Rhetorical Nationalism and Corporate Tax Avoidance: Insights from China

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Abstract

This study investigates the unexplored nexus between rhetorical nationalism and corporate tax avoidance. Analyzing Chinese firms from 2010 to 2022, it shows that companies with pronounced nationalistic rhetoric are significantly more prone to engage in tax avoidance. This finding highlights the profound impact of nationalistic sentiments on corporate financial strategies. The result holds through an instrumental variables approach, with an even stronger effect observed among state-owned enterprises. This research offers insights for policymakers and scholars interested in the intersection of nationalism and corporate behavior, paving the way for those looking to understand the drivers of tax avoidance.

JEL classifications: G38, H26, M14
Keywords: rhetorical nationalism, tax avoidance, China

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1 Introduction

The culture, identity, and economic perception of a firm significantly influence its strategic decisions and actions. These internal factors shape how a firm navigates its environment, including its approach to regulatory compliance, market positioning, and competitive behavior (Gorton and Zentefis, 2024; He et al., 2022; and Pasiouras et al., 2021). A firm's culture and identity can drive its commitment to ethical or aggressive practices. Similarly, how a firm perceives the economic landscape—whether it views it as an opportunity for growth, a field of fierce competition, or a landscape rife with regulatory challenges—can dictate its strategic priorities and operational tactics. Understanding these dimensions is crucial for comprehensively analyzing corporate behavior and forecasting future actions.

One aspect of culture not studied is that of rhetorical nationalism. Yue et al. (2024) give the following definition: *"Firm's rhetorical nationalism refers to their adoption of nationalistic language in their public communication to signal their commitment to act in line with the interests of a nation."* The impact of nationalism on firm outcomes remains an underexplored area of study, largely due to the challenges in quantifying it. Additionally, determining the specific mechanisms and directions through which rhetorical nationalism influences firm behaviors and performance is complex and ambiguous. This complexity arises from the multifaceted nature of nationalism.

Nationalism has been a driving force in China's socio-political landscape and has significantly influenced its economic trajectory (Zhao, 2004). Over the past few decades, the rapid expansion of the Chinese economy has amplified the importance of nationalism within Chinese firms (Lan and Li, 2015). This nationalistic sentiment not only fosters a sense of pride and identity but also shapes corporate strategies and behaviors (Lubinski et al., 2020). Companies often align their goals with national priorities, leveraging patriotic rhetoric to build domestic support and navigate regulatory landscapes more effectively. Consequently, nationalism plays a crucial role in how Chinese firms operate, compete, and grow in both domestic and international markets.

In this study, I investigate the relationship between rhetorical nationalism and tax avoidance. This is the first study to look at this question, to the best of my knowledge. I contribute in two ways to the literature. First, examining the nexus between rhetorical nationalism and tax avoidance is highly relevant, particularly given the rise of nationalistic rhetoric in China. Second,

this research enriches the existing body of knowledge on corporate tax avoidance by identifying rhetorical nationalism as a novel determinant.

2 Data and model

For this study, I utilize accounting data for Chinese firms spanning from 2010 to 2022. All firm control variables are sourced from the CSMAR database. The key variable of interest, rhetorical nationalism, is derived from a recent study by Yue et al. (2024). This dataset allows for a comprehensive analysis of the influence of rhetorical nationalism on corporate tax avoidance within the specified timeframe.

I use a standard OLS model of the following form:

$$TaxAvoid_{i,t} = \beta_0 + \beta_1 Nationalism_{i,t} + \boldsymbol{\beta_2 Controls_{i,t}} + \gamma_t + \delta_{IND} + u_{i,t}. \quad (1)$$

In the above specification, *TaxAvoid* represents three common proxies for corporate tax avoidance used in the literature. *Nationalism* is the main independent variable. *Controls* is a vector of accounting variables. γ_t and δ_{IND} indicate year and industry fixed effects, respectively, while $u_{i,t}$ is the error term.

A description of the variables and their summary statistics can be found in Tables 1 and 2 below.[1]

[Insert Table 1 about here]
[Insert Table 2 about here]

3 Results

For ease of exposition and to gauge the economic effect, all continuous variables have been standardized.

