Table 3. Therefore, the CAR analysis provides evidence supporting Hypothesis 1.

5.2.2. Market Reaction to PCID Resignation

Although treated firms have negative CAR around the release of Regulation No.18, the underlying mechanism is not clear. To test Hypothesis 2 and 3, I calculate CAR of treated firms around the announcement of PCID resignation. As discussed in Section 3, if the cash flow explanation holds, firms should not change in firm value around PCID resignation. On the contrary, if the political risk explanation is true, firms should gain in firm value after losing PCIDs. I use the same method to estimate CAR as in previous subsection, except that the event date is the announcement date of PCID resignation now, which is different across treated firms.

Table 4 shows that firms have large and significantly positive CAR around the announcements of PCID resignations. Overall, the treatment group has a 1.3% CAR in the 3-day window and the CAR further increases to 2.782% in the 7-day window and 3.681% in the 12-day window, after which it decreases to 3.579% in the 17-day window and 3.025% in the

22-day window. The last two columns show that both SOEs and non-SOEs have positive CAR, but their magnitudes are different. Non-SOEs have much larger CAR than SOEs in all windows, especially in the longer windows, suggesting that non-SOEs may be more affected by PCID resignation. The results are similar if I use total value weighted market return as shown in Panel A of Table IA3. I also use market-adjusted return and Fama-French three factor model to estimate CAR for robustness tests. The results are reported in Table IA3 and still consistent with the main results.

Next, to further address the causal effect of PCID resignation on firm value, I run regression model (3) for CAR around PCID resignation. The results are reported in Panel A of Table 5. $PCID$ has significantly positive coefficient in all windows, suggesting that treated firms have higher CAR around announcements of PCID resignations than controlled firms after controlling for other firm characteristics. The coefficient on $PCID$ is 0.519 in the 3-day window and further increases to 1.086 and 2.413 in the 7-day and 12-day window. Although the coefficients decrease in longer windows, they are still significant and economically large. The results using different methods to calculate CAR are reported in Table IA4 and are almost identical with those in Table 5. To conclude, Table 4 and 5 suggest that treated firms increase in firm value when their PCIDs resign, providing support for the political risk explanation. The results are also consistent with those in Ding et al. (2017). However, they mainly investigate the overall market reaction to the anti-corruption campaign, while I focus on the lose of political connections from PCIDs in this study.

As shown in Table 4, CAR of SOEs and non-SOEs are different in magnitude. To further explore whether the value effect is contingent on ownership structure, I estimate the cross-sectional regression for SOEs and non-SOEs separately. The results are reported in Panel B. The first five columns show that although SOEs still have positive coefficients on $PCID$, they are not significant. On the contrary, the coefficients in non-SOEs subs-sample are significant and even larger in magnitude than those in the full sample. For example, the coefficients are 2.413 and 2.013 in the 12-day and 17-day window for the full sample, while they are 4.554

and 4.009 for the non-SOEs subsample. Therefore, the positive value effect around PCID resignations are mainly driven by non-SOEs. One possible explanation is that non-SOEs decrease more in political risk than SOEs after their PCID resign. I will further explore this issue in the next subsection. My results are also consistent with Liu et al. (2018) who find that market reaction to the release of Regulation No.18 is significant for non-SOEs but not significant for SOEs. Results in the robustness tests are shown in Table IA5 and still consistent.

5.3. *Operating Performance and Firm Risk*

The previous subsection shows that treated firms have positive CAR around PCID resignation, suggesting that the political risk explanation may dominant the cash flow explanation. To further explore the two mechanisms, I perform a DID analysis on firm's operating performance and firm risk. DID methodology is ideally suited for establishing casual claims in a quasi-experimental setting. It eliminates the bias that comes from changes other than the regulation that could have affected the treatment group (Vig, 2013). The regression model is specified as follows:

$$y_{it} = \alpha + \beta_1 PCID_i + \beta_2 PCID_i \times Post_t + Controls_{t-1} + \omega_j + \gamma_t + \epsilon_{it}, \tag{4}$$

where $PCID_i$ is defined as above and $Post_t$ is a dummy variable which is equal to 1 after the PCID physically leaves the board. ω_j and γ_t are industry and year fixed effect. The regression model does not have the dummy variable $Post_t$ like a typical DID regression model since it has year fixed effect that overlaps with $Post_t$. The interaction dummy variable, $PCID_i \times Post_t$ is the main interest variable that reflects the change of treated firms after the event compared to controlled firms. The sample includes 418 treated firms and 418 controlled firms and the sample period is 2011-2016. The event date (year) for the DID analysis is the date when the PCID resignations take effect (when the PCIDs physically leave the board) as discussed in

Section 4.

Table 6 reports regression results of operating performance. In Panel A, I use ROE to measure operating performance. The first column shows that ROE of the treatment group does not change significantly after losing PCIDs compared to controlled firms. Column (2) and (3) further show that operating performance of both SOEs and non-SOEs is not affected by PCID resignation. In Panel B, I use CFO to measure operating performance. Similar to results in Panel A, the coefficients on $PCID \times Post$ are not significant in all three columns. I also use OPOA and CF as alternative measures of operating performance. The results are reported in Table IA6 of Internet Appendix and consistent with the main results. Therefore, firms do not have worse operating performance after losing political connections from PCID, providing consistent evidence with the CAR analysis that the cash flow explanation does not hold. Therefore, my results suggest that political connections built by PCIDs may not be so valuable for firm performance in China and cast doubt on the "helping hand" theory of political connections.

The regression results of firm risk is reported in Table 7. As shown in column (1) for the full sample, the coefficient of $PCID \times Post$ is negative but not significant. However, column (2) and (3) show different results for SOEs and non-SOEs. While the coefficient is not significant in SOEs subsample, it is significantly negative in non-SOEs subsample, suggesting that stock return volatility of non-SOEs in the treatment group decrease significantly after losing PCIDs. In Panel B, the results are similar that non-SOEs decrease significantly in policy sensitivity while SOEs' policy sensitivity does not change. One possible explanation for the different results is that SOEs have more other sources of political connections than non-SOEs because of their special relation with the government. Even their PCIDs leave, they still have other connections and thus similar political risk. On the contrary, PCIDs may be a main source of political connection for some non-SOEs. Therefore, their risk decreases significantly after losing this connection. The results are also consistent with the CAR around PCID resignation where I find the non-SOEs have more significant CAR than

SOEs. Since non-SOEs have lower firm risk after losing PCIDs, they gain in firm value when their PCIDs resign. Therefore, Table 7 provides supporting evidence for Hypothesis 3b, suggesting that political risk explanation dominates the cash flow explanation. Although political connections can bring various benefits to firms in China as shown in previous studies, they may also increase firm's political risk, especially during the anti-corruption campaign, which again cast doubt on the "helping hand" theory. Moreover, the results also provide novel evidence that political risk is priced by investors in China. To conclude, the previous two subsections suggest that treated firms lose in firm value after the release of Regulation No.18 because of higher political risk. After their PCIDs resign, they gain in firm value because of lower political risk after complying with the new regulation.

5.4. Corporate Governance

In this subsection, I investigate whether firm's governance improves after losing PCIDs. Specifically, I use regression model (4) to test the change in firm's independent director busyness, executive compensation, RPT, and ETC after PCIDs resign.

Panel A of Table 8 reports regression results on independent director busyness. As shown in column (1), independent directors of treated firms overall hold 0.113 less directorship after the PCIDs resign compared to those in controlled firms. There are two possible explanations for the decrease in independent director busyness. First, as firms are required by the CSRC to have at least one third board members as independent, some firms have to appoint non-connected independent directors who are less busy to replace the resigning PCIDs. Second, while some firms do not have to appoint new directors since they still have enough independent directors, their busyness also decreases because the resigning PCIDs are busier than the other directors. Although the second mechanism does not reflect real improvement in governance, it is very rare since most firms want to have as few independent directors as possible. Therefore, consistent with Hypothesis 4a, board monitoring efficiency increases after firms replace PCIDs. Column (2) and (3) show different results for SOEs and non-SOEs. While busyness of SOEs decreases even more than that of full sample, the decrease of non-SOEs is not significant, suggesting that SOEs have more improvement in board monitoring efficiency than non-SOEs. Because of the special ownership structure of SOEs, the government often appoints officials as independent directors to occupy more board seats in SOEs (Wang, 2015). Therefore, SOEs may have more PCIDs and thus busier independent directors before the release of Regulation No.18. As a result, the resignation of PCIDs leads to greater improvement in board monitoring efficiency for SOEs. Moreover, since it is well-known that Chinese SOEs have very serious governance problem and one of the aims of the anti-corruption campaign is to curb corruption in SOEs, they may have more improvement in corporate governance overall than non-SOEs.

Panel B reports regression results on executive compensation. Column (1) shows that although treated firms' executive compensation tend to decrease after replacing PCIDs, the decrease is not significant. However, column (2) and (3) suggest that the effect is again different for SOEs and non-SOEs. Similar to independent director busyness, while executive compensation of SOEs decreases significantly, compensation of non-SOEs does not change. Because both executives and PCIDs in SOEs are appointed by the government, executives are more likely to capture the PCIDs and entrench more. Therefore, the loss of PCIDs leads to greater decrease in management entrenchment. Panel B again suggests that SOEs improve more in corporate governance than non-SOEs.

Panel C reports regression results on RPT. Although RPT of the treatment group tend to decrease, the decrease is again not significant. However, similar to previous two tables, column (2) and (3) show that SOEs decrease significantly in RPT, but non-SOEs do not have any change in RPT. Since Chinese SOEs appoint politicians as independent directors in order to achieve political and social objectives, PCIDs tend to behave in the best interest of the State rather than minority shareholders. As a result, a large fraction of PCIDs increase RPT in SOEs. After replacing PCIDs, the non-connected directors are less likely to protect the interest of the State and thus better protect minority shareholders. Therefore, Panel

C provides more evidence that the resignations of PCIDs improve SOEs' governance. The decrease in RPT of SOEs is also consistent with the findings in Wang (2015).

