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ARTICLE

A Double-Edged Sword: The Two Faces of Political Connections in International Investments of Chinese Firms

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ABSTRACT

Political connections have been tested for correlation with outward foreign direct investment (OFDI). Both theoretical rationale and research evidence are mixed. To advance this debate, we conceptualize political connections as a dual-dimensional construct and hypothesize the differential effects of the breadth and the depth of political connections on OFDI. Employing a sample of 2,374 Chinese listed firms, encompassing 15,647 firm-year observations from 2008 to 2016, we find evidence supporting our hypotheses: (1) the breadth of political connections reduces the likelihood of a firm engaging in OFDI and (2) greater depth of political connections increases the likelihood of a firm engaging in the OFDI. Thus, we advise firms to exercise caution when adopting corporate political strategies for internationalization in general and OFDI in particular.

摘要

现有文献已讨论过政商关系与对外直接投资（OFDI）的相关性，但理论依据和研究证据尚不一致。为推进对这一议题的深步探讨，我们将政商关系视为一个双维度的概念，并讨论政商关系的广度和它的深度对 OFDI 的不同影响。我们通过对 2008 年至 2016 年间 2374 家中国上市公司、 15647 个公司年度观察值的样本进行分析，发现了支持假设的证据：（1）政商关系的广度降低公司实行 OFDI 的可能性；（2）政商关系的深度增高公司实行 OFDI 的可能性。鉴于政商关系不同维度的不同影响，我们建议企业在国际化，特别是对外投资方面，应谨慎施行政商战略。

Keywords: breadth; China; depth; outward foreign direct investment (OFDI); political connections

关键词: 对外直接投资（OFDI); 政商关系; 深度; 广度; 中国

Introduction

Research on the value of political connections to businesses has proliferated since the seminal work of Faccio (2006), with one of the main research streams being their role in firms' internationalization (for reviews, see Tihanyi et al., 2019; Wei, Jia, & Bonardi, 2023). On the one hand, political connections offer a valuable means for firms' international investment efforts, as politically connected firms are more likely to receive 'preferential treatment by government-owned enterprises (such as banks or raw material producers), lighter taxation, preferential treatment in competition for government contracts, relaxed regulatory oversight of the company in question, or stiffer regulatory oversight of its rivals, and many other forms' (Faccio, 2006: 369). On the other hand, it has been argued that the benefits derived from political connections can largely ensure firms' survival and growth in the domestic market, reducing their willingness for international expansion where these connections tend to have weak influence (Bai, Chen, & He, 2019; Bai, Chen, & Xu, 2021; Du & Luo, 2016). Unsurprisingly, empirical evidence on the impact of political connections on firms' internationalization in general, and outward foreign direct investment (OFDI) in particular, is mixed (see Appendix for a summary of research findings).

Notwithstanding the valuable contributions of prior studies, this inconclusive evidence indicates that our understanding of the impact of political connections on firm internationalization remains incomplete. Close inspection of the literature (see Appendix) reveals that most existing studies examine political connection from a unitary perspective – conceptually treating them as a monolithic concept, i.e., whether or not firms have connections with the government, and empirically measuring it as a dummy variable. However, such conceptualization and measurement often overlook the heterogeneity of political connections. First, governmental organizations have diverse functions (e.g., regulatory, administrative, and legislative) and they often offer distinct resources and support (Luo, Xue, & Han, 2010; Voss, Buckley, & Cross, 2009). Each connection, therefore, may offer unique value to firms. Second, government organizations at various hierarchical levels (e.g., state, provincial, and county) are empowered to hold the authority of regulation and administration according to their jurisdictions and offer diverse resources and support (Du & Girma, 2010; Jin, Qian, & Weingast, 2005; Park, Li, & Tse, 2006; Tan, Li, & Xia, 2007). For example, national government connections may facilitate access to preferential policies, diplomatic supports, and national tax incentives, whereas local government connections may aid firms to participate in investment promotion programs and offer them infrastructure and logistics support (Deng, Yan, & Sun, 2020; Ma, Ding, & Yuan, 2016).

Although a small number of studies have recognized the value of individual political connections (e.g., Bai et al., 2021; Guo et al., 2022; Wu & Ang, 2020), they often employ a count-based measure, e.g., counting the number of political connections of firm executives, or a share-based measure, i.e. the share of members with political connections across firm executives. However, these studies generally neglect to consider the hieratical level of these connections and fail to recognize multiple connections of an individual executive (e.g., one executive worked in several government organizations before taking up the position in a firm). Conversely, studies that do account for the hierarchical levels often use multiple dummy variables to capture connections at different levels. This approach overlooks the intrinsic value of each connection, ignoring the variability in the number of connections and masking the differences between firms that have few connections and those with extensive networks. Our study bridges these two points and extends the literature by establishing a comprehensive construct of political connection that incorporates the 'breadth' and the 'depth' of political connections (hereafter Breadth and Depth, respectively). This allows for a more nuanced analysis of the impact of political connections on the business strategy, specifically, the international investment strategy, leading to potentially more informative findings.

We define Breadth as the portfolio of government organizations of different functions with which firms establish connections through interpersonal ties between firm executives and government officials. Depth, on the other hand, refers to the extent of firms' embeddedness within the political hierarchy through interpersonal ties. This novel dual-dimensional approach captures both the scope of firms' connections with governmental organizations and the hierarchical significance of these connections, reflecting the political connections' complexity. Underpinning our work with resource dependency theory (Drees & Heugens, 2013; Hillman, Withers, & Collins, 2009; Pfeffer & Salancik, 2003) and drawing insights from the state capitalism literature (Musacchio, Lazzarini, & Aguilera, 2015; Wright, Wood, Musacchio, Okhmatovskiy, Grosman, & Doh, 2021), we develop a theoretical rationale for the differential effects of political connection breadth and political connection depth with respect to OFDI. Resource dependency theory highlights the importance of political connections in securing strategic resources to manage constraints and uncertainties. It has been extensively applied to the context of leveraging political connections for domestic business strategies and operations, and its application in international business research is increasingly recognized (Jiang, Luo, Xia, Hitt, & Shen, 2023). Simultaneously, international business and strategic management studies have emphasized state capitalism (Musacchio et al., 2015; Wright et al., 2021), which is defined as 'an economic system in which the state uses various tools for proactive intervention in economic production and the functioning of markets … [and] state interventions can occur within the home market and abroad, in the interest of domestic firms and for diplomatic purposes' (Wright et al., 2021: 2). Yet, despite the recognition that political connections are closely aligned with state capitalism, this stream of research has largely focused on the role of state ownership instead of political connections in OFDI decisions (e.g., Chen, Li, Zeng, Ma, & Lin, 2016; Li, Cui, & Lu, 2014). In this study, we contribute to theoretical discourse by combining resource dependency theory with the state capitalism perspective to explore the impact of the breadth and depth of political connections on OFDI.

