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Partisanship and Corporate Performance*

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Abstract

We present robust evidence that ruling party orientation plays a major role in determining corporate performance. We posit that firms more sensitive to policies traditionally viewed as ‘leftist’ – namely, stringent labour and environmental laws, higher taxes and interest rates – perform worse when left parties are in power. We also account for the fact that ‘leftist’ legislation is not necessarily associated with left governments. Our results remain robust when we account for potential endogeneity between political and financial outcomes.

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1. Introduction

Left parties have traditionally been viewed by economists as being less ‘business-friendly’ than their right counterparts. They have historically been associated with stringent labour and environmental legislation, as well as with high taxes and interest rates. Yet, evidence of the impact of ruling party orientation on financial outcomes is, at best, mixed. Santa Clara and Valkanov (2003) document significantly higher stock returns under Democratic presidencies. Snowberg, Wolfers, and Zitzewitz (2007) find higher equity prices, interest rates, and US dollar exchange rates under Republican presidencies.

Lack of consistent evidence is especially puzzling given growing literature on the impact of political uncertainty on financial outcomes (e.g., Julio and Yook (2011), Boutchkova et al. (2011), Pastor and Veronesi (2011)). The literature shows a material impact of uncertainty regarding party orientation and policies. Yet, there is no unambiguous evidence on the impact of actual (realized) party orientation.

We believe that lack of such evidence is due to a number of issues. First, it is intuitive to assume that not all firms are equally sensitive to ruling party orientation and policies it implements. More specifically, firms will not be uniformly affected by (presumably) adverse effects of leftist policies. Second, it has been documented in the literature¹ that the link between leftist legislation and ruling party orientation is sometimes weak. Third, much of the existing literature analysing the effects of government partisanship uses a dummy variable approach for ‘left-right’ classification, thus ignoring some potentially important characteristics (e.g., coalition governments or legislative and executive branches being controlled by different parties).

In order to address the first issue, we posit that ‘leftist’ legislation has four dimensions, and not all firms are equally affected by such ‘leftist policies. (1) labour legislation. Left governments are traditionally associated with pro-labour policies (Botero et al. (2004), Rueda (2005)). More labour-intensive industries are hypothesized to have greater sensitivity to potentially adverse effects of stringent labour legislation. (2) environmental legislation. Left parties are more likely to enact stringent environmental legislation, which, we hypothesize, will adversely affect highly polluting firms.² (3) high corporate tax rates. We expect firms with higher gross profit margin to experience the most adverse effects of increases of

¹ See, for example, Hibbs (1977), Bobbio (1996), Faust and Irons (1999), and Pagano and Volpin (2005).

² We do not dispute potential social benefits of environmental and labour policies, however, the analysis of such benefits is beyond the scope of this paper.

corporate tax burden. (4) higher interest rates. Left governments are traditionally associated with higher interest rates. We hypothesize that firms more affected by the cost of borrowing – that is, firms with high leverage – to experience drop in performance when interest rates are increased due to political pressure.³

History is ripe with examples of legislation traditionally associated with left governments actually passed when right governments were in power (see, for example, Pagano and Volpin (2005), and Bobbio (1996)). We believe that such imperfect correlation between ruling party orientation and policies it implements is yet another reason for lack of well-established relationship between ruling party orientation and corporate performance. The issue is addressed by performing two stage estimation. In the first stage, measures of ‘leftist’ policies (labour and environmental strictness, corporate tax rate and short-term interest rate) are regressed on the measure of left party orientation. In the second stage, we use leftist legislation explained by ruling party orientation.

Some of the literature on political cycles in economics and finance relies on a simple dummy variable approach to indicate ‘left’ ruling party orientation. While intuitive, such an approach ignores more complex government structures, i.e. when no party has an outright majority or when no single party controls all government branches.⁴ Richer measures of government party orientation have been developed in political science literature, but rarely applied in economics and finance.⁵ To address the issue, we develop a 5-point scale (based on the work of Woldendorp et al. (1998)), with a score of 5 corresponding to left-wing dominance, and a score of 1 representing right-wing dominance.

We expect industries more sensitive to leftist policies to perform worse when left parties are in power and enact such policies. More specifically, labour-intensive industries, industries emitting high quantities of pollutants, industries with high gross profit margin, and industries with high leverage to perform worse and experience lower returns under left governments.

Our results are consistent with the main hypothesis. We document that more labour-intensive industries have lower valuation (measured by Tobin’s Q), lower risk-adjusted stock returns,

³ The concept of political sensitivities has been utilized in the literature before. Boutchkova et al. (2011) document that more export-dependent, labour-intensive, and contract-dependent industries exhibit higher volatilities in times of high political risk. Julio and Yook (2011) find that more politically-sensitive firms experience sharper drop in investments in election years. Belo, Gala, and Li (2011) document that industries more dependent on government purchases perform better under Democratic administrations.

⁴ A dummy variable approach would therefore classify US ruling party orientation as ‘left’ both before and after the 2010 US Congressional elections, even though Democrats have lost control of the House of Representatives after the election.

⁵ Some exceptions are Arin et al. (2011), Tavares (2004).

and worse accounting performance (measured by ROA) when left governments are in power. We posit that stringent labour legislation often introduced by left governments creates rigidities in operations of labour intensive industries, increasing labour costs and making labour force adjustments more difficult. Furthermore, to empirically assess this channel, and to account for the fact that not all pro-labour legislation is passed under left governments, we regress labour law rigidity on left party orientation index. We confirm that explained part of the labour law has a significant negative influence on all three performance measures.

Polluting industries (industries with lower environmental responsibility rankings) also perform worse under left governments, with industry valuation and accounting performance affected adversely. This is not surprising, as stringent environmental legislation (which taxes pollution or restricts environmentally-unfriendly operations altogether) is traditionally associated with left governments. However, to empirically test this channel, we use rigidity of environmental regulation *explained* by left party orientation. We find that it has a significant negative effect for industry valuation.⁶

Left governments have traditionally been viewed as the ones in favour of higher corporate taxes. We document that industries with high average gross profit margin (thus, the ones most adversely affected by any increases in corporate tax rates) have lower industry valuations and return on assets under left governments. Corporate tax rate *explained* by left party orientation has a significantly negative effect on all three performance measures, confirming the existence of the interest rate channel.

Finally, high interest rates, which are also associated with left governments, increase the cost of borrowing, which, we hypothesize, is going to have the most adverse effect on highly leveraged industries. We indeed document that those industries have lower valuations and lower risk-adjusted returns under left governments. As with the other three sensitivities, we use short-term interest rates explained by left party indicator. The explained interest rates have a significantly negative effect on industry valuation and risk-adjusted stock returns. Unlike labour, environmental, and tax rate channels, interest rate influence is not directly legislated by the government. Therefore, our analysis is conditioned on the degree of independence of central bank within a country. We expect interest rate channel to have a stronger effect in countries with lower degree of independence. The results are consistent with such an assertion.

⁶ Stringent environmental legislation may, in principle, make an industry more competitive internationally in the long run. Analysis of such long-term effects is, however, beyond the scope of this paper.

We subject our findings to a number of robustness checks. We account for potential endogeneity between economic performance and ruling party orientation by (i) instrumenting party orientation index and (ii) regressing party index on past economic variables and using fitted values in regressions. We perform the analysis on sub-samples of presidential and parliamentary systems, and control for potential interdependence of political sensitivities.

We believe the results presented in this paper settle the argument on whether ruling party orientation matters for corporate performance. Left governments, by implementing a range of ‘leftist’ policies adversely affect accounting and stock performance of a range of firms exposed to such policies. The results have implications for corporate decision-making, as they highlight that choice to engage in certain lines of business may be disadvantageous under certain governments. Our findings may also invite formal asset pricing tests, as they indicate that party orientation may be a priced factor.

The rest of the paper is organised as follows. Section 2 describes measures of industry sensitivities to government partisanship. Section 3 presents variables and empirical specification. Section 4 describes the results. Robustness is addressed in section 5. Section 6 concludes.

