Political connections and organisational performance: evidence from Pakistan

By

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Declaration

I hereby certify that this thesis, submitted in partial fulfilment of the requirements for the degree of Master of Research, in the Department of Accounting and Corporate Governance of the Faculty of Business and Economics at the Macquarie University, is my own work and the product of my own research. It has not, nor any part of it, been submitted for the fulfilment of requirements or part requirements of a degree/diploma, to any university or institution other than Macquarie University.

I further certify that it does not contain, to the best of my knowledge, any material that has been previously published or submitted to any university, without acknowledgement. Any help and assistance received by me during this research and during the preparation of this thesis, has been duly acknowledged.

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List of Abbreviations

ANOVA	Analysis of Variance
BOI	Board of Investment
CCG	Code of Corporate Governance
CEO	Chief Executive Officer
CLA	Corporate Law Authority
DFI	Development Finance Institutions
ECP	Election Commission of Pakistan
EPB	Export Promotion Bureau of Pakistan
FATA	Federally Administered Tribal Areas
FBR	Federal Board of Revenue
FC	Federal Capital
IAROA	Industry Mean Adjusted Return on Assets
IAROE	Industry Mean Adjusted Return on Equity
IPO	Initial Public Offerings
ISE	Islamabad Stock Exchange
KPK	Khyber Pakhtunkhwa
KSE	Karachi Stock Exchange
LSE	Lahore Stock Exchange
NA	National Assembly
NAB	National Accountability Bureau
NIAT	Net Income after Tax
NIBT	Net Income before Tax
PATA	Provincially Administered Tribal Areas
PCP	Privatization Commission of Pakistan
PERF	Performance
POLCON	Political connection
ROA	Return on Assets
ROE	Return on Equity
SBP	State Bank of Pakistan
SECP	Securities and Exchange Commission of Pakistan
SRO	Statutory Regulatory Orders
VIF	Variance inflation factor

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Abstract

The study investigates the association between political connections and organisational performance in Pakistan. It is motivated by mixed findings in the literature regarding the impact of political connections on organisational performance. Further, there is a particular dearth of research on political connections in the South Asian region, thereby leaving an empirical gap in the literature. This study is primarily motivated to address this gap in the literature.

In view of a weak regulatory environment, poor implementation of the law and high level of corruption in Pakistan, the study hypothesises a positive association between political connections and organisational performance. Data was collected from 250 non-financial organisations listed on the Karachi Stock Exchange (KSE) of Pakistan. The results reveal that political connections in Pakistan are common across all industries, however, contrary to the expectations; political connections in Pakistan have a significant negative association with organisational performance. In particular, the study found a significantly negative effect of political connections on return on assets and return on equity. In addition, negative association of political connections with organisational performance is more pronounced for organisations having connections with politicians compared to those having connections with former government officials.

The study contributes to the existing literature on political connections by providing evidence of the impact of political connections on organisational performance in high corruption and weak regulatory environment. It is the first study which provides evidence of political connections and their impact on organisational performance in Pakistan. The findings can be generalised to other South Asian countries, with similar socio-economic, political and regulatory setting.

Keywords: Political connections, organisational performance, return on assets, return on equity.

Chapter 1
Introduction

The aim of this study is to examine the association between political connections and organisational performance in Pakistan. Specifically, the study examines how political connections effect organisational performance, measured as Return on Assets (ROA) and Return on Equity (ROE). This chapter is arranged into four sections. Section 1.1 provides an overview of political connections. Section 1.2 discusses the motivations of this study. Section 1.3 summarises the contributions of the study; while Section 1.4 outlines the overall structure of the thesis.

1.1. Overview of political connections

Business organisations adopt different ways to establish connections with politicians and government officials. For example, business owners establish relationships with politicians through lobbying (Blau, Brough and Thomas 2013), campaign contributions (Ramanna and Roychowdhury 2010), friendships, and family and social networking (Gomez and Jomo 1997) or they opt to enter into politics (Bunkanwanicha and Wiwattanakantang 2008). Alternatively, businesses appoint former and/or current politicians and (former) top government officials on their Boards of Directors to obtain benefit from their current or former connections (Jackowicz, Kozlowski and Mielcarz 2014). While political connections of business organisations may help them to obtain preferential access to scarce economic resources, they may also have a negative effect on non-connected organisations. This study follows Faccio (2006) to define an organisation as politically connected if any one of its top officers or a large shareholder, or a close friend/family member of a top officer or a large shareholder is working or has worked either as a parliamentarian or a minister or a head of the Government or the State, or as a top officer in the Government or the Military.

1.2. Motivations

1.2.1. To address the issue of mixed findings regarding the impact of political connections on organisational performance

There are a number of studies (e.g. Houston et al. 2014; Bliss and Gul 2012a; Boubakri, Cosset and Saffar 2012a; Wu et al. 2012c) which have examined the impact of political connections on business organisations. Evidence suggests that politically connected organisations show significantly higher accounting and stock returns (Cingano and Pinotti 2013; Boubakri et al. 2012a; Wu et al. 2012c; Niessen and Ruenzi 2010), have higher leverage (Boubakri, Cosset and Saffar 2008), have greater access to credit (Claessens, Feijen and Laeven 2008; Li et al. 2008; Khwaja and Mian 2005) and pay lower cost of debt (Houston et al. 2014). Further, politically connected organisations hold more cash (Boubakri, Ghoul and Saffar 2013; Su and Fung 2013), are often not penalised by regulators and tax authorities (Correia 2014) and pay lower taxes (Faccio 2010; Adhikari, Derashid and Zhang 2006).

Politically connected organisations also receive preferential treatment in procurement of government contracts (Goldman, Rocholl and So 2013), pay lower cost of equity capital (Boubakri et al. 2012b) and have greater market shares (Faccio 2010). They receive more government subsidies (Wu, Wu and Rui 2012b) and have more chances of being bailed out by the government in case of financial distress (Blau et al. 2013; Faccio, Masulis and McConnell 2006).

However, several studies (e.g. Bliss and Gul 2012a; Faccio 2010; Fan, Wong and Zhang 2007) have provided contrasting evidence, identifying a negative impact of political connections on organisational performance. For instance, Faccio (2010) and Boubakri et al. (2008) provide evidence of lower accounting performance of politically connected organisations. Mohamed et al. (2007) note that politically connected organisations have lower profitability and pay lower dividends. Other studies show that politically connected organisations have lower sales growth, lower earnings growth and lower return on sales (Jackowicz et al. 2014; Fan et al. 2007). In addition, there is evidence that politically connected organisations pay higher cost of debt (Bliss and Gul 2012a), are more likely to report negative equity (Bliss and Gul 2012b) and exhibit significantly lower ROA (Faccio 2010; Bertrand et al. 2006).

The above literature provides evidence of both positive and negative effects of political connections. Due to these conflicting findings, it remains a challenging task to prove, disprove or generalise the association between political connections and organisational performance, thereby providing the first motivation to conduct the current study.

1.2.2. To provide evidence of the association between political connections and organisational performance in Pakistan

There are two strands of studies which examine the association between political connections and organisational performance: cross-country studies and single country-specific studies. A number of studies (e.g. Siwapong 2013; Caprio, Faccio and McConnell 2011; Chen, Ding and Kim 2010; Riahi-Belkaoui 2004; Friedman, Johnson and Mitton 2003) have adopted a cross-country approach to examine the characteristics of politically connected organisations. There are, however, large differences among countries in terms of the nature and type of political connections, socio-political settings, governance mechanisms and cultural dimensions, which make cross-country comparisons difficult and often impractical. As a result, there is a growing interest in investigating political connections within a specific country.

Previous single country-specific studies on political connections have focused on the United States (US) (e.g. Houston et al. 2014; Luechinger and Moser 2014; Knoeber and Walker 2013) and some European countries including Germany, France, Poland, Spain and Italy (e.g. Bona-Sanchez, Perez-Aleman and Santana-Martin 2014; Jackowicz et al. 2014; Ferguson and Voth 2008; Bertrand et al. 2006). In the Asian region, research on political connections has focused mostly on Japan (Dow and McGuire 2009), Indonesia (Leuz and Oberholzer-Gee 2006), Malaysia (Ebrahim et al. 2014; Wahab et al. 2009; Fraser, Zhang and Derashid 2006), Thailand (Polsiri and Jiraporn 2012; Charumilind, Kali and Wiwattanakantang 2006), Taiwan (Chen, Shen and Lin 2013b; Yeh, Shu and Chiu 2013) and China (Du, Zeng and Du 2014; Zhang et al. 2014; Wu, Li and Li 2012a; You and Du 2012). There is, however, little research on political connections in the South Asian region, with the exception of Khwaja and Mian (2005) who examined the association between political connections and access to credit in Pakistan. It is important to undertake studies within the South Asian countries as several of these countries are characterised by high corruption, inefficient laws, poor implementation of laws and inferior code of ethics and governance practices. Hence, limited evidence of the influence of political connections on organisational performance, in politically instable and perceived as highly corrupt countries of South Asia, is another motivation of this study.

Pakistan is located in the South Asian region and is characterised as politically instable, with a weak socio-economic structure. There are a few laws concerning conflict of interest; governance mechanisms are inefficient and rule of law remains poor (Constable 2001). Transparency International (2014) consistently ranks Pakistan as one of the highly corrupt countries in the world. Further, a few families control a large proportion of nation’s economic resources. Many of these families are either directly involved in politics or have connections with politicians and allegedly use their political connections to maximise their wealth (Rehman 2006).

Khwaja and Mian (2005) posit that in Pakistan, politically connected organisations are likely to obtain more loans and their loans are more likely to be written off. The State Bank of Pakistan (SBP) has on several occasions published a list of loan defaulters (Amin 1994), with most of the defaults relating to politically connected organisations (Lodi 1999). A significant proportion of these defaults are wilful defaults (Husain 2002). Accordingly, Pakistan provides an excellent research setting to investigate the impact of political connections on organisational performance.

1.3. Contributions of this study

The study makes several contributions. Firstly, the results of the study help to address the mixed findings of previous literature, by providing evidence of the impact of political connections on organisational performance in an environment characterised by political instability, high level of corruption and a weak regulatory environment. Secondly, this is the first study which provides evidence of political connections and their impact on organisational performance in Pakistan. The findings of the study can be generalised to other South Asian countries, most of which have similar socio-economic, political and regulatory structures. The findings may also be generalised to several other developing countries with similar socio-economic and political conditions. The findings of the study also provide important insights for political and regulatory authorities.

1.4. Structure of the thesis

The remainder of this thesis is organised as follows. Chapter 2 provides definition of political connections; reviews the existing literature concerning political connections and organisational performance and discusses the political and governance context of Pakistan. It also provides some examples of political connections in Pakistan and develops relevant hypothesis concerning the association between political connections and organisational performance in Pakistan. In Chapter 3, the research methodology of the study is outlined, variables are defined and data collection procedures are described. Chapter 4 reports and discusses the descriptive statistics and the results of hypotheses testing. Finally, Chapter 5 provides conclusions, discusses implications and outlines contributions and limitations of the study.

Chapter 2

Literature review and hypotheses development

This chapter is structured as follows. Section 2.1 elaborates different definitions of political connections used in previous studies. Section 2.2 reviews the extant literature on the impact of political connections on organisational performance. Section 2.3 outlines the political and governance context of Pakistan and Section 2.4 provides an overview of political connections in Pakistan. Hypothesis concerning the association between political connections and organisational performance in Pakistan is developed in Section 2.5. Finally Section 2.6 provides a summary of the chapter.

2.1. Definition of political connections

Due to differences in the nature of political connections across countries, there are various definitions of political connections. Most research on political connections in the US tends to identify political connections in terms of campaign contributions and/or donations made by organisations to politicians and political parties. For instance, Ramanna and Roychowdhury (2010) used campaign contributions data to identify politically connected organisations in the US. Blau et al. (2013) identified similar connections by tracking lobbying expenditures made by the US organisations. Correia (2014) used both campaign contributions and donations made by the US organisations to identify politically connected organisations. However, political connections made through campaign contributions and donations are temporary and are beneficial only in the short-term (Faccio 2006). This definition can only be used where political donations and contributions are legal and documented.

Literature has also provided a variety of definitions to identify political connections in the European countries. For instance, Ferguson and Voth (2008), in their study on the impact of political connections in Nazi Germany, identified organisations as politically connected if their owners had provided financial and/or political support to the Nazi Party or Adolf Hitler[1]. However, a later study in Germany by Niessen and Ruenzi (2010), classified an organisation as politically connected if a member of the German "Bundestag"[2] was on the payroll of the organisation. In addition, Cingano and Pinotti (2013) used employment of a local politician by an Italian organisation as a measure of its political connection. Jackowicz et al. (2014), however, used a broader measure in Poland and included employment of current and/or former politicians to classify an organisation as politically connected. An even broader definition was used by Bona-Sanchez et al. (2014) in Spain, who identified an organisation as politically connected if any of its directors held a political position in the government at local, Spanish or European level. Inconsistency in defining political connections in European countries can be explained in the background of varying political structures across Europe and relatively stronger local governments in most European countries.

