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31 December 2010

Online at <https://mpra.ub.uni-muenchen.de/29184/>

MPRA Paper No. 29184, posted 22 Mar 2011 13:52 UTC

**Political Connections and Minority-Shareholder Protection:  
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Forthcoming: *Journal of Financial and Quantitative Analysis*

This Draft: March 25, 2009

We thank Ben Jacobsen, Paul Koch, Woody Wu, Jin Xui, seminar participants at DePaul University, George Washington University, Hong Kong University of Science and Technology, Monash University, University of Sydney, 2004 Australasia Finance and Banking Conference, 2004 China International Finance Conference, 2005 International Conference on Corporate Governance in Asia and China, 2005 Financial Management Association Annual Meeting, 2008 New Zealand Finance Colloquium, and 2009 American Finance Association Annual Meeting, and an anonymous referee for their helpful comments on earlier drafts.



**Political Connections and Minority-Shareholder Protection:  
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**Abstract:**

We examine the wealth effects of three regulatory changes designed to improve minority-shareholder protection in the Chinese stock markets. Using the value of a firm's related-party transactions as an inverse proxy for the quality of corporate governance, we find that firms with weaker governance experienced significantly larger abnormal returns around announcements of the new regulations than did firms with stronger governance. This evidence indicates that securities-market regulation can be effective in protecting minority shareholders from expropriation in a country with weak judicial enforcement. We also find that firms with strong ties to the government did not benefit from the new regulations, suggesting that minority shareholders did not expect regulators to enforce the new rules on firms where block holders have strong political connections.

**JEL classifications:** G32, G34, G38

**Keywords:** China, corporate governance, enforcement, expropriation, political connections, investor protection, minority shareholder, regulation, tunneling

## **Political Connections and Minority-Shareholder Protection: Evidence from Securities-Market Regulation in China**

### **I. Introduction**

Recent studies of corporate ownership around the world have found that diffuse ownership is relatively uncommon and most corporations are controlled by large block holders (see, e.g., La Porta, Lopez-di-Silanes, Shleifer and Vishny (1998), La Porta, Lopez-di-Silanes and Shleifer (1999), and Holderness (2008). Consequently, the primary concern of corporate governance has broadened from mitigating the agency conflicts between firm managers and diffuse shareholders (Berle and Means (1932), Jensen and Meckling (1976)) to protecting minority shareholders from expropriation by a controlling block holder and her management team (Shleifer and Vishny (1997), Johnson, La Porta, Shleifer and Vishny (2000)).<sup>1</sup>

In discussing needed governance reforms, La Porta, Lopez-de-Silanes, Shleifer and Vishny (2000) suggest that countries change the “rules and enforcement mechanisms” for protecting investors “towards some successful standard,”—a process they refer to as “legal convergence.” La Porta, Lopez-de-Silanes, Shleifer and Vishny (2002) support this guidance by demonstrating that firms in countries with better investor protection are more valuable than firms in countries with poorer investor protection.

In this study, we examine the market reactions to three examples of “legal convergence” that occurred in China when the government’s Chinese Securities Regulatory Commission (“CSRC”) introduced new regulations aimed at reducing expropriation from minority shareholders by controlling block holders. The three regulations were all introduced in the second quarter of 2000 and were partly motivated by China’s successful attempt to gain entrance into the World Trade Organization. The first new regulation substantially increased the rights of minority shareholders at a firm’s Annual Shareholders’ Meeting. Most importantly, the new regulation prohibited shareholders involved in related

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<sup>1</sup> Djankov and Murrell (2002) and Denis and McConnell (2003) provide surveys of the literature on international corporate governance.

party trading from voting on the related party trading. The second regulation prohibited the issuance of loan guarantees by a firm to its controlling shareholder, and the third regulation improved the transparency and regulation of asset transfers to related parties.<sup>2</sup>

Following Chhaochharia and Grinstein (2007), we use standard event-study methodology to analyze the link between investor protection and firm value, thereby reducing potential endogeneity problems inherent in the use of cross-sectional regressions. The causality between shareholder protection and firm value is clear: value changes, if any, are the result of the market's assessment that corporate governance has improved, reducing expected future expropriation of minority shareholders.

The prediction that share prices increase around the introduction of the new regulations assumes that the new regulations will be enforced by the regulator. This is consistent with the theoretical model of Glaeser, Johnson and Shleifer (2001), which predicts that, in emerging markets with relatively weak legal systems, regulators can provide an effective substitute for ineffective judicial enforcement. An alternative view is that the new regulations will not be enforced or will be enforced selectively, favoring companies with strong links to the government. If this is the case, we expect to see no or only a weak price reaction around the introduction of the new regulations, especially for firms most closely linked to the Chinese government.

The first part of our empirical analysis provides evidence of a ten-percent positive share market reaction around the introduction of the first regulation. This finding offers support for the model of La Porta et al. (2002, p.1168), which predicts that "poor shareholder protection is penalized with lower valuations." The market-wide price reactions around the second and third events are also positive but statistically insignificant. We discuss several reasons why our tests of market-wide price reactions might

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<sup>2</sup> The regulatory changes reflect the commitment of the Chinese government to improve corporate governance. The World Bank (2002, p. 102) concludes that "corporate governance has moved to the center stage of enterprise reform in China," and (p. 1) that many of the requirements for listed companies are "even stricter than in Hong Kong and other developed markets...and show the authorities' determination to protect minority shareholders."

have limited power to test the impact of the regulatory events. The most important reason is that the regulations might have benefited only specific subsets of firms—for example, firms with the weakest governance or firms with the weakest ties to the government.

Consequently, we focus on cross-sectional models in the remainder of our analysis, utilizing the expected differential reactions to the regulations by different subsets of firms. More specifically, we test the hypothesis that effective regulation will result in larger value increases for minority shareholders of firms that are more likely to be subject to expropriation by controlling block holders.

In our first set of cross-sectional tests, we use the total value of all potentially damaging related-party transactions occurring during the year before the regulations were introduced as a proxy for the degree of expropriation from minority shareholders.<sup>3</sup> Around all three events, we find that minority shareholders in firms with higher total values of related-party transactions experienced significantly larger abnormal returns than minority shareholders in firms with lower or zero total value of related-party transactions. This is strong evidence that investors perceived the regulations as effective.

We also find that, for the group of firms with the most direct ties to the Chinese government, abnormal returns are unrelated to the value of related party transactions. This latter result suggests that investors were skeptical that the CSRC—a State-controlled regulator—would enforce the new regulations at firms with close ties to the government.

Our second set of cross-sectional tests analyze the relation between abnormal returns and less direct measures of expropriation by the controlling block holder, such as the cash-flow rights and identity of the controlling block holder, the presence of foreign shareholders, and the total shareholding of non-controlling block holders. Our results suggest that minority shareholders of firms with weak corporate governance benefit disproportionately from the new regulations in the form of higher abnormal returns.

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<sup>3</sup> Related-party transactions include transactions between the listed company and either its large shareholders or entities controlled by those shareholders.

This finding is consistent with the argument in Klapper and Love (2003) that shareholders of firms with weak governance are more reliant upon legal and regulatory protection from expropriation by controlling block holders. Moreover, consistent with the notion that regulators selectively enforce the new regulations, we find that minority shareholders in firms with private controlling block holders enjoy the largest value increases around the announcement of the new regulations.

We contribute to the literature in at least four ways. First, we contribute to the literature on regulation as a substitute for judicial enforcement (La Porta et al. (2000), Glaeser, Johnson and Shleifer (2001), Klapper and Love (2003)). Using robust event-study methodology, we find significant positive abnormal returns accrue to firms with weak governance as proxied by the value of related-party transactions and a variety of less direct measures. We interpret these results as evidence that securities-market regulation can be effective in protecting minority shareholders from expropriation in a country with weak judicial enforcement

Second, we contribute to the literature on “tunneling” (Johnson et al. (2000)) that analyzes related-party transactions between listed firms and their controlling block holders (Cheung, Jin, Rau and Stouraitis (2007), Cheung, Rau and Stouraitis (2006), La Porta, Lopez-de-Silanes and Zamarripa (2003)). We use the value of related-party transactions to calculate our proxy for the degree of expropriation by controlling block holders and provide evidence that regulations designed to protect minority shareholders disproportionately benefited firms with higher values of related-party transactions.

Third, we contribute to the literature on the importance of political connections (Fisman (2001), Johnson and Mitton (2003), Faccio, Masulis and McConnell (2006), Fan, Wong and Zhang (2007), and Cheung et al. (2007)). We provide new evidence that, in a country with a weak judicial system, such as China, investors are skeptical that regulators will undertake actions that might harm controlling block holders with strong political connections. Specifically, we find that announcements of regulations designed to protect minority shareholders from expropriation by controlling block holders led to greater increases in value at firms with private block holders than at firms with government block holders, with market-oriented State-owned enterprises block holders falling in between.



Finally, we contribute to the growing body of work on corporate governance in China (Sun and Tong (2003), Cull and Xu (2005), Allen, Qian and Qian (2005), Wei, Xie and Zhang (2005), Fan, Wong and Zhang (2005, 2007))—especially the group of studies that have abandoned the “official” ownership scheme, which classifies owners of non-tradable shares primarily into two categories—*State Shares* and *Legal-Person Shares*—in favor of classifications based upon the identity of the ultimate owner (Firth, Fung and Rui (2006), Berkman, Cole and Fu (2007, 2009), Chen, Firth and Xu (2009)).

In the remainder of the article, we proceed as follows. Section 2 describes some of the salient institutional details of the Chinese share markets, while Section 3 describes each of the three regulatory changes designed to improve the protection of minority shareholders. In Section 4, we describe our data and methodology and develop our hypotheses. In Section 5, we present our results, which are followed by a summary and conclusions in Section 6.