2. **Government partisanship sensitivities**

The main premise of our paper is that not all industries are equally affected by party orientation of the chief executive. We now introduce four industry-level sensitivities to left party orientation: labour intensity, pollution intensity, corporate tax rate sensitivity, and interest rate sensitivity

2.1 Labour intensity

Labour could be a much politicised factor of production, with parties showing substantial differences in their attitude towards labour legislation. Furthermore, attitude towards labour regulation is often used as one of the factors in determining party orientation. Left governments have traditionally been associated with strict labour legislation. Botero et al. (2004), and Rueda (2005) provide evidence of that.⁷

Stringent labour legislation, in turn, has adverse effects on firms. Atanassov and Kim (2009) find that strong labour laws lead to asset sales for poorly performing firms in order to prevent

⁷ Other studies that document pro-labour attitude of left governments are Laver and Budge (1993), Alvarez, Garrett and Lange (1991), and Alt (1985).

large scale layoffs. Boutchkova et al. (2011) document higher volatility for labour-intensive industries under left governments. Stringent labour laws may increase cost of operation (through wage legislation), and make labour-capital substitution more difficult (through rigidities in hiring and firing workers). We thus expect labour-intensive industries to exhibit worse performance when left governments are in power.

Following Boutchkova et al. (2011), we compute labor intensity for industry ind by dividing the value of labor inputs over the total value of production inputs, $vl_{ind} / (vl_{ind} + vk_{ind} + ve_{ind} + vm_{ind})$, where vl_{ind} , vk_{ind} , ve_{ind} , and vm_{ind} denote the values of labor inputs, capital services, and intermediate inputs, such as energy and materials, respectively. Data are obtained from the input-output database developed by Dale W. Jorgenson and described in Jorgenson (1990) and Jorgenson and Stiroh (2000). The authors assembled a detailed dataset of values on labor, capital, energy, and material inputs, using information from the Bureau of Economic Analysis and Bureau of Labor Statistics. The dataset covers thirty-two sectors at the two-digit SIC level from 1959–2005. We use the data from 1990–2005. Labour intensity could be endogenous to political environment.⁸ In countries with strict labour legislation (which is, presumably, passed by left parties), firms may choose to employ fewer workers than they would otherwise. Therefore, we estimate labour intensities in the sample of US industries, and extrapolate them on industries in other countries. As a robustness check, we compute labour intensities using country-level data.

Column 6 of Table 2 reports labour intensities. The average value of labour intensity is 0.275. Petroleum refining is the least labour-intensive industry (value of 0.057); while measuring instruments (0.501) is the most labour-intensive industry.

2.2 Environmental legislation sensitivity

Left governments have traditionally been associated with legislation targeted at tightening environmental standards (e.g., Shipan and Lowry, 2001). Such legislation may include taxation of environmentally-unfriendly activities, pollution quotas, and outright bans on certain pollution types. We posit that less environmentally-friendly firms will be adversely affected by enactment of such legislation.

⁸ Consider the following example. Hotels industry is labour-intensive in the U.S. In Sweden, a country with much more stringent labour regulation, we expect this industry to perform worse because of such labour legislation. However, hotels industry is likely not to be as labour intensive in Sweden, as it is costly for it to hire many workers. Thus, the link between political environment, labour intensity, and performance will be obscured. Thus, we posit that hotels industry labour intensity observed in the U.S. is the *target* labour intensity for hotels in all countries. Rajan and Zingales (1998) use this approach analyzing the relationship between financial dependence and growth.

We use MSCI ESG database ratings (based on Intangible Value Assessment (IVA) methodology) to compute environmental sensitivity, compiled by Innovest Strategic Value Advisors. According to IVA methodology, firms are rated on four components: stakeholder capital, strategic governance, human capital, and environment. The stakeholder capital is divided into the following dimensions: regulators and policy makers, local communities/NGO's, customer relationships, alliance partners, and emerging markets. Strategic governance consists of strategic scanning capability, agility/adaptation, performance indicators/monitoring, traditional governance concerns, and international best practice. The dimensions for human capital are: labor relations, health and safety, recruitment and retention strategies, employee motivation, innovation capacity, knowledge development and dissemination, and progress in workplace practices. The environment component is divided into board and executive oversight, risk management systems, disclosure and verification, process efficiencies, health and safety, new product development, and environmental and climate risk assessment. For our analysis we use the average of the four components. Industry sensitivities are based on the sample of 3,094 U.S. companies and calculated as industry average values.

As with labour intensity, 'pollution intensity' may be endogenous to environmental legislation. In countries with strict environmental laws, firms that otherwise would choose high levels of pollution, are forced to choose lower (and thus suboptimal) levels. Therefore, as with labour intensity, we estimate sensitivity to environmental legislation in the sample of US industries, and extrapolate the measure on industries in other countries.

Column 9 of Table 2 reports environmental responsibility rankings. Average value is 5.41. Food products (SIC 2000) have the highest value (7.31), whereas Miscellaneous retail (SIC 5900) has the lowest value of 0.39.

2.3 Corporate tax rate sensitivity

Fiscal policy is a contentious issue in many electoral campaigns. Parties on the left side of the political spectrum are traditionally linked with higher corporate tax rates (Alesina, 1987; Djankov et al., 2010). High corporate taxes, in turn, decrease after-tax income, and have an overall adverse effect on entrepreneurial activity (Djankov et al., 2010).

We expect industries with larger profit margins (and, thus, larger tax base) are more prone to experience adverse effects of increases of tax rates. Thus, sensitivity to corporate taxes is measured by the ratio of EBIT to sales. Endogeneity between profit margins and corporate tax

rates is a concern, as firms can manage their earnings in response to high taxes. However, an assumption that US corporate tax rate sensitivities can be extrapolated onto industries in other countries, as profit opportunities may differ substantially across countries.

Average corporate tax rate sensitivities are reported in column 7 of Table 2. The average sensitivity value is 0.06. Tobacco products (SIC 2100) has the highest sensitivity value of 0.21, whereas Membership organizations (SIC 8600) have the lowest value of -0.39.

2.4 Interest rate sensitivity

Alesina and Rodrick (1994) is one of the papers documenting higher interest rates under left governments. These higher rates, in turn, increase the cost of borrowing (Chappell and Keech, 1988; Alesina, Roubini and Cohen, 1997; Fowler; 2006, among others). We posit that firms with high leverage – thus, firms that borrow more – are adversely affected by higher interest associated with left governments.

We measure leverage by the ratio of total debt to total assets. To avoid endogeneity, we estimate leverage in the sample of US firms and extrapolate these values onto industries in other countries. Industry-level values are presented in column 8 of Table 2. Average value of interest rate sensitivity is 0.21. Social services (SIC 8300) have the highest sensitivity of 0.49. Legal services (SIC 8100) have the lowest value of 0.001.

3. Variables and empirical specification

3.1 Dependent variables

We employ a number of variables to assess the impact of political orientation on firm performance. *Industry value* is defined as calculated as industry average values of firms' Tobin's Q, which, in turn, is defined as market value of equity and total assets less book value of equity over total assets. *Stock returns* are calculated as industry value-weighted average of annual returns. *Accounting performance* is measured by the return on assets (net income over total assets).

3.2 Political environment

In the analysis of the impact of ruling party orientation on economic and financial outcomes, much of the existing literature has relied on a dummy variable approach. Such an approach ignores some important dimensions of political environment, such as, for example, coalition governments. Measures that address such complexities have been developed in political

science literature (Woldendorp et al., 1993; Kim and Fording, 2002, to name a few), but largely ignored in empirical finance literature.