Table 3 presents the results of the baseline model. The analysis shows that the coefficient for nationalism is negative and statistically significant. This indicates that firms exhibiting higher

[1] The correlations of these variables can be found in Online Appendix Table OA1.

levels of rhetorical nationalism tend to have lower effective tax rates (ETRs), suggesting that they engage in greater tax avoidance.[2]

Several factors could explain these findings. First, firms with strong nationalistic rhetoric may feel a greater sense of entitlement or justification for minimizing their tax liabilities, believing that their contributions to the national economy through other means (such as employment and domestic investment) offset their tax responsibilities. This sense of economic patriotism can lead them to aggressively seek tax avoidance strategies. Second, nationalistic firms may enjoy closer relationships with government officials, which can result in more lenient enforcement of tax regulations. These firms might also leverage their nationalistic stance to garner public and political support, thereby reducing the risk of reputational damage from tax avoidance practices. Finally, in a highly nationalistic environment, firms might perceive that aligning with nationalistic goals allows them to focus on long-term growth and competitiveness, justifying tax avoidance as a strategic move to reinvest resources in the local economy.

[Insert Table 3 about here]

The results of my study thus far indicate a clear association between rhetorical nationalism and tax avoidance. To address potential endogeneity concerns, I employ an instrumental variables approach utilizing two instruments. The first instrument is an indicator of whether a firm was established after 2001. According to Yue et al. (2024), firms founded post-2001 are less likely to exhibit rhetorical nationalism. This is attributed to China's accession to the World Trade Organization in that year, leading to organizational structures and ideologies in newer firms that are less inclined towards nationalism. The second instrument is the average level of rhetorical nationalism among all other firms in the same industry, year, and city. This instrument helps isolate the firm-specific effect of nationalism by accounting for broader industry, temporal, and geographic influences. These instruments are expected to be correlated with rhetorical nationalism but unrelated to corporate tax avoidance directly.

Table 4 presents the results of the two-stage least squares (2SLS) model. In the first stage, we find that firms established after 2001 exhibit lower levels of rhetorical nationalism. Additionally, firms operating in industries and regions with higher overall levels of rhetorical nationalism tend

[2] The results in Table 3 encompass both SOE and non-SOE firms. For a focused analysis on SOE firms alone, refer to Online Appendix Table OA2, which indicates a stronger effect.

to have higher rhetorical nationalism themselves. In the second stage, the coefficient for rhetorical nationalism remains negative and statistically significant in most cases, consistent with the baseline findings. Furthermore, the first-stage F-statistics typically exceed the threshold of 10, indicating strong instruments. The Hansen's J statistics fail to reject the null hypothesis, suggesting that the instruments used are valid.

[Insert Table 4 about here]

4 Conclusion

This study is the first to explore the relationship between rhetorical nationalism and tax avoidance among Chinese firms. By examining firm-level data from 2010 to 2022, the analysis shows that firms with higher levels of rhetorical nationalism tend to engage in greater tax avoidance, as evidenced by lower effective tax rates. These findings are robust to endogeneity concerns, addressed through an instrumental variables approach. This study contributes to the literature by identifying rhetorical nationalism as a novel determinant of corporate tax avoidance, particularly relevant in the context of rising nationalistic rhetoric in China. The implications of these findings are significant for understanding how nationalistic sentiments shape corporate financial behavior and for policymakers aiming to regulate tax avoidance practices effectively.

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Table 1
Description of variables

Variable	Description
Dependent variables	
ETRgaap	Total tax expenses divided by pretax income. *Source: CSMAR*.
ETRsum	The three-year sum of income tax expense divided by the three-year sum of pretax income over years (*t*-2) to *t*. *Source: CSMAR*.
ETRcurrent	Current tax expense divided by profit before tax. *Source: CSMAR*.
Control variables	
Nationalism	The firm-level rhetorical nationalism measure developed by Yue et al. (2024).
ROA	The ratio of operating income to year-end total assets. *Source: CSMAR*.
Leverage	Total debt divided by year-end total assets. *Source: CSMAR*.
Size	The natural logarithm of the book value of year-end total assets. *Source: CSMAR*.
Cash	Cash and cash equivalents are divided by year-end total assets. *Source: CSMAR*.
CAPEX	Capital expense divided by year-end total assets. *Source: CSMAR*.
INTANG	Intangible assets are divided by year-end total assets. *Source: CSMAR*.
TobinQ	The sum of total assets plus the market value of equity, minus the book value of equity divided by total assets. *Source: CSMAR*.
FirmAge	A firm's age in years. This is the difference between the CSMAR year and the year a firm is established. *Source: CSMAR*.
After2001	An indicator taking value 1 for all firms established after 2001. *Source: CSMAR*
Nationalism_avg	This is the average value of nationalism for all other firms in the same industry, year, and city. *Source: Own calculation*.

