Government Relation and Firm Performance: An Empirical Study in Taiwan Stock Market

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[Abstract]

The government relation is traditionally regarded as one important factor to influence firm performance. On the operational level, firm behaviors are heavily affected by the regulations from the government and the degree of affinity between the firm and the agent. This research examines the extent how firm performance is impacted on the changes of government relations. By measuring the stock performance of some KMT-related companies after the event that KMT lost the Presidential election in 2000, the author finds there significantly exists negative abnormal returns. Abruptly losing the connections to the regulating party does have negative impacts on firm performance.

I. Introduction

In the field of government-firm relations, most of the researches traditionally regard firms as interest groups who affect the legislation and implementation of regulations through political involvements. Baysinger (1984) argue that business political activity may have three major objectives: (1) to gain special monetary and anticompetitive favors from government—domain management; (2) to manage environmental turbulence created by governmental threats to the legitimacy of organizational goals and purposes—domain defense; and (3) to manage similar threats to the methods by which organizations pursue their goals and purposes—domain maintenance. In the domain maintenance, the ways to influence regulation include lobbying, trade associations, agency in the legislation office, and so on.

Theories can be roughly divided into two approaches in the research of government-firm relations: Institutionalism and resource dependence perspective. Both approaches separate firms and government into two types of organizations with different objectives, conducts, and performance evaluation criteria. In firm's point of

view, governmental legislation and regulation are treated as one of the environmental factors. Institutionalism argues that governmental regulation is considered as one part of the social structure and firm's economic actions are embedded in the social structure. (Granovetter, 1985) The governmental pressure is one of major reasons why firms appear collective behaviors—coercive isomorphism. (DiMaggio & Powell, 1991) In the resource dependence perspective, government is conceived as one part of the external environment or necessary resources to the firm and the firm should adapt or manipulate it, however. (Pfeffer & Salancik, 1978) According to Institutionalism or the resource dependence perspective, firms and government or political parties, the major source to decide legislation in the democratic society, are in different social sectors. The normal interaction model between firms and political parties is that firms sponsor the activities held by specific political parties to win or exchange preferential treatments. In some countries, the dominant political party involves running the private business to make money or even applies the government power to protect or benefit its own business. Both theories don't have deep discussions on this kind of case.

La Porta et al. (1999) use data on ownership structures of large corporations in 27 wealthy economies to identify the ultimate controlling shareholders of these firms and find that relatively few of these firms are widely held. Rather, these firms are typically controlled by families or the State. The State- or party-owned enterprises may be not popular or permitted in Western democratic societies but do play a key role in many Eastern developed and developing countries.

With the increasingly important role played by Eastern economies in the world-wide markets and popularity of State- or party-owned companies in those economies, the research addresses two strategic questions: (1) What are the differences in behaviors between these State- or party-owned enterprises and traditional Western private firms? (2) To what extent is the performance of these enterprises influenced by the State power controlled by the party? Both questions provide a rationale for the empirical investigation of government relation on firm performance.

Specifically, the purpose of this research is threefold: (1) to contribute to a more comprehensive understanding of the behavior of State- or party-owned enterprises, which is seldom mentioned in Institutionalism, the resource dependence perspective, or other political economic theories; (2) to empirically test the effect of governmental power on firm performance; and (3) to lay a theoretical foundation on which further inquiries can be based.

This research applies event study methodology to evaluate the influence the change of government regulation on firm performance. The event in this research is

the Taiwan Presidential Election in 2000. In that election, the traditionally dominant party, KMT, lost the State power. KMT has governed Taiwan for more than 50 years and invested many private enterprises. In the past time, these enterprises depended on the State power to provide anticompetitive favors or preferential treatments. Once KMT lost the Presidential Election, these KMT-related enterprises[1] lack of efficiency faced heavy pressure immediately. It is a proper event for this research to evaluate the influence of State power on firm performance by tracking the abnormal returns of KMT-related public companies after 2000 Taiwan Presidential Election.

II. Theory Review and Proposed Hypotheses

Following this research will review two mainstream theories: Institutionalism and the resource dependence perspective and briefly describe how KMT expands its influences into Taiwan industries and controls its related business. Institutionalism reviews firm behaviors from the viewpoint of social structure, especially government. The resource dependence perspective mentions the issue of governmental regulations from the angle of the firm.