Panel D reports regression results on ETC. Column (1) shows that ETC of treated firms tend to decrease, but it is not significant. However, the subsample analysis suggests that the effect is still contingent on ownership structure. While ETC of SOEs decrease by 0.053 after losing PCIDs, non-SOEs' ETC do not change significantly. As in Cai et al. (2011) and Lin et al. (2016), ETC is a mix that includes grease money to obtain better government services and protection, spending on private benefits for top insiders, and normal business expenditures to build relational capital with suppliers and clients. Because SOEs have more political connections in nature, they may not need to spend on building connection and obtaining protection from the government. Most ETC of SOEs may be spending on private benefits for top insiders. Therefore, replacing PCIDs leads to less spending on private benefits of insiders and thus better governance in SOEs. On the contrary, although non-SOEs can also have less ETC on insiders' private benefits, they may have to spend more to build new political connections after losing connections from PCIDs. As a result, the total ETC of non-SOEs do not change.

To conclude, Table 8 suggests that while firms overall improve in corporate governance after replacing PCIDs, SOEs have more improvement than non-SOEs. There are two possible explanations for the different effect. First, since SOEs have more serious governance problem before the release of Regulation No.18, replacing PCIDs with non-connected independent directors has more impact on SOEs' governance. Second, because one of the aims of the anti-corruption campaign is to curb corruption in SOEs, governance of SOEs may be more affected by the new regulation. My results are consistent with previous studies that conclude political connections are associated with more governance problems in SOEs (Wang, 2015) and studies on Chinese anti-corruption campaign that find SOEs gain broadly from the campaign (Lin et al., 2016).

6. Conclusions

On October 19, 2013, the CPC Central Committee issued a new regulation known as Regulation No.18, which leads to a wave of PCID resignation in the following two years. Using this regulation as a quasi-natural experiment, I investigate the effects of losing PCIDs on Chinese listed firms. There are four main findings in this study. First, firms have significantly negative CAR around the release of the new regulation. Further analysis suggests that the decrease in firm value is probably because of increase in political risk. Second, firms have large and significantly positive CAR around resignation announcement of PCIDs, because their political risk decreases after replacing PCIDs and complying with the new regulation. The positive CAR is more prominent for non-SOEs than SOEs as SOEs may have more other connections with the government and thus their political risk does not change significantly. Third, using DID methodology, I show that firms' operating performance does not change after replacing PCIDs. Consistent with the CAR analysis, political risk of non-SOEs decreases significantly, while SOEs' political risk does not change. The previous three findings cast doubt on the "helping hand" theory of political connections. Although connections may bring benefits to firms and increase firm value, it can also increase firm risk and thus decrease firm value, especially during the anti-corruption campaign. Moreover, my results also suggest that political risk is priced by investors in China. Forth, I find SOEs have higher board monitoring efficiency, less management entrenchment, less expropriation on minority shareholders, and less ETC after replacing PCIDs, suggesting that corporate governance of SOEs improve significantly. On the contrary, in improvement of governance in non-SOEs is only marginal. This is probably because SOEs have more serious governance problem before the release of Regulation No.18 and the anti-corruption campaign also mainly aims at curbing corruption in SOEs. The improvement in governance of SOEs also suggest that the anti-corruption campaign is authentic.

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Appendix A. Variable Definitions

Variable	Definition
PCID	A dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise. The firm is in the treatment group if it has politically connected independent directors (PCID) resignation to comply with Regulation No.18 and 0 otherwise.
Post	A dummy variable which is equal to 1 after the resignation of politically connected independent director takes effect and 0 otherwise.
ROE	The ratio of net profit to book value of equity.
CFO	The ratio of cash flows from operation to total assets.
OPOA	The ratio of operating profit to total assets.
CF	The ratio of total cash flows to total assets.
Volatility (%)	Stock price volatility, which is calculated as the standard deviation of daily stock return, multiplied by 100.
Political sensitivity (%)	The sum of absolute cumulative abnormal return over the three-day window around announcements of the new regulatory documents issued by China Securities Regulatory Commission (CSRC) estimated using market model.
Busyness	Independent director busyness, which is defined as the average number of directorship the firm's independent directors hold.
Compensation (%)	Executive compensation, which is defined as the ratio of top three executives' total compensation to total assets, multiplied by 100.
RPT	Related party transactions, which is defined as the ratio of purchases or sales of goods/services from or to related parties to total assets.
ETC	Entertainment and traveling costs, which is defined as the ratio of firm's expenses on entertainment and traveling to total assets.
Size	The natural logarithm of total assets.
Leverage	The ratio of total liabilities to total assets.
Tangibility	The ratio of tangible assets to total assets.
ROA	The ratio of net profit to total assets.
B/M	The ratio of book value of equity to market value of equity.
Growth	The one-year lagged growth rate of net sales.
Top1	The ratio of shares held by the largest shareholder to total shares outstanding.
Age	The natural logarithm of firm age.
Independence	Board independence, which is defined as the ratio of the number of independent director to the total number of board member.
Board size	The natural logarithm of number of board members.
Beta	The beta obtained from market model.
Ivol (%)	Idiosyncratic volatility, which is defined as the standard deviation of daily stock return residuals from market model, multiplied by 100.
SOE	A dummy variable which is equal to 1 if the firm is a state owned enterprise and 0 otherwise.

Appendix B. Propensity Score Matching

Table B1: Logit Regression Results

This table reports regression results of propensity score matching using the following logit regression model: $PCID_i = \alpha + \beta_1 Size_i + \beta_2 Leverage_i + \beta_3 B/M_i + \beta_4 Growth_i + \beta_5 Top1_i + \beta_6 Independence_i + \beta_7 Board\ size_i + \epsilon_i$, where $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise. The firm is in the treatment group if it has politically connected independent directors resignation to comply with Regulation No.18. The matching year is 2010. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Size	0.137**
	(0.054)
Leverage	-0.174
	(0.197)
B/M	-0.207
	(0.204)
Growth	0.002
	(0.002)
Top1	0.002
	(0.004)
Independence	2.222**
	(0.993)
Board size	0.115***
	(0.033)
Constant	-5.407***
	(1.236)
Observations	1920
Pseudo R^2	0.012

Table B2: Summary Statistics after Matching

This table reports summary statistics of variables used in this study for the matched sample during the pre-event period. A firm is treated if it has politically connected independent directors resignation to comply with Regulation No.18. For each treated firm, I use one-to-one propensity score matching without replacement to find a controlled firm in the same industry and with the same SOE status in 2010. I report summary statistics for 2011, 2012, and 2013 separately. I also report difference between the treatment and control group and perform t-test on the difference. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. ***, **, and * represent statistical significance at the 1%, 5%, and 10%, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	2011			2012			2013		
	Treatment	Control	Difference	Treatment	Control	Difference	Treatment	Control	Difference
ROE	0.087	0.073	0.015**	0.066	0.046	0.020**	0.048	0.034	0.014
CFO	0.033	0.033	0.000	0.047	0.045	0.003	0.040	0.037	0.003
OPOA	0.051	0.041	0.009**	0.038	0.031	0.007*	0.034	0.026	0.008
CF	0.625	0.604	0.020	0.594	0.599	-0.004	0.580	0.584	-0.004
Volatility (%)	2.480	2.497	-0.017	2.439	2.482	-0.043	2.558	2.628	0.070*
Policy sensitivity (%)	5.238	5.269	-0.031	3.787	3.901	-0.114	4.510	4.571	-0.061
Busyness	1.904	1.893	0.011	2.071	2.033	0.038	2.152	2.129	0.023
Compensation (%)	0.062	0.062	-0.001	0.056	0.062	-0.006	0.053	0.057	-0.005
RPT	0.331	0.327	0.004	0.351	0.337	0.015	0.340	0.358	-0.018
ETC	0.244	0.233	0.011	0.246	0.234	0.012	0.225	0.213	0.012
Size	22.005	21.801	0.204	22.159	21.919	0.239***	22.285	22.042	0.243***
Leverage	0.463	0.458	0.005	0.471	0.458	0.013	0.474	0.471	0.003
Tangibility	0.952	0.954	-0.002	0.947	0.950	-0.003	0.947	0.948	-0.001
ROA	0.047	0.041	0.006	0.037	0.034	0.003	0.032	0.027	0.005
B/M	0.485	0.482	0.003	0.537	0.528	0.009	0.541	0.529	0.012
Growth	0.420	0.261	0.160**	0.165	0.176	-0.011	0.149	0.162	-0.013
Top1	0.372	0.373	-0.001	0.371	0.376	-0.005	0.368	0.368	0.000
Age	2.490	2.479	0.011	2.580	2.570	0.010	2.661	2.651	0.009
Independence	0.373	0.369	0.003	0.372	0.371	0.001	0.372	0.374	-0.002
Board size	2.204	2.197	0.007	2.207	2.198	0.009	2.204	2.191	0.013
Beta	1.187	1.185	0.003	1.241	1.241	0.000	1.087	1.088	-0.001
Ivol (%)	1.957	1.982	-0.026	1.876	1.935	-0.059	2.156	2.231	-0.075*
SOE	0.555	0.560	-0.005	0.565	0.560	0.005	0.567	0.562	0.005
N	418	418		418	418		418	418	

Figure B1: Propensity Score Density

This figure plots the density of propensity scores from the propensity score matching for the treatment and control group. The solid line plots propensity score density of the treatment group and the dashed line plots propensity score density of the control group. A firm is treated if it has politically connected independent directors resignation to comply with Regulation No.18. For each treated firm, I use one-to-one propensity score matching without replacement to find a controlled firm in the same industry and with the same SOE status in 2010. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