Several studies in South East Asia (e.g. Gomez and Jomo 1997; Johnson and Mitton 2003; Fisman 2001) have defined an organisation as politically connected if it is related to a top politician. For instance, Johnson and Mitton (2003), based on the analysis of Gomez and Jomo (1997)[3], classified an organisation in Malaysia, as politically connected if any of its top officers or large shareholders had close relationships with Mahathir Bin Muhammad[4], Daim Zainuddin[5], or Anwar Ibrahim[6]. Several other studies in Malaysia (e.g. Wahab, Zain and Rahman 2013;Adhikari et al. 2006; Gul 2006) have adopted the same definition of political

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[1] Adolf Hitler was German chancellor from 1933 to 1945. <http://www.history.co.uk/biographies/adolf-hitler>
[2] "Bundestag" is the name of the German parliament. <http://www.bundestag.de/htdocs_e/bundestag>
[3] Gomez and Jomo (1997), while providing a detailed analysis of political connections of Malaysian organisations, classified two types of organisations as politically connected i.e. a) Organisations having a direct or indirect link to powerful Malaysian politicians and b) Organisations having "Bhomiputra" directors on their board. This later classification is a unique phenomenon in Malaysia where the government promotes and favours businesses owned by ethnic Malays who are termed as "Bhomiputra" meaning "son of the soil".
[4] Dr. Mahatir Bin Muhammad won five terms as the Prime Minister of Malaysia, before resigning in October, 2003, thus ending a 22 years rule. <http://www.biography.com/people/mahathir-mohamad-9395417>
[5] Daim Zainuddin is a powerful Malaysian politician, having a long career in civil service, business and politics. He has been a member of Malaysian Senate from 1980 to 1982, a member of Malaysian parliament from 1982 to 2004, and finance minister of Malaysia from 1984 to 1991.<http://daimzainuddin.com/about.php>
[6] Anwar Ibrahim has headed several ministries including finance ministry of Malaysia. He has been deputy Prime Minister of Malaysia from 1993 to 1998.
<http://www.aljazeera.com/indepth/spotlight/malaysiaelections/2013/05/20135112593475097 2.html>

connections. Similar definition has been adopted in Indonesia as well, where Leuz and Oberholzer-Gee (2006), following Fisman (2001), used Suharto Dependency Index[7] to classify Indonesian organisations as politically connected if they were related to Indonesian President Suharto[8]. This identification of political connections with certain politicians in Malaysia and Indonesia is because of the relationship-based economy and long and unchallenged rule of Mahatir Bin Muhammad in Malaysia and Suharto in Indonesia.

Government control over socio-political policies and economic resources is a unique feature of China, which enables top government officials to provide the connected organisations preferential access to scarce economic resources. Consequently, several studies in China (e.g. Su, Fung and Yau 2013; Wu et al. 2012b; Fan et al. 2007) have classified an organisation as politically connected if any of its directors or Chief Executive Officer (CEO) or Chairman of the Board is a current or former officer of the central or local government, or if he/she has served in the military at or above a certain level. However, Li et al. (2008) while investigating the impact of political connections on financing and performance of Chinese firms, used entrepreneurs' membership of the Chinese Communist Party to classify an organisation as politically connected. This identification of connection with a political party has also been used in the US by Goldman, Rocholl and So (2009), who traced the connections of business organisations with the US Democratic and Republican parties.

The most comprehensive and broadly used definition of political connections is provided by Faccio (2006) who examined 20,202 public listed companies in 47 countries to classify political connections into two types, namely direct political connections and indirect political connections. An organisation is classified as directly connected if any one of its top officers or a large shareholder is a member of parliament or cabinet or is a head of the state. A top officer

[7] Suharto dependency Index is developed by the "Castle Group", which is a leading economic consulting firm in Jakarta, Indonesia. The index describes the level of association of Indonesian organisations with President Suharto (Fisman 2001).
[8] Mr. Suharto has been the president of Indonesia from 1967 to 1998.
<http://www.britannica.com/EBchecked/topic/572060/Suharto>

is defined as any one of the Board members, CEO, Chairman/President, Vice-Chairman/Vice-President and the Company Secretary; whereas a large shareholder is the one who holds at least 10% shares in the organisation. In addition, an organisation is classified as indirectly connected if any one of its top officers or a large shareholder is a close relative or is known to be a close ally/friend of a parliament member or a minister or head of the state.

The above cited definitions were used in different studies to identify political connections of organisation in different countries and under different socio-economic, political and institutional settings. It shows that there is no universal definition which can fit all types of political structures and which can successfully and comprehensively identify political connections across all countries. It is, therefore, important for this study, to carefully define political connections, in light of socio-economic, political and institutional system of Pakistan and its business, economic and cultural environment.

It is not feasible to use campaign contributions and political donations to identify political connections in Pakistan due to lack of publicly available information regarding campaign contributions and political donations. Further, unlike most European countries, the local government system in Pakistan is weak and provincial and central governments are the real power centres. Furthermore, opposite to Malaysia and Indonesia, Pakistan has experienced a high level of political instability since its independence in 1947. Although there are several powerful politicians and political families, no single politician or political party has governed the country for long periods. Additionally, contrary to China and the US, Pakistan has a multi-party system with several military takeovers during its short history. As a result, most popular definitions used in the US, Chinese and Malaysian studies are not suitable for identifying political connections in Pakistan.

This study, therefore, follows Faccio (2006) to identify politically connected organisations in Pakistan. The definition provided by Faccio (2006), has been widely used by many other studies (e.g. Guedhami, Pittman and Saffar 2014; Boubakri et al. 2012a; Chaney, Faccio and Parsley 2011; Faccio 2010). Following Faccio (2006), the study defines an organisation in Pakistan as politically connected if any one of its top officers or a large shareholder or one of their close friends or relatives, is a member of the Parliament or a minister or a head of the State or Government.

The study, however, makes a few adaptations to the definition in order to fit the specific context of Pakistan (discussed later in Section 2.3). Firstly, organisations in Pakistan, in their annual reports, provide the list of shareholders holding at least 5% shares; hence the study uses 5% threshold instead of 10% used by Faccio (2006). Secondly, according to Section 1(2) of The Constitution of Pakistan 1973, Pakistan is a federal republic, consisting of four Provincial Governments and a Federal Government, where Provincial Governments share several powers with the Federal Government. Therefore, the study identifies connections with provincial parliament members, provincial ministers and provincial heads as well. Thirdly, once someone becomes a parliamentarian in Pakistan and gains access to the power, political relationships translate into long term political, social and family networks and remain beneficial, even after someone ceases to be a member of the parliament. Thus, the study takes former as well as present politicians into account. Fourthly, since its independence in 1947, Pakistan has experienced three prolonged periods of military rule and top military officers are considered very powerful (Haqqani 2006). Consequently, the study considers an organisation as politically connected if any of its directors or a large shareholder has served in the military at the top level. Lastly, the study defines an organisation as politically connected, if any of its top officers or a large shareholder has worked in top regulatory, administrative or advisory role in a policy-making organisation like the Export Promotion Bureau of Pakistan (EPB), the Privatization Commission of Pakistan (PCP), the SBP or the Board of Investment (BOI) of the Federal or the Provincial Government.

2.2. Literature review concerning the impact of political connections on organisational performance

As elaborated in the Section 1.2.2, the literature concerning the impact of political connections on organisational performance can be broadly divided into two categories i.e. cross-country studies and single country-specific studies, with mixed findings. Several cross-country studies (e.g. Boubakri et al. 2012a; Chaney et al. 2011; Faccio 2006) have examined different characteristics of politically connected organisations. For example, Faccio (2006) found that political connections are more frequent in countries which have higher levels of corruption while less widespread in countries with strict regulations of political conflict of interest. Further, Faccio (2006) reported a significant increase in stock price of politically connected organisations at the time of election of their top officers to the parliament. The stock price increase was even greater when a businessman became the Prime Minister, implying that the establishment of a political connection enhances performance and that investors have a positive perception of the association between organisational performance and political connections.

Based on Faccio (2006) dataset, Boubakri et al. (2012a) used an international event study approach[9] to investigate 234 politically connected organisations from 12 developed and 11 developing countries. Consistent with Faccio (2006), Boubakri et al. (2012a) reported an increase in ROA of the organisations after the establishment of their political connection. Higher financial leverage and greater use of long term debt by the politically connected organisations were also noted.

Faccio and Parsley (2009) used a distinct method to evaluate the performance of politically connected organisations by identifying the dates of sudden deaths of 122 politicians in 35 countries. An analysis of the stock performance of 8,191 organisations connected to these

[9]An event study is an approach of statistical analysis which analyses the performance before and after the happening of a certain event.

politicians found a significant and immediate value loss for politically connected organisations, after the death of politicians associated with them. This value loss was followed by decrease in sales growth and access to debt of politically connected organisations and was more pronounced in countries with higher levels of corruption. Braun and Raddatz (2010) also report similar findings for banker-politician connections in 82 countries. In particular, they report higher profitability of politically connected banks. This implies that investors perceive politically connected organisations as better performers.

Some cross-country studies (e.g. Faccio 2010; Boubakri et al. 2008; Faccio et al. 2006) have also identified a negative impact of political connections on organisational performance. For instance, Faccio et al. (2006) studied 450 politically connected organisations across 35 countries to report that in case of financial distress; politically connected organisations have a higher likelihood of being bailed out by the government. However, the post-bailout financial performance, measured in terms of ROA and industry adjusted ROA, of politically connected organisations was significantly lower than their non-connected competitors. In addition, Faccio (2010) used Faccio's (2006) database to investigate 16,191 organisations in 47 countries and reported significantly lower accounting performance (in terms of ROA) of politically connected organisations. Results found higher leverage, higher market power and lower taxing of politically connected organisations. The difference in performance was slightly higher in more corrupt countries.

Another cross-country study by Boubakri et al. (2008) reported poor accounting performance (measured in terms of return on sales, sales growth and earnings growth) of politically connected organisations in 245 newly privatized organisations from 27 developing and 14 developed countries. They found that political connections were more prevalent in countries with lower judicial independence. Coverage of developing countries in cross-country studies is, however, limited due to data limitations (Faccio 2006) and hence the findings may not be generalised to many developing countries (Faccio and Parsley 2009).

Single country-specific studies examining the impact of political connections on organisational performance are mostly clustered in Europe, the US, South East Asia and China. The evidence of superior performance of politically connected organisations in Europe can be traced back to 1933, when a significant proportion of large German organisations were found strongly linked to Adolf Hitler and his National Socialist German Workers' Party (the Nazi Party). When Hitler was appointed German Chancellor in January 1933, organisations connected to him experienced significant gain in their stock prices (Ferguson and Voth 2008). A later study in Germany has also noted significantly higher stock performance and slightly higher accounting performance of organisations connected to German "Bundestag" in 2006 (Niessen and Ruenzi 2010). Interestingly, difference in stock performance significantly reduced after the introduction of a new conflict of interest law in Germany in 2006.

In Italy, organisations that had employed local politicians exhibited greater market power and higher profitability (Cingano and Pinotti 2013). Amore and Bennedsen (2013) concluded that in Denmark, which has strong institutions and is considered as one of the least corrupt economies, organisations connected with local politicians by family, exhibit better performance. In contrast, Bertrand et al. (2006) report that business organisations in France having former government officials as CEOs, have to create more jobs and have to postpone plant closures, particularly close to elections. The result is higher operating cost due to increased wages; hence, lower profits.

In Eastern Europe, Jackowicz et al. (2014) used 2428 firm-year observations for 316 listed non-financial organisations in Poland, covering the period from 2001 to 2011, and concluded that 33.2% of the organisations were politically connected because they either had a current or a former politician on their Board. However; politically connected organisations in Poland had significantly lower net income to sales ratio. The negative impact of political connections was more pronounced for organisations with multiple political connections. In addition, when profitability was measured on the basis of gross income to sales ratio, no significant difference was found between politically connected and non-connected listed organisations. In Russia, Slinko, Yakovlev and Zhuravskaya (2005) report overall higher performance of politically connected organisations because they were able to capture regulations, resulting in a negative impact on non-connected organisations and on economic growth.

In the US, Goldman et al. (2009) investigated performance of the US organisations connected to the Republican and the Democratic parties to report a significant increase in stock value of organisations connected to the Republican Party, after it won elections in 2000. In contrast, organisations connected to the Democratic Party experienced a considerable decrease in value. Luechinger and Moser (2014) report that politically connected organisations in the US show positive abnormal stock returns as a result of political appointments from the corporate sector, suggesting investors' positive perceptions of the value of political connections. Fisman et al. (2012), however, found no value of ties with Richard (Dick) Cheney[10] for business organisations in the US.

In South East Asia, research on political connections has mostly focused on Malaysia, Indonesia and Thailand. In highly relationship-based economy of Malaysia, politically connected organisations receive preferential treatment in allocation of resources (Johnson and Mitton 2003) and pay lower taxes (Adhikari et al. 2006). Chen et al. (2013a) have also noted preferential treatment of politically connected organisations in Malaysia, resulting in significant abnormal stock returns in response to political events, particularly during the Asian Financial Crisis of 1997. Civilize, Wongchoti and Young (2015), in their longitudinal

[10] Richard Bruce "Dick" Cheney has a long career in the US politics. He served as Chief of Staff to the President Ford from 1975 to 1975, a member of the US House of Representatives from 1979 to 1989, the US Secretary of Defence from 1989 to 1993 and the US Vice-President from 2001 to 2009.
<http://www.biography.com/people/dick-cheney-9246063#meeting-rumsfield-and-seat-in-congress>

study of 653 organisations in Thailand, note consistent and systematic higher stock returns of connected organisations, independent of extreme political events involving top politicians.