## **II. Institutional Details of the Chinese Share Markets**

During the 1990s, the Chinese government corporatized and partially privatized almost a thousand State-owned enterprises (SOEs) through share-issuance privatizations on the two primary Chinese stock exchanges—the Shanghai Stock Exchange (SHSE) and the Shenzhen Stock Exchange (SZSE). The corporatization and share-issuance privatization of large SOEs were central elements of the Chinese strategy towards creation of a “modern-enterprise system.”<sup>4</sup>

In China, there are two official types of controlling block holders: holders of *State* shares and holders of *Legal-Person* shares. *State* shares are those held by government agencies (e.g., the Bureau of State Property Management and local finance bureaus) and by some types of corporatized SOEs. *Legal-Person* (LP) shares are those owned by domestic corporations or other non-individual legal persons. Like

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<sup>4</sup> Jones, Megginson, Nash and Netter (1999) coin the term “share-issuance privatizations.” Sun and Tong (2003) evaluate the changes in financial performance of Chinese firms following their share-issuance privatizations.

*State* shares, *Legal-Person* shares cannot be traded on the two exchanges or transferred to foreign investors, but can be transferred to domestic corporations, when approved by the CSRC.

Individuals and domestic corporations are allowed to hold *Tradable-A* shares. *Tradable-A* shares are the only type of equity that can be publicly traded among domestic investors. Since December 16, 1996, both the Shanghai and Shenzhen Stock Exchanges have used a daily price limit of 10% based on the previous day's closing price for each stock. In this study, the market price of a listed company refers to the price of *Tradable-A* shares, and the prices of such shares are used to measure the valuation effects of the regulations aimed at improving the protection of minority shareholders.<sup>5</sup>

Regulators typically required that *Tradable-A* shares account for more than 25% of total outstanding shares when a company went public. Until July 1999, individuals were prohibited from holding more than 0.5% of total shares outstanding for any listed company; subsequently, the legal maximum for individual shareholders was increased to 5.0%. The legal maximum for individual shareholdings and the absence of cumulative voting procedures significantly enhance the control rights of a firm's largest shareholder. The World Bank (2002, p. xiii), concluded that, in China, “. . . large shareholders often overstep the bounds of shareholder meetings and boards of directors and exercise direct effective control.”

There are serious shortcomings in the official share classification for any analysis of corporate governance at listed firms in China. To illustrate the confusion, we refer to Table 5 in Delios, Wu and Zhou (2006), where the authors report the overlap between their 17 (ultimate) ownership categories and the official Share Classification. For example, of the 556 times a State

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<sup>5</sup> In addition to domestic shares, some firms have issued *foreign shares* (B-, H- and N-shares). B-shares are available to foreign investors and are traded on the two domestic exchanges, whereas H- and N-shares have an overseas listing. The governance structure for firms with an overseas listing is more restrictive, and we exclude firms with H- or N-shares from our later tests (see Xu and Wang, 1999).

Asset Management Bureau (SAMB) was classified as a top-10 shareholder of a listed firm in their sample, the SAMB was officially classified as holder of State shares 105 times (19%), as a Legal Person shareholder 221 times (40%), and, in 230 cases, as *Tradable-A* shareholder or “Other”. Similarly, private corporations were officially classified as holders of *State* shares in 7.4% of the cases, as holder of *Legal-Person* shares in 59.8% of the cases, and as holder of *Tradable-A* shares or “Other” in 32.8% of the cases.

Because of these ambiguities, we adopt the classification scheme of Chinese ownership developed by the National University of Singapore (“NUS”) Business School and described in Delios et al. (2006). NUS staff has analyzed the top ten block holders of each publicly traded Chinese firm over the period 1994 – 2002, and categorized each into one of 17 detailed categories. NUS has generously made these ownership data publicly available.<sup>6</sup>

Based upon NUS’ detailed classifications, we define three broad groups of ultimate owners. The groups are as follows (where we reference the Delios, Wu and Zhou (2006) detailed-classification number in parentheses).

*State Bureaucrats* includes central government (1); local governments (2); government ministries (3); government bureaus (4); State asset-investment bureaus (6); State asset-management bureaus (7); State research institutes (10); and State-owned banks (16).

*Market-Oriented SOEs* includes companies that formerly were government ministries (5); market-oriented state-owned enterprises (9); and infrastructure-construction companies (8).

*Private Entities* includes security companies (11); investment funds (12); private companies (13); private individuals (14); foreign companies and individuals (15); and work unions (17).

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<sup>6</sup> The ownership data constructed by Delios et al. (2006) are available for download from <http://www.bschool.nus.edu.sg/staff/bizakd/owner.htm>. The 17 detailed ownership classifications are described in Delios (2006), which documents the downloadable database.

We define these three broad groupings based on the closeness of the block holder's ties to the government, as well as upon the incentives and experience of the block holders. *State Bureaucrats* have the most direct ties to the State, as these block holders are (an integral part of) the government, government agencies, or government institutions. *MOSOE*s have the next closest ties to the State, as they are controlled by the State, but have been through a transition towards the market-oriented structure of for-profit organizations. *Private Entities* have the least direct ties to the State, in that their management is controlled by private firms and/or investors, even if the State has a partial ownership stake.

Beyond their closeness to the State, these three broad groupings also differ with respect to incentives and experience. *State Bureaucrats* typically have the least experience in running a company and are less concerned about the profits of the firm. *MOSOE*s are corporations with more experience in running a company and a stronger focus on profit-maximization. *Private Entities* have the greatest incentive to maximize profits because they receive the greatest degree of rewards based upon financial performance.

### **III. Regulations to Improve Minority Shareholder Protection**

In China, minority-shareholders enjoy only moderate legal protection against expropriation. Based on the index of investor protection developed by La Porta et al. (1999), MacNeil (2002) calculates an index score of two for China compared with a world average of three and a maximum of six. Djankov, La Porta, Lopez-de-Silanes and Shleifer (2008) construct an index of ex-post private control of self-dealing, and calculate a value of 0.53 for China as compared with a 0.52 world average.

The CSRC is designated as the regulator for securities activities. The CSRC has wide-ranging powers in respect of authorization, rule-making, investigation and enforcement of all aspects of the securities markets (see Zhu (2000)). The regulatory changes that we study were the first substantial improvement in minority-shareholder protection implemented by the CSRC, and suggest an increased willingness by the Chinese leadership to subordinate the interests of controlling block holders (usually the State) to the interests of other shareholders (MacNeil (2002) and World Bank (2002)). Consistent with the

argument in Glaeser, Johnson and Shleifer (2001), we expect that the regulation and enforcement by a specialized and relatively efficient regulator is an effective substitute for judicial enforcement.<sup>7</sup>

The three regulatory changes we study were announced within a two-month period during early 2000. We briefly review each regulation in this section and refer the reader to Appendix I for a more detailed description of each.

The first event is the introduction of a regulation that substantially increased the voting rights of minority shareholders at shareholder meetings. Among other things, this new regulation: prohibited shareholders involved in related party trading from voting at the shareholding meetings on the related party trading; empowered small shareholders to propose motions at a firm's shareholders Annual Meeting; required that candidates for directors be voted on individually rather than as a group; and granted new legal standing in Chinese courts to shareholders disputing procedures used or resolutions passed at a firm's Annual Meeting.

The second regulation prohibited a listed firm from issuing a loan guarantee to its controlling shareholder or related party. The third regulation greatly improved the transparency and regulation of asset transfers to related parties.

We expect the strongest market reaction to the first regulation since it is likely to have the greatest element of surprise and to have the widest impact because it affects all kinds of related-party transactions. The second and third regulation reinforced the signal to the market from the first regulation that the Chinese government was committed to improve corporate governance. In addition, these last two regulations are easy to monitor, and reduce the ability of controlling block holders to expropriate minority

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<sup>7</sup> Chen, Firth, Gao and Rui (2005) argue that the CSRC is not a "toothless tiger." They show enforcement actions by the CSRC result in negative stock returns, more frequent auditor changes and more frequent CEO dismissal. Chen, Firth, Gao and Rui (2006) report a marked increase in regulatory enforcement cases by the CSRC, rising from a total of only 18 in 1999 to a total of 69 in 2001.

shareholders in a very direct way. The following sections examine the effects of the introduction of the new regulations on the value of *Tradable-A* shares in the Chinese share markets.

#### **IV. Methodology and Data**

We use standard event-study methodology to analyze the link between investor protection and firm value. In addition to reducing potential endogeneity problems inherent in the use of cross-sectional regressions that relate investor protection to firm value, event studies analyze the change in value for the same sample of firms before and after the changes in the regulatory environment. As a result, we do not need to control for firm heterogeneity. A disadvantage of our approach is that market participants might anticipate the regulatory changes, in which case our results provide only a partial estimate of the value changes resulting from improving corporate governance.

##### **A. Market-Wide Cumulative Abnormal Returns**

To test the overall market impact of the new regulations, we form an equally weighted portfolio of all 887 sample firms (see below) and analyze the cumulative abnormal returns around the event. Our event window is taken from one day before the CSRC release of the new regulations until one day after the regulation was first published in the newspaper (Appendix I lists the exact dates for each event). We choose this definition of the event period, which results in relatively long event windows, based on our observation that share prices react around both the initial CSRC release day and the subsequent newspaper announcement. We conjecture that the prolonged reaction is the result of the initial release to a limited number of market participants including the securities regulatory offices, the stock exchanges, and the listed companies. The restricted release makes it likely that many, if not most, minority shareholders receive the information only after publication in the newspapers.