To test our hypotheses, we focus on the context of publicly listed firms in China. The Chinese corporate sector represents an important laboratory to advance research on the nexus of political connections and OFDI. First, Chinese firms' OFDI is significant to the global economy not only because of its rapid growth in volume, making China a major source country of FDI, but also because the entry of Chinese multinational enterprises, the agent of OFDI, has substantially transformed the effect on economic integration and global value chains (Alon, Anderson, Munim, & Ho, 2018; Deng, 2015; Paul & Benito, 2018). Second, China is often considered a prime example of state capitalism, where there is a prevalence of business–political connections (Guo et al., 2022). Despite transitioning from a centrally planned economy to a more open economy, with the market playing a vital role in the business environment, governments at different hierarchical levels retain pervasive control over capital, land, government contracts, and other resources, while government officials enjoy substantial discretion over the implementation of policies (Du & Girma, 2010; Jin et al., 2005; Park et al., 2006; Tan et al., 2007). The strong, ambiguous, and sometimes arbitrary government interference in listed companies is particularly pronounced (Guo et al., 2022; Wei, Hu, & Chen, 2020; Zhang, 2023). Thus, this group of firms constitutes an important setting to examine the extent to which political connections are a factor in directing firms' OFDI decisions.

This article offers significant theoretical and empirical contributions. Theoretically, we underpin our theoretical framework on resource dependence theory (Drees & Heugens, 2013; Hillman et al., 2009; Pfeffer & Salancik, 2003) and the state capitalism perspective (Jiang et al., 2023; Musacchio et al., 2015; Wright et al., 2021) to examine the impact of political connections on OFDI decision. We recognize both the bright and the dark side of political connections associated with the breadth and the depth of these connections, respectively. From an empirical standpoint, we conceptualize political connection as a dual-dimensional construct and measure it along the dimensions of breadth and depth. This approach offers an auspicious ground for examining corporate political strategies, moving beyond the unitary perspective of political connection.

Theoretical Background and Hypotheses Development

Political Connection as a Dual-Dimensional Construct

Building on established literature (Cui, Hu, Li, & Meyer, 2018; Fernandez-Mendez, Garcia-Canal, & Guillen, 2018; Sun, Mellahi, & Wright, 2012; Wei et al., 2023), we conceptualize political connections as the interpersonal ties between firm executives and government officials across all political hierarchical levels, through which they acquire strategic resources, including institutional resources and support. However, in contrast to previous studies that typically view political connections as the presence or absence of political connections of firm executives, or measure the count or share of firm executives with political connections (see Appendix), thereby neglecting the heterogeneity of political connections, we propose political connection as a dual-dimensional construct to include both breadth and depth.

Firms can cultivate multiple political connections in a government system of different functions and different levels within a hierarchy. Various government organizations specialize in different areas of governance and can provide distinct resources and support to firms (Martimort, 1996; Mishra & Anant, 2006). For example, economic ministries such as the Ministry of Finance, Ministry of Commerce, and Economic Development Agencies focus on economic policies, trade and FDI regulations, and economic development programs. They often offer financial incentives, tax benefits, and trade and investment support. Conversely, bodies such as the Environmental Protection Agency enforce regulations and standards and provide firms with guidelines, compliance assistance, and grants to meet regulatory requirements.

On different hierarchical levels, the state-level government design national policies, while local-level governments – including provincial, municipal, and county levels – are responsible for national policy implementation and making and enforcing local policies that regulate and promote local economic development (Du & Girma, 2010; Li & Lu, 2020; Tan et al., 2007). Local governments are often held administratively and politically accountable for the success and failure of the local economy, and they rely on local businesses to fulfill their financial and political goals (Li & Lu, 2020; Shi, Markóczy, & Stan, 2014). Government organizations at different levels possess differing regulatory powers and resource allocation capabilities, controlling and influencing firms' business activities to different degrees (Chen, Li, Luo, & Zhang, 2017; Du & Girma, 2010; Shi et al., 2014; Tan et al., 2007).

To capture the complexity of political connections, we define the breadth of political connections (Breadth) as the portfolio of government organizations with which firms establish connections, encompassing various regulatory, administrative, and legislative entities. The depth of political connections (Depth) denotes the extent of firms' embeddedness within the political hierarchy, indicating the level of contacts with different tiers of government from local, regional to national levels. This dual-dimensional approach provides a more comprehensive perspective of corporate political activities.

Political Connections and OFDI

Theoretically, political connections can exert both positive and negative impacts on firms' OFDI decisions. On the one hand, political connections can enable firms get access to institutional resources and receive policy and non-policy support (Hillman, 2005; Peng & Luo, 2000; Sun et al., 2012; Xin & Pearce, 1996). According to resource dependency theory, the performance of a firm hinges on its capability to manage constraints and uncertainties from its external environment (Pfeffer & Salancik, 2003), as it cannot independently control every resource it needs, it must interact with external actors who control those resources (Pfeffer & Salancik, 2003). The government, being one of the most important stakeholders of firms, has power in controlling valuable institutional resources (Dunning & Lundan, 2008; Jackson & Deeg, 2019; Peng & Luo, 2000). Political connections are one of the most important means for firms to obtain institutional resources from governments (Hillman, 2005; Peng & Luo, 2000). Compared to their non-connected counterparts, politically connected firms have a greater ability to communicate and interact with the government (Fernandez-Mendez et al., 2018), which gives them an advantage to access and acquire privileged resources such as licenses, low-interest loans, and administrative rights/considerations that facilitate business operations for OFDI (Deng, Yan & van Essen, 2018). Therefore, political connections can confer a competitive advantage to politically connected firms by ensuring access to strategic resources that are not readily available to competitors. Additionally, firms with political connections may also have better access to the information of foreign markets provided by the home government, e.g., through investment promotion agencies (Harding & Javorcik, 2012; Li, Meyer, Zhang, & Ding, 2018a; Marquis & Qiao, 2020; Pan, Teng, Supapol, Lu, Huang, & Wang, 2014), which enables them to discern and dissect potential costs and uncertainty regarding foreign business deals (Pan et al., 2014).

