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# Political and interlocking connections in the boardroom on private equity placements

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#### **Abstract**

This study examines the influence of directors, who are politically connected and/or have boardroom interlocking, on private equity placements (PEPs) in Chinese listed firms. We document that interlocked directors can significantly influence the propensity to apply for PEPs, approval of PEPs and reduce the cost of PEPs while providing greater access to proceeds from PEPs through lowering information asymmetry and information cost. Although politically connected directors have a significant role in the approval of PEPs, they are more likely to reduce the monitoring effects and increase agency problems which lead to increase cost of PEPs and reduced proceeds from PEPs. The results also reveal that political connection diminish the benefits of interlocking directors for firms having directors with both interlocking and political ties.

**Keywords:** Agency problem; Interlocked directors; Private Equity Placements; Politically connected directors; information asymmetry and monitoring effect

## 1. Introduction

Board diversity in terms of gender, ethnicity, age, educational and professional background, and life experience, as a monitoring device has been the focus of attention of many researchers in both developed and emerging markets over the last decade or so. However, there are few studies on the role of the information dissemination, monitoring, advisory, political and social ties of board members on corporate financing decisions under different institutional, regulatory and judicial backgrounds, suggesting that social connections enhance a board's advisory ability, but possibly at the cost of diminished efficacy in its monitoring function (Kramarz and Thesmar 2006; Schmidt, 2008; Hwang and Kim 2009).

The private equity placements (PEPs) have become the most important method of equity financing for listed firms since they were introduced in China in May 2006 (Lu et al. 2011; Cao et al. 2013). Cao et al. (2013) note that the Chinese security-offering regulations set strict profitability thresholds for the Seasonal Equity Offerings (SEO), but there is no such threshold for PEPs. When the regulations become stricter, firms tend to withdraw their proposals because there is a low probability that proposals will be approved within the valid period. Therefore, they argue that changes in the strictness of regulations can affect firms' decision for private equity (PE) financing (Liu et al. 2007; Cao et al. 2013). Therefore, Chinese firms' PE financing is comparatively easier than SEOs. PEPs are also moderately restricted by the security-offering regulations due to specific regulations for PEPs as explained in Section 2. The PEPs in China can be classified into two types based on their offering purposes (Cao et al. 2013). The first type is for investment financing. Because the China Security Regulation Commission (CSRC) does not set a profitability threshold for PEPs, as it does for SEOs, firms prefer PEPs to SEOs to finance investment projects. The second type is for capital restructuring. The CSRC encourages firms to use PEPs for restructuring in order to reduce related-party transactions and strengthen independence, and to improve asset quality and profitability. Therefore, Chinese firms issue

shares to the controlling shareholders for asset acquisition or for asset replacements. Due to these reasons, PEPs were preferred choice of financing tool in China and were issued by 85% of companies, accounted for 81% of the value of SEO during the period between 2006 and 2010 (Abidin et al. 2012; Fonseka et al. 2014; Yu and Xu, 2010).

This study focuses on political and interlocking connections of the board members in the firm financing decisions, in particular, PEP in Chinese listed firms. While China has attracted international attention in recent years as its stock market has been increasingly mature and integrated with the world market, the PEPs are also in the spot light where political and interlocking ties of some board members play an active role in securing low cost financing. Given the dearth of research in this area in Chinese context, the prime motivation of this research is based on the argument that board interlocking and political ties are mechanisms that can affect corporate strategies and financing decisions. The paper fills the gap in the literature and provides evidence that board members' interlocking out performs political connection in reducing the cost of PEP and providing greater access to proceeds from PEPs.

China is a country in which political power has traditionally been concentrated, with most decision-making authority vested in the hands of the government. Despite economic reforms, the ideological discrimination of firms with political connections (i.e. the Communist Party and the government) is a feature that sets China apart from other transitional economies (Li et al. 2008). Hung et al. (2015) note that the Chinese government has continued to retain substantial control over the corporate sector even after 20 years of state enterprise reform and political ties enable both state and non-state firms to engage in implicit and explicit contracts with the government and its related entities, ranging from capital financing, operational contracts to direct subsidies. When corporate executives, who have political ties, interact with government officials, bank managers and the heads of state institutions, they tend to create links with important political and economic leaders (Li et al. 2006). In Chinese context, academic researches show that political connections

are mostly defined as political participation in Chinese People's Congress (CPC) or the Chinese People's Political Consultative Conference (CPPCC) (Fan, Wong, and Zhang 2007; Ma, Ma, and Tian 2013; Xu, Xu, and Yuan 2013; He, Wan, and Zhou 2014), or the Communist Party (Li et al. 2008).

Xu et al. (2013) contend that the cultivation of political ties is very important in China, being a relationship-based economy. Building connections with the government, or even engaging in politics, can facilitate firms' private communications with authorities which might mitigate severe information asymmetry and many difficulties of doing business in China, especially in relation to accessing different sources of finance. Chan et al. (2012) document that firms having a CEO or chairman with strong political relationships are less likely to face financial constraints. Wang (2015) indicate that independent directors with political background or close ties with government can arrange different forms of financing and other advantages for the firms while avoiding 'political-pecking order'. Such political capital of firms acts as an effective informal mechanism enabling firms overcoming the drawback of market institutional problems (Luo and Tang 2009).

On the contrary, Dielemann and Boddewyn (2012) argue that for firms in emerging markets, political ties potentially reduce the autonomy of firms under government control, thereby increasing political costs. Fan et al. (2007) find that Chinese firms with politically-connected managers have poorer initial public offering (IPO) performance and Boubakri, Cosset and Saffar (2008) find that politically connected newly privatized Chinese listed firms exhibit poorer accounting performance than their non-connected counterparts. Moreover, politically connected directors distort investment efficiency (Chen et al. 2011) and lower capital allocation efficiency (Zhao, Wan, and Xu 2013).

Similar to political ties and connections, studies looking at the effects of networks on different areas of financial markets, such as lending markets (Garmaise and Moskowitz 2003),

venture capital (Sorenson and Stuart 2001; Hochberg et al. 2007) and strategic alliances (Robinson and Stuart 2007; Lindsey 2008) supporting the view that private information, accessible only via social networks, can influence diverse financial behaviours and outcomes. In the context of China, the success or failure of an enterprise generally depends on social resources and close relationships in obtaining valuable information, capturing market opportunities and occupying scarce resources (Xu et al. 2015; Ding et al 2015). Given that social network relationship is used extensively as a social resource or capital to obtain scarce resources, board interlocking (i.e. interlocking directorate) is very deep rooted in China because of social and corporate networking (i.e. *Guanxi* – an informal relationship between individuals to solicit special favours – Which is a social networking facility that has existed everywhere in Chinese society and has been considered an informal mechanism that may be an essential element in acquiring scarce resources). It is evident that *Guanxi* has become the lifeblood of business conducts and social interactions with a substantial influence in driving stronger and wider inner-and-outer-anchor relationships in Chinese managerial progression (Luo and Chen 1997; Chen and Chen 2004). As such, interlocking directorate is considered an external link of different boards as it connects different companies through directors. Such connected interlocking may be a ‘direct’ or ‘indirect’ interlock creating upper class connections between companies (Au et al. 2000). Also a connected interlocking directorate can form either ‘primary’ or ‘secondary’ interlocks to exchange significant information within the connected companies more promptly and have better institutional links and controls.

Extant literature documented extensively the importance of information exchange or transfer through board interlocks.<sup>1</sup> Interlocking directorates share information on different business practices, so firms can benefit from inter-corporate communication channels (Fohlin 1999; Brass et al. 2004; Non and Philip, 2007). Mizruchi (1996) suggests that an interlocking

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<sup>1</sup> board interlocks that enable firms imitating diverse contexts including firm political expenditures (Mizruchi, 1996), firm philanthropic activity (Galaskiewicz and Wasserman, 1989), the spread of antitakeover mechanisms such as poison pills (Davis, 1991), firm choices regarding mergers and acquisitions (Haunschild, 1993; Renneboog and Zhao, 2014) and the CEO searching process (Khurana, 2002).



board might influence a broader range of behaviours, such as political action, public policy, firms' organisational structure and their mergers and acquisitions. Board connected interlocks may enable the diffusion of undesirable firm practices.<sup>2</sup> Some studies also suggest that 'interlocked' directors could be poor monitors either because directors' independence is compromised (Hallock 1997; Fich and White 2003; Larcker et al. 2006) or board members are simply too busy to keep a watchful eye on management (Fich and Shivdasani 2006).

Both interlocked and politically connected directors are distinguished channels of information transmission between the parties involved in PEPs, as they facilitate direct communication flows. Nevertheless, prior literature argues that being interlocked and politically connected can have a negative impact on directors' monitoring roles and expedite agency problems (Core et al. 1999; Fich and Shivdasani 2006; Shivdasani and Yermack 1999). Hence, there is an imperative question that arises from this discussion: do interlocked and politically connected directors, by communicating privileged information during the PEPs process, help resolve the information asymmetry problems explained above or do they lead to a deterioration of their monitoring function and enhance agency problems? We attempt to investigate the role of both interlocked boards and boards that have links with the politically connected firms' propensity to be targeted in PE financing, the impact of these board networks on the costs associated with PE financing and proceeds from PEPs. We argue that politically connected directors' actions and motivations are different from directors with other types of ties such as connected interlocking directorates. Moreover, firms can have both political and interlocking networking ties. However, prior studies focus on examining the role of political and interlocking ties separately. We argue that both political connections and interlocked directors could have a momentous influence on firm financing activities but with different outcomes. We attempt to fill this gap in the literature by comparing the effect of political ties versus interlocking among firms in an emerging

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<sup>2</sup> Eg: stock options backdating (Bizjak et al., 2009) and earnings management (Chiu et al., 2013; Hirshleifer and Teoh, 2009), and the spill-over effects of reputational penalties in financial fraud reporting (Kang, 2008)

economy-China. Our paper extends this body of literature and understanding in that political link and interlocked directorates can lead to the spread of corporate practices, such as PEP in publicly listed firms.