Table 2
Summary statistics

This table shows the descriptive statistics of the variables used in the analysis. Variable definitions and their sources are in Table 1.

VARIABLES	Obs.	Mean	Std.dev	Min	P^{25}	P^{50}	P^{75}	Max
ETRgaap	15,210	0.190	0.125	0.000	0.122	0.161	0.238	0.998
ETRsum	11,068	0.191	0.118	0.000	0.127	0.163	0.235	1.000
ETRcurrent	13,236	0.213	0.145	0.000	0.131	0.178	0.262	0.993
Nationalism	15,210	0.653	0.484	0.000	0.324	0.532	0.848	4.552
ROA	15,210	0.664	0.529	0.001	0.374	0.554	0.792	10.691
Leverage	15,210	0.162	0.129	0.000	0.057	0.145	0.243	0.846
Size	15,210	22.489	1.410	16.702	21.477	22.279	23.315	28.607
Cash	15,210	0.018	0.109	-2.160	-0.025	0.006	0.042	0.970
CAPEX	15,210	0.055	0.051	0.000	0.019	0.041	0.076	0.603
INTANG	15,210	0.045	0.047	0.000	0.019	0.034	0.057	0.589
TobinQ	15,210	1.880	1.127	0.681	1.189	1.519	2.143	14.197
FirmAge	15,210	17.448	6.247	1.000	13.000	17.000	22.000	55.000
After2001	14,111	0.277	0.448	0	0	0	1	1
Nationalism_avg	14,111	0.631	0.237	0	0.514	0.515	0.717	4.034

Table 3
Baseline model

This table presents OLS results of tax avoidance proxies on rhetorical nationalism. The dependent variables are *ETRgaap*, *ETRsum*, and *ETRcurrent*. Robust standard errors are clustered at the firm level, and t-statistics are in parentheses. ***, **, and * indicate statistical significance at 1%, 5%, and 10%, respectively. Variable definitions and their sources are in Table 1.

	ETRgaap	ETRsum	ETRcurrent
	(1)	(2)	(3)
Nationalism	-0.024**	-0.032**	-0.025**
	(-2.29)	(-2.25)	(-2.43)
ROA	0.065***	0.031	0.022
	(3.68)	(1.38)	(1.30)
Leverage	0.099***	0.105***	0.106***
	(6.77)	(5.84)	(7.38)
Size	0.044***	0.022	0.047***
	(3.15)	(1.29)	(3.28)
Cash	-0.033***	-0.038**	-0.053***
	(-4.27)	(-2.58)	(-6.74)
CAPEX	-0.073***	-0.087***	-0.077***
	(-7.31)	(-7.09)	(-7.05)
INTANG	0.079***	0.070***	0.069***
	(4.70)	(3.99)	(3.82)
TobinQ	-0.083***	-0.074***	-0.115***
	(-6.62)	(-4.76)	(-8.89)
FirmAge	0.044***	0.051***	0.035**
	(3.00)	(2.94)	(2.37)
Constant	0.046***	0.016	0.046***
	(3.77)	(1.07)	(3.65)
Observations	15,210	11,068	13,236
Adjusted R-squared	0.169	0.197	0.149
Year effects	Yes	Yes	Yes
Industry effects	Yes	Yes	Yes
Cluster	Firm	Firm	Firm

Table 4
Instrumental variables

This table presents 2SLS results of tax avoidance proxies on rhetorical nationalism. The dependent variables are *ETRgaap*, *ETRsum*, and *ETRcurrent*. Robust standard errors are clustered at the firm level, and t-statistics are in parentheses. ***, **, and * indicate statistical significance at 1%, 5%, and 10%, respectively. Variable definitions and their sources are in Table 1.