We develop a five-point index of political party orientation, based on a similar index in Woldendorp et al. (1993), and supplemented by the ‘split government’ variable in Leblang and Mukherjee (2005). Index takes on a value of one if (a) for presidential systems, president is ‘right’ and the right party controls houses with legislative powers, (b) for parliamentary system, chief executive is ‘right’, and government party controls more than 2/3 of the parliament. Index is equal to five in the opposite case – left party (or parties) are in control. Table 1 presents detailed definitions of all of the index values, and column 7 of Table 2 (panel B) presents average index values across countries. The average index value is 3.017. China and South Korea have the highest (left-most) index value of 5. Pakistan has the lowest (right-most) value of 1.137.

3.3 Empirical specification

We regress the dependent variables (industry value, stock returns, and accounting performance) on the interaction of industry-level sensitivities to leftist policies with the index of political party orientation. Along with the levels of these variables and controls (described below), we include industry-, year-, and country-specific fixed effects to account for unobserved heterogeneity. The following panel regression is estimated.

$$\begin{aligned}
 DEP_VAR_{i,j,t} = & \alpha_i + \eta_j + \mu_t + \beta \cdot SENSITIVITY \times LEFT_{i,j,t} \\
 & + \lambda \cdot SENSITIVITY_{i,j,t} + \theta \cdot LEFT_{j,t} + \gamma \cdot CONTROLS_{i,j,t} + \varepsilon_{i,j,t}
 \end{aligned} \tag{1}$$

where i indexes industries, j indexes countries, and t years. Industries are defined at the two-digit SIC level. Such a setup allows us to examine whether industries more sensitive to leftist policies experience worse performance in countries and years when left governments are in power. Thus, the main regression coefficient of interest (β) measures the incremental decrease in performance⁹ given a unit increase in sensitivity to leftist policies conditional on the country’s ruling party orientation index. The standard errors are clustered by country, year, and industry to adjust for heteroscedasticity, time-series, and cross-sectional correlation. Control variables include log of total assets, R&D spending, and growth rate of sales. Detailed variable definitions are presented in Table 1.

⁹ Measured by Tobin’s Q, stock returns, or return on assets.

Such an empirical specification has two main advantages. First, by controlling for fixed effects and effectively analyzing differences in industry performance *within* each country, the issues of model misspecification and omitted variable bias, common to cross-country setups, are alleviated. Second, the sensitivity approach allows us to identify specific economically meaningful channels through which ruling party orientation affects industry performance.

3.4 How 'left' is left?

It has been well established in the literature that left parties are commonly associated with 'leftist' policies.¹⁰ However, empirical evidence on the link between left party orientation and leftist policies is somewhat mixed. Pagano and Volpin (2005), Bobbio (1996) point out that left government orientation may not always be a good predictor of pro-labour legislation. Hibbs (1977) provides examples of tax hikes under Republicans, as well as tax cuts under Democrats. Faust and Irons (1999) provide a similar counter-example for interest rates.

Thus, we posit that conflicting evidence regarding the influence of ruling party orientation on financial outcomes is, in part, due to imperfect link between party orientation and actual policies. Panels (a) – (d) of Figure 1 demonstrate the relationship between ruling party orientation index and four policy measures – labour laws, environmental legislation, tax rates, and interest rates respectively.

In order to test the relationship between policy measures and ruling party orientation, for each country j we run the regression of the following form:

$$LEFT_POLICY_VARIABLE_{j,t} = \eta_j + \mu_t + \beta \cdot LEFT_{j,t} + CONTROLS_{j,t} + \varepsilon_{j,t} \quad (2)$$

Left policy variables are: (1) rigidity of employment legislation; (2) corporate tax rates; (3) interest rates; (4) rigidity of environmental legislation. In every regression, we control for real per capita GDP growth rate, lagged inflation, lagged per capita GDP volatility and lagged exchange rate volatility.

The relationship is uniformly positive for all four policy variables (i.e., left governments are indeed associated with 'leftist' legislation). Statistical significance, however, depends on a particular policy measure. While the coefficients for environmental rigidity and corporate

¹⁰ Botero et al. (2004), Rueda (2005), Shipan and Lowry (2001), Alesina (1987), and Alesina and Rodrick (1997) are but a few examples of this.

taxes are significant at a 5% level, the relationship is significant only at a 10% level for labour rigidity, and not significant for interest rates.

To explicitly account for the imperfect link between party orientation and policies, we perform a two-stage least squares estimation. In the first stage, we regress the legislation measure (labour, environmental, tax, or interest rate) on party orientation index, collecting predicted values and residuals. In the second stage, we estimate the panel regression of the following form.

$$\begin{aligned}
 DEP_VAR_{i,j,t} = & \alpha_i + \eta_j + \mu_t + \beta \cdot SENSITIVITY \times LEFT_LAW_EXPLAINED_{i,j,t} \\
 & + \delta \cdot SENSITIVITY \times LEFT_LAW_UNEXPLAINED_{i,j,t} \\
 & + \lambda \cdot SENSITIVITY_{i,j,t} + \theta \cdot LEFT_{j,t} + \gamma \cdot CONTROLS_{i,j,t} + \varepsilon_{i,j,t}
 \end{aligned} \tag{3}$$

The independent variable of interest is the interaction between sensitivity to leftist legislation and legislation measure *explained* by the ruling party orientation. Similar to Equation (1), we include, time, industry, and country fixed effects, and cluster the standard errors.

4. Results

4.1 Labour intensity

The results for labour intensity are presented in Table 3. The regression coefficients for the interaction term of labour intensity with party orientation index are negative and statistically significant at the 1% level for all three performance measures. This implies that labour intensive industries have lower value, stock returns, and ROA when left governments are in power. This is consistent with our hypothesis.

It is important to note that level of labour intensity is not significantly related to any of the performance measures. Likewise, party orientation in itself has no significant impact on performance, which highlights the relevance of sensitivity methodology, i.e. explicitly accounting for the fact that not all industries are equally exposed to ruling party orientation.

The coefficients at the control variables are of expected signs. Companies with high growth potential (smaller companies with high R&D levels) have higher valuation (as measured by Q), larger ROA, and larger realized returns. Companies with better investment opportunities (measured by past growth in sales) also perform better.

The results of decomposing labour legislation into parts explained and unexplained by the party orientation index are presented in Table 7. The independent variable of interest is the

interaction between labour intensity and labour rigidity *explained* by ruling party orientation. The variable has a significantly negative impact on industry value (at the 1% level), and on stock returns (at the 10% level). The impact on accounting performance, while negative, is not statistically significant. Interaction of labour intensity with *unexplained* labour rigidity is significantly related (at the 10% level) to stock returns and ROA. We believe that such a difference in the impact of explained and residual labour legislation rigidity highlights the importance of taking into account the link between ruling party orientation and actual policy implementation.

4.2 Sensitivity to environmental legislation

The results are presented in Table 4. The interaction between sensitivity to environmental legislation and party orientation index has a negative and statistically significant effect on all three performance measures, which is consistent with our hypothesis. Industries more sensitive to environmental legislation have lower value, lower stock returns and ROA when left governments are in power. The level of the environmental sensitivity is positive which is consistent with Albuquerque et al. (2011) who show that, through customer loyalty, socially responsible companies are valued higher and generate positive return.

The results of decomposing environmental legislation are presented in Table 8. The interaction between sensitivity to environmental legislation with environmental legislation rigidity *explained* by ruling party orientation has a negative and statistically significant impact on all three performance measures. Interaction with *residual* environmental legislation rigidity, although negative, fails to reach statistical significance.

4.3 Corporate tax rate sensitivity

The results are presented in Table 5. The independent variable of interest is the interaction term between corporate tax rate sensitivity and party orientation index. It has a negative and significant impact on stock returns and accounting performance. This is consistent with our expectations. The impact on industry value is negative, but not statistically significant. Notice that the *level* of corporate tax rate sensitivity is positively related to all of the performance measures. This is not surprising, as this sensitivity measure is essentially an alternative performance proxy.

The results of decomposition of tax rate sensitivity are presented in Table 9. The interaction of tax sensitivity with the *explained* part of tax rates has a significantly negative impact on all

three performance measures. Interaction with *residual* corporate tax rates does not have a significant impact on performance.