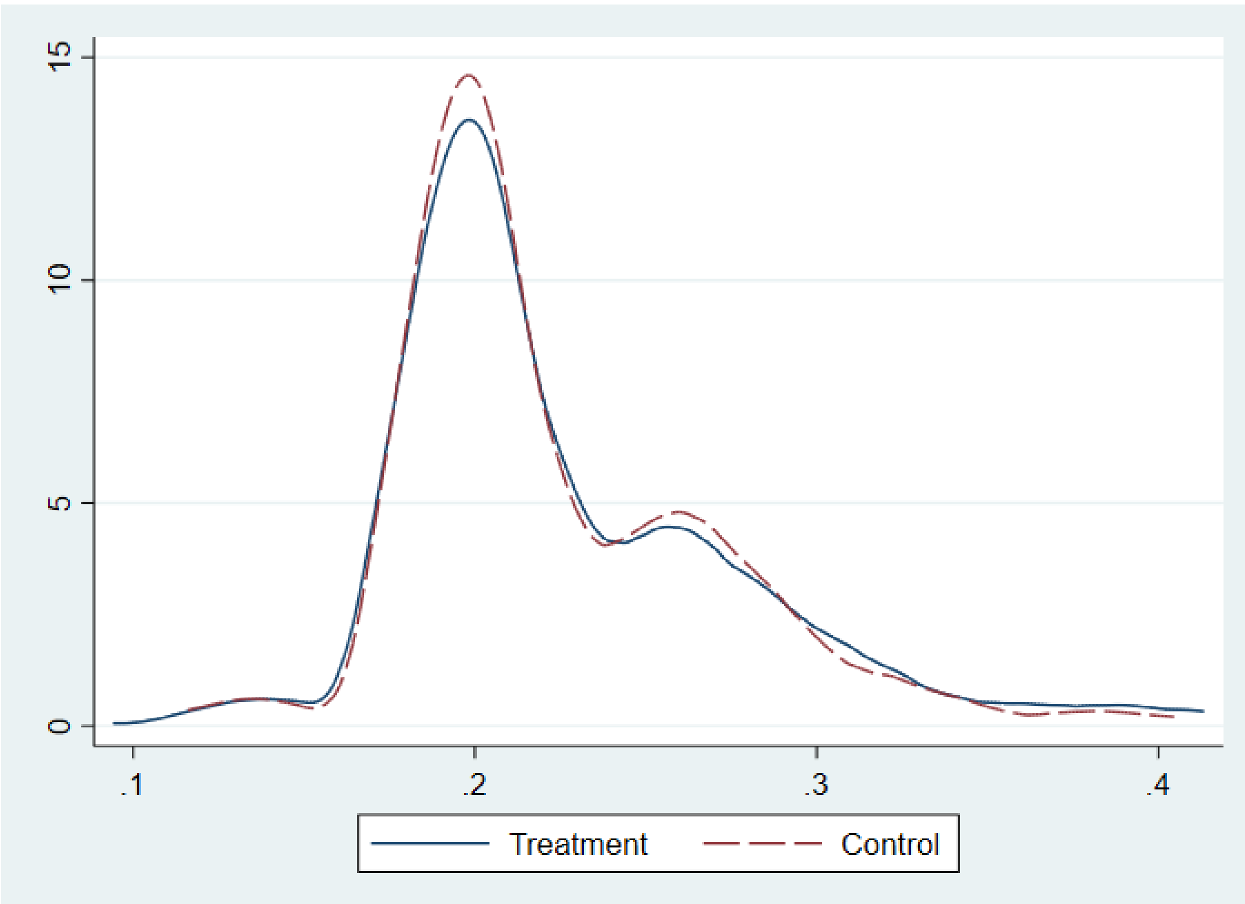


Table 1: Summary Statistics

This table reports summary statistics of variables used in this study. The sample in Panel A includes all non-financial A-share firms in China from 2011 to 2016. The sample in Panel B is a matched sample including treated firms and controlled firms. A firm is treated if it has politically connected independent directors resignation to comply with Regulation No.18. For each treated firm, I use one-to-one propensity score matching without replacement to find a controlled firm in the same industry and with the same SOE status in 2010.All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: all listed firms					
Variable	Mean	S.D.	p25	p50	p75
PCID	0.204	0.403	0.000	0.000	0.000
ROE	0.063	0.121	0.028	0.068	0.112
CFO	0.039	0.074	0.000	0.040	0.083
OPOA	0.040	0.063	0.011	0.038	0.072
CF	0.555	0.471	0.253	0.429	0.695
Volatility (%)	3.241	1.318	2.375	2.848	3.697
Policy sensitivity (%)	4.946	2.018	3.652	4.579	5.740
Busyness	2.144	0.789	1.500	2.000	2.667
Compensation (%)	0.072	0.080	0.021	0.047	0.092
RPT	0.398	0.510	0.076	0.239	0.521
ETC	0.230	0.255	0.058	0.158	0.310
Size	21.957	1.295	21.027	21.795	22.695
Leverage	0.431	0.222	0.250	0.418	0.600
Tangibility	0.953	0.052	0.941	0.966	0.984
ROA	0.039	0.055	0.013	0.036	0.066
B/M	0.394	0.270	0.199	0.336	0.515
Growth	0.204	0.608	-0.040	0.098	0.263
Top1	0.354	0.152	0.233	0.333	0.458
Age	2.642	0.431	2.398	2.708	2.944
Independence	0.374	0.053	0.333	0.333	0.429
Board size	2.143	0.198	1.946	2.197	2.197
Beta	0.975	0.589	0.631	1.063	1.367
Ivol (%)	2.579	1.217	1.840	2.289	2.947
SOE	0.433	0.496	0.000	0.000	1.000
N	15530				

Table 1 Continued

Panel B: matched sample					
Variable	Mean	S.D.	p25	p50	p75
PCID	0.500	0.500	0.000	0.500	1.000
ROE	0.051	0.145	0.022	0.062	0.108
CFO	0.042	0.072	0.003	0.041	0.085
OPOA	0.033	0.064	0.006	0.031	0.065
CF	0.560	0.479	0.248	0.434	0.698
Volatility (%)	2.949	0.963	2.285	2.702	3.338
Policy sensitivity (%)	4.681	1.587	3.566	4.474	5.539
Busyness	2.132	0.785	1.500	2.000	2.667
Compensation (%)	0.055	0.063	0.016	0.037	0.070
RPT	0.380	0.476	0.077	0.236	0.504
EE	0.205	0.241	0.046	0.133	0.281
Size	22.233	1.331	21.313	22.073	22.994
Leverage	0.464	0.218	0.287	0.469	0.632
Tangibility	0.950	0.059	0.939	0.966	0.984
ROA	0.032	0.057	0.009	0.030	0.059
B/M	0.442	0.300	0.232	0.370	0.573
Growth	0.185	0.607	-0.054	0.080	0.243
Top1	0.359	0.153	0.239	0.333	0.471
Age	2.684	0.408	2.485	2.773	2.996
Independence	0.373	0.054	0.333	0.355	0.400
Board size	2.182	0.205	2.079	2.197	2.197
Beta	1.147	0.237	0.989	1.165	1.312
Ivol (%)	2.287	0.749	1.758	2.163	2.706
SOE	0.554	0.497	0.000	1.000	1.000
N	5016				

Table 2: Market Reaction to Release of Regulation No.18

This table reports cumulative abnormal return (CAR) of treated firms around the release of Regulation No.18 on October 19, 2013. A firm is treated it has politically connected independent directors resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. I use float value weighted market return when estimating CAR. Standard errors are reported in parentheses. ***, **, and * represent statistical significance at the 1%, 5%, and 10%, respectively. All returns and standard errors are in %. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	-0.040	-0.235	0.397
	(0.172)	(0.213)	(0.282)
(-1, +5)	-0.543	-0.167	-0.832**
	(0.331)	(0.582)	(0.377)
(-1, +10)	-2.006***	-1.898***	-2.674***
	(0.371)	(0.493)	(0.778)
(-1, +15)	-1.729***	-1.605***	-2.199***
	(0.414)	(0.573)	(0.798)
(-1, +20)	-0.933*	-0.944	-0.920
	(0.495)	(0.607)	(0.821)
N	418	230	188

Table 3: Cross-sectional Regression of CAR around Release of Regulation No.18

This table reports results of the cross-sectional regression of cumulative abnormal returns (CAR) around release of Regulation No.18 using the following model: $CAR_i = \alpha + \beta_1 PCID_i + Controls + \omega_j + \epsilon_i$, where CAR_i is the CAR of firm i, $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, and ω_j is industry fixed effect. The firm is in the treatment group if it has politically connected independent directors resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and float value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = Ret_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
$PCID$	-0.342**	-1.047**	-1.267*	-1.437**	-0.989***
	(0.140)	(0.442)	(0.660)	(0.551)	(0.306)
Size	0.143***	-0.238	-0.026	0.045	0.067
	(0.046)	(0.283)	(0.268)	(0.366)	(0.470)
Leverage	-0.568	-1.207	-0.359	-2.870	-5.636***
	(0.353)	(1.449)	(1.637)	(1.960)	(1.434)
B/M	-0.290	-0.007	-0.423	-1.780*	-4.007***
	(0.181)	(0.692)	(0.673)	(0.862)	(1.248)
Growth	-0.099	-0.298	-0.245	0.018	-0.049
	(0.108)	(0.396)	(0.711)	(0.548)	(0.421)
ROE	0.764	1.842	1.184	1.382	2.933
	(0.757)	(1.084)	(3.531)	(4.569)	(3.468)
Top1	-0.386	0.857	3.250**	1.943	3.152
	(0.821)	(1.294)	(1.324)	(1.204)	(1.841)
Ivol	1.236***	-0.638	-0.193	0.384	3.663***
	(0.187)	(0.450)	(0.838)	(0.777)	(0.606)
SOE	-0.347	-0.571	0.384	-0.246	-0.009
	(0.201)	(0.357)	(0.479)	(0.888)	(0.770)
Constant	-5.150***	10.122	4.011	6.556	-0.615
	(1.202)	(6.071)	(5.562)	(7.794)	(9.782)
N	836	836	836	836	836
Adj. R^2	0.139	0.050	0.041	0.037	0.115

Table 4: Market Reaction to PCID Resignations

This table reports cumulative abnormal return (CAR) of treated firms around the announcement of politically connected independent directors (PCID) resignation. A firm is treated if it has PCID resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. I use float value weighted market return when estimating CAR. Standard errors are reported in parentheses. ***, **, and * represent statistical significance at the 1%, 5%, and 10%, respectively. All returns and standard errors are in %. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.300***	1.168***	1.462**
	(0.341)	(0.394)	(0.586)
(-1, +5)	2.782***	1.979***	3.764***
	(0.650)	(0.725)	(1.140)
(-1, +10)	3.681***	2.24***	5.445***
	(0.860)	(0.832)	(1.612)
(-1, +15)	3.579***	2.095**	5.394***
	(0.983)	(0.888)	(1.892)
(-1, +20)	3.025***	1.800*	4.524**
	(1.071)	(1.009)	(2.035)
N	418	230	188