In contrast, Mohamed et al. (2007) found that politically connected organisations in Malaysia show significantly lower profitability and pay lower taxes. In addition, Johnson and Mitton (2003) note a more pronounced decrease in stock prices of politically connected organisations in Malaysia during the Asian Financial Crisis of 1997, primarily because of loss of government subsidies to these organisations. Further, Fisman (2001) reported a greater volatility in stock prices of the politically connected organisations in response to bad news. Specifically, it was found that business organisations in Indonesia connected to President Suharto suffered a significant decrease in their stock price after the news of his illness. This decrease in stock price indicates that a significant portion of stock value of these organisations was derived from their political connections with President Suharto.

Political connections also seem to be very important in China. For example, politically connected organisations in China have higher stock returns and higher premiums (Yang, Wilson and Wu 2014; Su, Zhang and Zhang 2013). Su and Fung (2013) note that political connections of business organisations in China enable them to increase their sales as well as to lower their cost of sales; resulting in an overall better profits and returns. In addition, Wu et al. (2012b); Wu et al. (2012c) and Li et al. (2008) have documented evidence of higher performance (measured in terms of ROA, ROE and Tobin’s Q) of politically connected organisations in China.

Importance of political connections in China is further highlighted by the findings that politically connected Initial Public Offerings (IPOs) in China significantly outperform non-connected IPOs (Liu, Uchida and Gao 2012; Wu et al. 2012a). Fan et al. (2007), however, provide contrasting evidence in their analysis of three years’ post-IPO performance of Chinese organisations. In particular, they report 18% lower stock performance of politically connected organisations as well as significantly low sales growth, earnings growth and return on sales.

Further evidence of higher performance of politically connected organisations is available from Brazil and Tunisia. In Brazil, which is a South American country with moderate level of corruption[11], politically connected organisations exhibit higher stock returns because they are able to access bank loans on preferential terms (Claessens et al. 2008). Similar findings have been presented by Lassoued and Attia (2014) for a North African country of Tunisia, which also has moderate corruption levels[12].

The mixed findings regarding the impacts of political connections on organisational performance and limited research on political connections in South Asia warrant further research in the area. This study, therefore, examines the association between political connections and organisational performance (measured in terms of ROA and ROE) of business organisations in Pakistan. Pakistan is located in South Asia, characterised by poor laws, corruption, nepotism and weak socio-economic and political systems. Pakistan provides an excellent research setting to investigate the impact of political connections on organisational performance because most business organisations have direct or indirect political connections.

2.3. The political and governance context of Pakistan

Pakistan, officially known as "Islamic Republic of Pakistan" is a federal republic. It comprises four provinces, namely Punjab, Sindh, Khyber Pakhtunkhwa (KPK), and Baluchistan, and a capital territory namely Federal Capital (FC). Further, there are some

[11] According to the Corruption Perception Index (CPI) 2013, administered by the Transparency International, Brazil is ranked at 72 out of 175 countries. Its score is 42 out of 100 which demonstrates moderate level of corruption. Source: Corruption Perception Index (CPI) 2013, Transparency International. Available from:<https://www.transparency.org/cpi2013/results>

[12] According to Corruption Perception Index (CPI) 2013, Tunisia is ranked at 77 out of 175 countries. Its score is 41 out of 100 which demonstrates moderate level of corruption. Source: Corruption Perception Index (CPI) 2013, Transparency International. Available from: <https://www.transparency.org/cpi2013/results>

Federally Administered Tribal Areas (FATA) and some Provincially Administered Tribal Areas (PATA). While FATA and FC are directly administered by the Federal Government, PATA is managed and administered by the KPK Government. The four provinces have their own provincial governments and enjoy administrative and financial autonomy (*The Constitution of Pakistan*, 1973).

Appendix 1 discusses the political structure of Pakistan in detail and shows that political instability has been an invariable characteristic of Pakistan. Since its independence in 1947, no political government has been able to complete its tenure; however, military dictators and political governments backed by dictators are an exception (Constable 2001). Most of the political governments were either dismissed by the President or toppled by the military dictators on charges of inefficiency, misconduct, nepotism and corruption (Syed 1998). It was the first time in 2013 when Pakistan Peoples' Party Government, formed as a result of 2008 general elections, completed its 5 year's tenure.

Regulatory mechanisms

The corporate sector of Pakistan comprises financial and non-financial sectors which are governed by various statutes and regulatory institutions. Banks and Development Finance Institutions (DFIs) are established under the Banking Companies Ordinance 1962. The SBP is the regulatory body for banks and DFIs, which are beyond the scope of this study. Non-financial institutions in Pakistan are incorporated and managed under the Companies Ordinance 1984 and are governed by the Securities and Exchange Commission of Pakistan (SECP). Listed companies are also required to abide by the Code of Corporate Governance (CCG) of Pakistan, which is an essential part of listing requirements of the stock exchanges. Hence, Companies Ordinance 1984, the CCG of Pakistan, stock exchanges and the SECP comprise major regulatory mechanism for non-financial organisations in Pakistan.[13]

[13] Figure 1 presents organisational structure of regulatory mechanism in Pakistan.

The regulatory mechanism in Pakistan, although theoretically very strong, has several practical limitations. For instance, absence of conflict of interest laws facilitates powerful politicians and former civil servants to obtain private gains (Noorani 2015; Iqbal 2013; Rehman 2011; Daily Dawn 2004). Further, poor implementation of bankruptcy law allows business owners (particularly those with powerful connections) to default on bank loans (Khwaja and Mian 2005). Caveats in corporate regulatory systems are also evident from widespread allegations of manipulation (The Economist 2013) and insider trading (The Express Tribune 2014; Abbasi 2013) in the KSE. Hence, weak legal system, inefficient monitoring by the SECP, family control over companies and absence of penal provisions, result in poor implementation of good corporate governance practices in Pakistan (LawTeacher 2015).

The Federal Board of Revenue (FBR), the apex tax collection body, is often blamed of issuing Statutory Regulatory Orders (SROs) to facilitate powerful lobbies (UNDP Pakistan 2015; Daily Dawn 2013). Further, several discretionary powers in tax assessment allow corrupt practices in the FBR (Rana 2014; Daily Dawn 2010). Legal system in Pakistan remains weak and there is widespread anecdotal evidence of corruption in executive as well as in judiciary (US Department of State 2012). In addition, National Accountability Bureau (NAB) which is the apex authority to curb financial corruption lacks proper funding (US Department of State 2013) and is often accused of political interference (Kharal 2011).

An editorial of a Pakistani newspaper Daily Dawn (2014) best sums the regulatory atmosphere in Pakistan, stating: "…Rules are in place and sometimes inquiries are ordered. But, unlike the rest of the world, stiff punishments in Pakistani capital markets are unheard of."

Figure 1: Regulatory structure in Pakistan

Source: Official website of the Lahore Stock Exchange,
Available from: <http://www.lahorestock.com/#/Regulations/RegulatoryStructure.aspx>

2.4. Political connections in Pakistan

In Pakistan, connections with powerful elite are considered a matter of pride and legitimacy; and are expected to yield enormous social and financial benefits. A review of literature suggests that there is no law in place concerning the political conflict of interest. Absence of conflict of interest laws in Pakistan allows connections between businesses and politicians. For example, the current and third time Prime Minister of Pakistan is the director and the Chairman of Sharif Group[14], a prominent business group of Pakistan, having ownership stakes in steel, sugar and paper industries.

Another example is a big business group Yousaf Dewan Group, which has ten companies listed on the KSE. The group website, while reporting the profile of its Chairman, states *"…From 1999 to 2003, he remained a Minister in the Sindh Provincial Government for Industries, Labour, Transport, Mines & Mineral Development, Local Government, and Housing & Town Planning. He was also the Minister for Finance and Information,*

[14] <http://www.sharifgroupn.com/en/index.php?option=com_content&view=article&id=64&Itemid=81>

Government of Sindh."[15] Another example is Noon Sugar Mills Limited, which on its website states about one of its directors and a major shareholder as *"...He became one of the youngest members of the National Assembly of Pakistan. He also served on the Industries Committee of the National Assembly.*"[16]

Several companies also report their relationships with the Government and the military. An example is the annual report 2013 of Fatima Fertilizer Limited, which states about its Chairman as *"...He has served as Member of the Privatization Commission, Board of Investment, Tariff Reforms Commission and Securities and Exchange Ordinance Review Committee. Over the years, he has been nominated on the Board of Directors of a number of companies by the Government of Pakistan".*[17] Gammon Pak limited, a construction company, on its website, reports about one of its directors as *"...After a brilliant career spanning 37 years, General Ali retired from the Pakistan Army as its Chief of General Staff in 1998. .... On retirement from the Army, he joined his family business."*[18]

Anecdotal evidence suggests that business organisations obtain benefits from their political connections. This is reflected in the book "Capitalism's Achilles heel: Dirty money and how to renew the free-market system." It states, "*...During the 1980s and early 1990s, given Sharif's (present ruling family of Pakistan and the province of Punjab) political control of (the province of) Punjab and eventual Prime Ministership of the country (Pakistan), Ittefaq Industries grew from its original single foundry into 30 businesses producing steel, sugar, paper, and textiles, with combined revenues of $400 million, making it one of the biggest private conglomerates in the nation. As in many other countries, when you control the political realm, you can get anything you want in the economic realm...*" (Baker 2005)

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15 <http://www.yousufdewan.com/Our%20team.html>
16 <http://www.noonsugar.com/board_of_director's_profile.htm>
17 <http://www.fatima-group.com/fatimafertilizer/financialresults.php>
18 <http://www.gammonpakistan.com/html/management.html>

2.5. The association between political connections and organisational performance in Pakistan

Pakistan, like most other South Asian countries, has a high level of corruption, weak regulatory mechanisms and poor implementation of law. In particular, in the absence of conflict of interest laws, business organisations are expected to have frequent connections with politicians and government officials. Various studies argue that such context allows politically connected organisations to gain a competitive advantage over their non-connected competitors, thus resulting in superior performance. For instance, Lassoued and Attia (2014) find that due to weak regulatory environment, politically connected organisations in Tunisia have greater access to key resources. In particular, they have easier access to credit, receive more government subsidies and enjoy tax benefits; resulting in better financial performance.

Empirical evidence suggests that politically connected organisations in Pakistan have an easier access to credit and have significantly higher default rates (Khwaja and Mian 2005). In addition, anecdotal evidence reports favours provided by the Government to politically connected businesses. For instance, licenses to set up various industries are often issued as a political bribe (Iqbal 2013; Rehman 2011). Further, powerful politicians often pressurize government banks to provide loans to businesses connected with them (Pakistan today 2011). As these politically motivated loans are often issued against insufficient securities (Rana 2013), most of these loans become non-performing and are either restructured or are written off on political grounds (Gishkori 2015).

Apart from receiving preferential access to credit, politically connected organisations in Pakistan often receive subsidies from the Government (Daily Dawn 2004), and receive preferential treatment in procurement of government contracts (Noorani 2015), resulting in a loss to the national exchequer (Daily Dawn 2004). Further, the FBR is often blamed for issuing SROs to provide tax benefits to politically connected businesses (Business Recorder 2015).

In addition, politically connected businesses are often blamed of forming cartels to manipulate market prices in their favour (Bhutta 2015); however, the Competition Commission of Pakistan seldom takes any serious action against such coercive practices (Rana 2010). Further, in the absence of conflict of interest laws, one can expect that politically connected organisations can not only have insider information of future policy changes but also have the power and resources to get policies formulated according to their interests. Hence, it is hypothesised that:

In Pakistan, politically connected organisations are expected to perform better than non-connected organisations.

2.6. Summary

A review of literature suggests that the nature of political connections varies in different countries and in different political structures. As a result, previous studies have used several definitions to define and measure political connections. Literature also suggests that political connections may have positive as well as negative impacts on organisational performance. The discussion of the weak regulatory mechanisms, poor implementation of law and non-existence of conflict of interest laws in Pakistan leads to the expectation that politically connected organisations in Pakistan perform better than non-connected organisations.

Chapter 3
Research method

The objective of this chapter is to discuss the research method of this study. The chapter is structured as follows. Section 3.1 outlines the regression model used to test the hypothesis developed earlier in Chapter 2. Section 3.2 discusses the measurement of dependent variables. Section 3.3 provides definition and measurement of independent variables and Section 3.4 considers the measurement of control variables used in the study. While Section 3.5 describes the data collection method used in the study, Section 3.6 summarises the chapter.

3.1. Method of analysis

For the purpose of testing the hypothesis developed in Chapter 2, this study uses a quantitative approach. Quantitative methodology is suitable for this study because it allows for predicting and controlling cause effect relations in an objective way.