Our paper contributes to the growing stream of research on the effects of social networks in different areas of finance, such as strategic alliances (Robinson and Stuart 2007; Lindsey 2008), lending markets (Garmaise and Moskowitz 2003) and venture capital (Sorenson and Stuart 2001; Hochberg, Ljungqvist, and Lu 2007). Taking Social Capital Theory from sociological science we extend the literature by applying it within corporate finance research, thus expanding the scope of corporate social and political connection studies. Our specific contributions are: Firstly, we provide empirical support for board directors' level networks, namely connected interlocking and political ties, on private information flows, and these ties have differential access to this information can influence diverse financial behaviors and outcomes, in this case PE financing. We find evidence that interlocked directors, rather than political ties, are effective in cases of firms' propensity to apply for PEPs, while on the approval stage PEPs directors' political ties appear more essential than connected interlocking.

Secondly, interlocking and political connections enable those individuals to become conduits for information, knowledge, and experience across their boardroom and political networks. Our findings partially support the argument of Core et al. (1999), Fich and Shivdasani (2006) and Shivdasani and Yermack (1999), that only those directors who are politically connected have a negative influence on directors' monitoring role and expedite agency problems. Interlocked directors who have become conduits for information, knowledge and experience in their board rooms can reduce information asymmetry and do not significantly contribute to a deterioration of the monitoring effect or enhance agency problems related to PE financing. Thirdly, we find that political connections let down the benefits of interlocking directors for firms having directors with both interlocking and political ties. These findings enhance our

understanding and the existing literature related to a highly regulated, yet relationship-oriented, market - China.

Finally, we contributed to the growing literature of PE financing in publicly listed firms. Previous studies on PEPs suggest that in most markets private placements have market discounts (Wruck 1989; Hertznel and Smith 1993; Chen et al. 2002; Wu et al. 2005; Lu et al. 2011; Fonseca et al. 2014), as well as positive announcement effects (Hertznel and Smith 1993; Kato and Schallheim 1993; Krishnamurthy et al. 2005; Renneboog et al. 2007; Lu et al. 2013; Fonseca et al. 2014). While Wruck's (1989) explanation was based on ownership concentration level, other studies explained that monitoring benefits and information effects appear to be relatively more important than ownership effects. Hertznel et al. (2002) and Hertznel and Rees (1998) investigate the operating performance after PEPs and find that there is no significant improvements. However, Huang and Chen (2013) find that Taiwanese firms improved operating performance after PEPs. Xu et al. (2015) study the effect of quality of corporate governance on firms' choice of issuing method in private placements and discount on PEPs in Australia which is closely related to our research. Unlike prior studies, our study contributes to the effects of both political and interlocks connection of board on PEP decisions (firm's applying and approval of regulators), the price discount and proceed from PEPs and their theoretical explanation in the largest emerging market.

The remainder of the paper is organized as follows: Section 2 provides the institutional framework; Section 3 discusses the literature from which the research hypotheses have been developed; Section 4 presents the data and methodology; Section 5 presents the results and discussion; Section 6 outlines the conclusions.

## 2. Institutional Framework in China

China is commonly perceived as a country with weak legal institutions and strong government control of the corporate sector (La Porta et al. 1998; Allen, Qian, and Qian 2005) with explicit and implicit contracts based on political networks (Faccio 2006; Faccio et al. 2006). Government regulations create external uncertainties for firms' operations (Lang and Lockhart 1990) and restrict their capabilities to acquire external resources (Khawaja and Mian, 2005).

The state holds a significant stake, which greatly influences company operations in China and exerts enormous power in terms of resource allocation and enforcing regulations (Tsai 2008; Wu and Cheng 2011). Warner (2014) argues that extensive government intervention still exists in China as the country has not fully established the market economic order. Moreover, lack of a sound legal system makes transaction costs more expensive for firms. The government controls many scarce resources and the allocation of resources is largely dependent on close relationships in which firms will be treated according to their relationship with the government (Yu et al. 2016). Therefore, to get more resources and preferential treatment, companies are more inclined to build important and interpersonal relations as part of their business strategy (Xin and Pearce 1996). Under this Chinese interpersonal relationships 'structure', firms being networked by interlocking directorates can use interpersonal relationships of interlocking directors to better archive knowledge, public policies, contracts and resources, which facilitate the ability of settling uncertainty, relaxing resource constrains and reducing transaction cost, and hence yield economic benefits.

Sun and Tong (2003) demonstrate that the state's domination of ownership in listed firms is a prominent institutional feature in China. State owned enterprises (SOEs) enjoy preferential status in obtaining financial and other key inputs (Brandt and Li 2003; Chow et al. 2010; Li et al. 2008), while private firms are often denied access to sources of financing (Brandt and Li 2003). Zou and Xiao (2006) emphasize that ownership identity plays a vital role in corporate financing

decisions and, therefore, given tight regulatory controls and severe agency problems, managers have an incentive to raise equity. The Chinese stock market functions differently to those of the major market economies due to the tight regulatory regime (Bo et al. 2011). Chinese listed firms fall into three categories of ownership: state, institutional (legal person) and private. Prior to the reform of the private equity market in China, the proportion of state owned firms or institutions accounted for about 70% of total shares (Zou and Xiao 2006). In 2005, the China Securities Regulatory Commission (CSRC) initiated share split reform for listed companies and unfroze non-tradeable state-owned shares. Since the reform, publicly listed firms have relied primarily upon private placements to raise equity capital rather than other types of seasoned equity offerings for new investments (Fonseka et al. 2014).

### **2.1 Review of Chinese stock market regulations on PEPs**

Theories such as the information asymmetry and monitoring hypothesis are commonly employed to explain the wealth creation of PEP (Hertzel and Sumith 1993; Lu et al. 2011; Wruck 1989; Wruck and Wu 2009). However, the explanation and the applicability of supported theories vary between countries due to different institutional, regulatory and judicial backgrounds. The PEP-specific regulatory regime was introduced by the CSRC in 2006 which requires mandatory approval from the regulator before placements can be made. Such PEP approval system is quite different from the self-registration PEP system in other countries.

According to the CSRC, the regulations on PEPs are aimed to reduce related-party transactions, avoid competition, enhance independence, improve asset quality, improve financial stability and enhance the sustained profitability of companies. The PEP regulations are expected to ensure that non-public offerings generate legitimate benefits to shareholders and protect the rights of all shareholders. Further, companies offering PEPs should determine the PE issue price reflecting the best interests of all stakeholders. Regulations also govern the method for determining the PE price as well as the category and number of institutional investors/ block-

holders in a particular PE issue. However, there is no strict accounting based quantitative criteria (Eg: Threshold on Return on Equity) for approving PEP applications in new regulation compared to old regulation which is equally applied to PEP and SEO.

Regulations also place restrictions on the categories of investors who can be invited to subscribe to a PE issue. The regulations favor passive investors while limiting the number of institutional investors in any particular PE issue. PEPs can be sold to a maximum of 10 investors who belong to any type of investor category. There is no specific limit on the amount of a PE issue. However, if the board of directors disclose the maximum money they intend to obtain for a project, the PE issue cannot exceed the amount needed for that project. If the amount is not certain, firms should disclose the maximum amount expected to be raised from a PEP. The board of directors will determine the amount of shares in the non-public offering. If the amount of the non-public offering in shares is uncertain, the decision of the board of directors shall specify the range of the share amount which includes upper and lower limits. According to new PEPs regulation, PEPs issuing firm should sent the invitations to the top 20 shareholders (blockholders) and to investors who have submitted a subscription 'letter of intent', after the board's announcement of the resolutions. Invitees should comprise (1) not less than 20 securities investment fund management companies; (2) not less than 10 securities companies; (3) not less than 5 insurance institutional investors.

Firms issuing PEPs are required to determine an issue price based on the fair principles of justice reflecting on the best interests of all stakeholders and gain prior approval from the CSRC. The issuing price shall not be lower than the minimum price. According to the regulation, the average price is determined by the ration between total trading values of previous twenty trading days before pricing benchmark to total trading volume of previous twenty trading days.

The CSRC approval is a lengthy process and after the approval the PEPs should be listed within 6 months. Most countries have PEP resale restrictions. In China, newly issued PE shares are not

allowed to be sold within the following 12 months irrespective of the category of the investor. If shares are bought by the controlling stockholder or any other firm controlled by the controlling shareholder, they cannot be resold within the following 36 months.

### **3. Literature review and hypotheses developments**

#### **3.1 Boardroom network ties, propensity to apply for PEPs and approval of PEPs**

Prior studies find that political ties help firms to deal with government bureaucracy, to eliminate regulatory barriers and receive favours (Agrawal and Knoeber 2001), and to gain favourable access to resources (Khwaja and Mian 2005; Faccio 2006; Leuz and Oberholzer-Gee 2006; Fan et al. 2008). In China, political connections through membership in the CPC or the CPPCC can enhance their social status, which in turn helps in obtaining valuable resources (Fan, Wong, and Zhang 2007; Li et al. 2008; Berkman, Cole, and Fu 2010; Wu, Wu, and Rui 2012).

Close ties with the government help firms to surpass market and state failures and to avoid ideological discrimination. Those firms in China whose directors are politically involved and well connected with the government are more likely to garner favourable treatment than those without such ties by being able to circumvent government regulations. Thus, these firms usually apply for PEP when they know that their application will be approved with a large chance.

Having an interlocking board has also proven to be important. Interlocking directorates may become a means of exerting influence, formal or informal, among corporations by sharing one of the most influential resources in the organization: board of directors. The number of common board ties between directors in large companies as a good sign of networking ties between them (Seidel and Westphal 2004). As Davis's (1991) model indicates interlock ties as a form of social capital, interlocking provides potential access to key information among firms that flow through the network.