Table 5: Cross-sectional Regression of CAR around PCID Resignation

This table reports results of the cross-sectional regression of cumulative abnormal returns (CAR) around resignation of politically connected independent director (PCID) using the following model: $CAR_i = \alpha + \beta_1 PCID_i + Controls + \omega_j + \epsilon_i$, where CAR_i is the CAR of firm i, $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, and ω_j is industry fixed effect. The firm is in the treatment group if it has PCID resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and float value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = Ret_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. In Panel A, the sample includes 418 treated firms and 418 controlled firms matched with the treatment group. In Panel B, I report the subsample results for SOEs and non-SOEs. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: full sample	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.519*	1.086*	2.413***	2.013***	1.352**
	(0.262)	(0.567)	(0.450)	(0.463)	(0.513)
Size	-0.195	-0.444	-0.627	-0.383	0.273
	(0.351)	(0.539)	(0.538)	(0.549)	(0.653)
Leverage	-0.190	0.609	2.070	1.479	0.491
	(0.806)	(1.583)	(1.790)	(2.197)	(2.499)
B/M	-2.032*	-2.142	-1.515	-3.354*	-4.308**
	(1.065)	(1.487)	(1.791)	(1.668)	(1.916)
Growth	0.293	0.074	0.150	-0.336	-0.542
	(0.220)	(0.368)	(0.518)	(0.568)	(0.727)
ROE	0.135*	0.491***	0.767***	0.908***	0.877***
	(0.076)	(0.165)	(0.208)	(0.190)	(0.249)
Top1	1.366	2.616	0.842	2.318	0.515
	(2.446)	(5.472)	(5.720)	(5.853)	(6.816)
Ivol	-0.014***	-0.036***	-0.069***	-0.107***	-0.063***
	(0.004)	(0.011)	(0.016)	(0.016)	(0.016)
SOE	0.352	-0.753	-1.159	-1.308	-1.635
	(0.504)	(0.857)	(1.075)	(1.369)	(1.410)
Constant	4.305	10.092	12.729	6.999	-6.208
	(6.839)	(9.872)	(9.691)	(10.028)	(11.951)
N	836	836	836	836	836
Adj. R^2	0.026	0.030	0.035	0.035	0.028

Table 5 Continued

Panel B: sub-samples by ownership structure

	SOEs					non-SOEs				
	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.445	0.750	1.186	0.929	0.912	0.707*	2.025**	4.554***	4.009***	2.529*
	(0.587)	(1.307)	(1.089)	(1.015)	(0.883)	(0.379)	(0.778)	(0.993)	(1.058)	(1.420)
Size	-0.375	-0.427	-0.600	-0.540	0.178	-0.102	-1.008	-1.710	-1.220	-0.847
	(0.398)	(0.541)	(0.742)	(0.510)	(0.627)	(0.775)	(1.301)	(1.049)	(0.810)	(0.823)
Leverage	-0.604	-1.424	-0.820	-1.582	-2.366	0.475	3.439	6.075**	6.381**	4.636
	(0.874)	(1.806)	(2.030)	(2.024)	(2.395)	(2.111)	(2.845)	(2.570)	(2.162)	(3.581)
B/M	-0.615	0.011	0.948	0.608	0.378	-2.993*	-3.015	-1.080	-4.566	-6.008
	(1.181)	(1.740)	(2.056)	(2.111)	(2.492)	(1.685)	(2.366)	(2.801)	(3.210)	(4.070)
Growth	0.223	-0.541	0.276	-0.603	-1.747*	0.347	0.200	0.049	-0.271	-0.032
	(0.162)	(0.579)	(0.887)	(0.774)	(0.811)	(0.279)	(0.398)	(0.674)	(0.758)	(0.757)
ROE	0.617	3.310	7.585	6.165	4.434	0.127	0.524*	0.789***	0.960***	0.953***
	(2.012)	(5.155)	(8.491)	(7.806)	(6.977)	(0.131)	(0.255)	(0.194)	(0.100)	(0.126)
Top1	1.712	2.011	0.956	6.405*	4.246	2.143	6.478	6.563	3.391	2.947
	(1.551)	(3.313)	(3.085)	(3.238)	(3.283)	(3.570)	(6.826)	(5.960)	(8.002)	(10.601)
Ivol	0.682***	1.663***	1.815**	2.281***	2.676***	-0.024***	-0.055***	-0.086***	-0.135***	-0.091***
	(0.170)	(0.424)	(0.810)	(0.689)	(0.718)	(0.005)	(0.008)	(0.011)	(0.012)	(0.011)
Constant	6.944	6.531	8.495	2.945	-14.683	1.702	19.090	31.237	22.523	17.215
	(8.350)	(11.056)	(14.433)	(9.993)	(12.358)	(15.045)	(24.793)	(19.633)	(15.591)	(15.653)
N	460	460	460	460	460	376	376	376	376	376
Adj. R^2	0.052	0.059	0.073	0.066	0.059	0.045	0.052	0.067	0.077	0.073

Table 6: Loss of PCID and Operating Performance

This table reports change of firm's operating performance after politically connected independent director (PCID) resignation using the following regression model: $y_{it} = \alpha + \beta_1 PCID_i + \beta_2 PCID_i \times Post_t + Controls_{t-1} + \omega_j + \gamma_t + \epsilon_{it}$, where $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, $Post_t$ is a dummy variable which is equal to 1 after the PCID resignation takes effect and 0 otherwise, ω_j and γ_t are industry and year fixed effect. The firm is in the treatment group if it has PCID resignation to comply with Regulation No.18. Operating performance is measured using ROE in Panel A and cash flow from operations (CFO) in Panel B. ROE is defined as the ratio of net profit to book value of equity and CFO is defined as the ratio of cash flows from operations to total assets. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. I report results for the full sample, SOEs subsample, and non-SOEs subsample. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: ROE

	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
PCID	0.009	0.017*	0.003
	(0.006)	(0.009)	(0.006)
$PCID \times Post$	-0.000	-0.006	0.004
	(0.004)	(0.006)	(0.008)
Size	0.032***	0.035***	0.032***
	(0.005)	(0.005)	(0.006)
Tangibility	-0.165***	-0.227***	-0.103***
	(0.023)	(0.030)	(0.023)
Leverage	-0.001	-0.035	0.112
	(0.028)	(0.033)	(0.086)
B/M	-0.114***	-0.097***	-0.157***
	(0.021)	(0.027)	(0.015)
Growth	0.014***	0.022***	0.004
	(0.003)	(0.006)	(0.003)
Top1	0.020**	-0.025	0.077**
	(0.008)	(0.019)	(0.028)
Age	0.010*	0.015*	0.000
	(0.005)	(0.007)	(0.007)
Independence	0.006	-0.027	0.064
	(0.038)	(0.052)	(0.053)
Board size	-0.004	-0.008	0.031
	(0.016)	(0.023)	(0.018)
SOE	-0.026***		
	(0.006)		
Constant	-0.573***	-0.593***	-0.768***
	(0.076)	(0.091)	(0.079)
N	4,871	2,747	2,124
Adj. R^2	0.089	0.096	0.100

Table 6 Continued

Panel B: cash flow from operations (CFO)	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	0.001	0.001	0.001
	(0.002)	(0.003)	(0.004)
$PCID \times Post$	0.002	0.004	0.001
	(0.003)	(0.005)	(0.003)
Size	0.008***	0.008***	0.009***
	(0.001)	(0.002)	(0.003)
Tangibility	-0.024***	-0.022	-0.034**
	(0.008)	(0.014)	(0.012)
ROA	-0.040*	-0.013	-0.145***
	(0.021)	(0.016)	(0.023)
Leverage	0.255***	0.220***	0.268***
	(0.041)	(0.038)	(0.066)
B/M	-0.013	-0.013	-0.011
	(0.010)	(0.008)	(0.026)
Growth	-0.009***	-0.010***	-0.007**
	(0.003)	(0.003)	(0.003)
Top1	0.033***	0.020*	0.058***
	(0.007)	(0.010)	(0.016)
Age	0.004*	0.008	0.001
	(0.002)	(0.005)	(0.002)
Independence	-0.002	0.002	-0.017
	(0.029)	(0.032)	(0.023)
Board size	0.008	0.012	0.002
	(0.007)	(0.011)	(0.008)
SOE	-0.001		
	(0.002)		
Constant	-0.121***	-0.156***	-0.022
	(0.041)	(0.036)	(0.036)
N	4,871	2,747	2,124
Adj. R^2	0.118	0.109	0.138

Table 7: Loss of PCID and Firm Risk

This table reports change of firm risk after politically connected independent director (PCID) resignation using the following DID regression model: $y_{it} = \alpha + \beta_1 PCID_i + \beta_2 PCID_i \times Post_t + Controls_{t-1} + \omega_j + \gamma_t + \epsilon_{it}$, where $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, $Post_t$ is a dummy variable which is equal to 1 after the PCID resignation takes effect and 0 otherwise, ω_j and γ_t are industry and year fixed effect. The firm is in the treatment group if it has PCID resignation to comply with Regulation No.18. In Panel A, the dependent variable is stock return volatility (volatility), which is defined as the standard deviation of daily stock return, multiplied by 100. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. I report results for the full sample, SOEs subsample, and non-SOEs subsample. In Panel B, the dependent variable is political sensitivity, which is defined as the absolute cumulative abnormal return over the three-day window around announcements of the new regulatory documents issued by China Securities Regulatory Commission (CSRC) estimated using market model. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Table 7 Continued

Panel A: stock price volatility	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	-0.002	0.001	0.012
	(0.011)	(0.010)	(0.026)
$PCID \times Post$	-0.022	-0.010	-0.054***
	(0.014)	(0.019)	(0.016)
Size	-0.137***	-0.130***	-0.136***
	(0.007)	(0.009)	(0.019)
Leverage	0.223***	0.334***	0.064
	(0.039)	(0.042)	(0.041)
Tangibility	-0.018	0.011	0.230
	(0.089)	(0.121)	(0.333)
ROA	-0.611***	-0.579***	-0.768**
	(0.155)	(0.178)	(0.272)
B/M	0.069**	0.050	0.083
	(0.028)	(0.038)	(0.077)
Growth	0.067**	0.034	0.084**
	(0.025)	(0.021)	(0.029)
Top1	0.081**	0.026	0.187*
	(0.028)	(0.042)	(0.094)
Age	-0.052***	-0.037	-0.060***
	(0.015)	(0.031)	(0.011)
Independence	-0.264**	-0.323**	-0.328
	(0.117)	(0.148)	(0.191)
Board size	-0.068**	-0.055	-0.131***
	(0.029)	(0.049)	(0.035)
Beta	0.377***	0.372***	0.340***
	(0.029)	(0.051)	(0.022)
Ivol	0.217***	0.250***	0.190***
	(0.016)	(0.020)	(0.013)
SOE	-0.010		
	(0.016)		
Constant	4.769***	4.500***	4.750***
	(0.243)	(0.293)	(0.297)
N	4,867	2,745	2,122
Adj. R^2	0.741	0.754	0.720