The *level* of explained corporate tax rates (but not the residuals) has a negative and significant impact on performance. We believe this is consistent with the findings of section 3.4 – corporate tax rates are significantly related to ruling party orientation.

4.4 Interest rate sensitivity

We present the results in Table 6. Interaction of interest rate sensitivity with party orientation has a significantly negative impact on industry value and stock returns, which is consistent with our expectations. Industries more exposed to interest rate movements have lower returns and value when left governments are in power. The impact on accounting performance is negative, but not statistically significant.

The *level* of interest rate sensitivity has a positive impact on all performance measures.

The results of decomposition of interest rates are found in Table 10. Interaction of interest rate sensitivity with the *explained* part of interest rates is negative and significant for all performance measures. Interaction with *residual* interest rates has a significantly negative impact on impact on industry value and stock returns.

5. Robustness checks

5.1 Reverse causality

Analysis of the impact of political environment on financial outcomes is hampered by potential reverse causality. Our results establish that government party orientation has a significant impact on performance of policy-sensitive firms. However, economic performance has a potentially strong impact on electoral outcomes. Our sensitivity approach analyses industry performance within each country and it is less likely that within-country *differences* in performance have a strong systematic impact on political variables.¹¹ Also, financial and economic variables are more likely to impact the likelihood of an incumbent party remaining in the office, rather than systematically affect the left-right distribution.

Nevertheless, we explicitly address potential reverse causality in a number of ways. First, we control for past economic performance by including a number of lagged economic variables.

¹¹ Boutchkova et al. (2011) make a similar argument when analysing the impact of political variables on volatilities of politically-sensitive industries.

These variables are: real per capita GDP growth rate, inflation rate, external debt scaled by GDP, real GDP per capita volatility, and real exchange rate volatility.¹²

Second, we perform the analysis on sub-samples of presidential and parliamentary systems, as in the majority of countries with parliamentary systems electoral systems allow for ‘called’ elections, making strategic electoral timing possible.¹³

Third, we perform a two-stage regression. In the first stage, we regress the party orientation index on past economic variables. In the second stage, we use fitted values in interactions in equations (1) and (3). Our results remain robust.

Finally, we use size of labour unions within a country as an instrument for government party orientation index.¹⁴ We do not find qualitative differences in main regression coefficients when we employ an instrumental variable approach.

5.2 Interest rate channel

As interest rates are not directly legislated by the government, the magnitude of the interest rate channel depends on the degree of independence of central bank in a country. We rank country-years in the sample by the degree of central bank independence obtained from Polillo and Guillen (2005). We then perform the analysis in the quartiles of data with highest and lowest central bank independence. Using the Wald test of the regression coefficient equivalence between different sets of data, we find a significantly stronger effect of the interest rate channel in the quartile of country-years with low degree of central bank independence. This is consistent with our expectations. The difference in regression coefficients is even larger when we consider top and bottom deciles, rather than quartiles.

6. Conclusion

Interdependence of political and financial environments has been the subject of numerous academic inquiries. Whereas the impact of political uncertainty on performance measures (such as stock returns) and corporate decision-making (such as investments) has been relatively well established, the influence of ruling party orientation on financial outcomes is not clear-cut.

¹² Volatilities are computed using a 5-year rolling window. In addition, we include the ‘rule of law’ index obtained from the International Country Risk Guide.

¹³ In addition, in the subsample of parliamentary systems, we employ an alternative measure of political orientation – a percentage of seats in the parliament held by left parties (Kim and Fording, 2002).

¹⁴ Left parties are more likely to be in power when unions are large.

We posit that policies implemented by left parties will have detrimental effect on corporate performance. However, we explicitly account for the fact that not all industries are equally exposed to potentially detrimental effect of leftist policies. We assume that labour-intensive industries, highly polluting industries, industries with high profit margins (thus sensitive to corporate tax rates), and highly leveraged industries (thus sensitive to interest rates) will experience drop in performance when left parties are in power. Furthermore, we explicitly account for the fact that not all leftist legislation is passed by the left parties. We also account for potential complexities of government composition, thus going beyond the dummy variable definition of ruling party orientation.

We document that industries sensitive to leftist legislation experience lower valuations, stock returns and ROAs when left parties are in power and leftist legislation is enacted. Our results are robust when potential endogeneity between ruling party orientation and corporate performance is accounted for.

We believe our findings could be of interest to corporate managers when deciding to engage in activities potentially sensitive to party orientation, as well as to policy makers when considering certain policies in the presence of sensitive industries.

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Table 1. Variables, Definitions, and Sources

| Variables | Definitions | Sources |
|--|---|---|
| <i>Dependent variables</i> | | |
| Industry value | Measured by the sum of the market value of equity (stock price times the number of shares outstanding) and total assets less book value of equity over total assets. | Wordscope |
| Stock returns | Estimated from a one-factor market model as the difference between industry median return and country MSCI return | CRSP and Datastream |
| Accounting performance | Measured by return on assets which is net income over total assets. | Worldscope |
| <i>Partisanship sensitivity measures</i> | | |
| Labor intensity | The ratio of the value of labor inputs to the total value of inputs (labor inputs, capital services, material inputs, and energy inputs), annual from 1990–2006. | Jorgenson (1990) and Jorgenson and Stiroh (2000). Data are available at http://post.economics.harvard.edu/faculty/jorgenson/data.html . |
| Sensitivity to tax legislation | Measured by the sum of net income over total assets. | Compustat |
| Sensitivity to interest rates | Measured by the sum of long-term debt and short-term debt over total assets. | Compustat |
| Sensitivity to environmental legislation | Measured by corporate social responsibility. The MSCI ESG database ratings are based on Intangible Value Assessment (IVA) methodology, compiled by Innovest Strategic Value Advisors. According to IVA methodology, firms are rated on four components: stakeholder capital, strategic governance, human capital, and environment. The stakeholder capital is divided into the following dimensions: regulators and policy makers, local communities/NGO's, customer relationships, alliance partners, and emerging markets. Strategic governance consists of strategic scanning capability, agility/adaptation, performance indicators/monitoring, traditional governance concerns, and international best practice. The dimensions for human capital are: labor relations, health and safety, recruitment and retention strategies, employee motivation, innovation capacity, knowledge development and dissemination, and progressive workplace practices. The environment component is divided into board and executive oversight, risk management systems, disclosure and verification, process efficiencies, health and safety, new product development, and environmental and climate risk assessment. For our analysis we use the average of the four components. | MSCI's Environmental, Social and Governance (ESG) database |
| <i>Political and legislative variables</i> | | |
| Party orientation | A five-point scale defined as follows. 1. Presidential system: president is 'right' AND controls houses with legislative powers. Parliamentary system: chief executive is 'right', and government party controls more than 2/3 of the parliament. 2. Presidential system: president is 'right' but does not control all houses. Parliamentary system: chief executive is 'right' and government party controls between 1/3 and 2/3 of the parliament. 3. Both systems: chief executive is 'centrist'. 4. Presidential system: president is 'left' but does not control houses. Parliamentary system: chief executive is 'left' and government party controls between 1/3 and 2/3 of the parliament. 5. Presidential system: president is 'left' AND controls houses. Parliamentary systems: chief executive is 'left' and government party controls more than 2/3 of the parliament. | Computed by authors. Raw data obtained from World Bank Database of Political institutions, Journal of Democracy, Elections around the World, Election Guide, CIA Factbook, the PARLINE Database on National Parliaments, Keesing's Record of World Events |
| Party orientation (robustness) | A dummy variable equal to one in years when the chief executive's party orientation is classified as 'left', and 0 otherwise. Party orientation is determined according to the party of chief executive using the following rule: Right for parties that are defined as conservative, Christian-Democratic, or right-wing; Left for parties that are defined as communist, socialist, social-democratic, or left-wing; Center for parties that can be best described as centrist. Refer to Beck et al. (2001) for further details. | Computed by authors. Raw data obtained from World Bank Database of Political institutions, Journal of Democracy, Elections around the World, Election Guide, CIA Factbook, the PARLINE Database on National Parliaments, Keesing's Record of World Events |