(1) Institutional Theory

Unquestionably, government-firm relations affect firm performance. Economic theories traditionally regard the role of government as exogenous variables and do not consider it on the firm decision level. In contrast, Institutional theory adopts opposite viewpoints to argue economic actions and institutional arrangement are embedded in the social structure. (Granovetter, 1985, 1992) Based on this view, Granovetter (1992) criticizes that the traditional economic theories over-rationalize personal behaviors and overlook the relation to the social context. Traditional economic approach has the bias of undersocialization.

There are various perspectives in discussion of institutional factors. Some compared different views of sociological and economic theories from the concept of human being, the assumptions and constraints of economic behaviors, to the research objectives and methodologies. (Smelser & Swedberg, 1994) Some focus on the evolution of institutional theories to extend the research conclusions of informal organizational structures and behaviors to the observations and predictions of formal

[1] KMT controls its companies through equity and non-equity ways, such as totally owned, majority shareholding, pyramid, cross shareholding, interlocking in the board of director, and so on. This research labels these companies as “KMT-related enterprise”

organizations. (DiMaggio & Powell, 1991) Table 1 summarizes four perspectives on organization. (Biggart, 1997)

Table 1 Four Perspectives on Organization

	Market	*Cultural*	*Political Economy*	*Institutional*
Key variables	Economic	Values, symbols	State	Ideology, authority
Social action	Individual utilitarianism	Collective action	Class and interest groups	Dialectic of structure and individual action
Social order	Invisible hand/ self-interest	Enacted solidarity	Stratification (repression, majority rule)	Domination
Social change	Market forces	Continuity	Institutional contradictions/interest groups	Historical development
Organization	Most efficient structure	Symbolic expression of cultural values	Expressions of bureaucratic and market power	Structure of economic domination utilizing cultural understanding

Source: The Economic Organization of East Asian Capitalism (1997), p.5

Based on Biggart's comparison, Table 1 shows that institutional theories try to integrate traditional economic perspectives, social cultural perspectives, and political economy perspectives through an inter-disciplinary way.

On the issue that the governmental role in the economy system, Institutionalism proposes that the State plays a major role in facilitating institutional isomorphism of firms. (DiMaggio & Powell, 1991) The firms rooted in the same country usually have similar behaviors, called institutional isomorphism. The sources of the institutional isomorphism include: (1) Coercive isomorphism—organizations behave in a specific way because of the formal or informal pressures from other organizations, regulations of the government, for example; (2) Mimetic isomorphism—facing the uncertainty, organizations imitate the strategy of the winner in the industry through specific channels such as consultant companies and trade associations; and (3) Normative isomorphism—organizational members decide their organizations to behave similarly based on their professionalism which is formed by similar thoughts and skills from similar institutional environments and educational contexts.

The State plays a critical role in building the institutional environment to firms. Regulation policies such as industry subsidization, financial and monetary controls,

and environmental protections directly decide firms' behaviors then facilitate the coercive isomorphism. Eastern governments usually involve the activities of trade associations to get control by subsidizing expenses, supporting specific candidates in the election, and so on. High involvement into the trade associations makes mimetic isomorphism. The educational system, the key factor of normative isomorphism, is also designed by the government.

KMT has controlled the State power in Taiwan for more than 50 years. In this period the party's policies facilitated the isomorphism of Taiwan firm behaviors. By restriction, subsidization, and State-owned enterprises, KMT successfully developed key industries such as steel, petrochemistry, construction, information technology, and semiconductor for Taiwan's needs in different time. Taiwan's 3 key trade associations are used to be controlled by KMT. All the leaders of these associations are created by KMT's plan. Furthermore, 50-year KMT ruling shapes the Taiwan social structure then affects the formation of firm competence. For example, the policy allocating more resources on the scientific education creates abundant technology human resources for the development of Taiwan electronic/high-tech industries. Nowadays these high-tech industries are critical to Taiwan's upgrade.