Social Capital theory explains that interlocked directorships are likely to create bi-directional information flow between firms (Adler and Kwon 2002; Moran 2005), while Keister (1998) argues that interlocked directorates result in affiliated firms having stronger performance because of improved information and coordination between organizational entities. According to the Resource Dependence theory, interlocks are used as a cooperation strategy (Mizruchi 1996). Yet, Hillman et al. (2009) indicate that information flows in a single direction, benefiting the dominant (apex) firm. Haunschild and Beckman (1998) state that interlocked directorates are seen as tools for securing information or control within or between organizations, and interlocked directors are a credible and low-cost channel for information transfers between firms (Haunschild 1993). Ultimately, both accesses to information and networking ties among members affect corporate behaviour. So, it can be argued that application for PEPs and its subsequent approval indicate firms' abilities to find suitable investors due to board networks. Similarly, politically connected directors are likely to facilitate access to, and disseminate information between, issuing firms and regulator/investors in the PEP market.

We can argue that interlock directorship could have the potential to investor pools and those firms have a greater chance for applying PEPs and becoming successful. Where firms' board members have interlocked directorships, they more frequently accept equity offers in the event of a business acquisition (Renneboog and Zhao 2011; 2014). In a similar line, we can argue that political connected directors could help to overcome regulation hurdles and those firms have a greater chance for applying PEPs with subsequent approval guarantee. Based on the views outlined above, we propose the following two hypotheses:

***H<sub>1</sub>:** Firms with politically connected and interlocked directorates have a higher propensity to apply for PEP than firms without such ties.*



*H<sub>2</sub>: Firms with politically connected and interlocked directorates have a higher chance of getting PEP approval than firms without such ties.*

### **3.2. Boardroom network ties, information cost of PEPs and proceeds from PEPs**

Information asymmetry, monitoring effects and agency cost are key determinants in the decision to issue security via a private placement (Chemmanur and Fulghieri, 1999; Fulghieri and Lukin, 2001; Gomes and Phillips, 2012). Chung and Hwang (2010) indicate that the value of information and information acquisition costs have a greater impact on the level of the discount of private offerings. Thus, the size of the discount reflects the "information price" and "cost of the placement" to the PEP issuing firms (Chung and Hwang, 2010).

In China, considerable proportions of PEP buyers are affiliated or controlled by SOEs. Fonseca et al. (2014) find that state-owned institutional buyers are actively engaged in the PEP market in China, which create a negative market reaction due to their inefficient monitoring ability and agency problem. Claessens and Fan (2002) point out that the controlling shareholder (state-ownership in China) bears some of the agency costs in the form of share price discounts and expenditures on monitoring, bonding and reputation building. However, Fisman (2001) refers that political connection is valued by investors and shows a positive market reaction. Resource Dependency theory stipulates that firms should mitigate negative effects of political dependence by creating ties to the political system, for instance, by having ex-politicians serving on their board (Hillman et al. 2009). Hence, political connection provides some reassuring effects and investors have more confidence in the deal. Moreover, political connections are likely to obtain more information from their connection and pass such information to the potential buyers. This may help to reduce information asymmetry between parties involved in PEP deals. Firms with political connections enjoy advantages over firms that do not have political connections, such as time saving in the negotiation process (Cai and Sevilir 2010) and creating more trust between the parties involved in the PEP issuing process (Martynova and Renneboog

2009). With political connections, firms can also circumvent the CSRC regulation in setting a lower PEP issuing price which would benefit the PEP buyers result in a greater discount. This would also lead to the positive relationship between political connection and cost of PEPs as predicted by H2.

In China, considerable proportions of PEP buyers are interlocked firms. Interlocking directors who simultaneously sit on the boards of PEP issuance firms and buying firms during the PEP process are privy to important information about both. This access to information, along with the possibility of direct communication with decision makers (board members), makes interlocking directors a distinct channel of information transmission between parties involved in PEPs and reduces the negotiation cost. Following the concept of Resource Dependency Theory, the primary job of interlocking remains exchange of information and expertise between firms to reduce market uncertainties (Zang 1999). Cai and Sevilir (2010) demonstrate that interlocked directors who significantly reduce informational asymmetries also reduce the time spent in the negotiation process. This leads to an informational advantage between the parties involved which may convey trust between the parties (Martynova and Renneboog 2009), as connected firms more frequently accept equity offers in the context of mergers and acquisitions (M&A) (Renneboog and Zhao 2011; 2014). Wu (2011) points out that interlocked directorates can reduce the cost of information gathering for both parties and can help alleviate information asymmetry problems. Cukurova (2012) finds that interlocked firms are more likely to be selected as targets, particularly when there is greater information asymmetry, suggesting that interlocked directors mitigate inefficiencies that arise from information asymmetries.

From an information asymmetry point of view, politically connected and/or interlocked directors reduce information asymmetry between PEP issuing firms and investors. Hence, both politically connected and interlocked directors help reduce the "information price" and "cost of the placement" associated with PEP. In contrast, politically connected and/or interlocked directors

are likely to reduce the monitoring effects of corporate boards, thereby increasing "information price" and "cost of the placement" in PEP. With the competing views in the literature, in line with information asymmetry argument, we propose the following two hypotheses:

*H<sub>3</sub>: Firms with politically connected and interlocked directors have a lower cost of PEP than firms without such ties.*

*H<sub>4</sub>: Firms with politically connected and interlocked directors have strong positive influence on proceeds from PEPs than the firms without such members on their board.*

#### **4. Data and Methodology**

We have collected PEP data from the CSRC's monthly bulletin for the period 2006 to 2010. We have chosen 2006 as a starting year of the CSRC regulating PEP. Financial data for the sample period are collected from the China Stock Market and Accounting Research's (CSMAR) database. Our initial sample includes 518 firms that applied for the PEP and 428 firms that completed the PEP process. There are 89 rejections and withdrawals of PEP applications. Some firms with incomplete data, those in the financial industry, and companies listed overseas and dual-listed in Hong Kong are excluded from the sample. Therefore, our final sample stands at 290 firms.

The average board tenure for directors in China is three years. However, due to ongoing institutional transitions the overall interlock network pattern among all listed firms is changing much faster in China than the average for firms in other countries (Ren et al., 2009). We therefore collected director data on an annual basis and used two separate procedures to identify interlocking directors at the PEP application and completion stages. At the time of application, there is no share allotment and firms need to get approval from the CSRC. Hence, a board interlock is identified at the PEP application stage if a director has been employed by one or more firms other than the PEP applying firm. However, at the completion stage, a board interlock is

identified if a director has been employed by both the issuing and buying firm sat least one year prior to the PEP announcement and is still employed by both the issuing and buying firms at the completion of the PEP. To measure interlocking directorates we use a dummy variable which takes a value of 1 if both firms share at least one common director. In addition, we use the proportion of interlocked directors to the total number of directors of PEP issuing firms as a continuous variable.

We measure the political connections of board members as being the chairman, vice-chairman, party secretary or vice-secretary of the Communist Party at national, provincial or municipal level, membership with the People's Congress or the People's Political Consultative Conference (Fan et al., 2008). We use two separate procedures to identify politically connected directors at the PEP application and completion stages. At the application stage, the political connections of firms that applied for PEP are captured by the number of board members who have political affiliations with the Communist Party. However, at the application stage of PEP, we also considered the buying firm's ownership type when capturing the political connections of firms that successfully completed PEP. If one or more board members of a PEP issuing firm has a political affiliation with the Communist Party and the PEP is offered solely to investors other than state and provincial government owned institutions and companies, then the firm is scored as a 0 and 1 otherwise.

Based on prior studies and theory, we have selected several control variables. First, we include firm level characteristics such as firm size, firm age and type of ownership (Hertzel and Smith 1993; Lu et al. 2011; Fonseca et al. 2014) as control variables affecting PEP decision, approval by CSRC, cost and proceeds from PEPs.<sup>3</sup> Second, to control issuer's financial risk characteristics, we use financial leverage and financial distress of firms as control variables (Hertzel and Smith 1993; Lu et al. 2011, Fonseca et al. 2014) affecting PEP decision, approval by

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<sup>3</sup> Information asymmetry a major determinant of the discount offered (Hertzel and Smith, 1993; Wu, 2004; Erhemjants and Raman, 2012). As information asymmetry is expected to be lower for larger (Bhushan, 1989; Shores, 1990) and older (Berger and Udell, 1995) firms.

CSRC, cost and proceeds from PEPs. The availability of other sources of finances such as bank loan and public equity financing affects firms' decision to apply PEPs and we control them as well. Prior studies found that private placement issuers are typically small (Wruck 1989; Hertz and Smith 1993) and have a low MB (Anderson et al. 2006).<sup>4</sup> The size of PEP is measured by fraction which also affects discount and proceeds (Hertz and Smith 1993; Lu et al. 2011; Fonseca et al. 2014).<sup>3</sup>

The PEP decision is one of the important decisions taken by the board of directors and board characteristics such as average age, education, experience, gender diversity, board size and duality could influence such decision and help the interactions with CSRC and investors. Hence, we have included them as control variables affecting PEP decision, approval by CSRC, cost and proceeds from PEPs. Fonseca et al. (2014) find that government institutional investors (INS\_INV\_GOV) are the largest single block of shareholders in many firms and new shares of PEPs to them do not add to efficient monitoring or improving governance. On the other hand, they find that new shares of PEPs to private institutional investors (INS\_INV\_PVT) are the largest single block of shareholders who contribute to efficient monitoring and improving the governance. Hence, we have included INS\_INV\_GOV and INS\_INV\_PVT institutional investor buyer categories as control variables because they affect cost of PEPs and proceeds from PEPs. According to agency theory, the PEPs issue shares to outside blockholders who enhance the firm's external monitoring mechanism thereby reducing the agency problem and increasing firm value (Shleifer and Vishny 1986; Wruck 1989) and it helps reducing the agency problem for firms having poor governance mechanisms (Huang and Chen, 2013). The outside blockholders may affect discount of PEPs and proceeds from PEPs. Hence, we control the participation of outside blockholders by using proportion of shares issued to outside blockholders (OUT.BHOLD) in the PEP.