We estimate two models to test the market-wide price reaction to the regulatory changes. First, we estimate the cumulative mean-adjusted returns around each event using the following model:

$$(1) \quad \text{MARKET RETURN}_t = \beta_0 + \sum \beta_J \text{EVENT}_J + \varepsilon_t, \quad J = 1 \text{ to } 3$$

where:

MARKET RETURN<sub>*t*</sub> is the return for day *t* on the equally weighted market portfolio of firms only listed on the Chinese stock exchanges;<sup>8</sup>

$\beta_0$  is the mean portfolio return during the sample period;

EVENT<sub>*J*</sub>, *J* = 1 to 3, are dummy variables that equal 1 / *n<sub>J</sub>* for the dates within the event window of length *n<sub>J</sub>* days for the *J*th regulation, and 0 otherwise, where *n<sub>1</sub>* = 11, *n<sub>2</sub>* = 10 and *n<sub>3</sub>* = 23;<sup>9</sup>

$\beta_J$ , *J* = 1 to 3, are the estimated cumulative mean-adjusted returns during each event window *J*;

$\varepsilon_t$  is an i.i.d. random-error term for day *t*.

Second, as a robustness check intended to control for market-wide price movements unrelated to the regulations, we estimate a model that includes the contemporaneous return on an equally weighted portfolio of 24 firms from China that are listed on the Hong Kong Stock Exchange (HK RETURN<sub>*t*</sub>).<sup>10</sup>

The empirical model is:

$$(2) \quad \text{MARKET RETURN}_t = \beta_0 + \sum \beta_J \text{EVENT}_J + \beta_4 \text{HK RETURN}_t + \varepsilon_t$$

where:

HK RETURN<sub>*t*</sub> is the return for day *t* on the equally weighted portfolio of 24 firms from China that are listed on the Hong Kong Stock Exchange; and

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<sup>8</sup> When we use a value-weighted market index, we find similar results.

<sup>9</sup> We define the dummy variable as equal to 1/*n*, where *n* is the length of the event window, so that the coefficient on our dummy variable measures the cumulative adjusted return over the entire event window. Were we to define the dummy variable as equal to 1, then the coefficient would instead measure the average daily adjusted return over the event window.

<sup>10</sup> These firms have their headquarters and business activities in mainland China, but their shares are only listed on the Hong Kong Stock Exchange. We expect that the new regulations are of little importance to these firms, as Chinese companies with an overseas listing are subject to additional provisions in their articles of association that already substantially limited the power of their controlling shareholders. MacNeil (2002, p. 51) argues that the amendments in the articles of overseas listed firms “should be viewed as a considerable enhancement of the governance structure by comparison with domestic-only listed Chinese companies.”

MARKET RETURN  $\epsilon_t$ ,  $\beta_0$ , EVENT  $J$ ,  $\beta_J$  and  $\epsilon_t$  are defined as above.

We estimate each model over a period of 250 trading days that ends July 25, 2000—one day after the newspaper release of the asset transfer regulation (event 3).

As another test of robustness, we re-estimate equation (1) and equation (2) where we redefine the event windows to incorporate, for each regulation, two five-day event windows centered on the CSRC release date and first publication date. This shortens the length of our event windows so as to limit the effects of potentially confounding events. We refer to these as *Five-day Event Windows* whereas we refer to our primary windows as *Long Event Windows*.<sup>11</sup>

#### B. Cross-Sectional Differences in Cumulative Abnormal Returns

In addition to testing market-wide changes in value attributable to improved shareholder protection, we also test whether the new regulations have differential impacts on firms depending on the extent to which minority shareholders might be expropriated by the controlling block holders. We expect that firms where minority shareholders face greater expropriation should disproportionately benefit from the new regulations. In our first set of cross-sectional tests, we use the total value of the related-party transactions in the year preceding the announcement of the new regulations as an observable proxy for (potential) minority shareholder expropriation. We refer to this measure as EXPROP. We hypothesize that, during the event windows, firms with high values of EXPROP outperform firms with low values of EXPROP.

We also test whether the identity of the controlling block holder influences the relation between EXPROP and changes in firm value. Specifically, we test whether the relation is stronger among firms controlled by State Bureaucrats, MOSOEs or Private Entities. Because State Bureaucrats have the closest ties with the Chinese government, we conjecture that State Bureaucrats are least likely to be the target of regulatory action aimed at reducing expropriation. Consequently, we conjecture that, among firms that

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<sup>11</sup> We have estimated both models over longer periods of 500 and 750 trading days, and have extended model (2) by including the world market index. The results are robust to these changes.



have substantial related-party transactions, the beneficial effects of the new regulations is smallest for minority shareholders in listed firms controlled by State Bureaucrats. Similarly, because Private Entities have the weakest links with the government, we conjecture that minority shareholders of listed firms controlled by Private Entities will gain most from the new regulations.

In our second set of cross-sectional tests, we use several more indirect proxies of the likelihood of minority shareholder expropriation. In these tests, we focus on the hypothesis that shareholders of firms with weak governance are more reliant upon legal and regulatory protection from expropriation by controlling block holders than are shareholders of firms with strong governance (Klapper and Love (2003)). Therefore, shareholders of firms with weak corporate governance should benefit disproportionately from the new regulations.

As proxies for the quality of firm-specific corporate governance, we use: the cash-flow rights of the controlling shareholder, the type of controlling shareholder (“STATE BUREAUCRAT,” “MOSOE,” and “PRIVATE ENTITY”), the dominance of the controlling shareholder (“NON-CONTROLLING BLOCK HOLDERS”) and the presence of foreign shareholders (“B-SHARES”). In addition, we include dummy variables that indicate whether the CEO is the Chairman of the Board (“CEO IS CHAIR”) and whether or not the firm has at least one independent director (“INDEPENDENT DIRECTOR”).

### *C. Related-Party Transactions and Cumulative Abnormal Returns*

Cheung et al. (2006, 2007) classify related-party transactions into: i) transactions that are *a priori* likely to result in expropriation of the listed firm’s minority shareholders; ii) transactions likely to benefit the listed firm’s minority shareholders; and iii) strategic transactions that are, perhaps, not expropriation. Our direct, firm-specific measure of expropriation—EXPROP—is defined as the sum of the values of all transactions likely to result in expropriation of minority shareholders for each firm in 1999, scaled by the market capitalization of the firm as of the end of 1999.<sup>12</sup>

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<sup>12</sup> A list of the various types of related-party transactions is available from the authors on request. In calculating EXPROP, we exclude related-party transactions that are potentially beneficial to the firm. We obtain similar results

We hypothesize that, during the event windows, firms with high expropriation (proxied by high values of EXPROP) outperform firms with low expropriation (proxied by low values of EXPROP).<sup>13</sup> To test this hypothesis, we use a portfolio time-series regression, which is designed to deal with the econometric problem that arises when there is cross-correlation in the firm return processes from which the CARs are estimated. Cross-correlation is likely in our setting because, for each event, the event date and event windows are identical across sample firms. The portfolio time-series regression provides unbiased estimates of the coefficients along with standard errors that fully account for cross-sectional heteroskedasticity and cross-security dependence (see Sefcik and Thompson (1986)).<sup>14</sup>

We implement the portfolio time-series approach by forming a portfolio that is long in high-EXPROP firms and short in low-EXPROP firms. We define high-EXPROP firms as those in the highest EXPROP tercile and low-EXPROP firms as those in the lowest EXPROP tercile. As a test of robustness, we also show results for portfolios based upon the lower half (lowest fifth) and upper half (highest fifth) of the EXPROP distribution. We hypothesize that the regulatory changes are more beneficial for firms with high expropriation than for firms with low expropriation. In other words, we expect our portfolio to have positive abnormal returns during the event periods. To control for market risk, we include the return on an equally weighted portfolio of firms listed on the Chinese stock exchanges:

$$(3) R(\text{HIGH-EXPROP}_t) - R(\text{LOW-EXPROP}_t) = \beta_0 + \sum \beta_j \text{EVENT}_j + \beta_4 \text{MARKET RETURN}_t + \varepsilon_t$$

where:

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if we use alternative definitions of potentially beneficial transactions, if we use the unscaled value of related-party transactions, and if we scale by total assets or total revenue.

<sup>13</sup> This hypothesis rests on the assumption that investors are able to identify and discount firms with a high level of expropriation. In the results section, we present evidence that strongly supports this assumption.

<sup>14</sup> The problems of heteroskedasticity and cross-sectional dependence can, in principle, also be addressed in a generalized-least-squares (GLS) regression. Several studies, however, show that GLS tests are highly sensitive to errors in specifying the abnormal return model. (See, for example, Chandra and Balachandran (1990)).

$R$  (HIGH-EXPROP <sub>$t$</sub> ) is the return for day  $t$  on an equally weighted portfolio of the highest third (half, fifth) firms based upon EXPROP;

$R$  (LOW-EXPROP <sub>$t$</sub> ) is the return for day  $t$  on an equally weighted portfolio of the lowest third (half, fifth) firms based upon EXPROP;

$\beta_J$ ,  $J = 1$  to  $3$ , give the estimated differences in the cumulative abnormal returns (CARs) of the high-EXPROP and low-EXPROP portfolios during each event window  $J$ ; and

MARKET RETURN <sub>$t$</sub> , EVENT <sub>$J$</sub>  and  $\varepsilon_t$  are defined as above.

As before, we estimate the model over a period of 250 trading days that ends one day after the newspaper release of asset transfer regulation (Event 3).