By leveraging political connections, firms can influence policies through corporate political activities, e.g., lobbying (Lawton, McGuire, & Rajwani, 2013; Mellahi, Frynas, Sun, & Siegel, 2016). Government organizations also have vested interests in designing policy support to promote firms to conduct OFDI so as to, for example, acquire natural and technological resources for domestic development and international competitiveness, maintain diplomatic and political relations with foreign countries, and fulfil bilateral and multilateral treaties (Child & Rodrigues, 2005; Deng et al., 2018; Lu, Liu, Wright, & Filatotchev, 2014a; Luo et al., 2010). For instance, the Chinese state government (i.e., top hierarchical level) has continuously launched national policies to facilitate firms' internationalization, including initiatives 'Open-Door' in 1978, 'Go Global' in 2000, and 'Belt and Road' (BNR) in 2013 (Cai, 1999; Child & Rodrigues, 2005; Du & Zhang, 2018; Yan, Zhu, Fan, & Kalfadellis, 2018). In alignment with national guidelines, local governments have set up policies to promote the internationalization of firms within their jurisdictions (Luo et al., 2010; Ma et al., 2016). This policy support is believed to have contributed to China's growing OFDI activities (Buckley, Yu, Liu, Munjal, & Tao., 2016; Kolstad & Wiig, 2012). However, state intervention and investment promotion by governments are not limited to emerging economies like China. Earlier literature on the varieties of capitalism clearly recognizes the prominent role of the state in supporting businesses within the Coordinated

Market Economies (Hall & Soskice, 2001). Recent studies on state capitalism in the international context underscores the pivotal role of state agency (Wright et al., 2021). Recognizing the benefits of global economic integration, particularly through FDI, and the barriers posed by a lack of information for OFDI, as well as inward FDI, 'there are more than 189 investment promotion intermediaries at the national level and over a thousand at the subnational level' (Harding & Javorcik, 2012: 338). Many countries' embassies also have commercial sections/departments dedicated to supporting their firms' international business activities by providing business matchmaking, as well as market intelligence and compliance assistance.

Resource dependency theory highlights the importance of political connections in securing strategic resources, acquiring policy support, and influencing policies to create a more favorable operational environment. These can have a profound positive impact on firms' OFDI activities through managing constraints and uncertainties effectively.

Conversely, the rationale associated with market-oriented strategies and resource deployment underscores the proposition on the negative impact of political connections on OFDI. Politically connected firms with access to institutional resources tend to face soft budgetary constraints. This diminishes their reliance on stock markets to raise funding, leading to underdeveloped market-oriented strategies, such as international expansion (Bonardi, 2008; Sheng, Zhou, & Li, 2011; Sun et al., 2012). The weak market orientation would lead to firms' inability to capitalize on business opportunities and obtain resources through market channels (Du & Luo, 2016; Sun et al., 2012), which are critical to international competitiveness. This is in line with prior studies that firms with political connections tend to suffer from cost inefficiency (Fan, Wong, & Zhang, 2007; Sun, Mellahi, & Thun, 2010), giving them a disadvantageous position in international market penetration and competition. Additionally, the value of political connections tends to be more pronounced in the domestic arena in comparison to the international arena (Bai et al., 2019; Lu, Liu, Filatotchev, & Wright, 2014b). In other words, politically connected firms cannot expect to receive the same level of government support following the entry into a foreign market (Fernandez-Mendez et al., 2018). Firms leveraging political connections to navigate domestic markets may struggle to adapt to international markets, which sometimes require different or modified strategies. While executives who hold political connections need to demonstrate their ability to contribute to firm performance, they are likely to focus on the domestic market where their political connections can generate higher values (Fernandez-Mendez et al., 2018; Sun, Hu, & Hillman, 2016; Sun et al., 2012).

Moreover, the high government dependency necessitates politically connected firms to deploy resources to maintain political ties. This allocation would detract from the resources available for developing market-based capabilities, including new product development, cost control, and international R&D collaboration (Sun et al., 2012). Notably, some studies suggest that politically connected executives can use their political knowledge to forge relationships with foreign governments (Fernandez-Mendez et al., 2018). Nonetheless, developing and maintaining such relationships still demands substantial firm resources (Cui et al., 2018). Consequently, considering the resources commitments that need to be deployed for political connections, politically connected executives may be dissuaded to pursue OFDI.

The above arguments regarding the positive and negative effects of political connections on OFDI are equally compelling and well-documented in the literature (see Appendix). To punctuate these opposing arguments, we explore two dimensions of political connection breadth and political connection depth and OFDI.

Political connection breadth and OFDI

On political connection breadth, firms with a large number of political connections are able to obtain diverse array of institutional resources and policy support from several government organizations due to the separation of powers within the government (Boubakri, Guedhami, Mishra, & Saffar, 2012; Li & Zhang, 2007; Martimort, 1996; Mishra & Anant, 2006; Sheng et al., 2011). However, this expansive network carries the risk of 'over-reach', a concern particularly exacerbated by state capitalism.