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<sup>4</sup> Information asymmetry is more severe for firms whose value consists mostly of growth potential (Hertz and Smith, 1993; Erhemjants and Raman, 2012). Fraction Placed and BM (the book-to market ratio of equity).

The following equation (1) is used for multiple logistic regression to test whether firms with political connections (PC) and interlocked directorates (INTD) demonstrate higher application rates for PEP.

$$APP_{i,t} = \alpha + \sum_{j=1}^{13} \beta_{j,(t-1)} FC_{j,i,t} + \beta_{14,(t-1)} INTD_{i,t} + \beta_{15,(t-1)} PC_{i,t} + \varepsilon_{i,t} \quad (1)$$

Where  $APP_{i,t}$  is the dependent variable measured by a dummy variable, which takes the value of 1 for PEP applied firms and 0 otherwise.

Multiple logistic regression (2) is used to test whether firms with political connections (PC) and interlocked directorates (INTD) demonstrate higher approval rates for PEP.

$$APR_{i,t} = \alpha + \sum_{j=1}^{13} \beta_{j,(t-1)} FC_{j,i,t} + \beta_{14,(t-1)} INTD_{i,t} + \beta_{15,(t-1)} PC_{i,t} + \varepsilon_{i,t} \quad (2)$$

Where  $APR_{i,t}$  is the dependent variable measured by a dummy variable, which is 1 for firms that are approved for a PEP and 0 otherwise.

Multiple pool Ordinary Least Squares (OLS) robust regressions<sup>5</sup> with control of industry and year fixed effects (3) are used to test how PC and INTD affect information cost.

$$PEDis_{i,t} = \alpha + \sum_{j=1}^{16} \beta_{j,(t-1)} FC_{j,i,t} + \beta_{17,(t-1)} INTD_{i,t} + \beta_{18,(t-1)} PC_{i,t} + \beta_{19,(t-1)} INTD_{i,t} \times PC_{i,t} + \varepsilon_{i,t} \quad (3)$$

Where  $PED_{i,t}$  is the dependent variable measured by market discount on PEP (as a ratio), which is calculated by following prior researches (Wruck 1989; Hertz and Smith 1993; Krishnamurthy et al. 2005; Lu et al. 2011; Fonseka et al. 2014) in China and other markets.

Using proceeds from PEP, multiple pool OLS robust regressions with controls for industry and year fixed effects (4) are used to test how PCs and INTD affect access to the PE market.

$$Proceeds_{i,t} = \alpha + \sum_{j=1}^{16} \beta_{j,(t-1)} FC_{j,i,t} + \beta_{17,(t-1)} INTD_{i,t} + \beta_{18,(t-1)} PC_{i,t} + \beta_{19,(t-1)} INTD_{i,t} \times PC_{i,t} + \varepsilon_{i,t} \quad (4)$$

<sup>5</sup> The pooled OLS regression model technique (which includes dummy variables for year and firm fixed effects) is similar to the fixed effects regression model technique, and is used where there is a need to control for omitted variables that differ between cases, but are constant over time period (Wooldridge 2012). This technique has an advantage for controlling for omitted variables that may be constant over time but vary between cases, and others may be fixed between cases but vary over time (Wooldridge 2012).

Where Proceeds<sub>*i,t*</sub> is the dependent variable measured by the log value of money received from PEP.

The control variables, FC, is used to estimate the effects of firm and industry characteristics with a vector of  $\beta_{1-16}$  coefficients (year and industry dummy variables were unreported);  $\beta_{17}$  is the coefficient of INTD and a dummy variable estimates the effects of PC with the  $\beta_{18}$  coefficient. We also use an interaction effect of PC \* INTD, which shows effect of both political connected and interlocked directors of firms on PEPs. A summary of the definitions of the variables and data sources are reported in Table S1 (See the Supplementary Material, available online).

## 5. Results and discussion

### 5.1 Results of descriptive analyses

Figure S1 (See the Supplementary Material, available online) shows the number and value of PEP classified by year, indicating that the PEPs are relatively evenly distributed across the years and the use of PEP over the period also shows an increasing trend. Figure S2 (See the Supplementary Material, available online) shows the number and value of PEPs classified by CSRC industry category from 2006-2010.

Table S2 (See the Supplementary Material, available online) presents descriptive statistics of board and firm characteristics for the PEP issuing firms. We classify the descriptive statistics of PEP following two critical points: PEP application and PEP completion stages. We compare the descriptive statistics for each stage with and without firms that have successfully applied and completed PEP. Table S2, Section A, shows the corporate board characteristics of firms at the time of applying for PEP. It reveals that relatively younger and larger firms usually apply for PEP and their financial distress is slightly higher than firms that do not apply PEP while their financial leverage is almost similar to their counterparts. Firms that have applied for PEP have a higher

profitability and a slightly lower percentage of state-ownership than firms that have not applied for PEP. At the time of the PEP application, board interlocking directorate is captured by the number of directors who served on his or her own company's board and on at least one other company's board. On average, there are 6 interlocked directors serving on the boards of firms that do not apply for PEP, with the number of interlocked directors ranging from 0 to 14. In contrast, on average 7 interlocked directors are serving on the boards of firms that have applied for PEP, with the numbers ranging from 1 to 14. As for political connectedness, on average only one director has a political connection in both types of firms with the number of directors with political connections ranging from 0 to 10. Among firms that applied for PEP, the average education and experience of board members are slightly higher as compared to their counterparts.

Table S2, Section B shows the corporate boards characteristics of firms at the time of successful PEP completion. Although the average age of firms that completed PEP successfully is higher, relatively smaller firms are tended to complete PEP successfully and their financial leverage is significantly lower than firms that applied for PEP. Successfully completed PEP firms have higher profitability lower percentage of state-ownership and their board members have significantly higher education and more experience than firms that have applied for PEP. Regarding interlocking directorship of these successful firms, on average, 5 interlocked directors serve on the boards of firms, with the number of interlocked directors ranging from 1 to 14. The political connectedness of firms that successfully completed PEPs have one director with the number of politically connected directors on the board ranging from 0 to 8.

Table S3 (See the Supplementary Material, available online) shows Pearson's correlation matrices which suggest that there is no serious multicollinearity issues with the data.

## **5.2 Results of board-room network ties, and propensity to apply for PEPs and approval of PEPs**

Tables 1 and 2 present the results of multiple logistic regressions for the effects of the boardroom network ties on firms' propensity to apply for PEPs and firms' approval of PEPs, respectively.



We consider interlocked directors and board members' political links as our test variables to measure boardroom network ties. The results reported in Table 1 indicate that the existence of interlocked directorates significantly and positively influence the PEP decision after controlling availability of other type of capital such as bank loan and seasoned equity offerings (SEO) and it has increased the propensity to apply for PEP by 0.34 times. On the other hand, directors' political ties result in a positive but statistically insignificant coefficient, suggesting that political connection cannot influence the PEP application decision. Hence, the results only partially support *H1*, which indicates that the shared directorate enhances the propensity to apply for PEP. This finding supports the argument that interlocked directors function as managerial ties that can facilitate information exchange (Adler and Kwon 2002; Hillman et al. 2009; Moran 2005) and coordination (Keister, 1998; Mizuchi, 1996), and are considered to be beneficial resources for an affiliated firm.

In regards to control variables, Table 1 demonstrates that firm size, financial leverage, financial distress and profitability significantly, positively influence firms' decisions to apply for PEP. Interestingly, the age of the firm significantly but negatively affects the firm's propensity to apply for PEP suggesting that mature firms may prefer other types of equity financing than PEP that are not highly regulated in China. The average age of board members is the only board level control variable that has a significant negative influence on the PEP application decision.

However, we cannot come to a solid conclusion about the effects of boardroom connectedness on information asymmetry or monitoring efficiency by looking only at their influence at the application stage. Therefore, we look at the impact of these ties on the approval of PEP in China, as shown in Table 2.

The results reported in Table 2 reveal opposite findings from Table 1 we reported for political ties and networked directors. It shows that at the approval stage directors' political ties have positive significant impact on the PEP approval. On the other hand, interlocked directorates

have negative significant effect on the PEP approval. These findings suggest that political connected directors are very effective for the PEP approval while interlocked directorates are destructive. Thus, the results only partially support *H2*, which indicates that the politically linked directors enhance the approval for PEP.

For control variables, Table 2 exhibits similar findings as found in Table 1 for firm size, financial distress and profitability showing significant positively influence on firms' approval for PEP. Unlike Table 1, the age of the firm has significant positive effects on firm's approval for PEP. Ownership also has positive significant relationship, indicating that state ownership control is influential in getting such PEP approval. Again, the average board size is the only board level control variable that has a significant positive influence on the PEP approval.

Since the findings of Tables 1 and 2 are in opposite directions, we again cannot make concrete decisions on the effects of boardroom network ties on information asymmetry or monitoring efficiency by looking at their influence at the application and approval stages. Therefore, we now proceed to find the impact of these ties on the successful completion of PEP in China, as illustrated in Tables 3 and 4.

