

Essays on Political Economy, Corporate Investment, and Risk

A THESIS

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ABSTRACT

This thesis is a collection of three essays exploring the interplay between political forces and corporate finance. Scholarly attention in this domain has burgeoned in recent decades, both in the number of research works and the depth of topics explored.

In [essay 1](#), I explore whether political risk at the firm-level has the potential to contribute to financial contagion, which is estimated by an individual firm's systemic risk contribution. Using detailed firm-level data on US listed firms, I find evidence that firm-level political risk is positively linked to systemic risk contribution. The baseline findings remain consistent against a battery of tests aimed at ensuring robustness and addressing endogeneity concerns. This association is found to be amplified in the presence of strong board connections, and for firms occupying influential positions in the corporate lobbying and political contribution networks.

In [essay 2](#), the focus moves to domestic political factors beyond the atomic firm. I explore one such external political factor - corruption. Departing from the practice of using survey-based corruption estimates at the country level, I use criminal accusations of politicians elected to the Indian Parliament as a plausible proxy for local corruption in their jurisdiction. I use a regression discontinuity design and find causal evidence linking the election of criminally-accused politicians to higher default risk of firms headquartered in their district of jurisdiction. Channel analysis reveals that higher firm-level risk may be driven by suboptimal corporate decisions that aim to reduce the risk of expropriation.

Finally, [essay 3](#) studies global sources of political risk beyond domestic geographic borders. Using tools of textual analysis and a corpus of news and media text, I create and validate new indexes measuring the state of bilateral trade relations of the United States with their largest trading partners. Using these indexes and a cross-country firm-level dataset, I empirically illustrate that firm value and capital investment of non-US firms are positively linked to bilateral trade relations. Firms headquartered in low-income countries, and countries which have lower levels of financial development, are especially vulnerable. Finally, using data on location of foreign subsidiaries of US-listed multinationals, I find that firm value of these US multinationals are also associated with the state of US foreign trade relations.

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Appendix 3

TABLE A3: VARIABLE DESCRIPTION FOR CHAPTER 4

Panel A: Country-level Variables	
BR Index	Index of bilateral trade relations of the country with USA
Diplomacy Index	Index of bilateral diplomacy of the country with USA
Ln(GDP)	Natural logarithm of annual Gross Domestic Product (in constant 2015 USD)
Ln(Trade)	Natural logarithm of total trade conducted in a year
Ln(Trade with USA)	Natural logarithm of total trade conducted in a year with the USA
FX Rate	Exchange rate of the country's currency against USD
GDP Growth	Year-on-Year growth rate in GDP
Inflation	Inflation, consumer prices (annual % growth)
Pop. Growth	Annual population growth rate
Consump. Growth	Final consumption expenditure (annual % growth)
FP Disagreement	Foreign policy disagreement of the country with USA, computed as in

Panel B: Firm-level Variables	
Firm Size	Natural logarithm of book total assets
Sales Growth	Year-on-Year change in total sales
ROA	Earnings before interest and taxes scaled by total assets
Short-term Leverage	Debt in current liabilities scaled by total assets
Long-term Leverage	Total long term debt scaled by total assets
Cash Holdings	Cash and cash equivalents scaled by total assets
Asset Tangibility	Net PPE (property, plant, and equipment) scaled by total assets
Tobin's Q	Market value of equity plus book assets less book equity, scaled by book assets
CAPEX	Capital Expenditures scaled by previous-period gross PPE
BR Exposure	(For US MNCs) Average of BR Index of subsidiary host countries weighted by number of subsidiaries

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