In the political arena, each government organization/agency operates within its own space with unique institutional norms, habits, and rules (Aharoni, Maimon, & Segev, 1981; Luo et al., 2010). There is vertical fragmentation between levels of the political system and horizontal fragmentation between jurisdictions in a specific geographic location. Cultivating, monitoring, maintaining, and safeguarding these connections often require specific costs tied to the peculiarities of each organization (Hillman et al., 2009). These costs are further exacerbated by the fact that different organizations often have varying agendas, social, and political goals, which may often conflict (Martimort, 1996; Mishra & Anant, 2006). For instance, two agencies, respectively, responsible for economic development and environmental protection may impose different requirements on firms. The costs associated with maintaining political connection breadth may, therefore, offset the combined benefits associated with individual political connections. A large network of political connections magnifies the risk of government interference, particularly in situations involving numerous interactions between multiple organizations. State capitalism frequently involves long-term strategic planning influenced by government agendas. These multiple long-term agendas can limit corporate flexibilities and lock firms into multiple commitments (Chen, 2007; Okhmatovskiy, 2010) that prevent them to take advantage of international opportunities. The possible advantages of institutional resources and support associated with political connection breadth could be offset by governance problems, prompting suboptimal, non-market-oriented decisions.

In light of these circumstances, the negative effects of political connections are likely to outweigh the positive effects. Therefore, we observe an overall negative impact of political connection breadth on OFDI.

> *Hypothesis 1 (H1): The breadth of political connections is negatively associated with a firm's OFDI decision.*

Political connection depth and OFDI

Within a political system, the central government generally hold the majority of decision-making authorities (Maskin, Qian, & Xu, 2000; Naughton & Yang, 2004). Firms connected to central-level government organizations can secure more preferential access to institutional resources and support, including diplomatic protection and advocacy by their home government in foreign markets (Li et al., 2018a, Wang, Cui, Vu, & Feng, 2022). For example, Pan et al. (2014) suggest that firms that are connected with central legislative bodies have improved access to the information about host country's institutional environments, which enhances their capability to mitigate risks in the host country. Similarly, Li et al. (2018a) find that central-level political connections improve firms' access to diplomatic services, thereby facilitating access to foreign business information, intergovernmental business deals, and home government political support in the host country.

In contrast, the devolution of power that has occurred in many countries has empowered local governments the authority to design and implement local policies. As a result, this has increased the authority of local governments over local businesses, e.g., they can decide on who will be receiving preferential treatment, tax benefits, fiscal subsidies, and the waiver of liabilities. Nevertheless, local policies must align with the policies designed at the higher level of authority. Ultimately, their principles should be in common with those of national policies. Firms that are connected with high-level government organizations (e.g., politically connected at the state level and located in one city) can receive both local and state support; thus, they are more likely to implement OFDI (Lu et al., 2014a; Wang et al., 2022).

Furthermore, national policies are generally more stable and focus on longer-term goals compared to local policies. The former often involves more rigorous, complex legislative processes, in contrast to the latter which encompasses multiple layers of scrutiny, debate, and approval, and requires a broad consensus as well as inputs from multiple stakeholders. Additionally, under state capitalism, central-level government organizations typically have larger budgets and greater political clout than their local counterparts. This often results in more consistent, effective policy implementation and institutional support to firms (Schofield & Sausman, 2004; Wang, Hong, Kafouros, & Wright, 2012). In the realm of OFDI, a greater depth of political connections allows firms to better balance the costs while capitalizing on the benefits associated with these connections.

> *Hypothesis 2 (H2): The depth of political connections is positively associated with a firm's OFDI decision.*

Methods

Data and Sample

In this study, we utilize two distinct datasets. The first dataset is obtained from the China Stock Market & Accounting Research (CSMAR) database, which provides detailed information on the political connections variables among Chinese firms listed on the Shanghai and Shenzhen Stock Exchanges. Currently, CSMAR is one of the most reliable and comprehensive firm-level data sources in China and is frequently referenced in academic literature (e.g., Deng et al., 2018; Du & Luo, 2016; Liang, Ren, & Sun, 2015; Xia, Ma, Lu, & Yiu, 2014). It provides extensive information on the political backgrounds, government colleagues, alumni networks, kinships, and concurrent positions in other firms of senior executives of the Chinese listed firms since 2008. Additionally, the CSMAR database includes information on the listed Chinese firms regarding various attributes: firm name, location, industrial classification, ownership, number of employees, total sales, annual profit, R&D investment, year of establishment, and other important indicators. For the total number of OFDI projects undertaken by a firm, we manually coded the data based on firms' foreign subsidiary information disclosed in annual reports in CSMAR.

The second dataset is drawn from the Directory of Overseas Investment Institutions of Chinese Enterprises published by the Ministry of Commerce of China (MOC), a central government organization that systematically compiles all government-approved overseas investments by Chinese firms. This dataset provides information on OFDI project ID, firm name, country/region of investment, and the approval date from year 2006 to 2016. For the main measure of the dependent variable on whether firms engaged in OFDI or not, we obtained the data from this source.

After excluding the samples with incomplete information, the final sample comprises 2,374 Chinese listed firms with 15,647 firm-year observations from 2008 to 2016. Analyzing Chinese OFDI during this period is particularly pertinent for two reasons. First, the 2007 global financial crisis had a profound impact on international business, and in the period that followed, many Chinese firms adjusted their international investment strategies to take advantage of lower asset prices abroad, leading to a surge in OFDI from 2008, with a peak in 2016 (UNCTAD, 2024). Second, China's 'Go Global' policy initiated in the early 2000s gained substantial momentum by 2008. Between 2008 and 2016, China implemented numerous policy reforms aimed at facilitating and encouraging OFDI, including easing foreign exchange controls and providing additional financial support to firms undertaking OFDI. However, after 2017, geopolitical tensions have become more pronounced in the context of Chinese OFDI, with increased scrutiny to Chinese investment in certain regions, e.g. the US and the UK. Therefore, the timeframe of 2008–2016 captures a transformative phase for Chinese OFDI and presents an ideal setting for our research question.

Measures

Dependent variable

In the primary analysis, the dependent variable, OFDI, is measured by a dummy variable, which equals 1 if the firm conducted OFDI each year, and 0 otherwise. For robustness checks, we measured OFDI using the total number of OFDI projects undertaken by a firm. The data were manually coded based on firms' foreign subsidiary information disclosed in annual reports in CSMAR. Although the count measure provides a higher level of detail, we recognize potential inaccuracies with this measure, such as firms failing to report or delaying the reporting of the establishment of their foreign subsidiaries in their annual reports. Thus, we use the count measure to corroborate our primary findings that are based on a clear and straightforward measure that is more accurate.