### **5.3. Results of boardroom network ties, cost of PEPs and proceeds from PEPs**

Tables 3 and 4 report the results of OLS regressions for the effects of political ties and interlocked directors (as the proxy for the boardroom network ties) on firms' discounts on PEP (as the proxy for cost of PEP) and PEP proceeds (as the proxy for access to the PEP market), respectively. For the relationship between the boardroom network ties and firms' discounts on PEP in Table 3, the interlocked director dummy variable exhibits a negative coefficient significant at a 5% level, suggesting the presence of an interlocked director reduces the information cost of PEP by 0.04%. We use the proportion of interlocked directors as a robustness test and the results remain unchanged. This finding supports *H3*, indicating that interlocked directors facilitate information exchange (Adler and Kwon 2002; Hillman et al. 2009; Moran 2005), which in turn reduces

information cost. However, our findings do not support that the presence of interlocked directors reduces the monitoring role of the board or enhances the agency problem. On the other hand, the coefficient of politically connected directors dummy variable linked with government institutional buying is positive and significant at the 10% level, showing the presence of politically connected directors increases the information cost of PEP by 0.01%. We use the proportion of politically connected directors to check robustness and the estimation shows similar results at a 5% level. The finding of this estimation implies that the presence of politically connected directors leads to a reduction in the intensity of board monitoring, and thereby aggravating the agency problems while increasing information cost.

We also examine the interaction effect of both interlock and political ties on the cost of PEP. We find that firms with both interlock and political ties lead to a reduction in the cost of PEPs. Interaction effect shows that the present of both interlock and political ties in a firm reduces the cost of PEP by 0.007%. Moreover, the interaction effect of a 1% point increase in the proportion of interlock and political directors in a firm reduces the cost of PEP by 0.002%. For the robustness test, we also use the interaction variable of the present of interlock and proportion of political directors and, the interaction variable of the proportion of interlock and present of political directors, which gives qualitatively similar results. These results reveal that a firm with political ties threatens the benefits of interlocking directors.

As for control variables shown in Table 3, the coefficients of firm size are negative and significant at the 10% level. According to information asymmetry considerations, the discounts reflect the information cost of PEP (Hertzel and Smith 1993; Chung and Hwang 2010; Fonseca et al. 2014) and it is lower for large firms in China than smaller firms. The coefficients of both leverage and financial distress are significantly positive, indicating that investors are compensated by the larger discounts. The coefficient of firm growth is positive and significant at a 5% level. Firm profitability negatively affects the discount, indicating that profitable firms offer PEP at a

higher price than less profitable firms. The possible explanation for this outcome is that stock price run-ups before private placements causes a negative effect on the placement discount. The coefficient of 'Fraction', measured by the proportion of shares offered relative to the total shares outstanding after the PEP, has a significantly positive value at a 1% level indicating that when the fraction is higher, the information cost increases, which in turn shows a positive relationship between the discounts and the fraction of PEP.

We use board members' average age, education, experiences and gender diversity as human characteristics or skill factors that may be relevant to the success of PEP. As shown in Table 3, the coefficients of average education and gender diversity of board members negatively affect the discounts on PEP. The education levels of board members helps to reduce the information cost of PEP and the presence of a female director reduces the information cost of PEP by 0.03%.

In Table 4, we extend our analysis to reveal the relationship between the boardroom's network ties and access to the PEP market, measured by the size of PEP proceeds calculated as the natural log value of PEP proceeds in Chinese Yuan billion. The coefficient of interlocked director dummy variable is positive and significant at the 5% level and the presence of an interlocked director increases access to the PE market by 0.15%. Similarly, the proportion of interlocked directors shows consistent finding at the 1% level, supporting that an increase of interlocked directors on boards results in increasing proceeds from PEP. This result supports the view that multiple directorships can reduce information asymmetry and connected firms achieve better coordination of resources, which in turn reduces their information cost. Hence, hypothesis (H4) is supported. This finding also supports Keister (1998) and Mizruchi (1996) who stress that interlocked directors benefit firms by reducing their information cost. However, our finding does not support that having interlocked directors reduces the board's monitoring role or aggravates agency conflicts. On the other hand, the coefficient of politically connected director dummy

variable linked with government institutional buying has a negative and significant value at a 5% level, suggesting that the presence of a politically connected director decreases access to the PE market by 0.08%. When we use the proportion of politically connected directors, we find similar results. This confirms that the reduced monitoring role of politically connected directors and increased agency issues are likely to decrease the proceeds from PEP.

We also investigate the interaction effect of both interlock and political ties on proceeds from PEPs. We document that firms with both interlock and political ties lead to increase the proceeds from PEPs. Interaction effect shows that the presence of both interlock and political ties in a firm increases the proceeds from PEP by 0.01%. Moreover, the interaction effect of a 1% point increase in the proportion of interlock and political directors in a firm increases the cost of PEP by 0.05%. For the robustness test, we also use the interaction variable of the present of interlock and proportion of political directors and, the interaction variable of the proportion of interlock and present of political directors, which gives qualitatively similar results. These results further support that firms' political ties diminish the benefits of interlocking directors.

Regarding control variables shown in Table 4, the coefficients of firm size, financial distress, firm profitability and friction are positive and significantly related to the proceeds from PEP. As for human characteristics or skill factors of board members, the average experience of board members and gender diversity have positive effects on the proceeds from PEP.

#### **5.4 Robustness checks – endogeneity**

##### 5.4.1. Instrumental variables 2SLS regression analysis

It is possible that our baseline regression results reported in Tables 6–7 could be impacted by endogeneity (e.g. simultaneity and/or reverse causality) resulting in biased regression coefficient estimates.<sup>6</sup> Hence, as part of our robustness checks, we perform instrumental variables 2SLS regression analysis (e.g. Larcker and Rusticus 2010; Wooldridge 2010). In the first stage

<sup>6</sup> We suspect that there are unobservable variables that also affect PEP variables (Discount on PEP and Proceeds from PEP). PC and INTD variables may suffer from omitted variable biased. Hence, the Hausman Test for endogeneity can help us determine whether or not there is some of omitted variable biased in this regression. The Hausman test confirms that the only INTD leads to endogeneity and detailed results are available from the authors upon request.

regression model, we compute instrumental variables (IV) for PR\_INTD using the average value for the PR\_INTD at the industry level (INTD\_IND). Our IV is therefore consistent with the approaches of Liu et al. (2014) who use average female directors at the industry segment level (i.e. proportion of female directors in the firm's 1-digit CSRC coded industry classification) as an IV, Xu et al. (2015) who employ the industry average CSR score as an IV for their CSR index, and Xu et al. (2015) employ an instrumental variable approach, using industry-average governance quality of PEP firms as the instrument.

The results of the 2SLS regression for interlock and political ties of boardroom and cost of PEPs are shown in Table S4 (See the Supplementary Material, available online). In the first stage regression models (i.e. Models 1A and 2A), we find that our IV denoted by INTD\_IND<sup>7</sup> is significantly positively associated with EID ( $p < 0.01$ ), as expected. We also observe that several of the control variables (SIZE, MB, ROA, Friction, B\_SIZE, B\_EDU) are significantly associated with PR\_INTD ( $p < 0.10$  or better) in the regression model specifications.

In the second stage regression models (i.e. Models 1B and 2B), we find that the PR\_INTD regression coefficient is negatively and significantly associated with firms' discount on PEP ( $p < 0.05$ ) providing support for H3. Further, we find that the PR\_PC regression coefficient is also negatively and significantly associated with firms' discount on PEP ( $p < 0.01$ ) providing more support for H3. We also observe that the interaction term regression coefficients for PR\_PC \* PR\_INTD is significantly positively associated with the discount on PEP ( $p < 0.05$ ), thus H3 is again supported by the empirical results. Finally, for the control variables we find that SIZE, LEV, Fin.Dis., MB, ROA, Friction, INS.INV\_GOV, B\_AGE, B\_EDU and GENDER\_Dum are also significantly associated with EID ( $p < 0.10$  or better) in the regression model specifications.

The results of the 2SLS regression for interlock and political ties of boardroom and Proceeds from PEPs are shown in Table S5 (See the Supplementary Material, available online). In

<sup>7</sup> Stock and Yogo (2005) suggest an F-statistic in the first stage regression model of greater than ten indicates that 10 an IV is not weak. Our F-statistic of 53.69 and 57.33 for INTD\_IND therefore shows that it represents a suitable IV.

the first stage regression models (i.e. Models 1A and 2A), we find that our IV denoted by INTD\_IND<sup>8</sup> is significantly positively associated with EID ( $p < 0.01$ ), as expected. We also observe that several of the control variables (SIZE, MB, ROA, Friction, B\_SIZE, B\_EDU) are significantly associated with PR\_INTD ( $p < 0.10$  or better) in the regression model specifications.

In the second stage regression models (i.e. Models 1B and 2B), we find that the PR\_INTD regression coefficient is positively and significantly associated with firms' proceeds from PEP ( $p < 0.05$ ) providing support for H4. Further, we find that the PR\_PC regression coefficient is also negatively and significantly associated with firms' proceeds from PEP ( $p < 0.01$ ) providing more support for H4. We also observe that the interaction term regression coefficients for PR\_PC \* PR\_INTD is significantly positively associated with the proceeds from PEP ( $p < 0.05$ ), thus H3 is again supported by the empirical results. Finally, for the control variables we find that SIZE, ROA, Friction, B\_EXP and GENDER\_Dum are also significantly associated with EID ( $p < 0.10$  or better) in the regression model specifications.

## 6. Conclusions

Private equity issue to a relatively small group of investors may be motivated by relationships prior to the placement or the firm may want to create a new relationship as part of the placement process. Furthermore, boards of directors may have an incentive, based on their personal relationships, to release inside information about the issuing firm. This study sought to document the phenomenon of politically connected and interlocked directorates and their influence on selecting private equity as a source of funds in a relationship-based and highly regulated market setting - China.