#### D. Ownership Structure and Differences in Cumulative Abnormal Returns

Following La Porta et al. (2002), we assume that the ultimate owner of the largest shareholder has effective control over a firm. We consider three variables that might mitigate the incentive of the controlling shareholder to expropriate minority shareholders and positively impact a firm's value.

First, the incentive to expropriate outside investors is moderated by the cash-flow ownership of the controlling shareholder (see La Porta et al. (2002) and Claessens, Djankov, Fan and Lang (2002)). The greater are the cash-flow rights of the largest shareholder, the smaller is the difference in her cash-flow and control rights (where we assume that the ultimate owner of the largest shareholder has effective control). Hence, we expect the beneficial effect of the regulation for minority shareholders to decrease with the cash-flow rights of the controlling shareholder. Our empirical model includes a dummy variable CASH-FLOW RIGHTS > 30% that assumes a value of one if the largest shareholder owns more than 30% of all shares outstanding, and zero otherwise.<sup>15</sup>

Second, we define a variable that measures the control rights of the non-controlling block holders. NON-CONTROLLING BLOCK HOLDERS is equal to the sum of the shareholdings of the second

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<sup>15</sup> We would have preferred to use data on cash-flow rights and control rights of the ultimate controlling shareholder. Unfortunately this data for listed firms in China is only available from year-end 2002.

through tenth largest shareholder. Lins (2003) finds that large, non-management block holders can act as a partial substitute for weak institutional governance mechanisms. We expect the ability of the largest shareholder to expropriate firm value decreases as the relative shareholdings of block holders with the ability and incentive to monitor the actions of the largest block holder increase (see, for example, Bennesen and Wolfenzon (2000)).

Third, we include a dummy variable B-SHARE that is equal to one for firms having both A- and B-shares outstanding and equal to zero for all other firms. Some Chinese firms offer two classes of shares: Class-A shares, which can only be held by domestic investors, and Class-B shares, which can only be held by foreign investors.<sup>16</sup> Most Class-B shareholders are international financial institutions, whereas most Class-A shareholders are individual investors, with only limited ownership by domestic financial institutions (see Mei, Scheinkman and Xiong (2004)). In addition, firms with only Class-A shares use Chinese accounting rules (PRC GAAP) to prepare their financial statements, whereas firms with Class-A and Class-B shares report their results based on both PRC GAAP and International Accounting Standards (IAS). In general, IAS are regarded as providing superior transparency as compared to PRC GAAP (World Bank (2002)). Given these differences, we expect that controlling shareholders of firms with Class-B shares are less likely to expropriate minority shareholders.

We also include a variable that indicates whether the largest owner of the listed firm is a State Bureaucrat (“STATE BUREAUCRAT”), a MOSOE (“MOSOE”) or a Private Entity (“PRIVATE ENTITY”). As discussed before, the type of controlling block holder is important because it might proxy for the likelihood of regulatory action in case of expropriation by the controlling block holder. We expect regulators are most likely to pursue expropriation by private controlling block holders and least likely to pursue State Bureaucrat controlling block holders.

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<sup>16</sup> On February 19, 2001, the CSRC announced that Chinese citizens would be allowed to hold and trade Class-B shares.

Finally, we include dummy variables that equal one when the Chief Executive Officer is the Chairman of the Board, (“CEO IS CHAIR”) and when the firm has at least one independent director (“INDEPENDENT DIRECTOR”).

In estimating the association between the cumulative abnormal returns and the ownership variables, we include firm size and leverage as controls. FIRM SIZE is defined as the natural log of the total assets as per end of 1999. LEVERAGE is defined as the book value of debt divided by the book value of total assets.

As before, we employ the portfolio time-series regression methodology, which involves three steps. First, we orthogonalize our nine independent variables so that each has zero correlation with the other independent variables. Each of the nine variables is replaced by the residual from a regression of that variable on an intercept and the other eight independent variables. Second, for each of the nine orthogonalized variables, we construct a portfolio that is short on firms in the lowest third (half, fifth) and long on firms in the highest third (half, fifth) of the orthogonalized variable’s distribution. Third, we regress the returns for each of the nine portfolios on the market return and a dummy variable (EVENTS), using the following model:<sup>17</sup>

$$(4) R(OV-HIGH_t) - R(OV-LOW_t) = \beta_0 + \beta_1 \text{EVENTS}_t + \beta_2 \text{MARKET RETURN}_t + \varepsilon_t$$

where:

OV is one of nine orthogonalized variables—CASH-FLOW RIGHTS > 30%<sub>i</sub>, NON-CONTROLLING BLOCK HOLDERS<sub>i</sub>, B-SHARES<sub>i</sub>, MOSOE<sub>i</sub>, PRIVATE ENTITY<sub>i</sub>, CEO IS CHAIR<sub>i</sub>, INDEPENDENT DIRECTOR<sub>i</sub>, FIRM SIZE<sub>i</sub> or LEVERAGE<sub>i</sub>)

R(OV-HIGH<sub>t</sub>) is the return for day t on an equally weighted portfolio of the highest third (half, fifth) firms based upon orthogonalized variable OV;

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<sup>17</sup> We combine the three event-dummy variables (EVENT 1, EVENT 2, and EVENT3) into one dummy variable (EVENTS) that equals 1 / 44 during each day of the three event windows to increase the power of our tests. Results from analyzing each of the three events separately are available from the authors.

$R(OV-LOW_t)$  is the return for day  $t$  on an equally weighted portfolio of the lowest third (half, fifth) firms based upon orthogonalized variable  $OV$ ;

$EVENTS$  is a dummy variable that equals  $1/44$  for the dates within the three long event windows, and  $1/30$  for the dates within the three 5-day event windows;

$\beta_1$  gives the estimated difference in the cumulative abnormal return (CAR) of the high-OV and low-OV portfolios during the three event windows; and

$MARKET\ RETURN_t$  and  $\varepsilon_t$  are defined as above.

As before, the model is estimated over a period of 250 trading days that ends July 25, 2001.

#### E. Data

The data used in this study include information on accounting values, stock prices and ownership structure. We obtained accounting data and data on related-party transactions from the CSMAR/GTA database for 918 companies listed on the Chinese Stock Exchanges as of year-end 1999. We also obtained information on the number of independent directors, and the identity of the CEO and Chairman of the Board from CSMAR/GTA. We obtained daily share-price information for each of our sample firms from Datastream. Classification of the ten largest shareholders into State Bureaucrats, MOSOES, and Private Entities is based on Delios et al. (2006).<sup>18</sup>

From our initial sample of 918 firms, we delete 19 firms that are cross-listed on overseas exchanges (see footnote 8). We delete 2 firms for which we can not obtain sufficient information on the shareholdings of the largest 10 shareholders. Finally, we define 23 separate industry sectors at the level of two-digit standard industrial classification, which we obtained from the CSRC. To obtain reliable estimates of industry-adjusted  $Q$  for our sample firms, we delete 10 firms from our sample where there are fewer than five firms in the industry. The three sets of deletions leave us with a final sample of 887 firms.

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<sup>18</sup> The data are available from <http://www.bschool.nus.edu.sg/staff/bizakd/owner.htm>.

## V. Results

### A. Descriptive Statistics

Panel A of Table 1 presents descriptive statistics for the related-party transactions and shows that, in 1999, a total of 6,113 related-party transactions were recorded in the annual reports of our sample firms. Following Cheung et al. (2006, 2007), we classify 495 of these transactions as potentially beneficial for the listed company because it received cash, loans or guarantees from the related party. These transactions include fund transactions, guarantees or pledges and donations where the direction of the transaction is from the related party to the firm.<sup>19</sup>

#### INSERT TABLE 1

We classify the remaining 5,618 transactions as potentially harmful. Overall, the beneficial transactions have a value of RMB 39.77 billion whereas the harmful transactions have a value of RMB 296.34 billion.<sup>20</sup> Within the harmful transactions, the most numerous category involves sale or purchase of commodities (2,644) which also accounts for most of the aggregate value (RMB 211.22 billion or 71.5%); there also were 583 transactions involving provision of services, with a total value of RMB 13.76 billion or 4.7% and 540 transactions involving the purchase, transfer or swap of assets, with a total value of RMB 15.69 billion or 5.3%.

Panel B of Table 1 presents descriptive statistics for EXPROP—our expropriation proxy—which we calculate as the aggregate value of harmful related-party transactions for each firm during 1999 (2001) divided by the firm's year-end 1999 (2001) market capitalization. For the full sample, the mean and median values of EXPROP for 1999 were 5.6% and 1.9%, respectively. In 2001, the corresponding values were 5.5% and 1.6%. For the total sample, there is an insignificant decrease in the mean value of

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<sup>19</sup> A detailed description of the different types of related-party transactions is available from the authors on request.

<sup>20</sup> Cheung et al. (2007) analyze related-party transactions between Chinese listed firms and their State-owned block holders during 2001-2002.

EXPROP between 1999 and 2001 (t-statistic is -0.3).<sup>21</sup> In the last two columns of Panel B, Table 1, we report the proportion of firms with an increase in EXPROP from 1999 to 2001, and the z-statistic of the test of the null hypothesis that this proportion is 50%. For the whole sample, this proportion is 46.6%, which is significantly (at the 10% level) different from 50%.