Independent variables

Following the methodology of Faccio (2006), we measured political connections as based on their previous and/or current government employment experiences of all board members (Lu et al., 2014; Wu, Wood, & Khan, 2021). Therefore, the breadth of the political connection (Breadth) is quantified by the total number of political connections obtained by all board members, scaled by the size of the board. Specifically, we first code whether each board member has working experience in a government organization (e.g., Hillman, 2005; Sun et al., 2016). If the member worked in more than one government organization, it is counted as a separate political connection, recognizing that different government organizations bring distinct resources and support to firms (Luo et al., 2010; Voss et al., 2009). We then sum the total of each member's political connections and divide it by the number of board members (board size) to calculate the breadth of political connections for each firm in a given year.

The depth of political connection (Depth) is computed based on the hierarchical level of the government organizations with which the board members are affiliated. The CSMAR database categorizes five levels of government: state, provincial, municipal, county, and township. It is generally acknowledged that higher government levels (e.g., state) have substantially more institutional resources and information in China (Chen et al., 2016; Deng et al. 2020; Li, Xia, Shapiro, & Lin, 2018b; Li et al., 2014). In terms of hierarchical relationships, local government officials operate under the command of the central/state government, which determines their appointment and promotion (Lin, 2010; Naughton & Yang, 2004). Thus, following Wang et al. (2012), we assigned a value to each level, from 5 to 1, where the highest state level receives a value of 5, and the lowest township level receives a value of 1. We then code the highest levels of political connections for each board member. For instance, if a member is politically connected to three government organizations, two at the provincial level (4) and one at the county level (2), their personal political connection depth is the highest level among the three connections, which is 4. Each of the five hierarchical levels have equal weight in calculating the measure. Finally, we derived the firm's depth of political connection by finding the sum of each member's top hierarchical level, before dividing by the total number of board members.

Control variables

Following prior studies (e.g., Lu et al., 2014a; Wu, Wang, Hong, Piperopoulos, & Zhuo, 2016), we incorporate several control variables that are likely to influence firms' decision regarding OFDI. First, we use the natural logarithm of the total assets to control for firm size. The literature has stressed the positive effects of firm size on OFDI, since larger firms tend to possess greater resources that are advantageous for conducting OFDI (Lu et al., 2014b). We include return on equity (ROE) to control for firm performance. It has been suggested that firms with stronger performance have a greater likelihood to pursue international expansion (Wang, Hong, Kafouros, & Boateng, 2012). Next, we control for financial leverage, measured by the debt ratio (the ratio of debt to total assets), which can restrain a firm's financial capability (Deng et al., 2018). Highly leveraged firms usually are less able to engage in OFDI in comparison to lowly leveraged firms (Huang, Xie, Li, & Reddy, 2017; Wu et al., 2016). We also use the natural logarithm of the R&D expenses to control firms' R&D capability. Following Luo and Bu (2018) and Tseng, Tansuhaj, Hallagan, & McCullough (2007), R&D capability is expected to positively impact on OFDI. In addition, we measured board independence by the ratio of the number of independent directors and board size. To mitigate potential endogeneity issues, we lagged all control variables by one year. Finally, the industry dummy variables are included to control for industry-specific effects.

Results

Table 1 presents the descriptive statistics and a correlation matrix. OFDI propensity has a mean value of 0.073, indicating that a low percentage of Chinese listed firms engaged in OFDI between 2008 and 2016, suggesting a predominant focus on domestic markets. The correlation coefficients among variables are generally lower than 0.17, with the exception of the moderate correlation between Breadth and Depth being 0.541. Notably, all variance inflation factor (VIF) values are below 2, indicating no concern with multicollinearity in our model.

The results from the panel regression are reported in Table 2. Model 1 includes only control variables. Most of control variables have a significant impact on OFDI propensity. Specifically, the likelihood of a Chinese listed firm undertaking OFDI decreases with financial leverage and increases with firm size, ROE, and R&D. To test the hypotheses, Model 2 adds Breadth and Depth to Model 1. Breadth has a negative and significant impact ($b = -0.158$, $p = 0.046$) on OFDI propensity, supporting H1. Depth has a positive, significant coefficient ($b = 0.261$, $p = 0.034$), supporting H2.

Table 1. Descriptive statistics and correlation

		Mean	SD	1	2	3	4	5	6	7	8
1	Breadth	0.344	0.352	1							
2	Depth	0.342	0.207	0.541	1						
3	OFDI	0.073	0.26	−0.002	0.020	1					
4	Leverage	0.53	1.886	0.038	0.023	−0.008	1				
5	R&D	2.728	6.255	0.022	0.037	0.072	−0.016	1			
6	ROE	0.037	1.314	−0.003	0.016	0.016	−0.003	−0.004	1		
7	Firm size	22.568	1.359	0.037	0.012	0.166	−0.107	0.100	−0.016	1	
8	Board independence	0.372	0.072	0.048	0.091	0.048	0.004	0.054	−0.003	0.054	1

Table 2. Regression results

	Model 1				Model 2			
	Est.	S.E.	$p > z$	Sig.	Est.	S.E.	$p > z$	Sig.
(Intercept)	−9.162	0.508	0.000	***	−9.195	0.508	0.000	***
Industry	(Included)				(Included)			
Year	(Included)				(Included)			
Sigma	−0.626	0.035	0.000	***	−0.626	0.035	0.000	***
Firm size	0.320	0.021	0.000	***	0.321	0.021	0.000	***
Leverage	−0.655	0.122	0.000	***	−0.652	0.122	0.000	***
ROE	0.070	0.020	0.000	***	0.069	0.020	0.000	***
R&D	0.011	0.003	0.001	***	0.011	0.003	0.001	***
Board independence	0.112	0.285	0.695	***	0.098	0.286	0.731	
Breadth					−0.158	0.079	0.046	**
Depth					0.261	0.123	0.034	**
N	15,647				15,647			
Log-likelihood	−3,361.23				−3,358.396			

Notes: ***$p < 0.001$, **$p < 0.05$, *$p < 0.10$.