(2) Resource Dependence Perspective

In dealing with the relation between firms and the external environment, the resource dependence perspective bases on firm's viewpoint to state the ways that the organization can depend on critical resources, manage the environment, and achieve their objectives. Organizations need to gain or exchange key resources from the environment for their operations and growth. The term "environment" is defined as the collection of other organizations external to the organization. The focus of this perspective is on the issue that how organizations interact with their environment to get necessary resources. (Pfeffer & Salancik, 1978)

As one part of the external environment, the government is a key factor for firms to consider interdependence. Conceptually, business political activity may have three major objectives: (1) Domain management—to gain special monetary and anti-competitive favors from government; (2) Domain defense—to manage environmental turbulence created by governmental threats to the legitimacy of organizational goals and purposes; and (3) Domain maintenance—to manage similar threats to the methods by which organizations pursue their goals and purposes. (Baysinger, 1984) Table 2 summarizes the typology of business political activities.

From the perspective of resource dependence, domain maintenance may be the

most important political strategy of the firm. Basically, government affects the firm conduct or performance through two channels: directly inject cash into the firm or indirectly protect the firm from domestic or foreign competition. (Pfeffer & Salancik, 1978) Both channels can gain legitimacy through legislation activities. The objective of firms is to get beneficial legislations or preferential treatments. (Kotter, 1979)

Table 2 A Typology of Business Political Activities

Organizational Objective	Methods of Attaining Objectives (By External Focus)	
	Electoral	**Legislative/Regulatory**
Domain Management *Goal:* Gain at eh expense of others, especially through governmental assistance	PAC's In-kind support	Lobbying Trade associations Washington office Agency hearings
Domain Defense *Goal:* Challenge and rebuff threats to organizational goals and purposes, including those posed by government	PAC's In-kind support	Lobbying Public relations Trade associations Washington office
Domain Maintenance *Goal:* Challenge threats to the methods by which organizational goals and purposes are pursued, especially those posed by government	PAC's In-kind support Grass roots efforts	Lobbying Washington office

Note: "PAC" means Political Action Committee Source: Baysinger (1984)

Form the viewpoint of firms, the benefits of the business political activity are apparent, such as to gain inside information, influence the legislation of regulatory acts based on private relations with critical governmental officers, reduce transaction cost and uncertainty, and so on. (Hillman, Zardkoohi, & Bierman, 1999) From the perspective of firm strategy, business political activity can be considered as the "non-market" conduct to improve firm performance, compared to "market" conduct to create firm value. (Baron, 1995)

To test in Taiwan markets, the resource dependence perspective has explanatory power in firm conducts. Owing to KMT's regulations, most of the Taiwan firms have

a lot of political activities. The objectives of this kind of activities include looking for capital injections, winning contracts of government purchases, prevent unfavorable legislations, and so on. The role Taiwan government plays in the economic system is much more important than the role of government in the Western countries. Business political activity is a necessary "non-market" way for firms to operate in the Taiwan markets, not only a performance improving process.

(3) KMT Regulation on Taiwan Industries

After World War II, KMT-controlled government took over all of Japanese State-owned enterprises in Taiwan. The fields that these enterprises operated cover most of the industrial sectors such as financial institutions, transportations, telecommunications, industrial materials, metallurgical industry, mining, mechanical industry, fertilizer, cement, paper, water and electricity utilities, and most of the agricultural sectors like sugar, salt, tobacco, alcoholic drink, and forest. In the 50-year ruling, KMT itself established enormous State- or party-owned enterprises. All the State- or party-owned enterprises make up the "KMT-State Capitalism." (Chen et al., 1991)

The primary mission of KMT take-over action was to repair and recover the operation of Japanese production facilities and control military materials. At that time, the KMT-controlled government set up two principles to transfer Japanese assets into State-owned enterprises: (1) The business should be operated by the State, according to the government policies; and (2) The business that private sectors cannot operate. In 1950s, the Taiwan government ever privatized some State-owned enterprises to get capitals to support its land reform policy. In 1960s, even the export-oriented industries (Textile, Plastics, and Electronics) grew fast, the revenues of State-owned sectors never declined. Some new State-owned enterprises were established in this period of time, such as China Petroleum Corp. (1968), China Chemistry (1970), China Steel (1972), China Shipbuilding (1973), and so on.