The second part of Panel B shows the mean values of EXPROP for our three groups of controlling block holders—State Bureaucrats, MOSOEs and Private Entities. We also report the average quintile rank for each ownership type (ranks range from 0 for firms in the lowest quintile of the EXPROP distribution to 1 for firms in the highest quintile of the EXPROP distribution). In 1999, the highest mean value and the highest mean rank are observed at MOSOEs, whereas the lowest mean and the lowest mean rank are observed at State Bureaucrats. In 2001, MOSOEs retain the highest mean and the highest mean rank; however the lowest mean of EXPROP is now observed at Private Entities. The t-statistics indicate that the increase in the mean rank of EXPROP is statistically significant only for State Bureaucrats. However, consistent with the idea that State Bureaucrats were least responsive to the new regulation and that Private Entities were most responsive to the new regulations, we find that 55.5% of the State Bureaucrats had an increase in EXPROP, whereas for both MOSOEs and Private Entities less than 45% of the firms experienced an increase in EXPROP. The differences in these proportions are significant at the 1% level (not reported).

In the last two rows of Panel B in Table 1, we report the p-value from the test of whether the differences in EXPROP and  $\Delta$ EXPROP between the three ownership types are significant. When we use the values of EXPROP and  $\Delta$ EXPROP, the differences are not statistically significant; however, when we use the ranks, we find that the difference in EXPROP between the three ownership types is significant

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<sup>21</sup> Using the aggregate value of harmful related-party transactions for each firm during 1999 (2001) divided by the firm's year-end 1999 (2001) value of total assets, the mean value of EXPROP in 1999 is 15.1%, and the mean value of EXPROP in 2001 is 13.8%. This difference of 1.3% is significant at the 10% level.



both before and after the regulatory changes. We also find that there are significant differences between the ownership types in terms of the change in the mean rank, again suggesting that State Bureaucrats were least responsive to the new regulation and that Private Entities were most responsive to the new regulations.<sup>22</sup>

Table 2 presents descriptive statistics for our analysis variables both for the entire sample of 887 firms and for three groups of firms ranked into terciles based on the level of our expropriation proxy EXPROP (the sum of the value of all the potentially harmful related-party transactions that took place in 1999, scaled by the market value of the firm as of December 1999). The last column presents the p-value of a t-test that the means are the same for the group with low EXPROP and the group with high EXPROP.

#### INSERT TABLE 2

Table 2 shows a negative association between industry-adjusted Tobin's Q and EXPROP, suggesting that investors do discount firms that are exposed to more expropriation by the controlling block holder. Industry-adjusted Tobin's Q is measured as of year-end 1999 and is calculated as the sum of the market value of equity and the book value of debt divided by the book value of total assets. We control for differences in Q across industries by calculating the median Q for each industry and then by subtracting the appropriate industry median from each firm's Q. The average industry-adjusted Q for the high-EXPROP group is -0.25, whereas the average industry-adjusted Q for the low-EXPROP group is 1.04. This difference is significant at the 1% level.

There is no significant relation between *LEVERAGE* and EXPROP, but firms with higher EXPROP are significantly larger in terms of total assets.

Firms with a high level of expropriation are more likely to have a MOSOE as controlling block holder and are less likely to have a State Bureaucrat as controlling block holder. There is no significant

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<sup>22</sup> The conclusions do not change when we measure the relevant variables over a two-year period before the regulation and a two-year period after the regulations.

difference in the likelihood of having a Private Entity as controlling block holder for firms in the low-EXPROP and high-EXPROP groups.

Contrary to our expectations, but consistent with Cheung et al. (2007), we find that high-EXPROP firms are more likely to have controlling block holders that own more than 30% of the shares. Cheung et al. (2007) argue that expropriation is concentrated in listed firms with the highest state ownership because these are firms where the managers of the SOEs might find it easiest to carry out connected transactions. Consistent with this explanation, non-controlling block holders own a larger percentage of the shares of firms that have low expropriation than of firms with a high level of expropriation.

Surprisingly, low-expropriation firms are more likely to have the same person as CEO and Chairman of the Board. There is no significant difference between the low- and high-expropriation groups in the proportion of firms with independent directors or the proportion of firms with B-shares.

#### B. Market-Wide Impact of the Regulations

As detailed in section 3.A, we use standard event-study methodology to obtain mean-adjusted and market-adjusted abnormal returns around the announcements of each regulatory change. In Table 3, we present the results of this analysis. In Columns 2 and 3, we present results using the *Long Event Windows*, whereas, in Columns 4 and 5, we present the results using the *Five-day Event Windows*. For each of the three events, Columns 2 and 4 present cumulative mean-adjusted returns and Columns 3 and 5 present cumulative market-adjusted returns, where we use a portfolio of Chinese firms that trade on the Hong Kong Stock Exchange (“HKSE”) in an attempt to control for market-wide movements unrelated to the regulatory events.

#### INSERT TABLE 3

In Column 2 of Table 3, we see that the cumulative mean-adjusted return for the 11-day *Long Event Window* around the announcement of the shareholder-meeting regulation is a positive 10.1%. This increase in the market’s market value is significant at better than the five- percent level (p-value = 0.03). Around the announcements of the ban of related guarantees and the restriction on asset transfers, the

cumulative mean-adjusted returns are positive 1.1% and positive 1.9%, respectively, but these abnormal returns are not significantly different from zero. Column 3 of Table 3 shows that the correlation between the market return and the return on the portfolio of Chinese firms that trade on the HKSE is low, and that, consequently, the cumulative market-adjusted returns are very similar to the cumulative mean-adjusted returns shown in Column 2. Moreover, when we use *Five-day Event Windows*, the results are largely unchanged.

It is instructive to relate our estimates of the market's reaction to the new regulations to other research in this area. In a cross-country setting, La Porta et al. (2002) find that a two-point improvement in the score on the anti-director rights index raises Tobin's  $Q$  by 0.2, or about 17% of the 1.27 sample median. (Two points is the difference between the common-law and civil-law medians). In a study of Russian firms, Black (1999) reports that a one standard-deviation increase in governance ranking is associated with an eight-fold increase in firm value.

Given the substantial annual volume of related-party transactions—the average value of EXPROP was equal to 5.6% of market value in 1999 (as shown in Panel B of Table 1)—this evidence also suggests that effective regulation could have a dramatic impact on the discount in firm value associated with expected future expropriation. Consistent with this observation, Table 2 reports a difference in industry-adjusted Tobin's  $Q$  between firms in the low- and high-expropriation terciles of 1.3, or almost 250% of the 0.519 sample mean.

Even though the total increase in the value of the market around the three regulatory changes is substantial (around 13%), the high volatility in the Chinese stock market, combined with the long event windows, make it difficult to discern significant price reactions to market-wide events. An additional problem is the presence of several confounding events. The most significant confounding events were during the first event window: on May 19, the opening of a second board was announced, as was the

opening of the market to Qualified Foreign Institutional Investors (QFII).<sup>23</sup> It is important to note that these confounding events do not affect the cross-sectional results to the extent that the impact of these events on stock prices is not related to the level of expropriation or the quality of corporate governance.

In the next section, we investigate whether there is evidence of cross-sectional differences in share price reaction based on differences along these two dimensions.

### C. Related Party Transactions and Cross-Sectional Differences in CARs

This section presents the results of our cross-sectional tests based on EXPROP.<sup>24</sup> In Table 4, we report the results from estimating eq. (3)—our tests for difference in the CARs of the portfolio of the high and low expropriation firms. For each of the three regulatory changes, Panel A of Table 4 reports the results based on splitting the full sample into three groups based upon the value of EXPROP. In Panels B1 – B3 of Table 4, we present the results when the sample is further split based on the ownership type of the largest share holder. Finally, Panel C of Table 4 reports the cumulative abnormal returns for the hedge portfolio cumulated across all three events when the full sample is split into two, three and five groups based on the value of EXPROP.

#### INSERT TABLE 4

Panel A of Table 4 shows that the high-EXPROP portfolio outperforms the low-EXPROP portfolio for each of the three events, and that this outperformance is significant at the one-percent level for the shareholder-meeting regulation and the asset-transfer regulation, and the ten-percent level for the related-guarantee regulation. Around the announcement of the new shareholder-meeting rules, the portfolio of firms in the high-EXPROP tercile outperformed the portfolio of firms in the low-EXPROP

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<sup>23</sup> When we exclude May 19 from our event window, the abnormal return around the first event is around 8%. For all four models, CARs are significant at the 5% level.

<sup>24</sup> The validity of EXPROP as measure of firm-specific expropriation is confirmed in a cross-sectional regression, where we find a negative and statistically significant relation between EXPROP and Tobin's Q, after controlling for several corporate governance and firm characteristics. The results of this analysis are available from the authors upon request.

tercile by 3.5%. Around the announcement of the ban of related guarantees, this difference is 1.8%; and around the announcement of the tighter rules on asset transfers, the difference is 5.2%. If we sum across the three events, the total out-performance of the high-EXPROP group over the low-EXPROP group is more than ten percentage points.

Panels B1 – B3 of Table 4 present the CARs around the three regulatory events for different groups based on the identity of the controlling block holder (State Bureaucrat, MOSOE or Private Entity). More specifically, for the stocks in each ownership group, we form zero-cost portfolios that are long the tercile of high-expropriation stocks and short the tercile of low-expropriation stocks. For State Bureaucrats, there is no evidence that high-EXPROP firms significantly outperform low-EXPROP firms around the announcements of the new regulations. For the group of MOSOEs, the out-performance of high-EXPROP firms relative to low-EXPROP firms is positive for all events and significant at the 5% level for the shareholder meeting and asset transfer events. The most noticeable out-performance of high-EXPROP firms relative to low-EXPROP firms is observed for the group of firms controlled by Private Entities. The CAR around each of the events is significant at the 5%-level and the total CAR across all three events is 18.2%. These results are consistent with our hypothesis that the regulation is likely to be perceived as more (less) effective for firms where the controlling block holder has weaker (stronger) ties with the government.