The study used the following multiple linear regression model to test the association between political connections and organisational performance. The model is adopted from Su and Fung (2013) and has been used by other studies (e.g. Ding et al. 2014; Wu et al. 2012c) to investigate the impact of political connections on organisational performance.

$$\mathrm{PERF} = \alpha + \beta_1\mathrm{POLCON} + \beta_2\mathrm{FSize} + \beta_3\mathrm{Leverage} + \beta_4\mathrm{Growth} + \beta_5\mathrm{BInd} + \beta_6\mathrm{Top1} \\ + \beta_7\mathrm{ACInd} + \beta_8\mathrm{Auditor} + \beta_9\mathrm{CEODual} + \varepsilon$$

Where: PERF means organisational performance, measured as ROA and ROE. α is the intercept and POLCON stands for political connection. POLCON measures the political connection of an organisation. FSize means Firm Size at the end of the year 2013 and Leverage means leverage of an organisation at the end of the year. Growth represents sales growth percentage of an organisation. BInd is a measure of board independence and Top1 is the percentage of shares held by the largest shareholder. ACInd is a measure of audit committee independence and Auditor represents if the auditor is one of the BIG4 accounting firms. CEODual is a measure of CEO duality and ε is the error term.

Further explanation and measurement of the variables is provided in the next three sections.

3.2. Dependent variable

Organisational performance, represented in the regression model by PERF, is measured using two accounting measures, namely ROA and ROE. ROA and ROE are the most widely used accounting measures of organisational performance (Ding et al. 2014; Su and Fung 2013; Boubakri et al. 2012a). ROA is calculated as the ratio of net income before finance cost to total assets of the firm while ROE is calculated by dividing net income after interest and tax with shareholders' equity.

3.3. Independent variable

POLCON (political connection) is a dummy variable to measure political connections. It is a binary variable that is equal to 1 if the organisation is politically connected and otherwise equal to 0. As discussed earlier in Section 2.1, the study defines an organisation as politically connected:

1. If any one of its top officers or a large shareholder is a current or a former member of the Parliament or minister or head of the Government.

2. If any one of its top officers or a large shareholder has served at a top position in the Government or the military.

3. If any one of its top officers or a large shareholder is currently working or has previously worked in top regulatory or advisory role in a policy-making organisation like the EPB, the PCP, the SBP or the BOI of the Federal or a Provincial Government.

4. If a top officer or a large shareholder of an organisation is a close friend or a close relative of the persons mentioned in 1, 2 and 3.

A top officer means a member of the Board of Directors, CEO, Chairman/President and Vice-Chairman/Vice-President of an organisation. A large shareholder is one who owns at least 5% shares in the organisation. Parliament includes the National Assembly (NA) of Pakistan, the Senate of Pakistan and the Provincial Assemblies of the four provinces of Pakistan. Further, minister includes federal minister, minister of state, provincial minister and (special) adviser to the Prime Minister or a Chief Minister. Head of the Government includes the President of Pakistan, the Prime Minister of Pakistan, the Governors and the Chief Ministers of the four provinces of Pakistan.

Serving at a top position in the Government means working at least at Additional Secretary level in the Federal or a Provincial Government. Serving at a top position in the military means working at least as a two star general in the military i.e. Major General in Pakistan Army, Rear Admiral in Pakistan Navy and Air Vice Marshal in Pakistan Air Force.

To further investigate the impact of different types of political connections on organisational performance, independent variable POLCON is divided into two measures of political connections i.e. POLCON-P and POLCON-G. POLCON-P means political connection of an organisation with a politician. It is equal to 1 if a top officer or a large shareholder or a close friend or relative of a top officer or a large shareholder is a current or former member of the Parliament or minister or head of the Government/State, and is otherwise equal to 0. POLCON-G is equal to 1 if a top officer or a large shareholder of a politically connected organisation or one of their close friends or relatives has served at a top position in the Government or the military or has worked at a top regulatory or advisory position in a policy-making organisation, and is otherwise equal to 0. In summary, if a politically connected organisation is (directly or indirectly) connected with a politician, POLCON-P is equal to 1 and if the organisation is connected with former military or government officers or persons in an advisory role (directly or through friends and relatives); POLCON-G is equal to 1.

To further investigate what impact direct and indirect political connections have on organisational performance, POLCON is further divided into POLCON-D and POLCON-IND. POLCON-D means direct political connection of a politically connected organisation. It is equal to 1 if a politically connected organisation is directly connected i.e. if any of its top officers or a large shareholder himself/herself is a current or former member of the Parliament or a minister or head of the Government or has served at a top position in the Government or the military or has worked at top regulatory or advisory role in a policy-making organisation, and is otherwise equal to 0. POLCON-IND takes the value of 1 if a politically connected organisation is indirectly politically connected i.e. if a close friend or a close relative of any of its top officers or a large shareholder is a current or former member of the Parliament or a minister or head of the Government or has served at a top position in the Government or the military or has worked at top regulatory or advisory role in a policy-making organisation; and is otherwise equal to 0.

3.4. Control variables

In line with Su and Fung (2013), the study controls the following variables.

3.4.1. Firm size

Firm size, represented in the regression model as FSize, is measured as natural log of total assets of an organisation at the end of the year. Literature suggests that large firms are more likely to be politically connected and are expected to have better performance due to economies of scale (Niessen and Ruenzi 2010; Faccio 2006). Large firms are more likely to be politically connected because big business tycoons have more incentives and more resources to get involved in politics, to protect and grow their businesses. Hence, the study controls for Firm Size because of its potential impact on performance.

3.4.2. Leverage

Leverage is the organisation's debt to assets ratio at the end of the year. Leverage may have an impact on performance because leverage represents the ability of an organisation to attract debt. There is evidence that politically connected organisations tend to obtain more debt than their competitors (Claessens et al. 2008; Khwaja and Mian 2005). Hence, the study controls for leverage while investigating the association between political connections and organisational performance.

3.4.3. Growth opportunities

Growth represents an organisation's growth opportunities, measured as percentage of sales growth rate. Sales growth rate is measured as percentage change in sales from previous year i.e. 2012. Organisations having more growth opportunities are likely to have better performance, compared to organisations with less growth opportunities (Su and Fung 2013).

3.4.4. Board independence

Board independence (Bind) is a proxy of the quality of organisation specific corporate governance and is measured as the ratio of number of independent directors to the total number of directors on the Board. This control variable is in line with most corporate governance literature which suggests that an independent board helps improve financial performance (Nguyen and Nielsen 2010; Bhagat and Bolton 2008; Stanwick and Stanwick 2002).

3.4.5. Percentage of shares held by the largest shareholder

Top1 in the regression model represents the percentage of shares held by the largest shareholder. In line with Su and Fung (2013), the study controls for top shareholder because of its potential impact on management policies, thus effecting organisational performance.

3.4.6. Audit committee independence

Audit committee independence represented in the regression model as ACInd, is adopted from Bliss and Gul (2012a). It is a binary variable that is equal to 1 if the Chairman of the audit committee is an independent director and is otherwise equal to 0. Audit committee independence is included in the regression model because of the evidence that political connections have a negative impact on audit committee independence (Bliss, Gul and Majid 2011), which may have an effect on organisational performance.

3.4.7. Auditor

Adopted from Ding et al. (2014), Auditor is a dummy variable that is equal to 1 if the auditor is a Big4 audit firm and is otherwise equal to 0. Prior literature on political connections suggests that politically connected organisations pay higher audit fees (Wahab, Zain and James 2011) and they are more likely to appoint Big4 auditors (Guedhami et al. 2014). In addition, the evidence provided by Wahab et al. (2013) suggesting that political connections may have a negative impact on auditor independence, makes Auditor an important control variable.

3.4.8. CEO duality

CEO duality is represented in the model as CEODual. It is a dummy variable that is equal to 1 if positions of the CEO and the Chairman of the Board are held by the same person and otherwise equal to 0. Because of its potential impact on organisational performance, CEO duality has been controlled by several other studies (e.g. Ding et al. 2014; Gray, Harymawan and Nowland 2014; Yu 2010) while investigating the impact of political connections on business organisations.

3.5. Data collection

The study used an archival research method to test the hypothesis developed in Chapter 2. Data was obtained from annual reports for the year 2013, downloaded from official websites of the organisations listed on the KSE. As of 1st of August 2015, there are 909 organisations listed on the KSE. Following other studies (e.g. Bliss and Gul 2012b; You and Du 2012), 455 financial sector organisations are excluded from the analysis for two major reasons. First, regulation and governance of financial sector organisations is different from non-financial organisations. In particular, financial sector organisations in Pakistan are regulated by the SBP that imposes stiff regulatory requirements. Second, financial sector in Pakistan is not a traditional sector and is not expected to have many political connections. Sampling frame for this study, therefore, consists of 454 non-financial KSE listed organisations.

Out of 454 organisations in the sampling frame, 183 were excluded because of data limitations. For these organisations, either official websites were not found or they did not have 2013 annual report on their websites. These include some organisations which did not have any business activity during 2012 or 2013. Another 14 organisations were excluded because they had large accumulated losses on their balance sheets, as well as a negative equity, and the auditors had expressed concern on them being going concerns. Another 7 organisations were excluded from the analysis because they had outliers in one or more variables. As a result, the final sample of analysis consists of 250 non-financial organisations listed on the KSE.

All KSE listed organisations provide information about their external auditors (Auditor) and their Chairman and CEO (CEODual). Further, listing rules of the KSE require all organisations to include the statement of compliance with the CCG in their annual reports, from which data was obtained for firm level variables of audit committee independence (ACInd) and the ratio of number of independent directors to total number of directors (Bind). In addition, pattern of shareholding is an essential part of annual reports, which provided information about percentage of shares held by the largest shareholder (Top1).

Financial data for the year 2013 for total assets, total debt, finance cost, Net Income before Tax (NIBT) and Net Income after Tax (NIAT) was obtained from audited financial statements, which are an essential part of annual reports. Net Sales for the years 2012 and 2013 were also obtained from 2013 annual reports. This data was used to compute dependent variables (ROA and ROE) and financial control variables i.e. Firm size (FSize), Leverage (Leverage) and sales growth rate (Growth).

Data for independent variable i.e. political connection (POLCON) was collected using multiple sources. Data for names of top officers and large shareholders of the organisations was collected from annual reports of the organisations. Organisations report names of members of the Board of Directors, Chairman and CEO in their annual reports. Further, names of shareholders holding at least 5% shares are reported in the pattern of shareholding.

Data for politicians and former government and military officers was collected from several sources. Firstly, websites of the Federal[19] and the Provincial parliaments[20] of Pakistan and Office of the Prime Minister of Pakistan website[21] provide names of current as well as former parliament and cabinet members. Secondly, Election Commission of Pakistan (ECP) website[22] provides names of all the persons elected as parliament members since 1970, and in some cases names of runner ups as well. Thirdly, a website operated by a newspaper Daily Tribune[23], provides a comprehensive list of 21495 Pakistani politicians, their party affiliations and their membership details. Further, organisations often report profiles of their top officers on their websites and in their annual reports. These profiles provide information if a top officer has held a top position in the Government or the military or if he/she has served in a policy-making organisation.

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[19] Official website of the National Assembly of Pakistan <http://www.na.gov.pk/en/index.php>

[20] Official website of the Punjab Assembly of Pakistan http://www.pap.gov.pk/index.php/home/en>
Official website of Sindh Asembly of Pakistan <http://www.pas.gov.pk/index.php/home/en>
Official website of Balochistan Assembly of Pakistan <http://www.pabalochistan.gov.pk/index.php/home/en>
Official website of Khayber Pakhtunkhwah Assembly of Pakistan <http://www.pakp.gov.pk/2013>

[21] Official website of the office of the Prime Minister of Pakistan <http://www.pmo.gov.pk/index.php>

[22] Official website of the Election Commission of Pakistan <http://ecp.gov.pk>

[23] The website maintained by the Daily Tribune, Pakistan <http://elections.com.pk/candidatelist.php>

Politically connected organisations were identified by matching the names of their top officers and large shareholders with names of politicians and former government and military officers. Close relationships were identified using internet searches, as electronic and print media often report these ties in their stories. An organisation was only classified as politically connected if there was a match of full name. Whenever more than one connection was identified for a particular organisation, the connection which was more direct and was more powerful was counted. For example, if an organisation had two directors with political positions, one being a former government servant and the other being a minister, the organisation was classified as politically connected through minister. Similarly, if an organisation had a direct as well an indirect connection, it was classified as directly connected.

An organisation was classified as politically connected with the Government if such information was available through official website of the organisation or its annual report or from some credible news report. Organisations with missing data were deleted from the record.

The study collected data from the publicly available resources i.e. annual reports of listed organisations, official government websites, website of the ECP and newspaper websites. As there is no human interaction involved at any stage of the data collection process, hence, there are no ethical concerns pertinent to the study.

3.6. Summary

The study uses a quantitative methodology by employing a multiple linear regression model to examine the association between political connections and organisational performance of 250 non-financial organisations listed on the KSE of Pakistan. Organisational performance is measured using ROA and ROE as outlined in Section 3.2. Section 3.3 and 3.4 provide the definition and measurement of dependent variable and each control variable. Description of the sample and data collection procedure is provided in Section 3.5.