Besides the State-owned enterprises controlled by KMT, there are another two types of KMT-related enterprises: (1) The "disguised" State-owned enterprises which are invested by other State-owned enterprises; and (2) KMT-owned enterprises. (Chen et al., 1991) The disguised State-owned enterprise is in the form of private company but controlled by the government and KMT. The major investors of this kind of enterprises are government departments, State-owned enterprises, and KMT-owned investment institutions. For example, 58% shares of Chinese Security Corp. belong to China Petroleum, Taiwan Electricity, Chiao-Tung Bank, and Development Fund of

Taiwan Executive Yuan. This kind of disguised State-owned enterprises can avoid the supervision and regulation of the government to execute some special policies.

Furthermore, KMT-owned enterprises played a significant role in the Taiwan economy. KMT now has 12 wholly-owned companies and their diversifications. KMT is the largest financial company in Taiwan, except the State. KMT-owned enterprises and their diversifications have following characteristics: (1) joint venture with State-owned enterprises; (2) monopoly or oligopoly; and (3) highly related to the mass media business. Because KMT does not need to gather capitals from the stock market, most information of its business is not disclosed. This policy seemed to be changed after 1988 and KMT began to do business with conglomerate enterprises in private sectors. On one hand KMT tries to bind its interests with private enterprises then extends its influence. On the other hand those private enterprises hope set up channels to affect government regulations through joint venture with KMT. From the fact that many leaders of Taiwan conglomerate enterprises are members of KMT central standing committee and their governance structures usually include KMT capitals, we can find the popularity that Taiwan firms ally with KMT.

The channels KMT involves in the Taiwan economic system can be summarized as follows:

(1) Regulating the business scope of firms by controlling the licenses, such as mass media, infrastructure, transportation, banking, and so on.
(2) Influencing firm behaviors through policy implementation, such as using tax incentives in target industries or decreasing loans to punish those firms who cannot obey the policy.
(3) Utilizing the market power of State-owned enterprises.
(4) Utilizing the market power of diversifications of State-owned enterprises.
(5) Utilizing the market power of KMT-owned enterprises.
(6) Affecting firm conducts by non-market ways such as controlling the network of trade associations.

While losing the Presidential Election, KMT only has two channels in hand to involve the economic activities, its party-owned enterprises and some non-market means. Even the non-market channels are losing gradually because DPP[2] competes with KMT by controlling State-owned enterprises.

Decreasing KMT influence will have negative impact on those KMT-related companies. Without protection from ruling power, KMT-related companies cannot gain favors at the expense of their competitors. Some with lower performance cannot

[2] On March 18, 2000, DPP's Presidential candidate, Shiue-Bien Chen, won around 40% voter support to defeat KMT and other candidates.

sustain anymore because they have no low-cost capital and other resource subsidized by KMT. Hypothesis 1, (H1) 1a, (H1a) and 1b (H1b) conclude the statement.

H1: KMT-related enterprises cannot get anticompetitive protection and low-cost cash injection after KMT losing the ruling power. The KMT failure in the Presidential Election has a negative impact on the performance of its related enterprises.

H1a: Without KMT protection and subsidization, its related companies cannot perform better than competitors in the same industry.

H1b: KMT-related companies can get lower-cost capital through political protection. It will show higher debt ratio for those KMT-related firms.

III. Research Design

The methodology of this research is event study to measure the abnormal returns of KMT-related companies in the TSE and OTC markets after March 18, 2000. There are some preconditions that should be considered for the use of event study: (1) market efficiency; (2) unanticipated events; (3) confounding effects. (McWilliams & Siegel, 1997) In this research, the stock market anticipates KMT failure will hamper the performance of its related companies and their stock prices will show negative abnormal returns. (Market efficiency) KMT has ruled Taiwan since 1945, no one expects it to lose the election so fast. (Unanticipated events) When the election result was disclosed, PRC and other countries all kept calm. In addition, there are no important economic events happening within the event window, 90 trading days after March 18, 2000. The Presidential Election can be regarded as an independent event for this research.

1. Sample and Data

In the sample selection, this research defines the KMT-related business based on the channels that KMT involves in economic activities. The sample of KMT-related business has at least one of the following characteristics: (1) Key investors come from State- or KMT-owned enterprises; (2) Key managers are influential in KMT; (3) Directors in the board include key KMT members; (4) High financial interdependence with KMT; and (5) Joint venture with KMT.