Table 7 Continued

Panel B: political sensitivity	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	-0.028	0.018	-0.027
	(0.023)	(0.045)	(0.046)
$PCID \times Post$	-0.114	-0.058	-0.190***
	(0.072)	(0.122)	(0.054)
Size	-0.158***	-0.151***	-0.183***
	(0.018)	(0.030)	(0.035)
Leverage	0.383***	0.309**	0.386***
	(0.107)	(0.138)	(0.126)
Tangibility	0.268	0.419	0.113
	(0.345)	(0.314)	(1.055)
ROA	-2.168***	-2.456***	-1.773**
	(0.383)	(0.486)	(0.698)
B/M	-0.188**	-0.125*	-0.333*
	(0.066)	(0.061)	(0.160)
Growth	0.168**	0.190**	0.106*
	(0.060)	(0.064)	(0.050)
Top1	-0.007	-0.101	0.217
	(0.130)	(0.214)	(0.144)
Age	-0.256***	-0.362***	-0.191***
	(0.052)	(0.076)	(0.047)
Independence	-0.137	-0.329	-0.749
	(0.413)	(0.443)	(0.635)
Board size	-0.172	-0.019	-0.471*
	(0.107)	(0.136)	(0.233)
Beta	0.177***	0.186**	0.145
	(0.051)	(0.069)	(0.086)
Ivol	0.305***	0.333***	0.262***
	(0.035)	(0.052)	(0.025)
SOE	-0.182***		
	(0.041)		
Constant	8.602***	8.405***	9.688***
	(0.720)	(1.071)	(0.741)
N	4,862	2,743	2,119
Adj. R^2	0.286	0.267	0.304

Table 8: Loss of PCID and Corporate Governance

This table reports change of firm's corporate governance after politically connected independent director (PCID) resignation using the following regression model: $y_{it} = \alpha + \beta_1 PCID_i + \beta_2 PCID_i \times Post_t + Controls_{t-1} + \omega_j + \gamma_t + \epsilon_{it}$, where $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, $Post_t$ is a dummy variable which is equal to 1 after the PCID resignation takes effect and 0 otherwise, ω_j and γ_t are industry and year fixed effect. The firm is in the treatment group if it has PCID resignation to comply with Regulation No.18. In Panel A, I test the change of board monitoring efficiency. Board monitoring efficiency is measured using independent director busyness (busyness), which is defined as the average number of directorship the firm's independent directors hold. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. I report results for the full sample, SOEs subsample, and non-SOEs subsample. In Panel B, I test the change of management entrenchment. Management entrenchment is measured using executive compensation (compensation), which is defined as the ratio of top three executives' total compensation to total assets, multiplied by 100. In Panel C, I test the change of expropriation on minority shareholders. Expropriation on minority shareholders is measured using related party transactions (RPT), which is defined as the ratio of purchases or sales of goods/services from or to related parties to total assets. In Panel D, I test the change of entertainment and traveling costs (ETC). ETC is defined as the ratio of firm's expenses on entertainment and traveling to total assets. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Table 8 Continued

Panel A: independent director busyness	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	0.017	0.069	-0.054
	(0.038)	(0.065)	(0.032)
$PCID \times Post$	-0.113***	-0.164**	-0.049
	(0.038)	(0.054)	(0.030)
Size	0.040	0.031	0.067**
	(0.030)	(0.032)	(0.030)
Leverage	0.146	0.133	0.110
	(0.119)	(0.125)	(0.164)
Tangibility	0.008	-0.034	-0.041
	(0.324)	(0.389)	(0.316)
ROA	0.738***	0.263	1.055***
	(0.242)	(0.266)	(0.152)
B/M	0.117	0.120	0.244
	(0.067)	(0.072)	(0.147)
Growth	0.022	-0.012	0.041**
	(0.017)	(0.034)	(0.019)
Top1	-0.090	-0.052	-0.084
	(0.136)	(0.232)	(0.098)
Age	-0.058	-0.079	-0.048
	(0.077)	(0.180)	(0.032)
Independence	-0.775**	-0.938**	-0.378
	(0.348)	(0.374)	(0.409)
Board size	-0.267**	-0.326**	-0.091
	(0.116)	(0.126)	(0.128)
SOE	-0.004		
	(0.030)		
Constant	1.901***	2.475***	0.669
	(0.635)	(0.493)	(0.606)
N	4,871	2,747	2,124
Adj. R^2	0.047	0.037	0.081

Table 8 Continued

Panel B: executive compensation	(1)	(2)	(3)
	Full sample	SOEs subsample	Non-SOEs subsample
$PCID$	0.001	0.003*	0.001
	(0.002)	(0.002)	(0.005)
$PCID \times Post$	-0.002	-0.007***	0.004
	(0.002)	(0.002)	(0.003)
Size	-0.026***	-0.018***	-0.043***
	(0.002)	(0.002)	(0.004)
Leverage	-0.023**	-0.039**	0.007
	(0.008)	(0.014)	(0.018)
Tangibility	0.009	0.008	-0.000
	(0.018)	(0.009)	(0.060)
ROA	0.032	0.036	0.054
	(0.050)	(0.052)	(0.066)
B/M	-0.005	-0.006	-0.015
	(0.004)	(0.004)	(0.012)
Growth	-0.002	0.000	-0.003*
	(0.002)	(0.003)	(0.002)
Top1	-0.011	-0.026**	0.011
	(0.011)	(0.011)	(0.011)
Age	0.005*	-0.005	0.011***
	(0.002)	(0.003)	(0.003)
Independence	0.051**	0.040	0.015
	(0.023)	(0.030)	(0.027)
Board size	0.006	0.002	0.010
	(0.006)	(0.007)	(0.011)
SOE	0.002		
	(0.004)		
Constant	0.565***	0.448***	0.921***
	(0.045)	(0.054)	(0.087)
N	4,865	2,741	2,124
Adj. R^2	0.412	0.478	0.392

Table 8 Continued

Panel C: related party transactions (RPT)	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	-0.002	0.000	-0.004
	(0.023)	(0.028)	(0.055)
$PCID \times Post$	-0.027	-0.053**	0.000
	(0.017)	(0.020)	(0.027)
Size	-0.044*	-0.019	-0.082***
	(0.021)	(0.016)	(0.027)
Leverage	0.668***	0.522***	0.867***
	(0.036)	(0.056)	(0.066)
Tangibility	0.518***	0.464**	0.264
	(0.115)	(0.176)	(0.302)
ROA	-0.781***	-0.881***	-0.344
	(0.169)	(0.173)	(0.345)
B/M	-0.119***	-0.163***	0.012
	(0.026)	(0.035)	(0.044)
Growth	0.011	0.045**	-0.015**
	(0.007)	(0.016)	(0.006)
Top1	0.242***	0.294*	0.162**
	(0.059)	(0.158)	(0.063)
Age	0.087***	0.101**	0.059*
	(0.015)	(0.037)	(0.029)
Independence	-0.116	-0.135	-0.133
	(0.136)	(0.172)	(0.164)
Board size	0.050	0.078	0.003
	(0.039)	(0.056)	(0.052)
SOE	-0.017		
	(0.024)		
Constant	0.128	-0.367	1.198**
	(0.445)	(0.575)	(0.416)
N	4,750	2,720	2,030
Adj. R^2	0.139	0.118	0.199

Table 8 Continued

Panel D: entertainment and traveling costs (ETC)	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	0.013	0.018	0.003
	(0.008)	(0.012)	(0.013)
$PCID \times Post$	-0.011*	-0.023***	0.014
	(0.006)	(0.007)	(0.014)
Size	-0.022***	-0.017	-0.033
	(0.007)	(0.011)	(0.019)
Leverage	0.005	-0.067	0.089*
	(0.028)	(0.054)	(0.049)
Tangibility	0.020	0.005	0.055
	(0.109)	(0.080)	(0.233)
ROA	0.195	0.056	0.359*
	(0.141)	(0.112)	(0.173)
B/M	-0.090***	-0.047**	-0.216***
	(0.019)	(0.017)	(0.065)
Growth	-0.004	0.009*	-0.020**
	(0.007)	(0.005)	(0.009)
Top1	-0.077*	-0.124***	-0.010
	(0.038)	(0.034)	(0.117)
Age	-0.003	-0.023	-0.008
	(0.016)	(0.027)	(0.012)
Independence	-0.011	-0.109	0.179
	(0.110)	(0.088)	(0.300)
Board size	-0.059	-0.082*	0.020
	(0.035)	(0.038)	(0.053)
SOE	-0.021*		
	(0.010)		
Constant	0.926***	1.013***	0.818
	(0.128)	(0.191)	(0.493)
N	4,871	2,747	2,124
Adj. R^2	0.153	0.181	0.111

Figure 1: Resigning Dates of Independent Directors and PCIDs

This figure plots the number of independent director resignation and politically connected independent director (PCID) resignation every month during January 2013 to May 2017. The solid line plots the total number of independent director resignation and the dashed line plots the number of PCIDs resignation. Data source: website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