Chapter 4
Results

This chapter provides descriptive statistics for independent, dependent and control variables included in the regression analysis and reports results for analysis of variance and regression analysis used to test the hypothesis developed in Chapter 2. Further, validity of the regression model is examined by testing the assumptions of linearity, homoscedasticity, residual independence, normality and multicollinearity.

The chapter is structured as follows. Section 4.1 provides descriptive statistics for dependent, independent and control variables used in the study. Section 4.2 reports results of the regression analysis performed to test the hypothesis developed in Chapter 2. Section 4.3 presents results of additional analysis performed to examine the robustness of results of the main regression. Section 4.4 reports results of tests performed to examine the validity of multiple regression model. Finally, chapter summary is provided in Section 4.5.

4.1. Descriptive statistics

Table 1 presents descriptive statistics of politically connected organisations by industry, based on International Classification Benchmark (ICB)[24], adopted by the KSE. The results reveal that political connections are common in Pakistan with 52.40% of total organisations in the sample being politically connected. Table 1 also shows that political connections in Pakistan are common across all industries with oil and gas industry being the most politically connected (85.71%), closely followed by technology (83.33%) and utilities (80.00%). Healthcare industry, however, has the lowest percentage of political connections (28.57%). High percentage of political connections in oil and gas and utilities may be attributable to the fact that these two industries are highly controlled by the Government.

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[24] ICB is developed by FTSE International Limited (FTSE) which classifies companies into 10 industries, 19 super sectors, 41 sectors and 114 subsectors.
<http://www.icbenchmark.com/ICBDocs/Structure_Defs_English.pdf>

Further break-up of politically connected organisations, according to the nature of political connections, reveals that connections with politicians and with former government officials are equally common in Pakistan (connections with politicians 49.62% vs. connections with former government officials 50.38%). However, direct political connections (with politicians and/or former government officials) are more common in Pakistan (64.89%) as compared to indirect (through friends and relatives) political connections (35.11%).

Table 1: Descriptive statistics for political connections

Industry	No. of organisations	Politically connected organisations	
		No.	Percentage
Oil and gas	7	6	85.71
Technology	6	5	83.33
Utilities	10	8	80.00
Miscellaneous	9	6	66.67
Industrials	37	23	62.16
Basic materials	34	17	50.00
Consumer goods	140	64	45.71
Healthcare	7	2	28.57
Total	**250**	**131**	**52.40**

One-way Analysis of Variance (ANOVA) was conducted to test the difference in organisational performance (i.e. ROA and ROE) across different industrial groups. Table 2 below shows the results of ANOVA. It reveals that there is no significant difference in organisational performance across different industries, in terms of both ROA ($F = 1.358$, $p = 0.224$) and ROE ($F = 0.987$, $p = 0.441$).

Table 2: One-way Analysis of Variance, comparing organisational performance across different industries

Panel A: Dependent variable: return on assets (ROA)					
Industry	**N**	**Mean**	**Std. Deviation**	**F-stat**	**Significance**
Basic material	34	0.12	0.09	1.358	0.224
Industrials	37	0.11	0.09		
Consumer goods	140	0.11	0.09		
Healthcare	7	0.15	0.07		
Oil and gas	7	0.14	0.10		
Technology	6	0.07	0.18		
Utilities	10	0.13	0.05		
Miscellaneous	9	0.04	0.09		
Total	**250**	**0.11**	**0.09**		
Panel B: Dependent variable: return on equity (ROE)					
Industry	**N**	**Mean**	**Std. Deviation**	**F-stat**	**Significance**
Basic material	34	0.11	0.17	0.987	0.441
Industrials	37	0.10	0.17		
Consumer goods	140	0.11	0.21		
Healthcare	7	0.16	0.08		
Oil and gas	7	0.22	0.11		
Technology	6	0.01	0.26		
Utilities	10	0.19	0.11		
Miscellaneous	9	0.04	0.19		
Total	**250**	**0.11**	**0.19**		

4.1.1. Dependent variables

Descriptive statistics for the measures of organisational performance (ROA and ROE) are presented in Table 3 below. Average ROA is 11% (0.11), ranging from a minimum of –12% to a maximum of 37%, with standard deviation of 0.09. Average ROE is also 11%; however, it ranges from a low of – 71% to a high of 76%, with standard deviation of 0.19. Same mean values for ROA and ROE but greater range and higher standard deviation of ROE shows a higher variation in ROE than in ROA. Minimum values are negative for both ROA and ROE which are due to negative profits (losses) of one or more organisations during the year 2013.

Table 3: Descriptive statistics for measures of dependent variable

Variable(s)	Minimum	Maximum	Mean	Std. Deviation
Return on assets (ROA)	- 0.12	0.37	0.11	0.09
Return on equity (ROE)	- 0.71	0.76	0.11	0.19

4.1.2. Control variables

Descriptive statistics of categorical control variables used in the regression analysis are presented in Table 4, which shows that CEO duality is 25.6% among total sample as compared to 18.32% for politically connected organisations, implying that CEO duality is more common among non-connected organisations. Percentage of organisations with independent audit committee is higher for politically connected organisations (47.33% for politically connected organisations as compared to 41.6% for total sample). Similarly, politically connected organisations more frequently appoint Big4 accounting firms as their external auditors (politically connected 53.44% vs. total sample 51.6%). These three variables capture the quality of firm level corporate governance. Hence, a higher percentage of politically connected organisations has superior corporate governance measures in place.

Table 4: Descriptive statistics for categorical control variables

Variable(s)	Full sample			Politically connected organisations		
	N	#	%	N	#	%
CEO duality	250	64	25.6	131	24	18.32
Audit committee independence	250	104	41.6	131	62	47.33
Big 4 auditor	250	129	51.6	131	70	53.44

Descriptive statistics related to six continuous control variables used in the regression analysis, are presented in Table 5 below. Mean values for firm size (15.39), leverage (0.52) and sales growth (0.12) are close to the mid-point of their respective ranges. Standard deviation for firm size (1.43) is higher than for leverage (0.21) and for sales growth (0.22). Negative minimum value for sales growth is due to decrease in sales of one or more organisations for the year 2013, as compared to the previous year.

Board independence and percentage of shares held by the top shareholder have mean values (0.11 and 0.34) closer to the minimum value, which means that most organisations in the sample have scores closer to the minimum values.

Table 5: Descriptive statistics for continuous control variables

Variable(s)	Minimum	Maximum	Mean	Std. Deviation
Firm Size	10.97	19.45	15.39	1.43
Leverage	0.01	0.95	0.52	0.21
Sales growth	-0.67	0.92	0.12	0.22
Board independence	0.00	0.86	0.11	0.14
%age of shares held by the largest shareholder	0.04	1.00	0.34	0.21

4.2. Results of the regression analysis

The results of the regression analysis are reported in Table 6. Coefficients of Political connection (POLCON) for the dependent variables ROA and ROE are both negative and statistically significant (ROA: $\beta = -0.16$; $p = 0.01$; ROE: $\beta = -0.23$, $p = 0.00$). Such results indicate that political connections have a significantly negative association with organisational performance. Hence the hypothesis that, politically connected organisations in Pakistan are expected to perform better than non-connected organisations, is rejected.

Table 6 further reveals that firm size (FSize) is positively associated with both ROA ($\beta = 0.19$, $p = 0.00$) and ROE ($\beta = 0.22$, $p = 0.00$). A significantly positive association of organisation's growth opportunities (Growth) with both ROA ($\beta = 0.20$, $p = 0.00$) and ROE ($\beta = 0.26$, $p = 0.00$) is also identified. On the contrary, leverage is found to be negatively associated with both ROA ($\beta = -0.27$, $p = 0.00$) and ROE ($\beta = -0.22$, $p = 0.00$). Board independence (Bind), percentage of shares held by the largest shareholder (Top1), audit committee independence (ACInd) and auditor (Auditor), all have statistically insignificant coefficients (p-values > 0.05) for both ROA and ROE, implying that they do not have a significant association with organisational performance.

Further analysis was conducted to gain more insights into the association between political connection and organisational performance. Following Su and Fung (2013) and Wu et al. (2012c), POLCON was sub-divided into POLCON-P (organisations connected with politicians) and POLCON-G (organisations connected with former military and government officers). The results of the association of POLCON-P and POLCON-G with organisational performance are reported in Table 7. POLCON-P has highly significant negative coefficients for both ROA ($\beta = -0.23$, $p = 0.00$) and ROE ($\beta = -0.31$, $p = 0.00$). On the contrary, coefficients of POLCON-G are not significantly associated with both ROA ($\beta = -0.04$, $p = 0.53$) and ROE ($\beta = -0.09$, $p = 0.20$). It means that there is no association between POLCON-

G and organisational performance, while there is a negative association between POLCON-P and performance. Such results imply that the negative association between political connections and organisational performance of politically connected organisations in the main regression is primarily due to the significant negative association of political connections with politicians on organisational performance.

In addition, POLCON was sub-divided into POLCON-D (directly politically connected organisations) and POLCON-IND (indirectly politically connected organisations). Table 8 presents the results of the regression analysis of the association of direct and indirect political connections, with organisational performance. Coefficients of POLCON-D and POLCON-IND are negative and are statistically significant for both ROA and ROE, implying that both direct and indirect political connections are significantly negatively associated with organisational performance. However, slightly higher coefficients of POLCON-IND than POLCON-D (for ROA -0.15 vs. -0.14 and for ROE -0.25 vs. -0.18) indicate a slightly greater influence of indirect political connections on organisational performance.

Table 6: Results of the regression analysis of the association between political connections and organisational performance

Variables	Return on assets (ROA)			Return on equity (ROE)		
	Beta	**t-stat**	**p-value**	**Beta**	**t-stat**	**p-value**
Independent variable						
POLCON	-0.16	-2.59	0.01*	-0.23	-3.70	0.00*
Control variables						
FSize	0.19	2.84	0.00*	0.22	3.33	0.00*
Leverage	-0.27	-4.39	0.00*	-0.22	-3.58	0.00*
Growth	0.20	3.39	0.00*	0.26	4.38	0.00*
BInd	0.04	0.55	0.58	0.08	1.07	0.28
Top1	0.02	0.38	0.70	0.08	1.35	0.18
ACInd	0.11	1.52	0.13	0.09	1.28	0.20
Auditor	0.12	1.80	0.07	0.02	0.26	0.79
CEODual	-0.07	-1.10	0.27	-0.05	-0.74	0.46
(Intercept)		-0.46	0.64		-2.11	0.04
Model specifications						
F-stat			6.96			6.68
P-value			0.00*			0.00*
R Squared			0.21			0.20
Adjusted R Squared			0.18			0.17
N			**250**			**250**

* Denotes significance at 5% level. **POLCON** is a binary variable which is equal to 1 if a top officer or a large shareholder or a close friend or relative of a top officer or a large shareholder of an organisation, is a current or former, member of a Parliament or a minister or a head of the Government or has worked at a top position in the Government or in military or has worked at a top regulatory or administrative position in a policy-making Government organisation. Otherwise POLCON is equal to 0.**FSize** is firm size measured as natural log of total assets at the end of the year; **Leverage** is measured as the ratio of total debt to total assets; **Growth** is sales growth rate from previous year; **Bind** is board independence, measured as the ratio of number of independent directors to total number of directors on the Board; **Top 1** is the percentage of shares held by the largest shareholder; **ACInd** is audit committee independence which is equal to 1 if the Chairman of audit committee is an independent director and otherwise equal to 0; **Auditor** is equal to 1 if the auditor is one of the Big4 firms and otherwise equal to 0; **CEODual** means CEO duality which is equal to 1 if the positions of the Chairman of the Board and CEO are held by the same person and otherwise equal to 0.

Table 7: Results of the regression analysis of the association of political connections with parliamentarians and former government officials, with organisational performance

Variables	ROA			ROE		
	Beta	t-stat	p-value	Beta	t-stat	p-value
POLCON-P	-0.23	-3.60	0.00*	-0.31	-4.82	0.00*
POLCON-G	-0.04	-0.62	0.53	-0.09	-1.29	0.20
FSize	0.16	2.51	0.01*	0.19	2.97	0.00*
Leverage	-0.26	-4.25	0.00*	-0.21	-3.42	0.00*
Growth	0.20	3.42	0.00*	0.26	4.45	0.00*
BInd	0.04	0.54	0.59	0.08	1.07	0.29
Top1	0.03	0.45	0.65	0.09	1.45	0.15
ACInd	0.09	1.30	0.20	0.07	1.02	0.31
Auditor	0.09	1.40	0.16	-0.01	-0.20	0.84
CEODual	-0.07	-1.10	0.27	-0.04	-0.74	0.46
(Intercept)		-0.11	0.91		-1.71	0.09
Model specifications						
F-stat			7.11			7.18
P-value			0.00*			0.00*
R Squared			0.23			0.23
Adjusted R Squared			0.20			0.20
N			**250**			**250**

* Denotes significance at 5% level. **POLCON-P** is a binary variable which is equal to 1 if a top officer or a large shareholder or a close friend or relative of a top officer or a large shareholder of a politically connected organisation is a current or former, member of a Parliament or minister or head of the Government and is otherwise equal to 0. **POLCON-G** is equal to 1 if a top officer or a large shareholder or a close friend or relative of a top officer or a large shareholder of a politically connected organisation has worked at a top position in the Government or in military or has worked at a top position in a policy-making government organisation and otherwise equal to 0. All other variables are as defined earlier in Table 6.