Robustness Analysis

We conduct two additional tests to validate the robustness of our findings. First, we re-estimate Model 2 using alternative measures for two independent variables of Breadth and Depth based on the role of the executives. Specifically, CEOs and the chairman of directors are the two most important executives in making internationalization decisions (Du & Luo, 2016; Pan et al., 2014; Schweizer, Walker, & Zhang, 2019). Thus, political connections hold by the CEO and chairman are of great importance to OFDI. We use the total number of their political connections as the alternative measure of Breadth and the highest hierarchical level of their political connections as the alternative measure of Depth. The results are reported in Model 3 of Table 3. Breadth shows a negative but statistically insignificant ($p = 0.243$) impact on the firm's OFDI. Conversely, Depth shows a positive and marginally significant effect ($b = 0.031$, $p = 0.057$), supporting H2. In other words, CEOs and chairmen with connections to top-level government organizations are likely to promote the firm's OFDI.

Independent directors play an important advisory role in offering unbiased advice and perspectives to firms (Wang, Feng, & Xu, 2019). Their political connections can be valuable to the firms' resource acquisition and assist in strategic decision-making (Wang, 2015). Thus, we use the total number of political connections held by independent directors as another alternative measure of Breadth and the highest levels of their political connections (scaled by the number of independent directors) as a second alternative measure of Depth. The regression results are reported in Model 4 of Table 3. Breadth shows a negative and significant impact, whereas Depth exhibits a positive yet insignificant impact on OFDI. The finding is consistent with H1. Therefore, independent directors may utilize their political connections to assist the firm acquire essential resources in the domestic market, impeding the firm's likelihood of OFDI. This finding is consistent with the literature that many firms appoint politically connected independent directors so as to take advantage of their institutional resources to cope with domestic market challenges (Wang et al., 2019).

Second, we adjusted the measure of dependent variable to reflect the total number of OFDI projects conducted by the firm. Utilizing a negative binomial regression, we report the results in Table 4. In Model 5, the coefficient for the breadth of board members' political connection is negative and significant, confirming H1. In Model 6, which examines independent directors instead of the whole board of

Table 3. Robustness analysis using alternative political connection measures

	Model 3 (CEO/chairman)				Model 4 (Independent directors)			
	Est.	S.E.	$p > z$	Sig.	Est.	S.E.	$p > z$	Sig.
(Intercept)	−9.134	0.507	0.000	***	−9.196	0.508	0.000	***
Industry		(Included)				(Included)		
Year		(Included)				(Included)		
Sigma	−0.625	0.035	0.000	***	−0.624	0.035	0.000	***
Firm size	0.317	0.021	0.000	***	0.322	0.021	0.000	***
Leverage	−0.646	0.122	0.000	***	−0.646	0.122	0.000	***
ROE	0.070	0.020	0.000	***	0.070	0.020	0.000	***
R&D	0.011	0.003	0.001	***	0.011	0.003	0.001	***
Board independence	0.109	0.285	0.703		0.139	0.286	0.628	
Breadth	−0.024	0.020	0.243		−0.122	0.054	0.022	**
Depth	0.031	0.016	0.057	*	0.033	0.045	0.464	
N		15,647				15,647		
Log-likelihood		−3,359.398				−3,358.107		

Notes: ***$p < 0.001$, **$p < 0.05$, *$p < 0.10$.

Table 4. Robustness analysis using the number of OFDI projects

	Model 5 (Board of directors)				Model 6 (Independent directors)			
	Est.	S.E.	$p > z$	Sig.	Est.	S.E.	$p > z$	Sig.
(Intercept)	−22.002	0.583	0.000	***	−21.371	0.588	0.000	***
Firm size	1.071	0.026	0.000	***	1.047	0.026	0.000	***
Leverage	0.525	0.071	0.000	***	0.520	0.070	0.000	***
ROE	−0.023	0.025	0.350		−0.023	0.026	0.376	
R&D	0.007	0.003	0.018	**	0.007	0.003	0.008	***
Board independence	0.835	0.184	0.000	***	0.882	0.184	0.000	***
Breadth	−0.202	0.062	0.001	**	−0.223	0.038	0.000	***
Depth	0.080	0.085	0.347		0.092	0.030	0.002	***
N		13,530				13,530		
Log-likelihood		−4,637.983				−4,624.984		

Notes: ***$p < 0.001$, **$p < 0.05$, *$p < 0.10$.

directors, the number of OFDI projects increases with the depth and decreases with the breadth of political connections of independent directors. Hence, the results are consistent with both hypotheses.

Discussion

This study aims to enhance our understating of the role that (managerial) political connections play in a firm's internationalization strategy, with a particular focus on the context of OFDI. Differing to prior studies that often conceptualize and operationalize political connections in a monolithic manner and overlooks the heterogeneity of political connections in terms of government functions and political hierarchy, our study focuses on the political connection as a dual-dimensional construct: Breadth and Depth. Our results indicate that when firms have multiple political connections with various government organizations, the adverse effects of political connections dominate. Hence, the breadth of political connections causes firms to be less likely to engage in foreign investment activities. On the contrary, with firms that are politically connected with high-level government organizations (e.g., state, provincial), the positive effects of political connections prevail. Therefore, the depth of political connections leads firms to be more likely to initiate international expansion. Our findings underscore that the breadth and depth of political connections shape the firm's international investment strategy in a different way. Recognizing the heterogeneity of political connections and treating them as a multifaceted concept allow for a more nuanced understanding of their impact on strategic decisions related to OFDI. This approach helps to reconcile the mixed findings found in the existing studies, as our dual-dimensional approach captures the complexity and differentiated effects of political connections.