We first investigate the effect of boardroom networking on the propensity to apply for PEP and the empirical results suggest that interlocked directors positively influence the decision to apply for PEP in China. However, there is no evidence that political ties with buying firms

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<sup>8</sup> Stock and Yogo (2005) suggest an F-statistic in the first stage regression model of greater than ten indicates that 10 an IV is not weak. Our F-statistic of 53.69 and 57.33 for INTD\_IND therefore shows that it represents a suitable IV.

significantly influence the decision to apply for PEP. We secondly examine the effect of boardroom networking on approval of PEP, which signify that while politically connected directors positively influence the approval of PEP, interlocked directors' influence negatively the approval of PEP. We thirdly investigate the effect of network ties on monitoring effects, information asymmetry and the information cost of PEP, and our results reveal that shared directorates negatively affect discounts on PEP. This finding supports that interlocked directorates reduce information asymmetry and help to reduce the information cost of PEP. Further, we find that directors who are politically connected with PEP buyers positively affects the discount on PEP, supporting the argument that the political ties of board members increases information asymmetry, reduces the monitoring efficiency and could enhance agency conflicts. As a result, the political links of board members with the buyers of these equity issues increase the information cost of PEP. Finally, in analysing the impact of these connections on PEP proceeds, we find that interlocked directors have a positive impact on the proceeds of PEP, as they can reduce information asymmetry and help firms gain better access to the PEP market in China. Further, the outcome of our research suggests that politically connected directors who maintain ties with PEP buyers can negatively and significantly influence the proceeds of PEP. It appears that directors' political connections may reduce their monitoring role. The result reveals that firms' political ties oppose the benefits of interlocking directors. The overall results thus show that politically connected directors and interlocked directors may bring different benefits to firms; however the presence of interlocking directors in the boardroom significantly influences the choice of private equity decision as a source of finance in Chinese firms.



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Table 1: Logistic regression results of interlock and political ties of boardroom and firm propensity to apply for PEPs

Variable	Model 1		Model 2		Model 3		Model 4		Model 5		Model 6	
Firm Age	-		0.473**		-		-		-		-	
	0.464**	(0.204)	*	(0.203)	0.462**	(0.205)	0.464**	(0.204)	0.462**	(0.205)	0.472**	(0.203)
Firm Size	0.249**		0.245**		0.249**		0.249**		0.248**		0.245**	
	*	(0.056)	*	(0.056)	*	(0.056)	*	(0.056)	*	(0.056)	*	(0.056)
OWN	-0.197	(0.138)	-0.153	(0.140)	-0.200	(0.138)	-0.202	(0.138)	-0.169	(0.138)	-0.156	(0.139)
LEV	1.375**		1.383**		1.377**		1.378**		1.379**		1.385**	
	*	(0.308)	*	(0.310)	*	(0.308)	*	(0.309)	*	(0.309)	*	(0.311)
Fin. Dis.	0.285**		0.281**		0.286**		0.286**		0.286**		0.282**	
	*	(0.088)	*	(0.089)	*	(0.088)	*	(0.088)	*	(0.088)	*	(0.089)
MB		(12.15		(12.24		(12.16		(12.14		(12.15		(12.23
	13.742	5)	12.875	2)	13.636	4)	13.672	6)	13.670	2)	12.827	4)
ROA	3.391**		3.398**		3.389**		3.392**		3.389**		3.398**	
	*	(0.816)	*	(0.819)	*	(0.816)	*	(0.815)	*	(0.816)	*	(0.819)
SEO	0.001	(0.000)	0.001	(0.000)	0.001	(0.000)	0.001	(0.000)	0.001	(0.000)	0.001	(0.000)
Bank-loan	0.614	(0.377)	0.618	(0.382)	0.615	(0.379)	0.617	(0.381)	0.615	(0.379)	0.615	(0.379)
B_SIZE	0.220	(0.269)	0.234	(0.270)	0.214	(0.270)	0.218	(0.268)	0.214	(0.270)	0.233	(0.270)
B_AGE	-											
	1.577**											
	*	(0.807)	-1.447*	-0.813	-1.568*	(0.809)	-1.554*	(0.808)	-1.568*	(0.809)	-1.429*	(0.815)
B_EDU	-0.237	(0.199)	-0.236	(0.199)	-0.242	(0.200)	-0.244	(0.201)	-0.242	(0.200)	-0.240	(0.202)
B_EXP	0.208	(0.137)	0.202	(0.137)	0.206	(0.137)	0.204	(0.138)	0.206	(0.137)	0.198	(0.138)
Duality	0.062	(0.174)	0.045	(0.174)	0.063	(0.174)	0.061	(0.173)	0.063	(0.174)	0.044	(0.174)
GENDER- Dum	0.037	(0.121)	0.0249	(0.122)	0.038	(0.121)	0.036	(0.121)	0.038	(0.121)	0.024	(0.122)
PR_INTD			0.339**	(0.176)					0.338**	(0.174)	0.337*	(0.175)
PC_Dum					0.031	(0.123)			0.030	(0.122)		
PR_PC							0.083	(0.263)			0.064	(0.261)
Const	-2.571	(5.282)	-2.634	(5.276)	-1.967	(5.187)	-1.878	(5.362)	-2.698	(4.973)	-2.536	(4.891)
Industry & Year effects	YES		YES		YES		YES		YES		YES	
N	5525		5525		5525		5525		5525		5525	
Wald chi <sup>2</sup>	173.01		176.13		172.83		173.02		172.92		176.44	
Pseudo R <sup>2</sup>	0.064		0.0653		0.0639		0.0639		0.0639		0.0653	
Log pseudo likelihood	-		-		-		-		-		-	
	1164.86		1163.11		1164.83		1164.81		1164.82		1163.08	

Note: Dependent variable is  $APP_{i,t}$ , measured by a dummy variable, which is 1 for firm that applies for a PEP and 0 otherwise. Firm Age is the natural log of operating year of each firm at the beginning of the year. Firm Size is the natural log of the total assets prior to the private placement. OWN is ownership and a dummy variable, 1 if the controlling shareholder is the State and 0 otherwise (before PEP). LEV is financial leverage and it is the ratio of interest bearing liability to equity in each firm at the beginning of the year. Fin. Dis. is financial distress and it is calculated by Altman Z-Score. MB is Market to book value ratio at the beginning of the year. ROA is Return on Assets at the beginning of the year. B-SIZE is the natural log value of number of Board Members on the board at the beginning of the year. B\_AGE is the natural log value of average age of board members at the beginning of the year. B\_EDU is the natural log value of average education of board members at the beginning of the year. B\_EXP is the natural log value of average experience of board members at the beginning of the year. Duality is measured by dummy variable, 1 for if CEO and Chairman are same person and otherwise 0. GEND-Dum is a dummy variable if firm has one or more female director prior to the private placement. PR\_INTD is proportion of interlocked directors to total number of directors. PC-Dum is dummy variable if firm has one or more politically connected director. PR\_PC is proportion of politically connected directors to total number of directors. Robust standard errors clustered by both firm and time (year) are in parentheses. \* Indicates significance at 10%. \*\* Indicates significance at 5%. \*\*\* Indicates significance at 1%.

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Table 2: Logistic regression results of interlock and political ties of boardroom and firms' approval of PEPs

Variable	Model 1		Model 2		Model 3		Model 4		Model 5		Model 6	
Firm Age	0.337**	(0.061)	0.325**	(0.064)	0.472**	(0.051)	0.425**	(0.065)	0.476**	(0.048)	0.486**	(0.043)
Firm Size	0.045**	(0.019)	0.046**	(0.019)	0.063**	(0.035)	0.064**	(0.035)	0.064**	(0.035)	0.065**	(0.038)
OWN	0.303**	(0.014)	0.314**	(0.020)	0.241**	(0.007)	0.246**	(0.010)	0.242**	(0.007)	0.237**	(0.007)
LEV	0.475	(1.085)	0.475	(1.086)	0.661	(1.067)	2.507	(2.324)	0.662	(1.066)	2.448	(2.371)
Fin. Dis.	0.173**	(0.035)	0.171**	(0.035)	0.191**	(0.037)	0.195**	(0.038)	0.190**	(0.037)	0.189**	(0.037)
MB	4.358	(4.799)	4.160	(4.926)	4.818	(4.918)	5.138	(5.507)	4.820	(4.934)	5.161	(5.647)
ROA	3.518**	(2.068)	3.584***	(2.081)	3.871**	(2.048)	3.877**	(2.095)	3.874**	(2.026)	3.682**	(1.901)
B_SIZE	0.102**	(0.019)	0.103**	(0.019)	0.044*	(0.027)	0.041*	(0.025)	0.045*	(0.027)	0.045*	(0.027)
B_AGE	3.522	(2.094)	3.507	(2.098)	3.338	(2.074)	5.456	(5.136)	4.581	(4.768)	5.421	(5.165)
B_EDU	0.556	(0.475)	0.555	(0.475)	0.507	(0.472)	0.636	(0.798)	0.607	(0.762)	0.704	(0.895)
B_EXP	-0.026	(0.056)	-0.026	(0.056)	-0.084	(0.324)	0.293	(0.704)	0.014	(0.127)	0.273	(0.696)
Duality	-0.121	(0.409)	-0.117	(0.408)	-0.177	(0.418)	0.463	(0.879)	0.072	(0.218)	0.451	(0.876)
GENDER- Dum	0.072	(0.288)	0.072	(0.288)	0.097	(0.287)	0.835	(0.672)	0.197	(0.372)	0.829	(0.672)
PR_INTD			-0.127***	(0.029)					-0.321**	(0.143)	-0.316**	(0.141)
PC_Dum					0.637**	(0.288)			0.582**	(0.217)		
PR_PC							1.310**	(0.342)			1.312**	(0.343)
Const.	-6.575	(8.396)	-6.625	(8.388)	-5.986	(8.246)	-1.848	(2.550)	-3.682	(3.153)	-3.380	(2.763)
Industry & Year effects	YES		YES		YES		YES		YES		YES	
N	372		372		372		372		372		372	
Pseudo R <sup>2</sup>	0.102		0.102		0.114		0.214		0.201		0.214	