In Panel C of Table 4, we report the cumulative abnormal return where we cumulate across all three regulatory events, for portfolios that are long in HIGH-EXPROP firms and short in LOW-EXPROP firms. The results in the first (second/third) column are based on portfolios where the HIGH-EXPROP firms are those in the highest EXPROP half (third/fifth) and LOW-EXPROP firms are those in the lowest EXPROP half (third/fifth). For the full sample and also for the subsamples of MOSOEs and Private Entities, the cumulative abnormal return on the hedge portfolio increases if the portfolio contains stocks with more extreme values of EXPROP. For the total sample, the CAR increases from 7.4% to 11.7% when we move from two groups to five groups. For MOSOEs, the CAR is 9.0% when we split the sample in two groups, and 15.1% when we split the sample into five groups. Finally, for Private Entities, the

CAR across all three events equals 10.4% when we split the sample into two groups and equals 20.3% when we split the sample into five groups.

To summarize, our results suggest that the market found the three regulations to be credible attempts at improving corporate governance of Chinese firms. For each of the three events, we find large and statistically significant differences in the reactions of firms with high and low levels of expropriation, even though, as shown in Table 3, the market-wide reaction was positive but not significantly different from zero for the related-guarantee and asset-transfer events. Our evidence also shows the regulations were perceived to be ineffective for firms with controlling block holders with the closest ties to the government.

#### D. Other Governance Proxies and Cross-Sectional Differences in CARs

In the previous section, we demonstrated significant cross-sectional differences in the share price reactions of firms with high and low levels of expropriation as proxied by the total value of potentially harmful related-party transactions in the year before the regulations were announced. In this section, we provide additional evidence on cross-sectional differences in the share-price reactions of firms classified into low- and high-governance portfolios using seven traditional corporate governance proxies, including the cash-flow rights of the largest shareholder, the shareholding of non controlling shareholders, the presence of B-shares and the type of controlling shareholder.

The results from estimating our portfolio time-series models appear in Table 5. We present the results from the time-series model, equation (4), based upon three portfolios: long on the high-third (half/fifth) and short on the low-third (half/fifth) of firms based upon each orthogonalized explanatory variable. We present the results using both our *Long Event Windows* and our *Five-Day Event Windows*. Because the results are generally consistent across the six alternative specifications (two windows times three groupings), we focus our discussion primarily on the results based upon three groups of firms using the *Long Event Windows*.

INSERT TABLE 5

First, we find weak evidence that suggests CARs tend to be lower for firms where the cash-flow rights of the largest shareholder are higher than 30% (CASH-FLOW RIGHTS >30%).<sup>25</sup> Firms in the lowest third for this variable outperform the firms in the highest third by a statistically significant 2.7%. Similar results are obtained when we split the sample into two groups and when we use the five-day windows, but the CAR is insignificant when we split the sample into five groups. We conclude that there is only weak evidence that minority shareholders in firms where the largest shareholder has greater ownership benefit less from the regulations relative to those where the largest shareholder has less ownership.<sup>26</sup>

Second, we consistently find a negative and significant relationship between the CARs and our NON-CONTROLLING BLOCK HOLDERS variable. Firms with larger holdings by the non-controlling block holders experienced significantly smaller increases in value around the announcement of the new regulations than firms with smaller shareholding by non-controlling block holders. The total difference in the cumulative abnormal return around the three events between the high- and low-tercile portfolios is 5.9%, statistically significant at the 1% level.

Third, there is no significant relation between MOSOE and the CARs. This result is inconsistent with the notion that minority shareholders in market-oriented SOEs are more likely to benefit because the regulator is more likely to enforce the new regulations when a MOSOE is the controlling block holder than when a State Bureaucrat is the controlling block holder.<sup>27</sup> However, we do find that firms controlled

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<sup>25</sup> Note that we can split our sample into thirds based upon a dummy variable because it has been orthogonalized against the other eight explanatory variables, rendering it semi-continuous.

<sup>26</sup> Similar results are obtained if we use different cut-offs (20%, 40%), or actual ownership.

<sup>27</sup> Note that the results in Table 5 are based on a multivariate analysis and cannot be directly compared with those in Table 4. When we form a portfolio that is long MOSOEs and short State Bureaucrats, we find that MOSOEs outperform State Bureaucrats by 2.5% ( $t$ -statistic = 2.2) on the announcement of the regulations. Because MOSOEs are larger and less levered, this results in a less significant result for the MOSOE portfolio when we include these control variables.

by Private Entities have larger price increases around the introduction of the regulations. This is supportive of the idea that private controlling block holders are more likely to expropriate than State owners, as they actually receive cash flows from the firm, whereas cash flows of shares ultimately owned by the State accrue to the taxpayer rather than to the government bureaucrats who exercise the State's control rights. The result is also consistent with the idea that the regulator is more likely to enforce the regulations in case of expropriation by a private block holder. The total difference in the cumulative abnormal return around the three events between the highest and lowest tercile portfolios is 4.7% and is statistically significant at the 1% level.

Fourth, the presence of foreign shareholders (B-SHARES) has a negative effect on the abnormal return for the three announcements. These results are consistent with our hypothesis that controlling shareholders of firms with foreign shareholders are less likely to expropriate minority shareholders because of the greater transparency and greater sophistication of these minority shareholders. The total difference in CARs around the three events between the highest and lowest tercile portfolios is 8.6%, statistically significant at better than the 1% level.

There is no consistent evidence that shareholders in firms where the CEO is also the Chairman of the Board benefited from the new regulations. Using the *Long Event Windows*, the results suggest that shareholders in firms without independent directors benefit from the new regulations. However, when we use *Five-Day Event Windows*, the CARs are insignificant. We conclude that minority shareholders do not perceive themselves to be more at risk of expropriation at firms where the CEO also wears the Chairman's hat and at firms without independent directors.

Other results in Table 5 show that the CARs around the announcements are not related to leverage. This result is consistent with the idea that creditors in China play a very limited role in the governance of firms. The four largest banks in China control the majority of banking assets in the country and are directly controlled by the Chinese government. These banks typically allocate credit to individual

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firms on the basis of national policy rather than on financial condition or performance, and typically are not involved in active monitoring.<sup>28</sup>

The CAR is positively related to FIRM SIZE, indicating that larger firms benefited relatively more from the new regulations than smaller firms. This result is consistent with our finding in Table 2 that larger firms are engaged in more related party transactions (scaled by market capitalization) than small firms.

Overall, our results suggest that firms with higher levels of expropriation (proxied by several variables that have been used as indicators of the quality of corporate governance) benefited more from the regulations than firms with lower levels of expropriation.

## **VI. Summary and Conclusions**

Recent studies of corporate ownership around the world show that listed firms typically have controlling block holders. For such firms, the primary concern of corporate governance is the protection of minority shareholders from expropriation by a controlling block holder and her management team.

In this study, we examine whether securities-market regulations intended to improve minority shareholder protection in China—a civil-law transitional economy with poorly developed institutions—can be effective. Our results suggest that they can—at least for firms that do not have close ties to the government. We find that firms with higher levels of expropriation from minority shareholders disproportionately benefit from the regulations relative to firms with lower levels of expropriation from minority shareholders (whether proxied by a direct measure of expropriation based on the total value of related party transactions, or measures of firm-specific corporate governance such as the relative power of the largest shareholder, the presence of foreign shareholders and other corporate governance related variables).

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<sup>28</sup> In a study by the World Bank, the authors observe that “creditors are among the least effective instruments of corporate control in China” (World Bank (2002), p. xvi)

We also report evidence that suggests effectiveness of the new regulations is highest for firms with private controlling block holders and lowest for firms where the controlling block holder has the closest ties with the government. This evidence confirms the importance of political connections, as it suggests that Chinese minority shareholders expect the regulator to enforce the regulations when a private block holder engages in expropriation but not when State controlled entities engage in expropriation.

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**Appendix 1:**  
**Chinese Regulatory Changes Occurring During the First Quarter of 2000**

On May 18, 2000, the CRSC released a new regulation regarding the procedures for shareholder meetings, while emphasizing that all corporate directors have a fiduciary duty to conduct proper shareholder meetings. The new regulation was publicly announced on May 26, 2000.<sup>29</sup> The most important improvements in terms of minority investor protection are:

- i) Shareholders who hold, separately or jointly, more than five percent of the voting power may propose motions for discussion at the shareholders' Annual General Meeting.
- ii) When the meeting votes on associated trading, shareholders involved in the associated trading shall not participate in the voting, and their rights to vote shall not be counted among the aggregate shares possessing voting rights.
- iii) When a motion concerning the election of directors and members of the supervisory board is discussed at the shareholders' meeting, shareholders shall vote on the candidate for director or supervisor individually.
- iv) When disputes occur concerning the assembling and convening of a meeting, voting procedures, or the legitimacy and effectiveness of a resolution, the parties concerned can take legal action in a People's Court in order to resolve the dispute.

On June 6, 2000, the CSRC released a new regulation prohibiting listed firms from issuing loan guarantees to their shareholders, shareholders' subsidiaries, and individuals. In addition, if the firm should issue a loan guarantee to an unrelated party, it should obtain a mutual guarantee to control risk, and the firm's managers are prohibited from signing a loan guarantee contract without approval of the board, or approval at a shareholders' meeting. This regulation was first publicly reported in Chinese newspapers on June 15, 2000.