Theoretical Contributions

Our study offers a significant theoretical contribution to the literature on the nexus of political connections and firm internationalization. By combining resource dependency theory and the state capitalism perspective, we explain the characteristics of political connections and their impact on firms' international investments (Du & Luo, 2016; Hillman et al., 2009). Political connections are closely aligned with state capitalism, as they often play a crucial role in strategic decisions of firms within such an economic system. In state capitalism, cultivating political connections is crucial for firms to obtain institutional resources and government policy support to overcome constraints and uncertainties (Hillman, 2005; Peng & Luo, 2000; Pfeffer & Salancik, 2003; Sun et al., 2012). However, firms with connections to multiple government organizations are likely to experience a challenge of conforming with diverse, sometimes conflicting, government demands, which impose new uncertainties that divert firms' attention away from international expansion. Therefore, we argue that the breadth of political connections may hinder OFDI. Nonetheless, the primary interests of government at different hierarchical levels are aligned with the implementation of national policies. Compared with the non-connected ones, firms with political connections, especially at top levels (i.e., central, or provincial), are better positioned to gain institutional resources and support and exploit OFDI-related support, including information regarding foreign markets and diplomatic assistance. This enables firms to gain an advantage in pursuing international investments by mitigating the external uncertainties aboard. Hence, we argue that the depth of political connections promotes OFDI. In sum, our study enriches the application of resource dependency theory by combining it with the state capitalism perspective, providing a nuanced framework to explore the roles of managerial political connections in firm internationalization.

We also make a conceptual and empirical contribution to the debates on political connections and their impact by recognizing the multifaceted nature of these connections. Although recent studies have started to consider the heterogeneity of political connections, they still adopt a unitary approach with the concept and its measurements. Some studies recognize the differences in political hierarchical levels but remain to view all types of connections (connections with government organizations of different functions) as essentially similar, measuring the concept with multiple dummy variables. Others recognize the differences in government functions but do not consider connections of different levels as similar to each other and do not account for multiple connections held by one individual. They adopt a count-based or a share-based measure and quantify political connections by calculating the number of firm executives who have political connections (e.g., Bai et al., 2021; Guo et al., 2022; Wu & Ang, 2020). By recognizing that each political connection is unique and can bring specific institutional resources and support from those government organizations at different levels to the firm, we have considered (1) the number of political connections rather than the number of firm executives having political connections and (2) the connections between different government levels (e.g., one executive worked in several government organizations). We aim to reconcile prior inconsistent findings (see Appendix) by distinguishing political connections into two dimensions: Breadth and

Depth. Prior studies on the impact of political connections on firm internationalization report mixed findings. Under state capitalism, government objectives include influencing the firms' internationalization strategy. Significant research is required to explicate the mechanism through which the government offers institutional resources and support to achieve its political agenda. In this study, we argue that political connections play diverse roles in influencing OFDI through the burden of various government demands and the promotion of national policies. Empirically, we find that political connections are a double-edged sword for firms' OFDI decisions.

Managerial Implications

A better understanding of the intricacies of political connections enables firms to better leverage their non-market strategy and navigate the political landscape more effectively than their competitors. This study offers implications for business managers in large emerging economies with regional and complex hierarchical levels of political administrations. First, our findings demonstrate that the breadth of political connections is not beneficial for OFDI. Executives should conduct a thorough cost–benefit analysis to assess the value of maintaining numerous political connections for OFDI. While having broad political networks might offer some advantages, the costs associated with managing these connections may outweigh the benefits, particularly when firms aim to pursue internationalization. In this case, executives need to reduce their dependence on the large number of political connections to mitigate complexities and uncertainties. This entails streamlining their political connections and prioritizing the ones that offer the most strategic value to support internationalization. This helps firms to minimize the risk of conflicting demands and better respond to diverse requirements of various government organizations. Meanwhile, policymakers need to develop rules and regulations that promote effective communication and collaboration across different government organizations, creating a more cohesive regulatory environment.

Second, our findings show that the depth of political connections facilitates firms' OFDI. It suggests that firms need to actively develop relationships with the top-level government officials. These relationships can provide crucial support and facilitate international expansion. Board directors need to invest in political networking to cultivate personal connections with government officials and agencies at top levels and maintain ongoing relationships (Li & Zhang, 2007). They should proactively seek opportunities to deepen their political connections through participation in high-level forums and central government-led initiatives. On the policy hand, policymakers should establish frameworks that facilitate collaboration between firms and top-level government officials, such as creating platforms for interactions and cooperation.

In conclusion, board directors must strategically balance the breadth and depth of their political connections to optimize their pursuit of OFDI. Policymakers can support these efforts by fostering a political environment and an economic system of state capitalism that encourages effective communication and collaboration among different government agencies and firms.

Limitations and Future Studies

Our study has three limitations that provide promising avenues for future research. First, the strength of political connections may offer valuable insights to address the research question (e.g., Granovetter, 1973). A possible method to define and measure strong ties could be 'friendship with a head of state, government minister, or member of parliament' (Faccio, 2010: 907). However, our data lack such detailed information. Future studies could enrich this area by collecting data from interviews with firm executives (Peng & Luo, 2000). Second, although we account for the heterogeneity of political connections, we have not considered the role of managerial political networks. Network structures, such as centrality (Wu et al., 2021), connectedness, and cluster, can highlight the significance of different government organizations, which further influences the internationalization of firms. Third, our theoretical rationale builds on the state capitalism perspective. State capitalism manifests in various forms globally (Wright et al., 2021), and political connections are a universal phenomenon (Wei et al., 2023). While our hypotheses are formulated with broad applicability in mind, our empirical testing is confined to a single-country context. Although there are similarities between China and other interventionist entrepreneurial states (e.g., Brazil, Hungary, Kazakhstan, and Russia) (Wright et al., 2021), there are also other types of state capitalism with varying degrees of state ownership, statism ('the ability of the state to enter economic transactions with the business', p. 8), and government threat ('how government use tools or mechanisms to intervene in economic activities', p. 8). Further research across diverse contexts is essential to corroborate our findings.

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Data availability statement. Most of the data used in this study were obtained from the China Stock Market & Accounting Research (CSMAR) database, which is not publicly available. Access to the CSMAR database requires a paid subscription or purchase. Data on whether firms engaged in OFDI were sourced from the Directory of Overseas Investment Institutions of Chinese Enterprises published on the website of the MOC in 2020. However, the web link to this data is no longer operational.