Table 8: Results of the regression analysis of the association of direct and indirect political connections with organisational performance

Variables	ROA			ROE		
	Beta	t-stat	p-value	Beta	t-stat	p-value
POLCON-D	-0.14	-2.12	0.03*	-0.18	-2.68	0.01*
POLCON-IND	-0.15	-2.28	0.02*	-0.25	-3.85	0.00*
FSize	0.19	2.82	0.01*	0.22	3.32	0.00*
Leverage	-0.27	-4.40	0.00*	-0.22	-3.66	0.00*
Growth	0.20	3.41	0.00*	0.27	4.51	0.00*
BInd	0.04	0.55	0.58	0.08	1.08	0.28
Top1	0.03	0.41	0.68	0.09	1.46	0.15
ACInd	0.11	1.48	0.14	0.09	1.16	0.25
Auditor	0.12	1.75	0.08	0.01	0.14	0.89
CEODual	-0.07	-1.11	0.27	-0.05	-0.77	0.44
(Intercept)		-0.45	0.66		-2.07	0.04
Model specifications						
F-stat			6.27			6.30
P-value			0.00*			0.00*
R Squared			0.21			0.21
Adjusted R Squared			0.18			0.18
N			**250**			**250**

* Denotes significance at 5% level. **POLCON-D** is a binary variable which is equal to 1 if a politically connected organisation is directly connected i.e. any of its top officers or a large shareholder himself/herself is, a current or former, member of a Parliament or minister or head of the Government or has worked at a top position in the Government or in military or has worked at a top regulatory, administrative or advisory position in a policy-making government organisation, and is otherwise equal to 0. **POLCON-IND** is equal to 1if a politically connected organisation is indirectly connected i.e. through a close friend or a close relative. All other variables are as defined earlier in Table 6.

4.3. Robustness analysis

To test the robustness of the results, the study follows Su and Fung (2013) to use Industry Mean Adjusted Return on Assets (IAROA) and Industry Mean Adjusted Return on Equity (IAROE), as robustness measures of organisational performance. IAROA is calculated as ROA of the organisation minus average ROA of all organisations in the same industry group while IAROE is ROE of the organisation minus average ROE of all industries in the same industry group. The results of regression analysis with IAROA and IAROE as dependent variables are presented in Table 9 and Table 10.

Table 9 separately presents the results of regressing IAROA on POLCON, on POLCON-P and POLCON-G; and on POLCON-D and POLCON-IND. Table 10 separately reports the results of regression analysis of the association of IAROE with POLCON, with POLCON-P and POLCON-G; and with POLCON-D and POLCON-IND. The results in Table 9 show that POLCON and POLCON-P are significantly negatively associated with IAROA while the association of POLCON-G with IAROA is insignificant. Further, POLCON-D and POLCON-IND both are significantly negatively associated with IAROA. Table 10 shows results similar to Table 9, thus confirming the negative association of POLCON, POLCON-P, POLCON-D and POLCON-IND with IAROE. Hence, results of the main regression remain robust for both robustness measures of organisational performance i.e. IAROA and IAROE.

Table 9: Results of the regression analysis of the association between political connections and industry adjusted return on assets

Variables	**Dependent variable: Industry (mean) adjusted return on assets (IAROA)**								
	(1)			**(2)**			**(3)**		
	Beta	**t-stat**	**p-value**	**Beta**	**t-stat**	**p-value**	**Beta**	**t-stat**	**p-value**
POLCON	-0.17	-2.51	0.01*						
POLCON-P				-0.19	-2.79	0.01*			
POLCON-G				-0.10	-1.34	0.18			
POLCON-D							-0.14	-1.95	0.05*
POLCON-IND							-0.16	-2.38	0.02*
FSize	0.01	0.12	0.90	0.00	-0.04	0.97	0.01	0.11	0.91
Leverage	-0.12	-1.81	0.07	-0.11	-1.72	0.09	-0.12	-1.84	0.07
Growth	0.13	2.12	0.04*	0.13	2.12	0.04*	0.14	2.17	0.03*
BInd	0.09	1.11	0.27	0.09	1.10	0.27	0.09	1.11	0.27
Top1	0.04	0.60	0.55	0.04	0.64	0.53	0.04	0.65	0.52
ACInd	0.06	0.76	0.45	0.05	0.65	0.52	0.05	0.71	0.48
Auditor	0.12	1.73	0.08	0.11	1.53	0.13	0.12	1.66	0.10
CEODual	-0.09	-1.40	0.16	-0.09	-1.40	0.16	-0.09	-1.42	0.16
(Intercept)		-0.01	0.99		0.16	0.87		0.01	0.99
Model specifications									
F-stat			3.10			2.95			2.84
P-value			0.00*			0.00*			0.00*
R Squared			0.10			0.11			0.11
Adjusted R Squared			0.07			0.07			0.07
N			**250**			**250**			**250**

* Denotes significance at 5% level**. IAROA** is the ROA of an organisation minus average ROA of all the organisations in the same industry group. All other variables are as defined earlier.

Table 10: Results of the regression analysis of the association between political connections and industry adjusted return on equity

Variables	**Dependent variable: Industry (mean) adjusted return on equity (IAROE)**								
	(1)			**(2)**			**(3)**		
	Beta	**t-stat**	**p-value**	**Beta**	**t-stat**	**p-value**	**Beta**	**t-stat**	**p-value**
POLCON	-0.23	-3.46	0.00*						
POLCON-P				-0.27	-4.05	0.00*			
POLCON-G				-0.12	-1.66	0.10			
POLCON-D							-0.17	-2.47	0.01*
POLCON-IND							-0.25	-3.65	0.00*
FSize	0.06	0.82	0.41	0.04	0.55	0.58	0.05	0.79	0.43
Leverage	-0.13	-2.00	0.05*	-0.12	-1.86	0.06	-0.13	-2.08	0.04*
Growth	0.22	3.58	0.00*	0.22	3.60	0.00*	0.23	3.71	0.00*
BInd	0.12	1.57	0.12	0.12	1.57	0.12	0.12	1.59	0.11
Top1	0.11	1.66	0.10	0.11	1.72	0.09	0.11	1.76	0.08
ACInd	0.04	0.55	0.58	0.03	0.37	0.71	0.03	0.44	0.66
Auditor	0.01	0.16	0.88	-0.01	-0.15	0.88	0.00	0.03	0.97
CEODual	-0.11	-1.66	0.10	-0.11	-1.66	0.10	-0.11	-1.70	0.09
(Intercept)		-0.68	0.50		-0.40	0.69		-0.63	0.53
Model specifications									
F-stat			4.04			4.11			3.90
P-value			0.00*			0.00*			0.00*
R Squared			0.13			0.15			0.14
Adjusted R Squared			0.10			0.11			0.10
N			**250**			**250**			**250**

* Denotes significance at 5% level. **IAROE** is the ROE of an organisation, minus average ROA of all the organisations in the same industry group. All other variables are as defined earlier.

4.4. Tests of regression assumptions

To ensure the validity of results, the assumptions of regression model are tested in this section. Validity of regression model depends on satisfaction of several assumptions including linearity, homoscedasticity, residual independence, normality and multicollinearity, for which an assessment is provided below.

Assumption of continuous dependent variable is automatically satisfied because dependent variable (organisational performance) for this study is measured using two variables i.e. ROA and ROE, both of which are continuous. Similarly, presence of more than one independent/control variables in the regression model satisfies the second assumption of multiple regression models.

4.4.1. Linearity, homoscedasticity, residual independence and normality

Scatter plots of regression standardized predicted values and regression standardized residuals for both measures of dependent variable used in the study are presented in Figure 2 and Figure 3 on the next page.

In scatter plots below, regression lines pass approximately through the centre of the data of residuals for both ROA and ROE. Although there seem to be a few clusters for residual data of ROE, residuals seem to be fairly evenly distributed on both sides of the regression line. Further, there seems to be a random distribution of both positive and negative values of residuals and no specific patterns can be seen. Hence, assumptions of linearity, homoscedasticity, residual independence and normality are fairly reasonably met.

Figure 2: Scatter plot of regression standardized predicted values and regression standardized residuals: dependent variable ROA

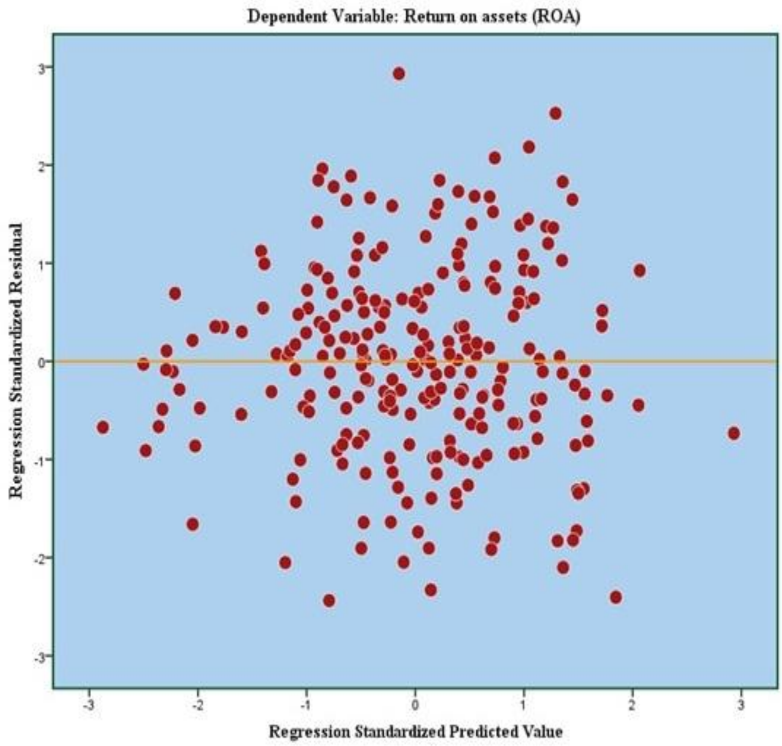
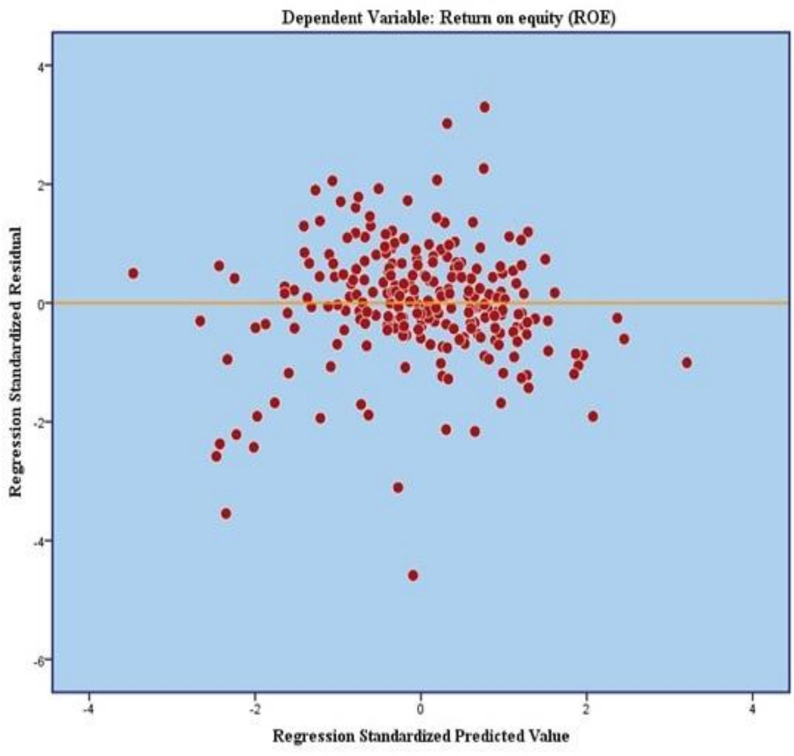


Figure 3: Scatter plot of regression standardized predicted values and regression standardized residuals: dependent variable ROE



The assumption of residual independence is further tested by Durbin-Watson statistic for the regression for both ROA and ROE, presented in Table 11 below. The value of Durbin-Watson can range from 0 to 4, where 0 means strong positive correlations and 4 means strong negative correlation. In the Table below, it can be seen that the value of Durbin-Watson for the regression is close to 2 (for ROA=2.07, for ROE=2.11) which shows that the residuals are not serially correlated; hence, meeting the assumption of independence of residuals.

Table 11: Durbin-Watson statistic

Dependent variable(s)	Durbin-Watson
ROA	2.07
ROE	2.11

As some clusters can be seen in scatter plot of residuals for ROE, the assumption of normality is further tested by creating histograms and P-P plots of regression standardized residuals for both ROA and ROE. Figure 4 and Figure 5 below show P-P plot and histogram of regression standardized residuals for ROA while Figure 6 and Figure 7 present P-P plot and histogram of regression standardized residuals for ROE. P-P plot in Figure 4 shows that residuals of ROA fairly move along the diagonal line which is confirmed by a fairly normal distribution in histogram of residuals in Figure 5.