On June 26, 2000, the CSRC released a new regulation regarding reorganizations of listed companies. The regulation, which was published in the newspapers on July 24, 2000, stipulates that if gross (net) assets are acquired or sold that account for more than 50% of the latest audited gross (net) assets of the listed company, or the profit from acquired or sold assets account for more than 50% of the latest audited profit of the listed company, then the listed company shall perform the following procedures:

- i) The board of directors shall conduct a feasibility study and disclose the information as if it was a public offering.
- ii) The board shall hire accounting and law firms qualified to conduct securities business to certify the relevant issues.
- iii) The board shall issue a resolution on the relevant issues and report to the Stock Exchange within two days after the resolution is made, and announce to the public the resolution with the comments of the intermediaries and the board of supervisors.
- iv) Upon examination and approval of the shareholders meeting, the listed company shall implement the plan of asset purchase or sale.
- v) If the counter-party has a tacit understanding with the controlling shareholder of the listed company, the transaction shall be deemed an affiliated transaction, which shall be subject to the relevant rules and regulations.
- vi) After the major purchase or sale of assets, the listed company shall ensure the separation of personnel, assets and accounting from its controlling shareholder.

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<sup>29</sup> Before publication in the newspapers, the regulatory changes were first released to a limited number of market participants: the securities regulatory offices, the stock exchanges and the listed companies.

**TABLE 1:**  
**Related-Party Transactions of Chinese listed firms in 1999**

Panel A presents frequency and average value of the different types of related-party transactions for 887 Chinese listed firms in 1999. (Source: the GTA/CSMAR Related-Party Transactions Database). Transactions are classified as potentially beneficial for the listed company if the listed firm received cash, loans or guarantees from the related party; all other related-party transactions are classified as harmful. A detailed description of each type of related-party transaction is available from the authors. Panel B reports descriptive statistics for the variable  $EXPROP_i$ , which is the sum of the value of potentially harmful related-party transactions in 1999 (2001), scaled by the market value of firm  $i$  as of year-end 1999 (2001). We winsorize  $EXPROP_i$  at the 99 percentile. STATE BUREAUCRAT is a dummy variable equal to one if the largest block holder classified as a State Bureaucrat; MOSOE is a dummy variable equal to one if the largest block holder is a market-oriented State-owned enterprise; PRIVATE ENTITY is a dummy variable equal to one if the largest block holder is a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established researchers at the National University of Singapore as described in Delios et al. (2006). The  $t$ -statistic in Panel B tests whether  $\Delta EXPROP$  is statistically different from zero, and the  $z$ -statistic in the last column tests whether the proportion of firms with an increase in  $\Delta EXPROP$  is statistically different from 0.50. The  $p$ -values in the last two rows are based on tests of equality of means (medians) across the three classifications of the largest block holder.

<b>Panel A: Related Party Transactions for Chinese firms in 1999</b>			
Transaction	Observations	Mean Value (in million RMB)	
Beneficial	495	80.34	
Harmful	5,618	52.75	
Detailed Classification of Harmful Related Party Transactions			
	Observations	Mean value	% of total
Commodity	2,644	79.89	71.5
Asset	540	29.06	5.3
Services	583	23.60	4.7
Commission	165	47.72	2.7
Fund Transfer	420	27.24	3.9
Guarantee	360	43.36	5.3
Lease	402	16.08	2.2
Operating trust	33	9.22	0.1
Non-Monetary Transaction	2	0.00	0.0
Stock Transaction	203	43.74	3.0
Debt Transaction	34	42.88	0.5
Cooperative Project	67	36.92	0.8
R&D	34	0.73	0.0
Manager Remuneration	22	9.60	0.1
License	81	0.44	0.0
Other Events	28	32.01	0.3

Panel B: Descriptive Statistics for EXPROP

		EXPROP 1999	EXPROP 2001	$\Delta$ EXPROP	t-stat	% +	z-stat
All	Mean	0.056	0.055	-0.001	-0.3	46.6	1.9
	Median	0.019	0.016	-0.004			
STATE BUREAUCRAT							
	Mean	0.043	0.049	0.006	0.7	55.5	1.5
	Mean rank	0.381	0.439	0.058	2.5		
MOSOE							
	Mean	0.062	0.059	-0.003	-0.6	44.4	-2.6
	Mean rank	0.545	0.527	-0.017	-1.1		
PRIVATE ENTITY							
	Mean	0.052	0.044	-0.008	-1.0	41.6	-1.4
	Mean rank	0.489	0.461	-0.028	-0.5		
Equality of means: p-value		0.09	0.34	0.50			
Equality of ranks: p-value		0.01	0.01	0.03			



**TABLE 2:**  
**Sample Descriptive Statistics by Expropriation Terciles**

The sample consists of 887 publicly traded Chinese firms, segmented into three terciles based upon the sum of the value of potentially harmful related-party transactions in 1999, scaled by the market value of the firm as of December 1999. Q is a proxy for Tobin's Q, measured as the sum of the market value of equity and the book value of debt divided by the book value of total assets measured as of year-end 1999. INDUSTRY-ADJUSTED Q is industry-adjusted Q, where we control for differences in Q across industries by calculating the median Q for each industry and then subtracting the appropriate industry median from each firm's Q. FIRM SIZE is a firm's total assets expressed in millions of RMB. LEVERAGE is the book value of debt divided by the book value of total assets as of year-end 1999. STATE BUREAUCRAT is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; MOSOE is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; PRIVATE ENTITY is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore as described in Delios et al. (2006). CASH FLOW RIGHTS > 30% is a binary variable that is equal to one if the largest shareholder owns more than 30% of all outstanding shares and 0 otherwise. NON-CONTROLLING BLOCK HOLDERS is the sum of the shareholdings of the second through tenth largest shareholders. B-SHARES is a binary variable that is equal to one for firms that have both A- and B-shares outstanding and equal to zero otherwise. CEO IS CHAIR is a binary variable that is equal to one if the Chief Executive Officer is also the Chairman of the Board and zero otherwise, and INDEPENDENT DIRECTORS is a dummy variable that is equal to one when the firm has at least one independent director and zero otherwise. For each variable identified in the first column, the last two columns report the difference in the means of firms in terciles one and three, followed by the corresponding *p*-value.

	All			Expropriation			Low - High	p-value
	Min	Max	Mean	Low	Medium	High		
INDUSTRY-ADJUSTED Q	-3.822	16.772	0.519	1.036	0.773	-0.249	1.285	0.001
FIRM SIZE	5,884	2,703,343	146,473	103,692	122,353	213,230	- 109,538	0.001
LEVERAGE	0.02	1	0.428	0.432	0.420	0.432	0.000	0.986
STATE BUREAUCRAT	0	1	0.239	0.333	0.241	0.141	0.192	0.001
MOSOE	0	1	0.656	0.546	0.669	0.753	-0.208	0.001
PRIVATE ENTITY	0	1	0.096	0.112	0.084	0.091	0.021	0.407
CASH FLOW RIGHTS > 30%	0	1	0.733	0.631	0.757	0.811	-0.180	0.001
NON-CONTROLLING BLOCKHOLDER	0	0.495	0.168	0.191	0.184	0.128	0.063	0.001
B-SHARES	0	1	0.079	0.061	0.088	0.088	-0.027	0.215
CEO IS CHAIR	0	1	0.117	0.149	0.111	0.091	0.058	0.030
INDEPENDENT DIRECTORS	0	1	0.023	0.024	0.007	0.037	-0.013	0.343

**TABLE 3:**

**Cumulative Abnormal Returns around Regulatory Events**

This table reports the cumulative abnormal returns (CARs) around announcements of three new regulations intended to improve corporate governance at Chinese publicly listed firms. The first new regulation substantially increased the rights of minority shareholders at a firm's Annual Shareholders' Meeting; the second prohibited the issuance of loan guarantees by a firm to its controlling shareholder; and the third improved the transparency and regulation of asset transfers to related parties. We estimate CARs using an equally weighted portfolio consisting of all 887 sample firms. The results in column two (four) and three (five) are based on eq. (1) and eq. (2), respectively:

$$(1) \text{ MARKET RETURN}_t = \beta_0 + \sum \beta_j \text{ EVENT } J + \varepsilon_t$$

$$(2) \text{ MARKET RETURN}_t = \beta_0 + \sum \beta_j \text{ EVENT } J + \beta_5 \text{ HK RETURN}_t + \varepsilon_t$$

where MARKET RETURN<sub>t</sub> is the return on an equally weighted market portfolio during day t; EVENT J, J = 1 to 3 are dummy variables that equal 1/n for the dates within the event window of length n for the first, second and third regulation and equal zero otherwise; HK RETURN<sub>t</sub> is the return for day t on an equally weighted portfolio of 24 Chinese firms listed on the Hong Kong Stock Exchange; and β<sub>j</sub>, J = 1 to 3 are the estimated cumulative adjusted returns associated with each event window. The model is estimated over 250 trading days ending July 25, 2000 (one day after the newspapers published the third regulation). The *Long Event Windows* for Events 1, 2 and 3 are 11, 10 and 23 trading days, respectively, and span the period from one day before the initial announcement of the regulation by the CSRC to one day after the first publication by the financial press. The *Five-Day Event Windows* span the five days centered on the CSRC announcement and the five days centered on the first publication by the financial press.

t-statistics are in parentheses.

\*\*\*, \*\*, and \* indicate statistical significance at the .01, .05, and .10 levels, respectively.