	1st stage	*2nd stage*	*1st stage*	*2nd stage*	*1st stage*	*2nd stage*
Dependent Variable →	Nationalism	ETRgaap	Nationalism	ETRsum	Nationalism	ETRcurrent
	(1)	(2)	(3)	(4)	(5)	(6)
After2001	-0.160***		-0.151**		-0.154***	
	(-3.05)		(-2.48)		(-2.83)	
Nationalism_avg	0.145***		0.123***		0.169***	
	(4.03)		(3.31)		(4.15)	
$\widehat{\text{Nationalism}}$		-0.227		-0.436**		-0.254*
		(-1.57)		(-2.16)		(-1.83)
ROA	-0.017	0.064***	-0.006	0.031	-0.018	0.021
	(-0.87)	(3.51)	(-0.27)	(1.30)	(-0.90)	(1.13)
Leverage	-0.014	0.095***	-0.018	0.100***	-0.002	0.102***
	(-0.90)	(6.39)	(-0.98)	(5.08)	(-0.15)	(6.76)
Size	0.191***	0.085***	0.191***	0.106**	0.188***	0.095***
	(8.76)	(2.62)	(7.51)	(2.35)	(8.27)	(2.98)
Cash	-0.023***	-0.036***	-0.019	-0.047***	-0.023**	-0.057***
	(-2.73)	(-4.14)	(-1.32)	(-2.77)	(-2.54)	(-6.48)
CAPEX	-0.070***	-0.086***	-0.081***	-0.122***	-0.075***	-0.090***
	(-6.35)	(-5.69)	(-5.68)	(-5.41)	(-6.55)	(-5.66)
INTANG	0.026*	0.076***	0.032*	0.078***	0.028	0.071***
	(1.68)	(4.28)	(1.74)	(3.78)	(1.64)	(3.65)
TobinQ	0.031*	-0.076***	0.036*	-0.054***	0.031*	-0.108***
	(1.90)	(-5.66)	(1.96)	(-2.97)	(1.82)	(-7.55)
FirmAge	-0.035	0.050***	-0.036	0.059***	-0.035	0.042**
	(-1.13)	(3.03)	(-1.01)	(2.72)	(-1.07)	(2.54)
Observations		14,111		10,138		12,414
1st stage F-stat		13.38		8.85		13.19
Hansen J stat (p-value)		0.952		0.308		0.552
Year effects	Yes	Yes	Yes	Yes	Yes	Yes
Industry effects	Yes	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm	Firm

Online Appendix

(Not Intended for Publication)

To accompany the paper:

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This appendix contains the following elements:

Table OA1: Correlations table
Table OA2: Baseline model for SOEs only

Table OA1
Correlations

		1	2	3	4	5	6	7	8	9	10
ETRgaap	(1)	1									
Nationalism	(2)	-0.027	1								
ROA	(3)	0.042	-0.009	1							
Leverage	(4)	0.146	0.033	-0.013	1						
Size	(5)	0.173	0.235	0.044	0.283	1					
Cash	(6)	-0.045	-0.029	-0.018	-0.083	-0.054	1				
CAPEX	(7)	-0.143	-0.102	0.001	0.052	-0.147	-0.067	1			
INTANG	(8)	0.034	0.003	-0.003	0.010	-0.043	-0.068	0.126	1		
TobinQ	(9)	-0.144	-0.072	-0.005	-0.236	-0.387	0.014	0.071	0.060	1	
FirmAge	(10)	0.106	0.155	-0.008	0.157	0.321	-0.077	-0.199	-0.025	-0.102	1

Table 3
Baseline model for SOEs

This table presents OLS results of tax avoidance proxies on rhetorical nationalism for SOE firms only. The dependent variables are *ETRgaap*, *ETRsum*, and *ETRcurrent*. Robust standard errors are clustered at the firm level, and t-statistics are in parentheses. ***, **, and * indicate statistical significance at 1%, 5%, and 10%, respectively. Variable definitions and their sources are in Table 1.

	ETRgaap	ETRsum	ETRcurrent
	(1)	(2)	(3)
Nationalism	-0.042**	-0.051***	-0.040**
	(-2.57)	(-2.78)	(-2.54)
ROA	0.083***	0.056	0.035
	(2.72)	(1.38)	(1.20)
Leverage	0.140***	0.163***	0.107***
	(5.65)	(5.16)	(4.43)
Size	0.068***	0.025	0.078***
	(2.68)	(0.84)	(3.03)
Cash	-0.048**	-0.051*	-0.073***
	(-2.32)	(-1.65)	(-3.54)
CAPEX	-0.065***	-0.091***	-0.079***
	(-2.65)	(-2.89)	(-3.23)
INTANG	0.071**	0.083***	0.050*
	(2.55)	(2.70)	(1.73)
TobinQ	-0.095***	-0.099***	-0.127***
	(-3.47)	(-2.87)	(-4.99)
FirmAge	0.059*	0.047	0.059*
	(1.88)	(1.34)	(1.95)
Constant	0.140***	0.134***	0.108***
	(5.52)	(3.65)	(4.36)
Observations	5,868	4,181	5,039
Adjusted R-squared	0.165	0.217	0.157
Year effects	Yes	Yes	Yes
Industry effects	Yes	Yes	Yes
Cluster	Firm	Firm	Firm