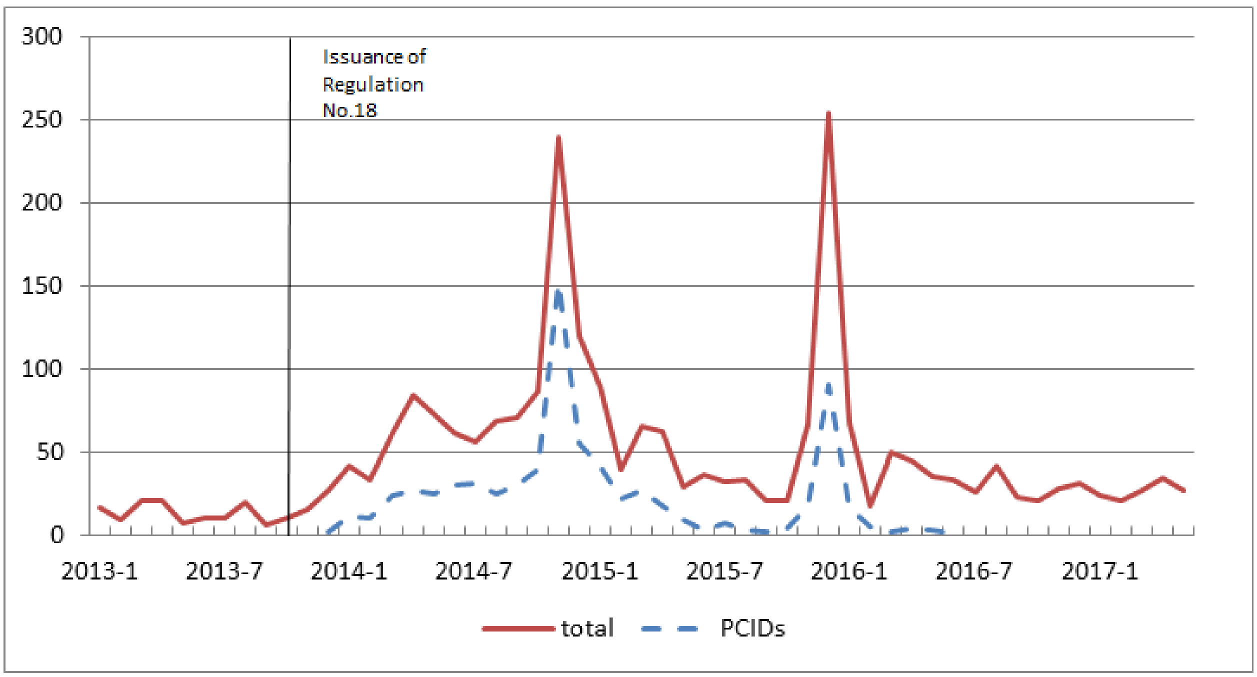
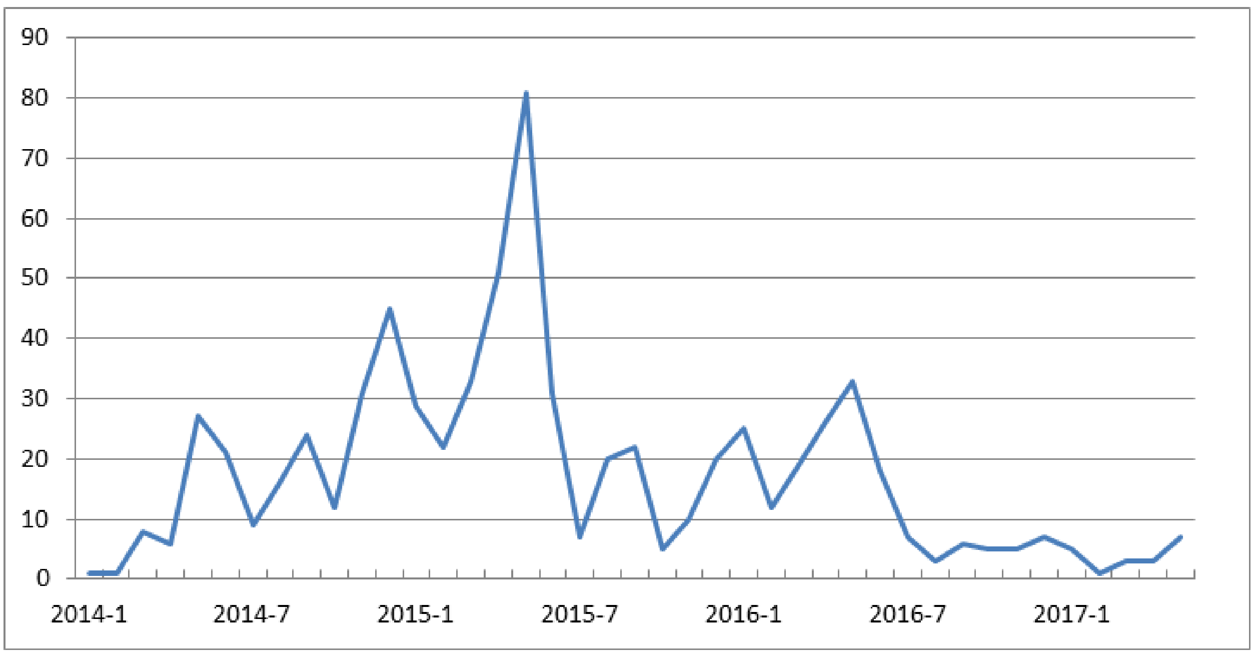


Figure 2: Leaving Dates of Resigning PCIDs

This figure plots the actual leaving dates of resigning politically connected independent directors (PCIDs) after the release of Regulation No.18. Data source: website of Shanghai Stock Exchange and Shenzhen Stock Exchange.



Internet Appendix

Value of Politically Connected Independent Directors: Evidence from the Anti-Corruption Campaign in China

May 31, 2019

Table IA1: Robustness test of CAR around Release of Regulation No.18

This table reports cumulative abnormal return (CAR) of treated firms around the release of Regulation No.18 on October 19, 2013. A firm is treated it has politically connected independent directors resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. I use total value weighted market return when estimating CAR. Standard errors are reported in parentheses. ***, **, and * represent statistical significance at the 1%, 5%, and 10%, respectively. All returns and standard errors are in %. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	-0.195	-0.475**	0.169
	(0.173)	(0.214)	(0.282)
(-1, +5)	-0.587*	-0.206	-0.879**
	(0.331)	(0.582)	(0.377)
(-1, +10)	-1.893***	-1.553***	-2.335***
	(0.438)	(0.494)	(0.777)
(-1, +15)	-1.546***	-1.285**	-1.885**
	(0.474)	(0.574)	(0.797)
(-1, +20)	-0.870*	-0.878	-0.859
	(0.495)	(0.608)	(0.821)
N	418	230	188

Table IA2: Robustness test of Cross-sectional Regression of CAR around Release of Regulation No.18

This table reports results of the cross-sectional regression of cumulative abnormal returns (CAR) around release of Regulation No.18 using the following model: $CAR_i = \alpha + \beta_1 PCID_i + Controls + \omega_j + \epsilon_i$, where CAR_i is the CAR of firm i, $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, and ω_j is industry fixed effect. The firm is in the treatment group if it has politically connected independent directors (PCID) resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and total value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = Ret_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
$PCID$	-0.420	-1.043**	-1.262*	-1.444**	-1.000***
	(0.243)	(0.442)	(0.661)	(0.553)	(0.305)
Size	-0.120	-0.241	-0.021	0.042	0.053
	(0.107)	(0.283)	(0.267)	(0.367)	(0.472)
Leverage	-0.243	-1.263	-0.375	-2.906	-5.537***
	(0.746)	(1.445)	(1.627)	(1.963)	(1.434)
B/M	0.268	-0.030	-0.417	-1.817*	-4.082***
	(0.225)	(0.694)	(0.669)	(0.866)	(1.272)
Growth	-0.286	-0.287	-0.232	0.029	-0.050
	(0.172)	(0.392)	(0.706)	(0.547)	(0.426)
ROE	-0.203	1.894	1.266	1.468	3.060
	(1.236)	(1.087)	(3.522)	(4.574)	(3.490)
Top1	0.136	0.835	3.244**	1.944	3.190*
	(0.710)	(1.295)	(1.311)	(1.203)	(1.801)
Ivol	1.645***	-0.569	-0.192	0.415	3.628***
	(0.193)	(0.455)	(0.832)	(0.777)	(0.610)
SOE	-0.472	-0.600	0.376	-0.273	-0.021
	(0.398)	(0.359)	(0.478)	(0.893)	(0.777)
Constant	-0.319	10.150	4.084	6.519	-0.793
	(2.105)	(6.090)	(5.546)	(7.807)	(9.815)
N	836	836	836	836	836
Adj. R^2	0.083	0.050	0.041	0.038	0.116

Table IA3: Robustness test of CAR around PCID Resignation

This table reports cumulative abnormal return (CAR) of treated firms around the announcement of politically connected independent director (PCID) resignation using different models to estimate abnormal return. A firm is treated if it has PCID resignation to comply with Regulation No.18. In Panel A, I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and total value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. In Panel B and C, the abnormal return is estimated using market-adjusted return: $AR_{i,\tau} = R_{i,\tau} - R_{m,\tau}$. I use float value weighted market return and total value weighted market return in Panel B and Panel C, respectively. In Panel D and E, I estimate the Fama-French three factor model to obtain abnormal return: $R_{i,t} = \beta_{1,i} R_{m,t} + \beta_{2,i} SMB_t + \beta_{3,i} HML_t + \epsilon_{i,t}$, where $R_{i,t}$, $R_{m,t}$, SMB_t, and HML_t are excess return of stock i, market risk premium, size premium, and value premium on day t, respectively. The estimated coefficients $\hat{\beta_{1,i}}$, $\hat{\beta_{2,i}}$, and $\hat{\beta_{3,i}}$ are used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - (\hat{\beta_{1,i}} R_{m,\tau} + \hat{\beta_{2,i}} SMB_\tau + \hat{\beta_{3,i}} HML_\tau)$, where $R_{i,\tau}$, $R_{m,\tau}$, SMB_τ, and HML_τ are realized excess returns of stock i, realized market risk premium, size premium, and value premium on day τ, respectively. I use float value weighted market return and total value weighted risk premium in Panel D and Panel E, respectively. Standard errors are reported in parentheses. ***, **, and * represent statistical significance at the 1%, 5%, and 10%, respectively. All returns and standard errors are in %. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: market model with total value weighted market return	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.325***	1.187***	1.494**
	(0.338)	(0.390)	(0.581)
(-1, +5)	2.783***	1.991***	3.752***
	(0.644)	(0.719)	(1.129)
(-1, +10)	3.668***	2.254***	5.397***
	(0.851)	(0.824)	(1.596)
(-1, +15)	3.581***	2.127**	5.36***
	(0.974)	(0.876)	(1.877)
(-1, +20)	3.094***	1.944*	4.502**
	(1.055)	(0.992)	(2.006)
N	418	230	188