Table 1 continued

| | | |
|---------------------------------------|--|---|
| Rigidity of employment legislation | An annual index ranging from 0–100, where larger values corresponding to more rigid employment regulations. The index is available from 2004– 2006. It is calculated as average values of three sub-indexes: difficulty of hiring index (applicability and maximum duration of fixed-term contracts and minimum wage for trainee and first-time employees); rigidity of hours index (scheduling of nonstandard work hours and annual paid leave); and difficulty of firing index (notification and approval requirements for termination of a redundant worker or a group of redundant workers, obligation to reassign or retrain and priority rules for redundancy and reemployment). | Doing Business Report database (World Bank) |
| Corporate taxes | Average corporate tax rates. | World Bank |
| Interest rates | Three-month (or closest) interest rate | World Bank |
| Rigidity of environmental legislation | An annual index ranging from 0-10, with larger values representing more stringent labour laws. | World Bank |
| <i>Control variables</i> | | |
| Log of total assets | | Worldscope |
| R&D spending | | Worldscope |
| Growth of sales | | Worldscope |
| Degree of central bank independence | The index ranges from 0 (small degree of independence) through 1 (large degree of independence) and it consists of two attributes: (i) financial independence (the ability given to the government to finance government expenditures either directly or indirectly through central bank credits), (ii) policy independence (maneuvering room given to the central bank in the formulation and execution of monetary policy), and (iii) personnel independence (the influence the government has in appointment procedures). | Polillo and Guillen (2005) |

Table 2 Descriptive statistics. Panel A: Descriptive statistics by industry

| Industry name | SIC code | Industry value | Stock returns | Accounting performance | Labour intensity | Tax sensitivity | Interest rate sensitivity | Environmental sensitivity | Number of firms for US | Number of country-years |
|--------------------------------------|----------|----------------|---------------|------------------------|------------------|-----------------|---------------------------|---------------------------|------------------------|-------------------------|
| Agricultural crops | 100 | 3.238 | 5.947 | 0.049 | 0.245 | 0.055 | 0.188 | 4.796 | 8 | 230 |
| Agriculture livestock | 200 | 1.759 | 0.000 | 0.091 | - | 0.082 | 0.350 | 5.972 | 2 | 382 |
| Forestry | 800 | 1.085 | 3.847 | 0.064 | - | 0.060 | 0.233 | 5.409 | 7 | 201 |
| Fishing and hunting | 900 | 2.682 | 6.454 | 0.116 | - | 0.109 | 0.353 | 4.569 | 7 | 86 |
| Metal mining | 1000 | 4.925 | 23.669 | -0.008 | 0.183 | -0.016 | 0.139 | 4.026 | 78 | 378 |
| Coal mining | 1200 | 1.971 | 12.608 | 0.096 | 0.291 | 0.104 | 0.258 | 4.938 | 8 | 187 |
| Oil and gas extraction | 1300 | 2.528 | 20.253 | 0.122 | 0.132 | 0.127 | 0.256 | 5.960 | 193 | 326 |
| Quarrying of minerals | 1400 | 2.985 | 5.157 | 0.010 | 0.283 | 0.011 | 0.181 | 5.469 | 14 | 230 |
| Building construction | 1500 | 1.898 | 14.057 | 0.098 | 0.369 | 0.089 | 0.287 | 5.972 | 44 | 1241 |
| Food products | 2000 | 2.079 | 5.485 | 0.127 | 0.174 | 0.128 | 0.219 | 7.309 | 112 | 714 |
| Tobacco products | 2100 | 2.989 | 12.692 | 0.213 | 0.154 | 0.205 | 0.320 | 4.980 | 11 | 233 |
| Textile mill products | 2200 | 1.865 | 1.176 | 0.089 | 0.250 | 0.095 | 0.296 | 5.646 | 16 | 444 |
| Apparel | 2300 | 2.333 | 5.622 | 0.109 | 0.303 | 0.114 | 0.165 | 6.885 | 50 | 443 |
| Lumber and wood products | 2400 | 3.949 | 12.448 | 0.075 | 0.257 | 0.071 | 0.232 | 5.673 | 24 | 337 |
| Furniture and fixtures | 2500 | 2.688 | 3.883 | 0.139 | 0.372 | 0.147 | 0.194 | 6.535 | 28 | 392 |
| Paper and allied products | 2600 | 2.201 | 5.188 | 0.109 | 0.255 | 0.106 | 0.282 | 5.371 | 75 | 528 |
| Printing and publishing | 2700 | 1.521 | 3.949 | 0.088 | 0.423 | 0.080 | 0.206 | 4.995 | 66 | 528 |
| Chemicals and allied products | 2800 | 2.265 | 16.963 | -0.086 | 0.195 | -0.086 | 0.141 | 4.821 | 470 | 684 |
| Petroleum refining | 2900 | 2.331 | 19.605 | 0.161 | 0.057 | 0.168 | 0.188 | 4.415 | 44 | 439 |
| Rubber and plastics products | 3000 | 2.705 | 3.506 | 0.131 | 0.333 | 0.121 | 0.229 | 4.497 | 59 | 221 |
| Leather and leather products | 3100 | 1.992 | 3.807 | 0.137 | 0.245 | 0.139 | 0.118 | 3.020 | 32 | 370 |
| Stone, clay, and glass | 3200 | 4.421 | 5.117 | 0.110 | 0.344 | 0.106 | 0.251 | 6.822 | 34 | 570 |
| Primary metal industries | 3300 | 5.311 | 6.619 | 0.078 | 0.195 | 0.084 | 0.246 | 5.120 | 69 | 460 |
| Fabricated metal products | 3400 | 4.216 | 5.404 | 0.125 | 0.303 | 0.125 | 0.237 | 5.363 | 74 | 491 |
| Industrial and computer equipment | 3500 | 1.529 | 10.615 | 0.025 | 0.330 | 0.023 | 0.121 | 5.070 | 300 | 342 |
| Electronic and electrical equipment | 3600 | 2.170 | 10.615 | 0.038 | 0.274 | 0.041 | 0.114 | 6.715 | 419 | 390 |
| Transportation equipment | 3700 | 5.443 | 7.090 | 0.111 | 0.139 | 0.104 | 0.200 | 5.205 | 132 | 566 |
| Measuring instruments | 3800 | 4.331 | 12.337 | 0.000 | 0.501 | -0.007 | 0.108 | 4.408 | 356 | 337 |
| Miscellaneous industries | 3900 | 2.601 | 12.606 | 0.074 | 0.272 | 0.070 | 0.174 | 6.707 | 44 | 422 |
| Railroad transportation | 4000 | 3.278 | 9.573 | 0.104 | 0.354 | 0.098 | 0.291 | 5.438 | 18 | 175 |
| Highway passenger Transportation | 4100 | 4.447 | 6.239 | 0.078 | - | 0.072 | 0.029 | 4.654 | 4 | 276 |
| Motor freight transportation | 4200 | 3.669 | 12.709 | 0.133 | - | 0.127 | 0.233 | 4.963 | 43 | 348 |
| Water transportation | 4400 | 3.221 | 5.895 | 0.120 | - | 0.120 | 0.368 | 4.877 | 30 | 522 |
| Transportation by air | 4500 | 4.559 | 16.163 | 0.080 | - | 0.078 | 0.286 | 5.199 | 33 | 491 |
| Pipelines, except natural gas | 4600 | 1.568 | 18.892 | 0.072 | - | 0.075 | 0.213 | 5.441 | 2 | 164 |
| Transportation services | 4700 | 2.396 | 41.527 | -0.037 | - | -0.041 | 0.149 | 6.853 | 16 | 467 |
| Communications | 4800 | 3.578 | 16.083 | -0.003 | 0.223 | 0.006 | 0.293 | 6.983 | 125 | 593 |
| Electric, gas, and sanitary services | 4900 | 2.750 | 9.777 | 0.093 | 0.191 | 0.090 | 0.304 | 5.277 | 267 | 597 |
| Wholesale trade-durable goods | 5000 | 2.448 | 10.236 | 0.070 | 0.453 | 0.076 | 0.191 | 3.325 | 116 | 549 |
| Building materials | 5200 | 2.768 | 28.123 | 0.067 | - | 0.071 | 0.216 | 5.651 | 9 | 190 |
| Eating and drinking places | 5800 | 5.095 | 8.049 | 0.134 | - | 0.127 | 0.260 | 5.718 | 62 | 312 |
| Miscellaneous retail | 5900 | 2.263 | 6.789 | -0.033 | - | -0.039 | 0.154 | 0.389 | 86 | 102 |
| Depository institutions | 6000 | 1.617 | 20.976 | 0.023 | 0.223 | 0.028 | 0.113 | 5.600 | 539 | 749 |
| Security and commodity brokers | 6200 | 1.712 | 18.236 | 0.028 | - | 0.018 | 0.075 | 4.683 | 66 | 532 |
| Insurance carriers | 6300 | 2.419 | 10.930 | 0.027 | - | 0.022 | 0.057 | 4.785 | 196 | 317 |
| Real estate | 6500 | 3.149 | 8.008 | 0.070 | - | 0.065 | 0.304 | 5.873 | 55 | 319 |
| Investment offices | 6700 | 3.774 | 0.879 | 0.077 | - | 0.084 | 0.348 | 5.855 | 877 | 688 |
| Hotels | 7000 | 4.963 | 14.849 | 0.080 | 0.481 | 0.071 | 0.379 | 6.522 | 14 | 501 |
| Business services | 7300 | 5.750 | 17.260 | -0.125 | - | -0.116 | 0.084 | 6.234 | 376 | 536 |
| Motion pictures | 7800 | 3.895 | 25.424 | 0.030 | - | 0.022 | 0.187 | 6.125 | 16 | 203 |
| Amusement services | 7900 | 3.702 | 10.880 | 0.075 | - | 0.068 | 0.341 | 6.068 | 66 | 358 |
| Health services | 8000 | 3.958 | 10.061 | 0.084 | - | 0.079 | 0.234 | 4.218 | 109 | 326 |
| Legal services | 8100 | 1.255 | 12.140 | 0.206 | - | 0.196 | 0.001 | 5.353 | 5 | 55 |
| Educational services | 8200 | 4.663 | 21.273 | 0.057 | - | 0.062 | 0.098 | 6.649 | 13 | 213 |
| Social services | 8300 | 2.070 | 5.429 | 0.063 | - | 0.067 | 0.495 | 5.896 | 6 | 120 |
| Museums and art galleries | 8400 | 2.248 | 9.137 | -0.015 | - | -0.010 | 0.116 | 7.084 | 73 | 93 |
| Membership organizations | 8600 | 2.581 | 9.070 | -0.397 | - | -0.391 | 0.033 | 5.881 | 65 | 28 |
| Average | | 3.010 | 11.251 | 0.064 | 0.275 | 0.063 | 0.213 | 5.408 | 106.368 | 385.894 |
| Minimum | | 1.085 | 0 | -0.397 | 0.057 | -0.391 | 0.001 | 0.389 | 2 | 28 |
| Maximum | | 5.75 | 41.52666 | 0.213 | 0.501 | 0.205 | 0.495 | 7.309 | 877 | 1241 |
| Total | | | | | | | | | 6063 | 21996 |
| Number of industries | | 57 | 57 | 57 | 57 | 57 | 57 | 57 | 8 | 57 |