Log pseudo	-		-		-		-		-		
likelihood	189.021		-189.005		186.403		161.619		174.321		161.593
Wald chi <sup>2</sup>	45.53		45.62		48.81		62.95		52.64		61.34

Note: Dependent variable is  $APR_{it}$ , which is measured by a dummy variable, which is 1 for a that approved for a PEP and 0 otherwise. Firm Age is the natural log of operating year of each firm at the beginning of the year. Firm Size is the natural log of the total assets prior to the private placement. OWN is ownership and a dummy variable, 1 if the controlling shareholder is the State and 0 otherwise (before PEP). LEV is financial leverage and it is the ratio of interest bearing liability to equity in each firm at the beginning of the year. Fin. Dis. is financial distress and it is calculated by Altman Z-Score. MB is Market to book value ratio at the beginning of the year. ROA is Return on Assets at the beginning of the year. B-SIZE is the natural log value of number of Board Members on the board at the beginning of the year. B\_AGE is the natural log value of average age of board members at the beginning of the year. B\_EDU is the natural log value of average education of board members at the beginning of the year B-EXP is the natural log value of average experience of board members at the beginning of the year. Duality is measured by dummy variable, 1 for if CEO and Chairman are same person and otherwise 0. GEND-Dum is a dummy variable if firm has one or more female director prior to the private placement. INTD-Dum is dummy variable if firm has one or more interlocked director. PR\_INTD is proportion of interlocked directors to total number of directors. PC-Dum is dummy variable if firm has one or more politically connected director. PR\_PC is proportion of politically connected directors to total number of directors. Robust standard errors clustered by both firm and time (year) are in parentheses. \* Indicates significance at 10%. \*\* Indicates significance at 5%. \*\*\*Indicates significance at 1%.

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Table 3: OLS Regression results of interlock and political ties of boardroom and cost of PEPs

Variable	Model1		Model2		Model3		Model 4		Model 5		Model 6		Model 7		Model 8		Model 9	
Firm Age	0.03 1	(0.0 45)	0.03 2	(0.0 45)	0.03 3	(0.0 45)	0.03 2	(0.0 45)	0.03 3	(0.0 46)	0.03 3	(0.0 46)	0.03 3	(0.0 46)	0.03 3	(0.0 46)	0.03 3	(0.0 46)
Firm Size	- 0.02 1*	(0.0 12)	- 0.02 0*	(0.0 12)	- 0.02 1*	(0.0 12)	- 0.02 2*	(0.0 12)	- 0.02 2*	(0.0 12)	- 0.02 0*	(0.0 12)	- 0.02 0*	(0.0 12)	- 0.02 2*	(0.0 12)	- 0.02 2*	(0.0 12)
OWN	- 0.00 8	(0.0 34)	- 0.00 9	(0.0 34)	- 0.00 8	(0.0 34)	- 0.00 7	(0.0 34)	- 0.00 7	(0.0 34)	- 0.00 8	(0.0 34)	- 0.00 8	(0.0 34)	- 0.00 8	(0.0 34)	- 0.00 8	(0.0 34)
LEV	0.06 7**	(0.1 20)	0.08 3**	(0.1 22)	0.07 2**	(0.1 22)	0.06 7**	(0.1 22)	0.06 9**	(0.1 22)	0.08 7**	(0.1 25)	0.08 7**	(0.1 25)	0.07 2**	(0.1 24)	0.07 2**	(0.1 24)
Fin. Dis.	0.01 1***	(0.0 27)	0.01 3***	(0.0 27)	0.01 2***	(0.0 27)	0.01 1***	(0.0 27)	0.01 2***	(0.0 27)	0.01 3***	(0.0 27)	0.01 2***	(0.0 28)	0.01 3***	(0.0 27)	0.01 2***	(0.0 28)
MB	0.01 4**	(0.0 05)	0.01 36**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)	0.01 4**	(0.0 05)
ROA	- 0.88 9*	(0.5 17)	- 0.87 5*	(0.5 16)	- 0.89 2*	(0.5 17)	- 0.89 0**	(0.5 19)	- 0.88 8**	(0.5 19)	- 0.87 1*	(0.5 19)	- 0.89 3*	(0.5 19)	- 0.87 2**	(0.5 19)	- 0.89 3**	(0.5 19)
Friction	0.40 7***	(0.1 00)	0.40 7***	(0.0 99)	0.40 3***	(0.1 00)	0.40 7***	(0.1 01)	0.40 8***	(0.1 02)	0.40 9***	(0.1 01)	0.40 4***	(0.1 00)	0.40 8***	(0.1 01)	0.40 4***	(0.1 00)
INS. INV- PVT	- 0.03 7	(0.0 73)	- -0.03 73)	(0.0 73)	- 0.03 4	(0.0 75)	- 0.03 7	(0.0 73)	- 0.03 7	(0.0 73)	- 0.02 8	(0.0 72)	- 0.03 3	(0.0 75)	- 0.03 0	(0.0 73)	- 0.03 4	(0.0 75)
INS. INV- GVT	0.08 7	(0.0 66)	0.07 9	(0.0 66)	0.08 5	(0.0 68)	0.08 7	(0.0 67)	0.08 7	(0.0 67)	0.07 8	(0.0 66)	0.07 9	(0.0 66)	0.08 4	(0.0 69)	0.08 5	(0.0 69)
OUT.BHOL D	- 0.03 4	(0.0 78)	- 0.02 9	(0.0 71)	- 0.03 1	(0.0 72)	- 0.03 4	(0.0 77)	- 0.03 4	(0.0 77)	- 0.02 9	(0.0 71)	- 0.03 0	(0.0 71)	- 0.03 1	(0.0 72)	- 0.03 1	(0.0 72)
B_SIZE	- 0.05 4	(0.0 92)	- 0.04 5	(0.0 91)	- 0.05 6	(0.0 92)	- 0.05 3	(0.0 92)	- 0.05 4	(0.0 92)	- 0.04 5	(0.0 92)	- 0.04 5	(0.0 92)	- 0.05 0	(0.0 91)	- 0.05 5	(0.0 92)
B_AGE	- 0.30 4	(0.2 00)	- 0.30 2	(0.2 01)	- -0.3 4	(0.2 02)	- 0.30 4	(0.1 99)	- 0.30 5	(0.2 00)	- 0.30 2	(0.2 01)	- 0.30 2	(0.2 01)	- 0.30 1	(0.2 01)	- 0.30 1	(0.2 01)
B_EDU	- 0.03 0**	(0.0 52)	- 0.03 1**	(0.0 51)	- 0.02 9*	(0.0 51)	- 0.03 0**	(0.0 53)	- 0.02 9*	(0.0 52)	- 0.02 8*	(0.0 51)	- 0.02 8*	(0.0 51)	- 0.02 8*	(0.0 51)	- 0.02 8*	(0.0 52)
B_EXP	0.03 1	(0.0 49)	0.03 2	(0.0 49)	0.03 0.03	(0.0 49)	0.03 1	(0.0 49)	0.03 1	(0.0 49)	0.03 1	(0.0 49)	0.03 1	(0.0 49)	0.03 1	(0.0 49)	0.03 1	(0.0 49)
GENDER Dum	- 0.03	(0.0 31)	- 0.02	(0.0 32)	- 0.02	(0.0 31)	- 0.03	(0.0 31)	- 0.02	(0.0 31)	- 0.02	(0.0 32)	- 0.02	(0.0 32)	- 0.02	(0.0 31)	- 0.02	(0.0 31)

	0**	8**	9**	0**	9**	8**	8**	9**	9**							
INTD Dum		- 0.03 7**	(0.0 35)				- 0.03 8**	(0.0 36)	- 0.03 6**	(0.0 35)						
PR_INTD				0.03 2**	(0.0 11)							0.03 2**	(0.0 11)	0.03 2**	(0.0 11)	
PC_Dum						0.00 8*	(0.0 03)				0.00 9*	(0.0 03)		0.01 0*	(0.0 05)	
PR_PC								0.01 1**	(0.0 06)				0.01 4*	(0.0 07)	0.02 1**	(0.0 69)
INTD Dum x PC_Dum											0.00 7*	(0.0 08)				
INTD Dum x PR_PC													0.01 0*	(0.0 09)		
PR_INTD x PR_PC															- 0.00 2**	(0.0 00)
PR_INTD x PC_Dum													0.00 5**	(0.0 02)		
Industry & Year effects	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
N	290	290	290	290	290	290	290	290	290	290	290	290	290	290	290	290
R <sup>2</sup>	0.32 8	0.33 2	0.32 9	0.32 8	0.32 8	0.32 8	0.33 2	0.33 4	0.32 8	0.32 8						

Note: Dependent variable is discount on PEP and it is measured by the  $(\text{Closing Price on tenth day after announcement} - \text{Placement Price}) / (\text{Closing Price on tenth day after announcement})$ . Firm Age is the natural log of operating year of each firm at the beginning of the year. Firm Size is the natural log of the total assets prior to the private placement. OWN is ownership and a dummy variable, 1 if the controlling shareholder is the State and 0 otherwise (before PEP). LEV is financial leverage and it is the ratio of interest bearing liability to equity in each firm at the beginning of the year. Fin. Dis. is financial distress and it is calculated by Altman Z-Score. MB is Market to book value ratio at the beginning of the year. ROA is Return on Assets at the beginning of the year. Cumulative abnormal return for the period from 59 to 2 days prior to private placement date is used to measure stock-price run-up. Fraction is the proportion of the offered shares relative to the total shares outstanding after the PEP. INS. INV-PVT is ownership change of private institutional investors and it is measured by  $(\text{INS. ownership after PEP} - \text{INS. Ownership before PEP}) / (\text{INS. ownership before PEP})$ . INS. INV-GVT is ownership change of government institutional investors and it is measured by  $(\text{Gvt. ownership after PEP} - \text{Gvt. Ownership before PEP}) / (\text{Gvt. Ownership before PEP})$ . OUT.BHOLD is the proportion of share issued to outside blockholders and it is calculated by the 1- proportion of shares issued to blockholders. B\_SIZE is the natural log value of number of Board Members on the board at the beginning of the year. B\_AGE is the natural log value of average age of board members at the beginning of the year. B\_EDU is the natural log value of average education of board members at the beginning of the year. B-EXP is the natural log value of average experience of board members at the beginning of the year. GEND-Dum is a dummy variable if firm has one or more female director prior to the private placement. INTD-Dum is dummy variable if firm has one or more interlocked director. PR\_INTD is proportion of interlocked directors to total number of directors. PC-Dum is dummy variable if firm has one or more politically connected director. PR\_PC is proportion of politically connected directors to total number of directors. Robust standard errors clustered by both firm and time (year) are in parentheses. \*Indicates significance at 10%. \*\* Indicates significance at 5%. \*\*\*Indicates significance at 1%.