Panel B: market adjusted return with float value weighted market return	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.329***	1.178***	1.514***
	(0.335)	(0.388)	(0.575)
(-1, +5)	2.844***	2.039***	3.828***
	(0.641)	(0.708)	(1.130)
(-1, +10)	3.749***	2.273***	5.555***
	(0.853)	(0.821)	(1.601)
(-1, +15)	3.790***	2.165**	5.777***
	(0.975)	(0.887)	(1.869)
(-1, +20)	3.252***	1.756*	5.083**
	(1.055)	(0.976)	(2.014)
N	418	230	188

Table IA3 Continued

Panel C: market adjusted return with total value weighted market return			
	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.350***	1.189***	1.546***
	(0.332)	(0.385)	(0.571)
(-1, +5)	2.849***	2.041***	3.837***
	(0.636)	(0.702)	(1.120)
(-1, +10)	3.744***	2.271***	5.547***
	(0.844)	(0.812)	(1.584)
(-1, +15)	3.805***	2.176**	5.797***
	(0.965)	(0.874)	(1.852)
(-1, +20)	3.332***	1.859*	5.134**
	(1.039)	(0.959)	(1.986)
N	418	230	188

Panel D: Fama-French three factor model with float value weighted risk premium			
	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.287***	1.047***	1.581**
	(0.372)	(0.391)	(0.675)
(-1, +5)	2.053***	1.387*	2.867*
	(0.787)	(0.709)	(1.519)
(-1, +10)	2.626**	1.583*	3.902*
	(1.068)	(0.808)	(2.160)
(-1, +15)	2.788***	0.951	5.036**
	(1.014)	(0.853)	(1.991)
(-1, +20)	2.373**	1.054	3.987*
	(1.066)	(0.951)	(2.063)
N	418	230	188

Panel E: Fama-French three factor model with total value weighted risk premium			
	Full sample	SOEs subsample	Non-SOEs subsample
(-1, +1)	1.357***	1.111***	1.658***
	(0.354)	(0.389)	(0.626)
(-1, +5)	2.166***	1.453**	3.038**
	(0.725)	(0.703)	(1.362)
(-1, +10)	2.772***	1.609**	4.195**
	(0.953)	(0.801)	(1.876)
(-1, +15)	2.921***	1.012	5.256***
	(0.987)	(0.853)	(1.921)
(-1, +20)	2.525**	1.105	4.261**
	(1.033)	(0.957)	(1.971)
N	418	230	188

Table IA4: Robustness test of Cross-sectional Regression of CAR around PCID Resignation

This table reports results of the cross-sectional regression of cumulative abnormal returns (CAR) around resignation of politically connected independent directors (PCID) estimated from different models using the following model: $CAR_i = \alpha + \beta_1 PCID_i i + Controls + \omega_j + \epsilon_i$, where CAR_i is the CAR of firm i, $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, and ω_j is industry fixed effect. The firm is in the treatment group it has PCID resignation to comply with Regulation No.18. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. In Panel A, I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and total value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = Ret_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. In Panel B and C, the abnormal return is estimated using market-adjusted return: $AR_{i,\tau} = R_{i,\tau} - R_{m,\tau}$. CAR is calculated as the same as in Panel A. I use float value weighted market return and total value weighted market return in Panel B and Panel C, respectively. In Panel D and E, I estimate the Fama-French three factor model to obtain abnormal return: $R_{i,t} = \beta_{1,i} R_{m,t} + \beta_{2,i} SMB_t + \beta_{3,i} HML_t + \epsilon_{i,t}$, where $R_{i,t}$, $R_{m,t}$, SMB_t, and HML_t are the excess return of stock i, market risk premium, size premium, and value premium on day t, respectively. The estimated coefficients $\hat{\beta_{1,i}}$, $\hat{\beta_{2,i}}$, and $\hat{\beta_{3,i}}$ are used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - (\hat{\beta_{1,i}} R_{m,\tau} + \hat{\beta_{2,i}} SMB_\tau + \hat{\beta_{3,i}} HML_\tau)$, where $R_{i,\tau}$, $R_{m,\tau}$, SMB_τ, and HML_τ are realized excess returns of stock i, realized market risk premium, size premium, and value premium on day τ, respectively. I use float value weighted market return and total value weighted risk premium in Panel D and Panel E, respectively. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: market model with total value weighted market return

	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.515*	1.047*	2.371***	1.971***	1.330**
	(0.265)	(0.562)	(0.456)	(0.463)	(0.488)
Size	-0.196	-0.439	-0.629	-0.394	0.211
	(0.347)	(0.532)	(0.527)	(0.533)	(0.637)
Leverage	-0.238	0.652	2.067	1.595	0.802
	(0.791)	(1.590)	(1.805)	(2.212)	(2.461)
B/M	-1.912*	-1.858	-1.135	-2.926*	-3.676*
	(1.041)	(1.451)	(1.765)	(1.585)	(1.799)
Growth	0.301	0.083	0.155	-0.321	-0.523
	(0.203)	(0.344)	(0.485)	(0.533)	(0.688)
ROE	0.127	0.469**	0.739***	0.876***	0.841***
	(0.077)	(0.164)	(0.207)	(0.189)	(0.248)
Top1	1.200	2.359	0.727	2.221	0.516
	(2.410)	(5.352)	(5.589)	(5.683)	(6.545)
Ivol	-0.014***	-0.036***	-0.069***	-0.105***	-0.063***
	(0.004)	(0.010)	(0.015)	(0.014)	(0.015)
SOE	0.344	-0.754	-1.150	-1.302	-1.551
	(0.487)	(0.842)	(1.066)	(1.361)	(1.390)
Constant	4.201	10.008	12.891	7.573	-4.855
	(6.784)	(9.757)	(9.517)	(9.765)	(11.697)
N	836	836	836	836	836
Adj. R^2	0.025	0.029	0.033	0.034	0.027

Panel B: market adjusted return with float value weighted market return

	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.524*	1.065*	2.317***	1.972***	1.322**
	(0.272)	(0.513)	(0.432)	(0.486)	(0.523)
Size	-0.195	-0.449	-0.675	-0.510	0.105
	(0.358)	(0.573)	(0.600)	(0.616)	(0.714)
Leverage	-0.223	0.379	1.928	1.650	0.691
	(0.817)	(1.636)	(1.763)	(2.103)	(2.328)
B/M	-2.100*	-2.281	-1.404	-2.877*	-3.947**
	(1.089)	(1.515)	(1.783)	(1.483)	(1.646)
Growth	0.328	0.112	0.208	-0.284	-0.501
	(0.224)	(0.343)	(0.477)	(0.525)	(0.702)
ROE	0.130	0.466**	0.747***	0.892***	0.877***
	(0.075)	(0.163)	(0.211)	(0.197)	(0.264)
Top1	1.152	2.242	0.324	1.632	-0.184
	(2.272)	(5.366)	(5.683)	(5.727)	(6.769)
Ivol	-0.019***	-0.038***	-0.063***	-0.081***	-0.043***
	(0.003)	(0.010)	(0.014)	(0.013)	(0.013)
SOE	0.403	-0.417	-0.741	-0.962	-1.496
	(0.480)	(0.855)	(1.059)	(1.372)	(1.388)
Constant	4.485	10.479	13.896	9.656	-2.686
	(6.947)	(10.455)	(10.678)	(11.084)	(12.921)
N	836	836	836	836	836
Adj. R^2	0.027	0.031	0.036	0.037	0.031

Table IA4 Continued

Panel C: market adjusted return with total value weighted market return	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.519*	1.037*	2.288***	1.949***	1.315**
	(0.273)	(0.508)	(0.434)	(0.485)	(0.504)
Size	-0.199	-0.452	-0.694	-0.531	0.045
	(0.354)	(0.564)	(0.587)	(0.598)	(0.700)
Leverage	-0.290	0.383	1.901	1.696	0.895
	(0.800)	(1.638)	(1.773)	(2.115)	(2.313)
B/M	-1.976*	-1.997	-1.004	-2.454	-3.362**
	(1.062)	(1.473)	(1.742)	(1.417)	(1.564)
Growth	0.338	0.120	0.204	-0.272	-0.485
	(0.210)	(0.321)	(0.443)	(0.487)	(0.657)
ROE	0.124	0.448**	0.725***	0.868***	0.848***
	(0.075)	(0.162)	(0.210)	(0.197)	(0.263)
Top1	1.005	1.999	0.230	1.555	-0.205
	(2.241)	(5.252)	(5.550)	(5.554)	(6.527)
Ivol	-0.018***	-0.038***	-0.061***	-0.077***	-0.042***
	(0.003)	(0.009)	(0.013)	(0.012)	(0.012)
SOE	0.386	-0.449	-0.774	-1.016	-1.501
	(0.467)	(0.842)	(1.059)	(1.377)	(1.394)
Constant	4.461	10.602	14.453	10.464	-1.238
	(6.869)	(10.304)	(10.448)	(10.786)	(12.681)
N	836	836	836	836	836
Adj. R^2	0.027	0.030	0.035	0.036	0.031

Panel D: Fama-French three factor model with float value weighted market return	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.433*	0.273	0.958	1.186**	0.491
	(0.235)	(0.581)	(0.845)	(0.459)	(0.518)
Size	-0.148	-0.426	-0.555	-0.822*	-0.606
	(0.327)	(0.537)	(0.542)	(0.454)	(0.571)
Leverage	-0.816	-0.366	-0.174	1.992	1.643
	(1.207)	(3.055)	(3.660)	(2.829)	(2.915)
B/M	-1.311	0.417	2.489	2.157	2.966
	(1.118)	(1.637)	(1.807)	(1.818)	(2.047)
Growth	0.353***	0.185	0.264	-0.092	-0.324
	(0.099)	(0.180)	(0.247)	(0.378)	(0.413)
ROE	0.015	0.192	0.360*	0.454**	0.320
	(0.084)	(0.167)	(0.191)	(0.162)	(0.235)
Top1	0.039	-0.569	-2.713	1.698	1.721
	(3.027)	(6.424)	(6.902)	(5.074)	(5.601)
IVol	-0.014**	-0.040**	-0.065**	-0.090***	-0.061***
	(0.006)	(0.017)	(0.023)	(0.014)	(0.015)
SOE	0.222	-0.506	-0.671	-2.141	-1.993
	(0.690)	(1.535)	(1.878)	(1.544)	(1.528)
Constant	2.629	10.346	13.770	18.928**	13.718
	(6.381)	(9.364)	(9.283)	(8.491)	(10.580)
N	836	836	836	836	836
Adj. R^2	0.020	0.018	0.019	0.029	0.023