This table contains summary statistics by industry (average values across countries and years from 1990–2006). SIC code is two-digit Standard Industry Classification code. All of the variables are defined in Table 1. *Number of country-years* is the aggregate number of country observations across industries and sample years. The last row contains the number of industries for each variable.

Table 2 continued. Panel B: Descriptive statistics by country

| Country | GDP per capita (in 2000 US\$) | Industry value | Stock returns | Accounting performance | Availability of return series | Party orientation | Number of industry-years | Number of firms |
|----------------|-------------------------------|----------------|---------------|------------------------|-------------------------------|-------------------|--------------------------|-----------------|
| Argentina | 7,334 | 2.871 | 9.297 | -1.050 | 1990–2006 | 1.943 | 156 | 97 |
| Australia | 19,854 | 2.340 | 13.803 | 15.727 | 1990–2006 | 2.822 | 847 | 1603 |
| Austria | 22,684 | 1.067 | 11.026 | 13.019 | 1990–2006 | 3.699 | 360 | 120 |
| Belgium | 21,384 | 2.461 | 12.343 | 13.097 | 1990–2006 | 1.884 | 535 | 187 |
| Brazil | 3,641 | 2.677 | 11.258 | -2.400 | 1991–2006 | 3.417 | 434 | 294 |
| Canada | 21,989 | 3.125 | 7.124 | 14.713 | 1990–2006 | 3.531 | 813 | 1724 |
| Chile | 4,572 | 2.178 | 3.821 | 9.878 | 1990–2006 | 1.705 | 345 | 245 |
| China | 880 | 4.747 | 14.753 | 4.473 | 1992–2006 | 5.000 | 602 | 1575 |
| Colombia | 2,427 | 3.792 | 7.745 | 8.689 | 1991–2006 | 2.691 | 152 | 38 |
| Czech Rep. | 5,507 | 4.397 | 17.807 | 30.222 | 1996–2006 | 3.127 | 86 | 23 |
| Denmark | 28,130 | 2.994 | 13.077 | 6.015 | 1990–2006 | 2.943 | 496 | 273 |
| Egypt | 1,332 | 3.067 | 14.835 | 21.418 | 1996–2006 | | 44 | 27 |
| Finland | 21,905 | 1.710 | 20.386 | 10.201 | 1990–2006 | 3.711 | 433 | 178 |
| France | 21,358 | 2.678 | 18.931 | 5.128 | 1990–2006 | 2.587 | 945 | 1021 |
| Germany | 22,012 | 3.088 | 23.659 | 4.034 | 1990–2006 | 2.766 | 864 | 1165 |
| Greece | 11,329 | 4.285 | 35.155 | 7.869 | 1994–2006 | 3.411 | 360 | 415 |
| Hungary | 4,541 | 5.374 | 13.815 | 6.350 | 1994–2006 | 3.764 | 121 | 39 |
| India | 433 | 4.925 | 24.906 | 6.907 | 1990–2006 | 3.293 | 401 | 745 |
| Indonesia | 811 | 3.438 | 17.687 | 6.905 | 1990–2006 | | 554 | 397 |
| Ireland | 21,891 | 2.014 | 10.338 | 16.404 | 1990–2006 | 2.823 | 301 | 100 |
| Israel | 17,998 | 2.671 | 6.376 | 1.673 | 1990–2006 | 2.472 | 206 | 224 |
| Italy | 18,309 | 2.837 | 1.149 | -8.347 | 1990–2006 | 2.705 | 565 | 350 |
| Japan | 36,289 | 2.880 | 13.368 | 5.108 | 1990–2006 | 2.177 | 1040 | 5719 |
| Luxembourg | 42,342 | 1.330 | 13.000 | 5.211 | 1991–2006 | 3.000 | 135 | 46 |
| Malaysia | 3,765 | 2.834 | 13.963 | 11.805 | 1990–2006 | | 822 | 1251 |
| Mexico | 5,547 | 4.192 | 10.650 | 15.032 | 1991–2006 | 3.939 | 327 | 132 |
| Morocco | 1,338 | 2.225 | 0.504 | 7.644 | 1993–2006 | | 32 | 32 |
| Netherlands | 22,286 | 1.945 | 13.716 | 4.294 | 1990–2006 | 3.061 | 626 | 276 |
| New Zealand | 12,805 | 2.758 | 6.476 | 9.929 | 1990–2006 | 2.763 | 462 | 144 |
| Norway | 34,932 | 1.896 | 5.425 | 4.534 | 1990–2006 | 2.943 | 473 | 184 |
| Pakistan | 530 | 2.061 | 6.017 | 4.245 | 1994–2006 | 3.137 | 195 | 151 |
| Peru | 1,996 | 1.754 | 17.572 | 9.883 | 1991–2006 | 1.873 | 104 | 61 |
| Philippines | 959 | 3.298 | 12.053 | 11.333 | 1990–2006 | 3.000 | 377 | 278 |
| Poland | 4,034 | 2.272 | 3.301 | 1.645 | 1996–2006 | 4.415 | 201 | 100 |
| Portugal | 10,086 | 2.220 | 26.818 | 3.191 | 1990–2006 | 2.944 | 294 | 90 |
| Russia | 1,987 | 2.674 | 24.472 | 16.099 | 1996–2006 | | 81 | 45 |
| Singapore | 20,860 | 2.339 | 14.185 | 13.348 | 1990–2006 | | 742 | 622 |
| South Africa | 3,095 | 1.484 | 18.403 | -0.900 | 1990–2006 | 3.827 | 484 | 436 |
| South Korea | 10,565 | 3.465 | 23.648 | -0.320 | 1990–2006 | 5.000 | 395 | 1290 |
| Spain | 13,452 | 2.459 | 4.920 | 5.767 | 1990–2006 | 3.048 | 590 | 211 |
| Sri Lanka | 794 | 2.269 | 17.113 | 10.926 | 1996–2006 | 4.069 | 37 | 42 |
| Sweden | 26,118 | 2.683 | 16.007 | 8.836 | 1990–2006 | 3.647 | 639 | 369 |
| Switzerland | 33,761 | 3.338 | 12.039 | -1.598 | 1990–2006 | | 588 | 385 |
| Taiwan | 12,931 | 4.016 | 33.892 | 5.411 | 1990–2006 | 1.353 | 456 | 1219 |
| Thailand | 1,961 | 4.522 | 31.101 | 5.858 | 1990–2006 | 1.900 | 667 | 629 |
| Turkey | 3,881 | 3.456 | 24.528 | 4.203 | 1990–2006 | 2.463 | 248 | 344 |
| United Kingdom | 23,294 | 2.148 | 3.822 | 12.162 | 1990–2006 | 3.060 | 1063 | 2500 |
| United States | 32,454 | 3.075 | 19.428 | 3.008 | 1990–2006 | 2.813 | 1154 | 6063 |
| Venezuela | 4,939 | 3.176 | 3.457 | -5.538 | 1991–2006 | 2.000 | 83 | 30 |
| Zimbabwe | 594 | 1.088 | 22.973 | 8.978 | 1993–2006 | | 61 | 26 |
| Average | 12,958 | 2.852 | 14.443 | 7.420 | | 3.017 | 429.92 | 670.300 |
| Minimum | 433 | 1.067 | 0.504 | -8.347 | | 1.137 | 32 | 23 |
| Maximum | 42,342 | 5.374 | 35.155 | 30.222 | | 5 | 1154 | 6063 |
| Total | | | | | | | 21996 | 33515 |