Variable	Long Event Windows		Five-Day Event Windows	
	Model (1)	Model (2)	Model (1)	Model (2)
Intercept	0.002 (1.6)	0.001 (1.4)	0.002 (1.5)	0.001 (1.4)
EVENT 1: Shareholder Meeting	0.101 ** (2.1)	0.117 ** (2.3)	0.099 ** (2.1)	0.107 ** (2.3)
EVENT 2: Related Guarantees	0.011 (0.2)	0.001 (0.0)	0.011 (0.2)	-0.001 (-0.0)
EVENT 3: Asset Transfer	0.019 (0.3)	0.006 (0.1)	0.023 (0.5)	0.011 (0.3)
HK RETURN		0.086** (2.0)		0.079* (1.9)

**TABLE 4:**

**Difference in Cumulative Abnormal Returns by Degree of Expropriation**

This table reports on the relation between EXPROP and cumulative abnormal returns (CARs). Each cell in Panels A and B1-B3 presents the difference in the CARs of the HIGH-EXPROP and LOW-EXPROP groups around each of the three announcements of new regulations. Panel C reports the cumulative abnormal returns for the hedge portfolio cumulated across all three events when the full sample is split into two, three and five groups based on the value of EXPROP. The first new regulation substantially increased the rights of minority shareholders at a firm's Annual Shareholders' Meeting; the second prohibited the issuance of loan guarantees by a firm to its controlling shareholder; and the third improved the transparency and regulation of asset transfers to related parties. EXPROP is defined as the sum of the value of potentially harmful related-party transactions in 1999, scaled by the market value of the firm as of December 1999. We estimate the following model:

$$(3) R(\text{HIGH-EXPROP}_t) - R(\text{LOW-EXPROP}_t) = \beta_0 + \sum \beta_J \text{EVENT } J + \beta_5 \text{ MARKET RETURN}_t + \varepsilon_t$$

where:  $R(\text{HIGH-EXPROP}_t)$  is the return for day  $t$  on an equally weighted portfolio of the highest third of firms based upon EXPROP;

$R(\text{LOW-EXPROP}_t)$  is the return for day  $t$  on an equally weighted portfolio of the lowest third of firms based upon EXPROP;

$\beta_J$ ,  $J = 1$  to  $3$ , are the estimated differences in the cumulative abnormal returns (CARs) of the HIGH-EXPROP and LOW-EXPROP portfolios during each event window  $J$ ;

The model is estimated over 250 trading days ending July 25, 2000 (one day after the newspapers published the third regulation). Panel A presents results from estimating the relation between EXPROP and CARs for the full sample while Panel B1-B3 presents the results for three mutually exclusive sub-samples containing only firms controlled by State Bureaucrats, MOSOEs or Private Entities. These results are based upon splitting each sample into three groups on the basis of EXPROP. The *Long Event Windows* for Events 1, 2 and 3 are 11, 10 and 23 trading days, respectively, and span the period from one day before the initial announcement of the regulation by the CSRC to one day after the first publication by the financial press. The *Five-Day Event Windows* span the five days centered on the CSRC announcement and the five days centered on the first publication by the financial press.  $t$ -statistics are in parentheses. \*\*\*, \*\*, and \* indicate statistical significance at the .01, .05, and .10 levels, respectively.

(1)	(2)	(3)	(4)	(5)
	Shareholder Meeting	Related Guarantees	Asset Transfers	All Three Events
Panel A: All Firms				
Long Event Windows	0.035 *** (2.9)	0.018 * (1.7)	0.052 *** (3.0)	0.101 *** (4.1)
Five-Day Event Windows	0.026 ** (2.2)	0.016 (1.5)	0.024 ** (2.1)	0.065 *** (3.2)
Panel B1: STATE BUREAUCRAT				
Long Event Windows	0.003 (0.2)	0.010 (0.7)	0.003 (0.2)	0.015 (0.6)
Five-Day Event Windows	0.009 (0.8)	0.009 (0.8)	-0.016 (-1.3)	0.002 (0.1)
Panel B2: MOSOE				
Long Event Windows	0.039 ** (2.4)	0.023 (1.5)	0.052 ** (2.3)	0.110 *** (3.3)
Five-Day Event Windows	0.027 * (2.5)	0.021 (2.0)	0.030 ** (2.0)	0.078 *** (3.4)
Panel B3: PRIVATE ENTITY				
Long Event Windows	0.065 ** (2.5)	0.048 ** (2.0)	0.074 ** (2.0)	0.182 *** (3.4)
Five-Day Event Windows	0.041 * (1.7)	0.045 * (1.9)	0.037 (1.5)	0.123 *** (2.8)

Panel C: Total CARs for different groups

	(1) High vs. Low Half	(2) High vs. Low Third	(3) High vs. Low Fifth
<b>All Firms</b>			
Long Event Windows	0.074 *** (4.1)	0.101 *** (4.1)	0.117 *** (3.6)
Five-Day Event Windows	0.047 *** (3.1)	0.065 *** (3.2)	0.066 ** (2.5)
<b>STATE BUREAUCRAT</b>			
Long Event Windows	0.032 (1.4)	0.015 (0.6)	0.021 (0.7)
Five-Day Event Windows	0.018 (0.9)	0.002 (0.1)	-0.016 (0.0)
<b>MOSOE</b>			
Long Event Windows	0.09 *** (3.9)	0.110 *** (3.3)	0.151 *** (3.2)
Five-Day Event Windows	0.058 *** (3.0)	0.078 *** (2.9)	0.092 ** (2.4)
<b>PRIVATE ENTITY</b>			
Long Event Windows	0.104 ** (2.2)	0.182 *** (3.4)	0.203 *** (3.2)
Five-Day Event Windows	0.069 * (1.9)	0.123 *** (2.8)	0.137 *** (2.6)

**TABLE 5:**  
**Corporate Governance and Differences in Cumulative Abnormal Returns**

This table presents the results from estimating the relation between a set of governance-related variables and the cumulative abnormal returns around announcements of three new regulations intended to improve corporate governance at Chinese listed firms. The first new regulation substantially increased the rights of minority shareholders at a firm's Annual Shareholders' Meeting; the second prohibited the issuance of loan guarantees by a firm to its controlling shareholder; and the third improved the transparency and regulation of asset transfers to related parties. We use a portfolio time-series regression model to regress an event-window dummy on the returns from a portfolio that is long on the highest and short on the lowest half/third/fifth of firms based upon orthogonalized explanatory variable OV: (CASH-FLOW RIGHTS > 30%, NON-CONTROLLING BLOCK HOLDERS, B-SHARES, MOSOE, PRIVATE ENTITY, CEO IS CHAIR, INDEPENDENT DIRECTORS, FIRM SIZE or LEVERAGE; which are defined in Table 2). The model is as follows:

$$(4) \quad R(\text{HIGH-OV}_t) - R(\text{LOW-OV}_t) = \beta_0 + \beta_1 \text{EVENTS} + \beta_2 \text{MARKET RETURN}_t + \varepsilon_t$$

where: EVENTS is a dummy variable that equals 1 / 44 for the dates within the three event windows (or 1 / 30 for dates within the 5-day event windows), and zero otherwise; R (HIGH-OV<sub>t</sub>) is the return on the HIGH-OV portfolio; R (LOW-OV<sub>t</sub>) is the return on the LOW-OV portfolio; MARKET RETURN<sub>t</sub> is the market return on day t; and ε<sub>t</sub> is an i.i.d. error term. Each cell gives the difference in the CARs of the HIGH-OV and LOW-OV Portfolios during the event window around the three regulatory changes. The models are estimated over 250 trading days ending July 25, 2000 (one day after the newspapers published the third regulation). The *Long Event Windows* for Events 1, 2 and 3 are 11, 10 and 23 trading days, respectively, and span the period from one day before the initial announcement of the regulation by the CSRC to one day after first publication by the financial press. The *Five-Day Event Windows* span the five days centered on the CSRC announcement and the five days centered on the first publication by the financial press. *t*-statistics appear in parentheses.

\*\*\*, \*\*, and \* indicate statistical significance at the .01, .05, and .10 levels, respectively.

	Long Window			Five-Day Window		
	High vs. Low Half	High vs. Low Third	High vs. Low Fifth	High vs. Low Half	High vs. Low Third	High vs. Low Fifth
CASH-FLOW RIGHTS > 30%	-0.046 (-3.1)	*** -0.027 (-1.8)	* 0.003 (0.2)	-0.029 (-2.4)	** -0.024 (-2.0)	** -0.012 (-0.8)
NON-CONTROLLING BLOCKHOLDERS	-0.057 (-3.2)	*** -0.059 (-2.8)	** -0.052 (-2.2)	-0.035 (-2.4)	** -0.034 (-2.0)	** -0.029 (-1.5)
MOSOE	0.011 (0.9)	0.011 (0.7)	-0.014 (-0.8)	-0.002 (-0.2)	0.001 (0.1)	-0.006 (-0.4)
PRIVATE ENTITY	0.047 (3.2)	*** 0.047 (3.2)	*** 0.05 (2.6)	0.023 (1.9)	** 0.032 (2.2)	** 0.028 (1.8)
B-SHARES	-0.069 (-3.5)	**** -0.086 (-3.5)	*** -0.101 (-3.3)	-0.037 (-2.2)	*** -0.04 (-2.1)	** -0.043 (-1.7)
CEO IS CHAIR	0.032 (2.6)	*** 0.030 (1.7)	* -0.001 (-0.0)	0.015 (1.5)	0.014 (1.0)	-0.001 (-0.0)
INDEPENDENT DIRECTORS	-0.043 (-2.6)	** -0.055 (-2.5)	** -0.054 (-2.5)	-0.013 (-1.0)	-0.022 (-1.2)	-0.021 (-1.1)
LEVERAGE	-0.023 (-1.4)	-0.028 (-1.3)	-0.033 (-1.2)	-0.008 (-0.6)	-0.011 (-0.6)	-0.016 (-0.7)
FIRM SIZE	0.093 (4.2)	*** 0.129 (4.3)	*** 0.15 (4.4)	0.052 (2.9)	*** 0.068 (2.7)	*** 0.083 (2.9)