Strictly speaking, most of the companies in TSE and OTC companies have some degree of relations to KMT. To get sample with stronger KMT characteristics, this

research adopt narrower definition of KMT-related companies as follows:

(1) Invested directly by KMT-owned financial institutions, including Central Investment Company, Kwan-Hwa Investment Company, Chi-Lu Enterprise, Yu-Tai Enterprise, and China Development Corp.[3]

(2) Chairman is or was the member of KMT central standing committee, such as Chin-Yuan Kao (President of President Enterprise), Yo-Chen Wang (Li-Ba Conglomerate Enterprise), and so on.

(3) Joint venture with KMT, such as Acer, Ton-Yuan, Tuntex, and so on.

According to above 3 criteria, this research selects 66 TSE companies and 41 OTC ones. Excluding 12 OTC companies because they go public after October 1999, there are 95 firms as the sample. Table 3 summarizes their industrial distribution.

Table 3 Industry mix of KMT-related firms

Industry	No. of firms	Industry Situation
Cement	5	Governmental Regulation/Oligopoly
Food	2	
Petrochemistry	6	
Textile	5	Key industry in 1970s
Shipping Warehousing	4	Governmental Regulation/Oligopoly
Mechanical Electronics	7	Conglomerates with close government relation
Electronics	23	
Construction	11	Close interaction with government departments
Banking	14	Governmental Regulation/Oligopoly
Others	18	Many are regulated, natural gas, for example

Source: Taiwan Economic Journal (TEJ) and this research

The sensitivity analysis about the sample size and error term distribution of mean excess returns shows that it is close to normal distribution while sample size is larger than 50. (Brown & Warner, 1985) The total sample size in this research is 95 and the TSE sample size is 66. The assumption of normal distribution is effective.

The research set the event window as 90 trading days after March 18, 2001. In addition, the robustness test will be implemented as the event window of 30 and 60 trading days. Besides March 18, May 20[4] is another important day for this event. This

[3] China Development Corp. (CDC) is a public industrial banking but used to play role of high-tech investment for KMT in the past time. Thai-Yin Liu, Chairman of CDC, is previous chairman of KMT financial management committee. Most of the electronic OTC companies in the sample have the CDC representative.

[4] The day new President swears to assume office

research will also test if the abnormal return exists in 90 trading days after May 20, 2000.

2. Measurement

This research adopts the daily close price of TSE and OTC stocks as the variable to measure firm performance. Calculation of abnormal returns is based on the process proposed by Mikkelson and Partch (1986):

(1) Calculate α and β in the relation of market return and return for common stock of the specific firm.

$$R_{jt} = \alpha_j + \beta_j R_{mt} + \varepsilon_{jt} \quad (1.1)$$

Where R_{jt} = the continuously compounded rate of return for the common stock of firm j on day t

β_j = estimated market risk of firm j on day t

R_{mt} = the continuously compounded rate of return for the equally weighted index of the market on day t

ε_{jt} = error term of return for the common stock of firm j on day t

(2) Estimate the normal return for the specific common stock in the event window based on the α and β estimated prior to the event. The post-event abnormal return (AR) can be shown as below.

$$AR_{jt} = R_{jt} - (\alpha_j + \beta_j R_{mt}) \quad (1.2)$$

(3) Tests of statistical significance are based on standardized abnormal return (SAR) as following equations.

$$SAR_{jt} = \frac{AR_{jt}}{S_{jt}} \quad (1.3)$$

$$\text{Where } S_{jt} = \left\{ V_j^2 \left[1 + \frac{1}{ED} + \frac{(R_{mt} - \overline{R}_m)^2}{\sum_{i=1}^{ED} (R_{mt} - \overline{R}_m)^2} \right] \right\}^{1/2} \quad (1.4)$$

In (1.4), V_j^2 is the residual variance of firm j's market model regression, ED is the number of days in the period used to estimate the market model and is 180 days in this research, $\overline{R}_m$ is the mean market return in the estimation period, and R_{mt} is the market return on day t.