Table IA4 Continued

Panel E: Fama-French three factor model with total value weighted market return					
	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.499**	0.390	1.208*	1.395**	0.714**
	(0.215)	(0.505)	(0.654)	(0.502)	(0.327)
Size	-0.157	-0.444	-0.625	-0.880*	-0.677
	(0.320)	(0.515)	(0.506)	(0.442)	(0.547)
Leverage	-0.806	-0.082	0.399	2.595	2.442
	(1.058)	(2.677)	(2.995)	(2.399)	(2.351)
B/M	-1.343	0.338	2.206	1.860	2.671
	(1.046)	(1.525)	(1.726)	(1.713)	(1.893)
Growth	0.342***	0.164	0.212	-0.132	-0.386
	(0.093)	(0.174)	(0.231)	(0.400)	(0.478)
ROE	0.014	0.200	0.376*	0.475**	0.329
	(0.083)	(0.162)	(0.187)	(0.162)	(0.234)
Top1	0.235	0.064	-1.412	2.836	2.995
	(2.819)	(5.924)	(6.057)	(4.418)	(4.787)
Ivol	-0.015***	-0.039**	-0.063***	-0.085***	-0.060***
	(0.005)	(0.015)	(0.019)	(0.011)	(0.011)
SOE	0.195	-0.640	-0.907	-2.304	-2.247
	(0.620)	(1.350)	(1.559)	(1.402)	(1.412)
Constant	2.718	10.409	14.610	19.500**	14.492
	(6.274)	(9.069)	(8.845)	(8.396)	(10.356)
N	836	836	836	836	836
Adj. R^2	0.021	0.020	0.022	0.034	0.027

Table IA5: Robustness Test of Cross-sectional Regression of CAR around PCID Resignation by Ownership Structure

This table reports results of the cross-sectional regression of cumulative abnormal returns (CAR) around resignation of politically connected independent directors by ownership structure using the following model: $CAR_i = \alpha + \beta_1 PCID_i + Controls + \omega_j + \epsilon_i$, where CAR_i is the CAR of firm i, $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, and ω_j is industry fixed effect. The firm is in the treatment group if it has PCID resignation to comply with Regulation No.18. I use market model to obtain abnormal return: $R_{i,t} = \beta_i R_{m,t} + \epsilon_{i,t}$, where $R_{i,t}$ and $R_{m,t}$ are the excess return of stock i and total value weighted market excess return on day t. The estimation window is 280 days to 90 days before the release of Regulation No.18. The estimated coefficients $\hat{\beta}_i$ is used to construct the abnormal return as $AR_{i,\tau} = R_{i,\tau} - \hat{\beta}_i R_{m,\tau}$, where $R_{i,\tau}$ and $R_{m,\tau}$ are realized excess returns of stock i and market on day τ. CAR is calculated as $\sum_{\tau=-1}^{T} AR_{i,\tau}$, where T is equal to 1, 5, 10, 15, and 20 for different event windows. The SOEs sample includes 230 treated firms and 230 controlled firms matched with the treatment group. The non-SOEs sample includes 188 treated firms and 188 controlled firms. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

	SOEs					non-SOEs				
	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)	(-1,+1)	(-1,+5)	(-1,+10)	(-1,+15)	(-1,+20)
PCID	0.432	0.683	1.120	0.832	0.840	0.716*	2.023**	4.541***	4.038***	2.561*
	(0.592)	(1.315)	(1.096)	(1.025)	(0.907)	(0.376)	(0.763)	(0.986)	(1.045)	(1.394)
Size	-0.365	-0.394	-0.566	-0.514	0.145	-0.118	-1.040	-1.747	-1.286	-0.935
	(0.399)	(0.537)	(0.736)	(0.515)	(0.627)	(0.764)	(1.279)	(1.018)	(0.764)	(0.769)
Leverage	-0.701	-1.439	-0.853	-1.510	-2.011	0.523	3.626	6.188**	6.694***	4.991
	(0.888)	(1.848)	(2.061)	(2.052)	(2.431)	(2.036)	(2.775)	(2.509)	(2.152)	(3.505)
B/M	-0.585	0.099	1.002	0.679	0.586	-2.811	-2.613	-0.480	-3.922	-5.102
	(1.170)	(1.674)	(1.957)	(2.028)	(2.341)	(1.687)	(2.347)	(2.752)	(3.142)	(3.967)
Growth	0.242	-0.524	0.279	-0.530	-1.630*	0.342	0.194	0.034	-0.296	-0.065
	(0.160)	(0.563)	(0.860)	(0.754)	(0.782)	(0.269)	(0.385)	(0.648)	(0.742)	(0.746)
ROE	0.705	3.350	7.578	6.188	4.391	0.120	0.506*	0.765***	0.936***	0.921***
	(2.013)	(5.168)	(8.495)	(7.877)	(7.089)	(0.131)	(0.254)	(0.191)	(0.096)	(0.126)
Top1	1.528	1.739	0.891	6.376*	4.379	2.001	6.217	6.268	3.128	2.636
	(1.528)	(3.186)	(2.962)	(3.094)	(3.158)	(3.512)	(6.732)	(5.937)	(7.833)	(10.195)
Ivol	0.649***	1.599***	1.708*	2.156***	2.526***	-0.023***	-0.054***	-0.084***	-0.132***	-0.090***
	(0.170)	(0.413)	(0.786)	(0.664)	(0.689)	(0.005)	(0.008)	(0.010)	(0.012)	(0.010)
Constant	6.651	6.032	8.336	3.222	-13.566	1.961	19.744	31.996	24.100	19.256
	(8.368)	(10.959)	(14.330)	(10.136)	(12.388)	(14.871)	(24.380)	(19.009)	(14.713)	(14.619)
N	460	460	460	460	460	376	376	376	376	376
Adj. R^2	0.050	0.057	0.072	0.065	0.058	0.044	0.051	0.065	0.074	0.070

Table IA6: Robustness test of Operating Performance

This table reports change of firm's operating performance after politically connected independent director (PCID) resignation using the following regression model: $y_{it} = \alpha + \beta_1 PCID_i + \beta_2 PCID_i \times Post_t + Controls_{t-1} + \omega_j + \gamma_t + \epsilon_{it}$, where $PCID_i$ is a dummy variable which is equal to 1 if the firm is in the treatment group and 0 otherwise, $Post_t$ is a dummy variable which is equal to 1 after the PCID resignation takes effect and 0 otherwise, ω_j and γ_t are industry and year fixed effect. The firm is in the treatment group if it has PCIDs resignation to comply with Regulation No.18. Operating performance is measured using operating profits (OPOA) in Panel A and total cash flow (CF) in Panel B. OPOA is defined as the ratio of operating profit to total assets and CF is defined as the ratio of total cash flows to total assets. The sample includes 418 treated firms and 418 controlled firms matched with the treatment group. I report results for the full sample, SOEs subsample, and non-SOEs subsample. All variables are winsorized at 1% to 99% except dummy variables. All variables are defined in Appendix A. Standard errors are clustered at the industry level and reported in parentheses. ***, **, and * represent statistical significance at the 1% level, 5% level, and 10% level, respectively. Data source: CSMAR and website of Shanghai Stock Exchange and Shenzhen Stock Exchange.

Panel A: operating profits (OPOA)	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
PCID	0.005	0.010**	-0.003
	(0.004)	(0.004)	(0.004)
PCID × *Post*	-0.001	-0.002	0.001
	(0.002)	(0.003)	(0.003)
Size	0.020***	0.019***	0.024***
	(0.003)	(0.003)	(0.002)
Tangibility	-0.151***	-0.159***	-0.147***
	(0.009)	(0.013)	(0.007)
Leverage	0.006	-0.019	0.043
	(0.015)	(0.016)	(0.028)
B/M	-0.061***	-0.049***	-0.095***
	(0.008)	(0.008)	(0.006)
Growth	0.010***	0.013**	0.006**
	(0.003)	(0.005)	(0.002)
Top1	0.015***	-0.003	0.044***
	(0.005)	(0.011)	(0.009)
Age	0.005*	0.008*	0.002
	(0.003)	(0.004)	(0.003)
Independence	0.005	-0.005	0.024
	(0.026)	(0.027)	(0.028)
Board size	0.007	0.000	0.026***
	(0.005)	(0.009)	(0.008)
SOE	-0.013***		
	(0.003)		
Constant	-0.380***	-0.339***	-0.528***
	(0.049)	(0.047)	(0.034)
N	4,871	2,747	2,124
Adj. R^2	0.259	0.272	0.272

Table IA5 Continued

Panel B: total cash flow (CF)	(1) Full sample	(2) SOEs subsample	(3) Non-SOEs subsample
$PCID$	-0.015	-0.022	-0.009
	(0.015)	(0.028)	(0.025)
$PCID \times Post$	0.020	0.003	0.032
	(0.018)	(0.024)	(0.022)
Size	0.026	0.052**	0.013
	(0.017)	(0.024)	(0.018)
Tangibility	0.386***	0.251**	0.482***
	(0.054)	(0.094)	(0.069)
ROA	0.405***	0.398***	0.157
	(0.085)	(0.129)	(0.130)
Leverage	1.001***	1.004***	0.806**
	(0.216)	(0.219)	(0.374)
B/M	-0.155***	-0.180***	-0.136
	(0.043)	(0.031)	(0.127)
Growth	0.024	0.052	0.007
	(0.016)	(0.035)	(0.005)
Top1	0.254	0.174	0.416***
	(0.170)	(0.194)	(0.129)
Age	0.021	0.049	-0.017
	(0.040)	(0.091)	(0.028)
Independence	-0.210	-0.154	-0.375**
	(0.238)	(0.330)	(0.138)
Board size	-0.071	-0.051	-0.105***
	(0.048)	(0.071)	(0.019)
SOE	0.078***		
	(0.016)		
Constant	-0.517	-0.985*	0.080
	(0.368)	(0.513)	(0.428)
N	4,871	2,747	2,124
Adj. R^2	0.241	0.256	0.226