For ROE, diagonal line is not a perfect fit for some of the residuals (Figure 6); however, histogram in Figure 7 shows an approximate normal distribution of residuals. Hence, assumption of normality is fairly met.

Figure 4: Normal P-P plot of regression standardized residuals: dependent variable ROA

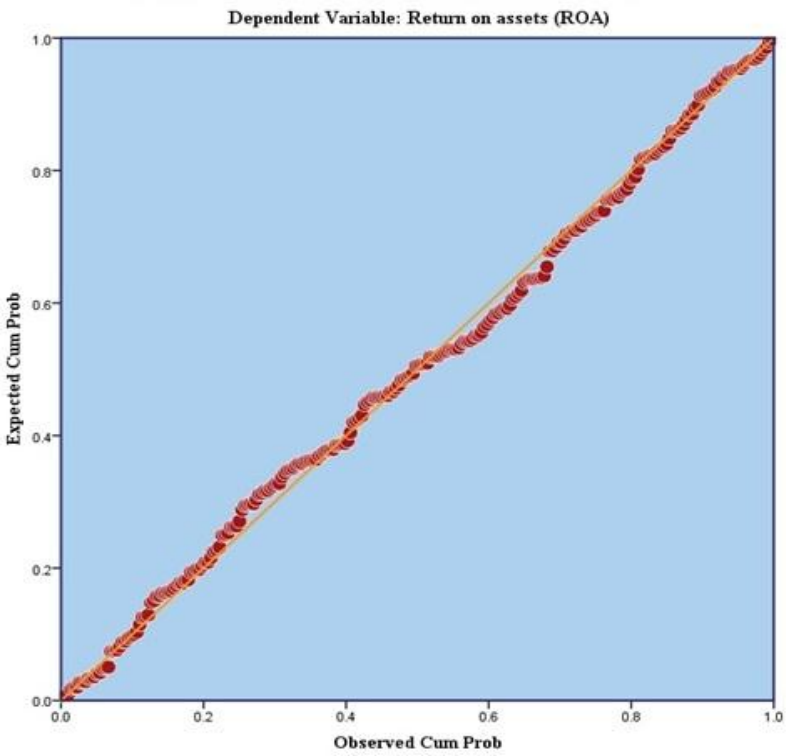


Figure 5: Histogram of regression standardized residuals: dependent variable ROA

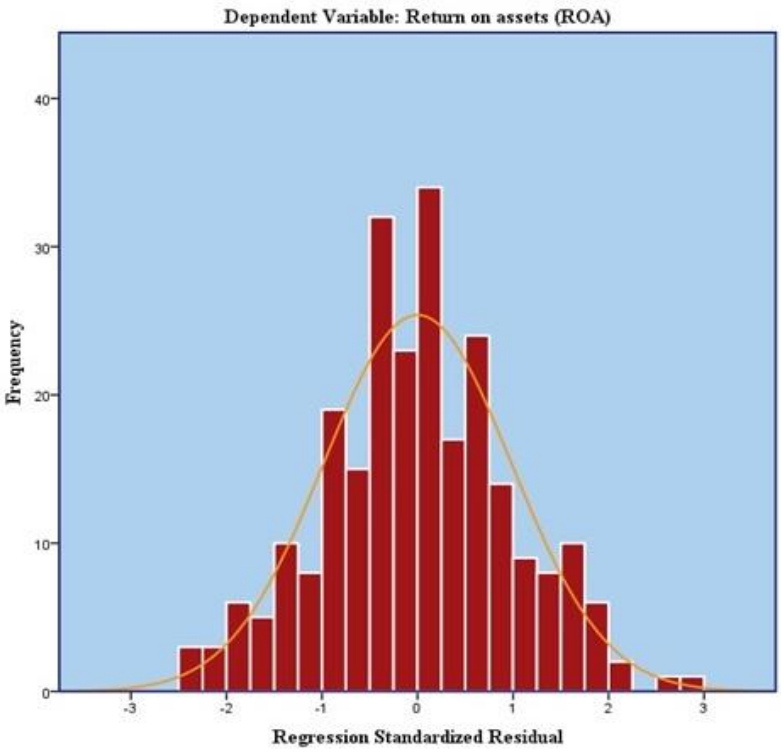


Figure 6: Normal P-P plot of regression standardized residuals: dependent variable ROE

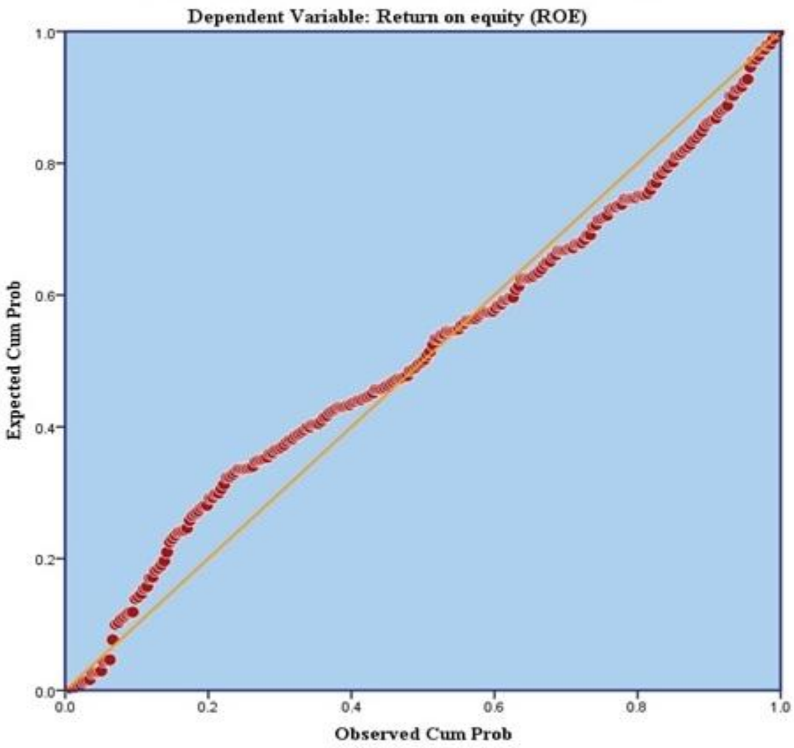
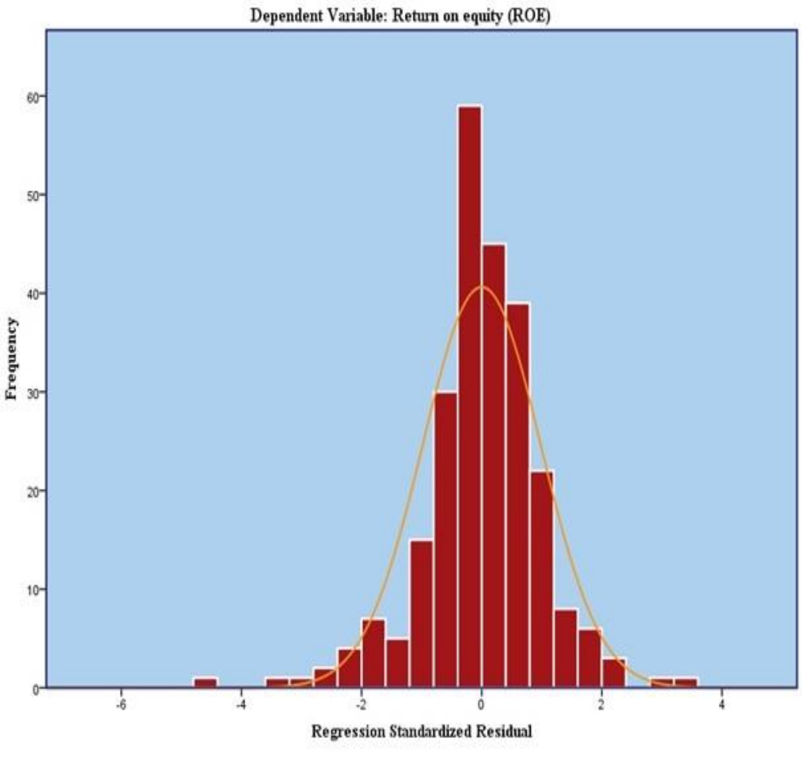


Figure 7: Histogram of regression standardized residuals: dependent variable ROE



4.4.2. Multicollinearity

Multicollinearity in the regression model refers to high correlation of independent variables, thus making results invalid. A valid multiple regression model therefore assumes that independent variables are not highly correlated.

In this study, a correlation matrix of all independent variables, presented in Table 12 below, was used to test the presence of multicollinearity among independent variables. In addition, collinearity diagnostics i.e. variance inflation factor (VIF) and tolerance for all independent variable are reported in Table 13.

Correlation matrix in Table 12 shows that several correlation coefficients are statistically significant; however, correlation coefficients are low. The highest correlation is between board independence and audit committee independence (0.60), followed by 0.33 between firm size and auditor. As independent and control variables have correlation coefficients less than 0.70, there is little chance of multicollinearity.

Multicollinearity is further tested by looking at tolerance and VIF scores. As shown by Table 13, VIF values for independent and control variables are far below 10 (maximum value being 1.68) and tolerance values are sufficiently greater than 0.1 (lowest value being 0.60). Hence, it can be concluded that multicollinearity among variables is not a problem in the analysis.

Table 12: Pearson correlation matrix of independent variables

Variable(s)	CEODual	ACInd	TOP1	Auditor	BInd	FSize	Leverage	Growth	POLCON
CEODual	1								
ACInd	-0.160* (.011)	1							
TOP1	-0.06 (.324)	.15* (.016)	1						
Auditor	-.257** (.000)	0.15* (.016)	0.26** (.000)	1					
BInd	-0.162* (.010)	0.60** (.000)	0.13* (.035)	0.22** (.000)	1				
FSize	-0.1 (.120)	0.18** (.006)	0.19** (.003)	0.33** (.000)	0.19** (.002)	1			
Leverage	0.126* (.046)	0.04 (.562)	0.06 (.353)	-0.17 (.006)	-0.02 (.741)	0.13* (.036)	1		
Growth	0.12 (.059)	0.02 (.776)	-0.12 (.06)	-0.06 (.347)	0.02 (.805)	0.03 (.615)	0.16* (.012)	1	
POLCON	-0.175** (.006)	0.12 (.054)	0.09 (.178)	0.04 (.544)	0.22** (.000)	0.32** (.000)	0.1 (.119)	0.09 (.155)	1

* Denotes that correlation is significant at 5% level (2-tailed).
** Denotes that correlation is significant at 5% level (2-tailed).
p-values have been presented in the parentheses below the correlation coefficients.

Table 13: Colliniearity diagnostics

Dependent variables: 1: ROA 2: ROE	Collinearity statistics	
	Tolerance	VIF
CEODual	0.87	1.15
ACInd	0.62	1.62
TOP1	0.89	1.13
Auditor	0.74	1.35
BInd	0.60	1.68
FSize	0.77	1.31
Leverage	0.89	1.12
Growth	0.94	1.07
POLCON	0.83	1.21

All variables are as defined earlier.

4.5. Summary

The results presented in this chapter suggest that political connections in Pakistan are common across all industries; however, there is no significant difference in organisational performance across different industries. The results also suggest that politically connected organisations have better corporate governance measures in place; however, politically connections were found having significant negative association with organisational performance; thus rejecting the hypothesis. Additional tests reveal that negative performance of the politically connected organisations is mainly attributable to connections with parliamentarians, whereas political connections with former government and military officers do not have a significant impact on organisational performance. The results remain robust for additional measures of organisational performance.

Chapter 5

Discussion and conclusion

In this chapter, the discussion of the results and their implications are provided in Section 5.1. The contributions of the study are outlined in Section 5.2. Finally, Section 5.3 discusses the limitations of the study and suggests future direction of research and Section 5.4 summarises.

5.1. Discussion of the results and their implications

The objective of this study was to investigate the association between political connections and organisational performance in Pakistan, which is perceived as a country with high level of corruption, inefficient regulatory mechanism, poor implementation of the law and low judicial independence. For the purpose of the study, a regression analysis was conducted on data collected from 250 non-financial organisations listed on the KSE.

The results showed that political connections are common in Pakistan. The high frequency of political connections in Pakistan is consistent with the findings of previous studies (e.g. Boubakri et al. 2008; Faccio 2006) which have noted widespread political connections in countries with higher levels of corruption, poor implementation of the law and lower judicial independence. Further analysis of the data revealed that in Pakistan, political connections are prevalent across all types of industries. Consistent with some previous studies (e.g. Okazaki and Sawada 2014; Su and Fung 2013), political connections were found more common in industries like oil and gas and utilities. These industries are highly controlled by the Government due to their strategic significance. This implies that political connections are expected to help organisations in the allocation of licenses and the procurement of government contracts in such industries.

The political connections of the organisations were evenly distributed between connections with politicians and connections with former government and military officers. Direct political connections, however, were found to be more common than indirect political connections. The higher frequency of direct political connections may be attributable to few laws regarding political conflict of interest and poor implementation of the law (Faccio 2006).