(4) Calculate average standardized cumulative abnormal return (ASCAR) in the event window.

$$ASCAR_{T_1,T_2} = \frac{1}{N} \sum_{J=1}^{N} \left[\sum_{T_1}^{T_2} \frac{SAR_{jt}}{(T_{2_j} - T_{1_j})^{1/2}} \right] \quad (1.5)$$

Where

N = Sample size, it's 95 in this research

T_1 = Beginning of the event

T_2 = End of the event

(5) The Z-statistic is computed as the following equation.

$$Z = \sqrt{N}(ASCAR_{T_1,T_2}) \quad (1.6)$$

Besides the measurement of cumulative abnormal returns, this research sets additional conditions as follows:

(1) Time horizon prior to the event: This research selects 180 trading days before the event, from July 14, 1999 to March 18, 2000, as base time to estimate α and β. In addition, the result of Election is difficult for investors to predict because of insignificant gap between 3 major candidates. It does not need to exclude the data points in the days near the event.

(2) Event time: In addition to March 18, 2000, this research decides May 20, 2000 as another event time. The differences between two days are that DPP

success has psychological impact on the investors on March 18 but the preferential treatments for KMT-related enterprises stop on May 20. From March 18 to May 20, investors can rationally anticipate how KMT failure will impact on the performance of its related companies, so this research still adopt the same α and β estimators to measure abnormal returns after May 20.

(3) Event window: This research chooses 90 trading days as the event window, from March 18 to July 15 or from May 20 to September 15. The robustness is also tested in this research.

(4) Market portfolio: This research uses two market portfolios, weighted average index of TSE/OTC and Industrial stock group. Return for common stock of the specific firm is simultaneously affected by firm performance and industry cycles. If there exists significantly negative abnormal returns for KMT-related companies compared to the Industrial stock index, it means that KMT-related firms without government protection perform worse than their competitors in the market.

IV. Results

1. Abnormal Returns

The results are shown in Tables 4 and 5. Both analyses are based on the same α and β estimated by the 180 trading days before the event on March 18, 2000.

Table 4 The Abnormal Return of KMT-related Firms to TSE/OTC Index

KMT-related Companies in TSE & OTC	180 Trading Days before 3/18(1999/7/14-2000/03/17)					
	90 Trading days after 3/18 (03/20-07/15)			90 Trading days after 5/20 (05/20-09/15)		
	Average Abnormal Return (%)	Z-Statistic	Sample Size	Average Abnormal Return (%)	Z-Statistic	Sample Size
TSE	-4.20	-3.52***	66	-6.04	-5.06***	66
OTC	-3.29	-1.87**	29	-6.41	-3.64***	29
TSE/OTC	-3.92	-4.03***	95	-6.16	-6.33***	95

***p<0.01; **p<0.05

Table 4 show the result that either in TSE or in OTC, KMT-related companies have significantly negative abnormal returns compared to TSE/OTC index. H1 is not

rejected.

Table 5 The Abnormal Return of KMT-related Firms to Industrial Stock Index

KMT-related Companies in TSE & OTC	180 Trading Days before 3/18(1999/7/14-2000/03/17)					
	90 Trading days after 3/18 (03/20-07/15)			90 Trading days after 5/20 (05/20-09/15)		
	Average Abnormal Return (%)	Z-Statistic	Sample Size	Average Abnormal Return (%)	Z-Statistic	Sample Size
TSE	-3.26	-2.73***	66	-5.72	-4.79***	66
OTC	-3.34	-1.09**	29	-7.00	-3.97***	29
TSE/OTC	-3.29	-3.38***	95	-6.11	-6.28***	95

***p<0.01; **p<0.05

In Table 5, KMT-related companies again perform worse than the industrial stock index. The abnormal return comes from two levels of effects. One is the firm-level effect and the other is the industry-level effect. The negative abnormal returns of KMT-related firms to the industrial stock index mean that these firms cannot perform better than the competitors in the same industry, after KMT losing the ruling power. Under protection of KMT, the KMT-related firms have weaker incentives to improve their operational efficiency than their competitors. H1(a) is significantly supported.