This table contains summary statistics by country (average values across industries and years from 1990–2006). All of the variables are defined in Table 1. *Number of industry-years* is the aggregate number of industry observations across countries and sample years. *Number of firm-years* is the aggregate number of firm observations across countries and sample years used to calculate the volatility measures.

Table 3. Performance of labour intensive industries conditional on party orientation

| | Industry value | Stock returns | Accounting performance |
|---|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Labour Intensity with Party Orientation</i> | -0.101*** (0.00) | -0.027*** (0.00) | -0.017*** (0.00) |
| <i>Labour Intensity</i> | 0.416 (0.30) | 0.112 (0.33) | 0.100 (0.34) |
| <i>Party Orientation</i> | 0.209 (0.25) | 0.010 (0.26) | 0.010 (0.26) |
| <i>Log of Total Assets</i> | -0.514*** (0.00) | -0.102*** (0.00) | -0.034*** (0.00) |
| <i>R&D Spending</i> | 4.813*** (0.00) | 0.319*** (0.00) | 0.122*** (0.00) |
| <i>Growth in Sales</i> | 0.102*** (0.00) | 0.017*** (0.00) | 0.021*** (0.00) |
| Country fixed effects | included | included | included |
| Industry fixed effects | included | included | included |
| Year fixed effects | included | included | included |
| Regression R ² -adj. | 0.129 | 0.130 | 0.132 |
| Number of observations | 10,142 | 10,142 | 10,142 |

This table reports the results of OLS regressions of the industry value, stock returns, and accounting performance on the interaction terms of industry labour intensity with party orientation, and control variables. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 4. Performance of industries sensitive to environmental legislation conditional on party orientation

| | Industry value | Stock returns | Accounting performance |
|---|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Sensitivity to Environmental Legislation with Party Orientation</i> | -0.013*** (0.00) | -0.004* (0.10) | -0.010*** (0.00) |
| <i>Sensitivity to Environmental Legislation</i> | 0.162** (0.02) | 0.020** (0.00) | 0.021** (0.02) |
| <i>Party Orientation</i> | 0.314 (0.22) | 0.015 (0.22) | 0.018 (0.22) |
| <i>Log of Total Assets</i> | -0.176*** (0.00) | -0.011*** (0.00) | -0.033*** (0.00) |
| <i>R&D Spending</i> | 0.609*** (0.00) | 3.109*** (0.00) | 0.111*** (0.00) |
| <i>Growth in Sales</i> | 0.015*** (0.00) | 0.098*** (0.00) | 0.026*** (0.00) |
| Country fixed effects | included | included | included |
| Industry fixed effects | included | included | included |
| Year fixed effects | included | included | included |
| Regression R ² -adj. | 0.123 | 0.128 | 0.129 |
| Number of observations | 13,808 | 13,808 | 13,808 |

This table reports the results of OLS regressions of the industry value, stock returns, and accounting performance on the interaction terms of industry sensitivity to environmental legislation with party orientation, and control variables. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 5. Performance of industries sensitive to corporate tax rates conditional on party orientation

| | Industry value | Stock returns | Accounting performance |
|---|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Corporate Tax Rate Sensitivity with Party Orientation</i> | -0.093 (0.14) | -0.078** (0.03) | -0.114*** (0.00) |
| <i>Corporate Tax Rate Sensitivity</i> | 0.833*** (0.00) | 0.312*** (0.00) | 0.304*** (0.00) |
| <i>Party Orientation</i> | 0.003 (0.32) | 0.004 (0.43) | 0.004 (0.43) |
| <i>Log of Total Assets</i> | -0.102*** (0.00) | -0.007*** (0.00) | -0.031*** (0.00) |
| <i>R&D Spending</i> | 4.813*** (0.00) | 0.482*** (0.00) | 0.129*** (0.00) |
| <i>Growth in Sales</i> | 0.207*** (0.00) | 0.009*** (0.00) | 0.026*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| <i>Regression R2-adj.</i> | 0.126 | 0.121 | 0.120 |
| <i>Number of observations</i> | 13,808 | 13,808 | 13,808 |

This table reports the results of OLS regressions of the industry value, stock returns, and accounting performance on the interaction terms of industry sensitivity to corporate tax rates with party orientation, and control variables. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 6. Performance of industries sensitive to interest rates conditional on party orientation

| | Industry value | Stock returns | Accounting performance |
|--|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Interest Rate Sensitivity with Party Orientation</i> | -0.276* (0.10) | -0.094** (0.05) | -0.099 (0.14) |
| <i>Interest Rate Sensitivity</i> | 0.434*** (0.00) | 0.412*** (0.00) | 0.435*** (0.00) |
| <i>Party Orientation</i> | 0.087 (0.29) | 0.013 (0.34) | 0.012 (0.23) |
| <i>Log of Total Assets</i> | -0.081*** (0.00) | -0.009*** (0.00) | -0.014*** (0.00) |
| <i>R&D Spending</i> | 4.813*** (0.00) | 0.301*** (0.00) | 0.082*** (0.00) |
| <i>Growth in Sales</i> | 0.102*** (0.00) | 0.015*** (0.00) | 0.020*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| Regression R ² -adj. | 0.126 | 0.123 | 0.118 |
| Number of observations | 13,808 | 13,808 | 13,808 |