Table 4: OLS Regression results of interlock and political ties of boardroom and proceeds from PEPs

Variable	Model 1		Model 2		Model 3		Model 4		Model 5		Model 6		Model 7		Model 8		Model 9	
Firm Age	0.08 7	(0.1 57)	0.09	(0.1 56)	0.06 9	(0.1 55)	0.09 7	(0.1 57)	0.11 5	(0.1 58)	0.11 5	(0.1 57)	0.11 0	(0.1 52)	0.09 5	(0.1 56)	0.08 9	(0.1 55)
Firm Size	0.58 2***	(0.0 37)	0.58 0***	(0.0 37)	0.58 1***	(0.0 37)	0.58 2***	(0.0 37)	0.58 1***	(0.0 37)	0.57 8***	(0.0 37)	0.58 1***	(0.0 37)	0.57 9***	(0.0 37)	0.58 0***	(0.0 37)
OWN	0.08 3	(0.0 95)	0.08 8	(0.0 93)	0.08 3	(0.0 93)	0.08 7	(0.0 96)	0.09 7	(0.0 97)	0.10 1	(0.0 96)	0.09 8	(0.0 96)	0.08 9	(0.0 94)	0.08 7	(0.0 94)
LEV	0.21 1	(0.2 01)	0.26 1	(0.2 10)	0.25 6	(0.2 06)	0.18 5	(0.2 03)	0.17 5	(0.2 04)	0.22 5	(0.2 14)	0.23 0	(0.2 09)	0.22 8	(0.2 11)	0.23 1	(0.2 09)
Fin. Dis.	0.21 1**	(0.1 00)	0.20 6	(0.0 98)	0.19 9**	(0.0 99)	0.21 6**	(0.0 99)	0.21 6**	(0.0 99)	0.21 1	(0.0 98)	0.21 1	(0.0 98)	0.20 5	(0.0 98)	0.20 5	(0.0 98)
MB	0.00 6	(0.0 17)	0.00 8	(0.0 17)	0.00 6	(0.0 17)	0.00 8	(0.0 17)	0.00 7	(0.0 17)	0.00 9	(0.0 16)	0.00 9	(0.0 16)	0.00 7	(0.0 17)	0.00 7	(0.0 17)
ROA	2.32 1***	(1.4 84)	2.29 5***	(1.4 77)	2.38 2***	(1.4 71)	2.24 1***	(1.4 81)	2.34 1***	(1.4 93)	2.31 5***	(1.4 88)	2.32 1***	(1.4 85)	2.31 1***	(1.4 86)	2.30 4***	(1.4 70)
Friction	2.61 6***	(0.2 91)	2.62 0***	(0.2 90)	2.66 6***	(0.2 93)	2.62 9***	(0.2 90)	2.64 5***	(0.2 86)	2.64 5***	(0.2 86)	2.64 4***	(0.2 86)	2.67 9***	(0.2 92)	2.67 8***	(0.2 92)
INS. INV- PVT	0.11 8	(0.2 49)	0.14 7	(0.2 47)	0.16 1	(0.2 46)	0.10 4	(0.2 50)	0.10 7	(0.2 48)	0.13 4	(0.2 48)	0.14 4	(0.2 47)	0.13 6	(0.2 49)	0.14 6	(0.2 47)
INS. INV- GVT	-0.01	(0.2 37)	0.04 2	(0.2 38)	0.04 6	(0.2 35)	0.00 8	(0.2 40)	0.00 2	(0.2 38)	0.03 2	(0.2 40)	0.03 1	(0.2 40)	0.02 9	(0.2 39)	0.02 8	(0.2 39)
OUT.BHOL D	0.02 4	(0.0 63)	0.01 9	(0.0 56)	0.02 1	(0.0 58)	0.02 3	(0.0 61)	0.02 4	(0.0 62)	0.01 9	(0.0 56)	0.01 7	(0.0 52)	0.02 4	(0.0 61)	0.02 2	(0.0 56)
B_SIZE	0.22 3	(0.2 00)	0.18 7	(0.1 99)	0.24 8	(0.1 95)	0.22 9	(0.1 98)	0.21 5	(0.1 97)	0.18 3	(0.1 97)	0.25 1	(0.1 94)	0.23 0	(0.1 98)	0.25 3	(0.1 95)
B_AGE	0.86 6	(0.5 79)	0.86 5	(0.5 68)	0.81 2	(0.5 66)	0.88 8	(0.5 81)	0.86 1	(0.5 77)	0.86 1	(0.5 67)	0.83 8	(0.5 70)	0.86 2	(0.5 76)	0.83 3	(0.5 67)
B_EDU	0.01 5	(0.1 35)	0.01 6	(0.1 33)	0.00 6	(0.1 34)	0.03 4	(0.1 33)	0.05 2	(0.1 33)	0.04 9	(0.1 31)	0.05 1	(0.1 32)	0.04 8	(0.1 30)	0.01 3	(0.1 32)
B-EXP	0.03 6*	(0.1 27)	0.03 6*	(0.1 26)	0.05 8**	(0.1 28)	0.03 2*	(0.1 26)	0.03 2*	(0.1 26)	0.03 3*	(0.1 25)	0.05 1*	(0.1 26)	0.03 4**	(0.1 25)	0.05 3**	(0.1 27)
GENDER- Dum	0.07 9**	(0.0 70)	0.08 4**	(0.0 70)	0.07 9**	(0.0 70)	0.08 2**	(0.0 70)	0.07 8**	(0.0 70)	0.08 2**	(0.0 70)	0.08 1**	(0.0 71)	0.08 2**	(0.0 70)	0.08 2**	(0.0 70)
INTD Dum			0.15 1**	(0.0 84)							0.13 6**	(0.0 86)	0.14 8**	(0.0 79)				
PR_INTD					0.44 5***	(0.2 38)									0.44 8**	(0.2 40)	0.44 0**	(0.2 37)
PC Dum							0.08 5**	(0.0 72)			0.08 2**	(0.0 71)			0.08 0**	(0.0 69)		

								-						-				-	
PR_PC								0.25	(0.1					0.23	(0.1			0.22	(0.1
								4**	63)					1**	59)			***	66)
INTD Dum x PC Dum										0.01	(0.0								
										4**	08)								
INTD Dum x PR_PC														0.01	(0.0				
														0*	09)				
PR_INTD x PR_PC																		0.05	(0.0
																		4**	13)
PR_INTD x PC_Dum																0.06	(0.0		
																1**	15)		
Industry & Year effects	YES		YES		YES		YES		YES		YES		YES		YES		YES		
N	290		290		290		290		290		290		290		290		290		
R <sup>2</sup>	0.73		0.74		0.74		0.74		0.74		0.74		0.74		0.74		0.74		
	0		2		2		0		1		4		3						

Note: Dependent variable is the natural log value of Private Equity Placement proceeds in billions of Yuan (Chinese currency). Firm Age is the natural log of operating year of each firm at the beginning of the year. Firm Size is the natural log of the total assets prior to the private placement. OWN is ownership and a dummy variable, 1 if the controlling shareholder is the State and 0 otherwise (before PEP). LEV is financial leverage and it is the ratio of interest bearing liability to equity in each firm at the beginning of the year. Fin. Dis. is financial distress and it is calculated by Altman Z-Score. MB is Market to book value ratio at the beginning of the year. ROA is Return on Assets at the beginning of the year. INS. INV-PVT is ownership change of private institutional investors and it is measured by (INS. ownership after PEP - INS. Ownership before PEP)/(INS. ownership before PEP). INS. INV-GVT is ownership change of government institutional investors and it is measured by (Gvt. ownership after PEP - Gvt. ownership before PEP)/(Gvt. ownership before PEP). OUT.BHOLD is the proportion of share issued to outside blockholders and it is calculated by the 1- proportion of shares issued to blockholders. B\_SIZE is the natural log value of number of Board Members on the board at the beginning of the year. B\_AGE is the natural log value of average age of board members at the beginning of the year. B\_EDU is the natural log value of average education of board members at the beginning of the year. B-EXP is the natural log value of average experience of board members at the beginning of the year. GEND-Dum is a dummy variable if firm has one or more female director prior to the private placement. INTD-Dum is dummy variable if firm has one or more interlocked director. PR\_INTD is proportion of interlocked directors to total number of directors. PC-Dum is dummy variable if firm has one or more politically connected director. PR\_PC is proportion of politically connected directors to total number of directors. Robust standard errors clustered by both firm and time (year) are in parentheses. \*Indicates significance at 10%. \*\* Indicates significance at 5%. \*\*\*Indicates significance at 1%.