Comparing the abnormal returns on 318 and 520 respectively, the 90-trading-day ASCAR of 520 is higher than the value of 318, either based on TSE/OTC index as the market portfolio (t-value = 1.32, $p<0.1$) or based on industrial stock index as the market portfolio (t-value = 1.64, $p<0.1$). It means after May 20 there are more investors expecting bad performance of KMT-related firms and believing DPP to remove all preferential treatments from the KMT-related firms.

The major reason to cause negative abnormal returns of KMT-related companies is lack of efficient and effective management. For example, most of the KMT-related firms enjoy lower capital costs in the past KMT time and have higher debt ration relative to the other companies. (t-value = 1.68, $p<0.05$) H1b is not rejected. Under protection and subsidization, KMT-related companies can raise higher percent of debt ration to compensate lower profitability. Once KMT losing ruling power, its related firms have no cheap cash injection and cannot create enough profits to attract investors in the stock market. The negative abnormal return is the natural result.

2. Robustness

Table 6 and 7 shows the average abnormal returns based on different event windows: 30, 60, and 90 trading days after 318, compared to TSE/OTC and industrial stock index.

In Table 6, it shows that the abnormal return is not significantly only in the OTC sample in 30-trading-day event window. It means two short event window and too small sample size introduce uncertain factor in the abnormal return measurement. Too short window may cause the market not to reflect the investor expectation completely enough and too small sample size may introduce a error distribution totally different from normal distribution, violating the assumption of Z-statistic methodology.

In Table 7, the same situation happens again. The OTC sample in 30-trading-day event window cannot show significantly negative abnormal returns for KMT-related companies.

Table 6 Robustness of Abnormal Return of KMT-related Firms: TSE/OTC Index

KMT-related Companies in TSE & OTC	Sample Size	180 Trading Days before 3/18(1999/7/14-2000/03/17)					
		30 Trading days after 3/18		60 Trading days after 3/18		90 Trading days after 3/18	
		Average Abnormal Return (%)	Z-Statistic	Average Abnormal Return (%)	Z-Statistic	Average Abnormal Return (%)	Z-Statistic
TSE	66	-2.46	-3.56***	-2.27	-2.33***	-4.20	-3.52***
OTC	29	-0.70	-0.68	-3.55	-2.47***	-3.29	-1.87**
TSE/OTC	95	-1.92	-3.41***	-2.66	-3.34***	-3.92	-4.03***

***p<0.01; **p<0.05

Table 7 Robustness of Abnormal Return of KMT-related Firms: Industrial Index

KMT-related Companies in TSE & OTC	Sample Size	180 Trading Days before 3/18(1999/7/14-2000/03/17)					
		30 Trading days after 3/18		60 Trading days after 3/18		90 Trading days after 3/18	
		Average Abnormal Return (%)	Z-Statistic	Average Abnormal Return (%)	Z-Statistic	Average Abnormal Return (%)	Z-Statistic
TSE	66	-1.25	-1.81**	-1.61	-1.66**	-3.26	-2.73***
OTC	29	-0.35	-0.34	-2.67	-1.86***	-3.34	-1.09**
TSE/OTC	95	-0.97	-1.73***	-1.94	-2.44***	-3.29	-3.38***

***p<0.01; **p<0.05

Generally speaking, under the conditions that large enough is the sample size and long enough is the event window, KMT-related firms show significant under-performance in the stock market after KMT losing the Presidential Election.

V. Conclusions and Suggestions for Further Research

The hypotheses in the research are all significantly supported. The firms protected by government regulations or preferential treatments suffer negative impacts if their relations to government weaken or disappear.

Both event days, 318 and 520, face the same policy change event: the new DPP government used "National Security Fund" to try to stabilize the falling stock market resulted from worldwide economic recession and some faults of the green-handed government. DPP's stabilization policy focuses on the TSE index by buying the stocks with higher weights in the market. This policy indirectly increases the degree of negative abnormal returns for KMT-related firms.

On the methodology of event study, this research adopts equally weighted approach to measure the abnormal return, even the value weighted approach can show a better results in measuring the long-term performance. (Lyon et al., 1999) Business political activity can create both short-term and long-term influences on firm performance. If further researchers try to measure the long-run performance, value weighted (buy-and-hold) abnormal return should be considered to make a comparison with the equally weighted abnormal return.

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