This table reports the results of OLS regressions of the industry value, stock returns, and accounting performance on the interaction terms of industry labour intensity with party orientation, and control variables. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are p -values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 7. Performance of labour intensive industries conditional on labour legislation explained and unexplained by party orientation

| | Industry value | Stock returns | Accounting performance |
|--|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Labour Intensity with Labour Legislation Rigidity Explained by Party Orientation</i> | -0.128*** (0.00) | -0.016* (0.10) | -0.014 (0.14) |
| <i>Interaction of Labour Intensity with Labour Legislation Rigidity Unexplained by Party Orientation</i> | -0.249 (0.12) | -0.042* (0.10) | -0.046* (0.10) |
| <i>Labour Intensity</i> | 0.507 (0.41) | 0.112 (0.34) | 0.113 (0.30) |
| <i>Explained Labour Legislation Rigidity</i> | -0.309 (0.36) | -0.050 (0.18) | -0.080 (0.20) |
| <i>Unexplained Labour Legislation Rigidity</i> | -0.036** (0.03) | -0.017** (0.05) | -0.081* (0.10) |
| <i>Log of Total Assets</i> | -0.022*** (0.00) | -0.309*** (0.00) | -0.028*** (0.00) |
| <i>R&D Spending</i> | 0.318*** (0.00) | 4.861*** (0.00) | 0.119*** (0.00) |
| <i>Growth in Sales</i> | 0.029*** (0.00) | 0.118*** (0.00) | 0.045*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| Regression R ² -adj. | 0.135 | 0.180 | 0.116 |
| Number of observations | 10,142 | 10,142 | 10,142 |

This table reports the results of the second stage of the 2SLS estimation. In the first stage, rigidity of employment legislation is regressed on the party orientation index. Explained and residual values of employment rigidity are collected and used in the second stage interactions. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 8. Performance of industries sensitive to environmental legislation conditional on environmental legislation explained and unexplained by party orientation

| | Industry value | Stock returns | Accounting performance |
|---|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Sensitivity to Environmental Legislation with Environmental Legislation Rigidity Explained by Party Orientation</i> | -0.052* (0.10) | -0.040** (0.05) | -0.009*** (0.00) |
| <i>Interaction of Sensitivity to Environmental Legislation with Environmental Legislation Rigidity Unexplained by Party Orientation</i> | -0.056 (0.31) | -0.050 (0.28) | -0.006 (0.26) |
| <i>Sensitivity to Environmental Legislation</i> | 0.028*** (0.00) | 0.026*** (0.00) | 0.021** (0.02) |
| <i>Explained Environmental Legislation Rigidity</i> | -0.017* (0.10) | -0.111 (0.16) | -0.201 (0.14) |
| <i>Unexplained Environmental Legislation Rigidity</i> | -0.029 (0.26) | -0.021 (0.19) | -0.205* (0.10) |
| <i>Log of Total Assets</i> | -0.011*** (0.00) | -0.048*** (0.00) | -0.136*** (0.00) |
| <i>R&D Spending</i> | 0.309*** (0.00) | 0.127*** (0.00) | 4.822*** (0.00) |
| <i>Growth in Sales</i> | 0.026*** (0.00) | 0.022*** (0.00) | 0.151*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| Regression R ² -adj. | 0.130 | 0.162 | 0.117 |
| Number of observations | 13,808 | 13,808 | 13,808 |

This table reports the results of the second stage of the 2SLS estimation. In the first stage, rigidity of environmental legislation is regressed on the party orientation index. Explained and residual values of environmental rigidity are collected and used in the second stage interactions. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 9. Performance of industries sensitive to corporate tax rates conditional on tax rates explained and unexplained by party orientation

| | Industry value | Stock returns | Accounting performance |
|--|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Tax Rate Sensitivity with Corporate Tax Rates Explained by Party Orientation</i> | -0.076* (0.10) | -0.045** (0.05) | -0.020*** (0.00) |
| <i>Interaction of Tax Rate Sensitivity with Corporate Tax Rates Unexplained by Party Orientation</i> | -0.045 (0.20) | -0.030 (0.26) | -0.014 (0.28) |
| <i>Corporate Tax Rate Sensitivity</i> | 0.245*** (0.00) | 0.317*** (0.00) | 0.119*** (0.00) |
| <i>Explained Corporate Tax Rates</i> | -0.032** (0.02) | -0.032** (0.04) | -0.060** (0.04) |
| <i>Unexplained Corporate Tax Rates</i> | -0.080 (0.32) | -0.076 (0.38) | -0.109 (0.17) |
| <i>Log of Total Assets</i> | -0.034*** (0.00) | -0.025*** (0.00) | -0.119*** (0.00) |
| <i>R&D Spending</i> | 0.433*** (0.00) | 0.149*** (0.00) | 4.816*** (0.00) |
| <i>Growth in Sales</i> | 0.028*** (0.00) | 0.028*** (0.00) | 0.122*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| Regression R ² -adj. | 0.134 | 0.130 | 0.128 |
| Number of observations | 13,808 | 13,808 | 13,808 |

This table reports the results of the second stage of the 2SLS estimation. In the first stage, corporate tax rates are regressed on the party orientation index. Explained and residual values of corporate tax rates are collected and used in the second stage interactions. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.

Table 10. Performance of industries sensitive to interest rates conditional on interest rates explained and unexplained by party orientation

| | Industry value | Stock returns | Accounting performance |
|--|----------------------------|----------------------------|----------------------------|
| Specification | 1 | 2 | 3 |
| <i>Interaction of Interest Rate Sensitivity with Interest Rates Explained by Party Orientation</i> | -0.513*** (0.00) | -0.131*** (0.00) | -0.116* (0.10) |
| <i>Interaction of Interest Rate Sensitivity with Interest Rates Unexplained by Party Orientation</i> | -0.409* (0.10) | -0.212* (0.10) | -0.108 (0.14) |
| <i>Interest Rate Sensitivity</i> | 0.435*** (0.00) | 0.019*** (0.00) | 0.025*** (0.00) |
| <i>Explained Interest Rates</i> | -0.219*** (0.00) | -0.049** (0.03) | -0.017*** (0.00) |
| <i>Unexplained Interest Rates</i> | -0.020 (0.21) | -0.028 (0.20) | -0.001 (0.50) |
| <i>Log of Total Assets</i> | -0.030*** (0.00) | -0.125*** (0.00) | -0.024*** (0.00) |
| <i>R&D Spending</i> | 0.434*** (0.00) | 4.830*** (0.00) | 0.145*** (0.00) |
| <i>Growth in Sales</i> | 0.026*** (0.00) | 0.125*** (0.00) | 0.021*** (0.00) |
| <i>Country fixed effects</i> | included | included | included |
| <i>Industry fixed effects</i> | included | included | included |
| <i>Year fixed effects</i> | included | included | included |
| Regression R ² -adj. | 0.129 | 0.134 | 0.128 |
| Number of observations | 13,808 | 13,808 | 13,808 |

This table reports the results of the second stage of the 2SLS estimation. In the first stage, interest rates are regressed on the party orientation index. Explained and residual values of interest rates are collected and used in the second stage interactions. All of the variables are defined in Table 1. Every regression includes industry, country, and year fixed effects. The numbers in parentheses are *p*-values. The coefficients significant at the 10% level (based on a two-tailed test) or higher are in bold face. *, **, *** indicate significance at the 10%, 5%, and 1%, respectively. Standard errors are clustered by countries and years to adjust them for heteroscedasticity, cross-sectional, and time-series correlations.