Appendix

A Summary of Firm-Level Studies on the Effects of Political Connections on Internationalization

Study	Conceptualization of political connection	Political connection measure		Internationalization measure	Finding
Pan et al. (2014)	Political connection or political tie is conceptualized as 'the connection of the firm to the legislative branch of the home country government' (p. 1030).	Dummy	*Legislative connections of CEO/chairman, board member, or large shareholder (>10%)*	Foreign subsidiary ownership level	+
Liang et al. (2015)	Political connection is conceptualized as a way of control, i.e., '…*political connection control* functions in the opposite way in globalization. … the administrative institutional environment was conducive to the use of political personnel control to influence SOE managers' decision making …' (p. 226).	Dummy	*Managerial political connections*	Globalization propensity (pre-reform)	+
				Globalization propensity (post-reform)	–
		Ratio	*Board political connections*	Globalization propensity (pre-reform)	+
				Globalization propensity (post-reform)	n.s.
Du and Luo (2016)	Political connection is conceptualized as managers' prior political backgrounds (p. 104), which implies ties with political organizations.	Dummy	*Political experience of CEO/chairman*	Ratio of foreign sales to total sales (FSTS)	–
				Internationalization dummy indicating whether FSTS > 0	
Ma et al. (2016)	Political connection is conceptualized as 'political capital with high and low levels of government' and in the context of China, 'high-level (including the central and provincial-level) and low-level (including municipal-, county-, and township-level) governments show significant differences in size, responsibility, authority, and efficiency' (p. 846).	Dummy	*Political capital with a high-level government*	FSTS	n.s.
			Political capital with a low-level government		+

(*Continued*)

(*Continued*.)

Study	Conceptualization of political connection	Political connection measure		Internationalization measure	Finding
Deng et al. (2018)	Political connection is conceptualized as 'formal and informal ties between firms and the state' (p. 893) and can be differentiated into ascribed political connections arising from dominant-state ownership and acquired political connections 'if [a firm's] executives participate actively in activities of the government legislation bodies or the military' (p. 894).	Dummy	*Acquired political connections*	OFDI propensity	+
				OFDI project number	+
		Dummy	*Ascribed political connections*	OFDI propensity	–
				OFDI project number	–
Bai et al. (2019)	Political connection is conceptualized as '[a] firm's connections to the government in the home country' (p. 545).	Count	*Number of TMT/board members who are politically connected*	FSTS	–
Schweizer et al. (2019)	Political connection is conceptualized as the connections of TMT members with the government (p. 65).	Dummy	*Politically connected CEO/chairman*	CBMA completion	+
Deng et al. (2020)	Political connection is conceptualized as 'the political status of emerging market firms … namely, (a) central SOEs, (b) local SOEs, (c) private firms with political connections, and (d) private firms without political connections' (p. 472).	Dummy	*Central SOEs, local SOEs, private firms with political connections, private firms without political connections*	OFDI propensity OFDI project number	+
Wu and Ang (2020)	Political connection is conceptualized as '[d]omestic political ties … when senior managers concurrently hold or have previously held senior positions in key government or political organizations, or when senior politicians or government officials concurrently hold or have previously held top positions in firms …' (p. 2).	Count	*Sum of individual's domestic political ties across the TMT members*	OFDI propensity	+
Fung et al. (2020)	Political connection is conceptualized as 'a unique managerial resource in emerging economies' (p. 3) and concerns whether 'top leader (Board chair or CEO) is politically connected based on either one of the conditions: (1) they once worked or currently work in a national or provincial government	Dummy	*Politically connected CEO/chairman*	OFDI propensity Foreign subsidiary number	+

(*Continued*)

(*Continued.*)

Study	Conceptualization of political connection	Political connection measure		Internationalization measure	Finding
	agency, including ministries, bureaus, commissions, courts of law etc.; or (2) they were or currently are a member of national or provincial legislations and other similar institutes, including the People's Congress and the People's Political Consulting Committee' (p. 5).				
Sharma et al. (2020)	'Political connections are defined as informal social connections with officials at various levels of administration in the local, state or central government and regulatory agencies such as tax authorities, securities commission, and stock exchanges' (p. 25).	Ratio	*Ratio of the number of political connections held by board members*	Export dummy	–
Bai et al. (2021)	Political connection is conceptualized as connections with the home country government through two mechanisms: legislative-branch and executive-branch (p. 5) and legislative-branch political connections refer to 'the TMT and board members who are delegates either to the People's Congress or to the Chinese People's Political Consultative Conference', whereas executive-branch political connections are about 'the TMT and board members who have formerly worked in a government institution' (p. 6).	Count	*Legislative-branch political connections*	OFDI project number	n.s.
		Count	*Executive-branch political connections*		–
Lebedev et al. (2021)	Political connection or political ties is conceptualized as 'boundary-spanning personal and institutional linkages between firms and the constituent parts of public authorities' (p. 2).	Ratio	*Ratio of the number of directors with political connections*	Degree of internationalization index	–
Wu et al. (2021)	Political connection or political ties is conceptualized as TMT's 'personal ties with governments and its agencies' (p. 5).	Count	*Sum of individual's domestic political ties across the TMT members*	Likelihood of entering a foreign market	+

(*Continued*)

(*Continued.*)

Study	Conceptualization of political connection	Political connection measure		Internationalization measure	Finding
Guo et al., (2022)	Political connection is conceptualized as 'both formal and informal connections between firms and local (national) governments' (p. 536).	Dummy	*At least one TMT and board members with political connection*	Greenfield value Greenfield number Greenfield dummy	–
		Count	*Sum of TMT and board members with political connection*		
		Ratio	*Share of TMT and board members with political connection*		
Li et al. (2022)	Political connection is conceptualized as 'a bridge between entrepreneurs and government officials, political participation' (p. 1063), and '*Primary* political participation refers to 'participation in the formation and execution of public policy through legally sanctioned channels, such as Congress… *secondary* political participation refers to participation in the formation and execution of public policy through government-controlled or government-sponsored channels, such as industry associations' (p. 1064).	Dummy	*Primary political participation (at national and/or provincial level)*	Engagement in high-commitment entry mode	+
			Secondary political participation (government-directly controlled industry association or a government-partiallysponsored federation of industry and commerce)		+

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