Widespread connections of the business organisations with politicians and former government and military officers, large number of direct political connections and a high frequency of political connections in industries under government control have important implications for legislation and policy-making. In particular, they suggest the need for improvements in conflict of interest laws, which at present are neither sufficient nor efficient. It is even more important to formulate and strengthen institutions to ensure just and impartial implementation of laws to restrict political conflict of interest.

The results also reveal that political connections are negatively associated with organisational performance, thereby rejecting the hypothesis. The findings contrast those of some previous studies (e.g. Lassoued and Attia 2014; Su and Fung 2013; Wu et al. 2012c; Li et al. 2008), which have identified higher accounting performance of politically connected organisations. The results, however, support the findings of those studies that have noted lower performance of politically connected organisations in countries with low economic development and high level of corruption (Faccio 2010), and in countries with lower judicial independence and higher political instability (Boubakri et al. 2008). The analysis further revealed that connection with former government and military officers is not significantly associated with performance; however, connections with politicians have a significantly negative impact on organisational performance.

The results of the study raise a fundamental question that what drives the negative association between politically connected organisations and organisational performance in a weak regulatory environment that is conducive to obtain benefits by the politically connected organisations? It is possible that politically connected organisations extract benefits from their powerful connections; however, these benefits do not translate into an overall higher performance due to management inefficiencies. In this case, it can be suggested that politically connected organisations should audit their management functions to find and remove any inefficiencies.

Another possible reason is that politically connected organisations may have to finance political activities of the politicians connected to them; thus resulting in lower profitability. This possibility is consistent with the findings that connections with politicians result in significantly negative performance while connections with former government officials are not significantly associated with organisational performance. If this is the case, it has significant implications for the auditors who need to be more cautious in assessing that business assets are used solely for the purpose of the business and that the arm's length principle is being consistently applied.

Another possible explanation may be that most politically connected organisations are part of big business groups, which comprise several public listed and private unlisted organisations. These public and private organisations are controlled predominantly by a political family through direct and/or indirect shareholdings. Politically powerful businessmen may extract government benefits through their private unlisted businesses and place the burden of their political costs upon the listed businesses. As a consequence, on the one hand, profitability of unlisted connected organisations may increase and, on the other hand, performance of politically connected listed organisations may deteriorate. It could be more beneficial to use non-listed organisations to obtain government benefits because they do not have mandatory audit requirements and have little reporting requirements. This possibility suggests the need for improving and formulating regulations to effectively monitor both public listed and private unlisted organisations.

Finally, there may be another possible scenario, which although extreme, cannot be completely dismissed. In his book “Who owns Pakistan”, Rehman (2006) states that these politically connected organisations are “*Big and beautiful but looking small and ugly*”. It implies that they may have better earnings than what they declare. Profitability may be lowered for many reasons such as to avoid media attention, to pay less tax and to justify their bank loan defaults. In this regard, an important piece of evidence has been provided by Khwaja and Mian (2005) who report that politically connected organisations in Pakistan have 50% higher default ratios than non-connected organisations. Higher default ratios may, therefore, be a cause as well as an effect of low profitability of politically connected organisations in Pakistan.

The possibility of showing lower profits by the politically connected organisations cannot be completely dismissed due to the existing evidence which suggests that political connections have a negative effect on the quality of accounting information (Bona-Sanchez et al. 2014; Chaney et al. 2011); and on audit committee and auditor independence (Wahab et al. 2013; Bliss et al. 2011). This scenario demonstrates the necessity of improving regulations and ensuring the implementation of law. Further, the accounting profession may need to enhance its audit quality by ensuring audit independence. The accounting profession also needs to ensure consistent application of the arm’s length principle by the business organisations.

Consistent with previous studies (e.g. Su and Fung 2013; Li et al. 2008), the analysis found that firm size and growth are significantly positively associated with organisational performance. It implies that larger organisations and organisations with higher growth opportunities have better performance because they are able to reduce their operating costs due to economies of scale. Further, consistent with Bliss and Gul (2012b), leverage was found significantly negatively associated with organisational performance. It may be attributable to larger debt of politically connected organisations, resulting in higher finance cost and financial distress; thus lower performance.

In contrast with previous evidence suggesting that political connections have a significantly negative effect on corporate governance (Wahab, How and Verhoeven 2007), the results show that politically connected organisations in Pakistan may have better corporate governance measures in terms of CEO duality and audit committee independence. In particular, a higher percentage of politically connected organisations have an independent director as the Chairman of the audit committee and do not have CEO duality. Further, a higher number of politically connected organisations have appointed one of the Big4 accounting firms as their external auditor. This last finding is consistent with Guedhami et al. (2014) who posit that politically connected organisations are more likely to appoint Big4 accounting firms as their auditors because these organisations are eager to exhibit transparency in their corporate affairs. The results of the study show that none of these corporate governance measures are significantly associated with organisational performance. Despite having better corporate governance measures, poor performance of politically connected organisations suggests the need to improve corporate governance regulations and their implementation.

5.2. Contributions

The study contributes to both literature and practice. Firstly, it contributes to political connections literature by examining the association between political connections and organisational performance. In particular, the study contributes to the political connections literature relevant to developing countries with high corruption and weak regulatory environment. Secondly, this is the first single country-specific study that has examined the impact of political connections on organisational performance in a South Asian country i.e. Pakistan.

The study offers several practical contributions in relation to policy-making, regulation, governance and accounting practice. Firstly, the findings of the study suggest that policy makers need to formulate more effective laws to curb political conflict of interest. Secondly, the study highlights the need to review the effectiveness and efficiency of corporate governance regulations. Thirdly, the study suggests that governance mechanisms should be strengthened to improve implementation of laws and regulations in a judicial and equitable manner. Fourthly, the study suggests that the accounting profession reviews and improves its audit procedures and ensures that audit independence is not compromised.

Lastly, the findings of the study have implications for overall economy of developing countries in general and South Asian countries in particular. South Asia has a population of over 1.4 billion with approximately half of the Worlds' poor living in this region (The World Bank 2015b). In addition, the worlds' largest working age population is in the South Asian region (The World Bank 2015a). As politically connected organisations comprise a significant proportion of the economy, their lower performance has severe negative consequences for the economy. The study, therefore, suggests effective monitoring of these politically connected organisations to enhance their performance.

5.3. Limitations

The study is subject to several limitations. Firstly, in the absence of any established database, data was hand collected from the financial statements of organisation listed on the KSE, which was a time consuming process. Due to the time limit, this study analysed the association between political connections and organisational performance for the year 2013 only. Future studies may further explore this association across a longer time period data.

Secondly, widespread political connections in public listed organisations suggest that political connections may be even more common among private non-listed organisations. This study, however, is limited to examining the association between political connections and organisational performance among public listed organisations. Future studies may include private unlisted organisations in the analysis.

Thirdly, the study was limited to examining the association between political connections and accounting performance of the organisations. Future studies may investigate the impact of political connections on stock performance as well. Finally, while this study identified a negative association between political connections and organisational performance, future studies may explore factors resulting in such an association. The possible reasons provided in this study could be a starting point for future studies.

5.4. Summary

The main aim of this study was to investigate the impact of political connections on organisational performance in Pakistan. In view of the weak regulatory environment, few laws regarding conflict of interest and poor implementation of law, it was hypothesised that politically connected organisations in Pakistan are expected to perform better than non-connected organisations. Contrary to the expectations and in contrast with several previous studies, political connections in Pakistan, particularly connections with parliamentarians, are found significantly negatively associated with organisational performance.

The study contributes to the existing literature by providing evidence of the impact of political connections on organisational performance in a weak regulatory environment. The study suggests formulating conflict of interest of laws in Pakistan, strengthening governance and management practices of the politically connected organisations and improving audit practices of the accounting profession.

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Appendix 1
The political structure of Pakistan

The Government of Pakistan comprises three constitutional pillars; the legislature, the executive and the judiciary. The legislature is composed of the President (as head of the state) and a bicameral parliament: the NA and the Senate. NA is the lower house of the Parliament, which is composed of general members and some special members. General members are directly elected by the people for a period of five years, who in turn elect special members. Senate is the upper house of the Parliament, comprising 104 members in all, who are elected by the provincial assemblies for a period of six years. Table 14 provides break-up of NA and Senate membership.

The Prime Minister, elected by the NA by majority vote, is the chief executive of the country and is vested with all the executive powers. Prime Minister has the right to appoint ministers (called federal ministers) and deputy ministers (called ministers of state) from within the parliament members; however, the Prime Minister may appoint a limited number of advisers from outside the Parliament. President is the head of the state who is elected for a period of 5 years. All the four provincial assemblies, the NA and the Senate constitute Electoral College for election of the President. Office of the President has a ceremonial role, with most powers vested with the office of the Prime Minister.

Members of the provincial assemblies are elected directly by the people of the province for a period of 5 years. Provincial assemblies comprise both general members and special members, elected on the same principle which is followed in the NA. While provincial assemblies are vested with powers of legislating on most matters related to the province, they also approve provincial budget, thus making provinces financially autonomous. Provinces are administered by the Chief Ministers who are elected by the provincial assemblies by majority vote. Chief Ministers appoint their cabinet members (from within the provincial assembly members) and advisers (from outside the provincial assembly) to administer the province. Table 15 provides a break-up of seats of the four provincial assemblies of Pakistan. Every province is headed by a Governor, which is appointed by the Federal Government. Like the President, Governor is also a ceremonial post, which is considered a federal representative to the province and serves as a communications link between the Provincial and the Federal Government.

Unlike the US, which has a two party system, Pakistan has a multi-party system. Presently, there are 270 parties registered with the ECP. 148 political parties contested 2013 general elections while 21 of them have representation in the national and provincial assemblies (*Election Commission of Pakistan*, 2015). Table 16 provides a chronological list of political parties who have been in provincial and federal governments since 1972.

While Table 17 provides a list of Governor Generals and Presidents of Pakistan; Table 18 provides a chronological account of the Parliaments and the Prime Ministers since 1947.While Table 17 and 18 portray a picture of political instability, they also show that political governments in Pakistan have seldom completed their tenure.

Table 14: Break-up of seats of the National Assembly and the Senate of Pakistan

Panel A: Break-up of seats of the National Assembly of Pakistan							
	Punjab	**Sindh**	**KPK**	**Balochistan**	**FAT**	**FC**	**Total**
General	148	61	35	14	12	2	272
Women	35	14	8	3	0	0	60
Non-Muslims	-	-	-	-	-	-	10
Total	183	75	43	17	12	2	342
Panel B: Break-up of seats of the Senate of Pakistan							
	Punjab	**Sindh**	**KPK**	**Balochistan**	**FAT**	**FC**	**Total**
General seats	14	14	14	14	8	2	66
Technocrats	4	4	4	4	0	1	17
Women	4	4	4	4	0	1	17
Non-Muslims	1	1	1	1	0	0	4
Total	23	23	23	23	8	4	104

Source: Official website of the National Assembly of Pakistan. <http://www.na.gov.pk/en/index.php>

Table 15: Break-up of seats of the Provincial Assemblies of Pakistan

	Punjab	**Sindh**	**KPK**	**Balochistan**
General Seats	297	130	99	51
Women	67	29	22	11
Non-Muslims	8	9	3	3
Total	372	168	124	65

Source: Official website of the Election Commission of Pakistan. <http://ecp.gov.pk/>

Table 16: List of political parties who have been in Provincial and Federal Governments since 1971

Period		Punjab	Sindh	Baluchistan	KPK	Federal Government
From	To					
1972	1977	PPP	PPP	NAP/ PPP	JUI/ PPP	PPP
1977	1985	Martial law. No Chief Ministers or Prime Minister. General Zial-ul-Haq assumed office of the President/Chief Martial law administrator and provinces were ruled through Governors/ Martial law administrators, appointed by him.				
1985	1988	IND/PML	IND/PML	IND/PML	IND/PML	IND/PML
1988	1990	IJI	PPP	IJI BNA	PPP	PPP
1990	1993	IJI	PPP IND IJI	IJI	IJI	IJI
1993	1996	PML(J)	PPP	IND	PML(N) PPP	PPP
1997	1999	PML(N)	PML	BNP IND	PML(N)	PML (N)
1999	2002	Martial law. No Chief Ministers or Prime Minister. General Pervaiz Musharraf assumed office of the CEO and provinces were ruled through Governors, appointed by him.				
2002	2007	PML(Q)	PML(Q)	PML(Q)	MMA	PML(Q)
2008	2013	PML(N)	PPP	PPP	ANP	PPP
2013	To	PML(N)	PPP	NP	PTI	PML (N)

ANP: Awami National Party, **BNA:** Baluchistan National Alliance, **BNP:** Baluchistan National Party, **IJI:** IslamiJamhooriIttehad, **IND:** Independent, **JUI**: JamiatUlema e Islam, **MMA:** MuttehidaMajlas e Amal, **NAP:** National Awami Party, **PML:** Pakistan Muslim League, **PML(J):** Pakistan Muslim League (Junejo), **PML(N):** Pakistan Muslim League (Nawaz), **PML(Q):** Pakistan Muslim League (Quaid e Azam), **PPP:** Pakistan People's Party, **PTI:** Pakistan Tehreek e Insaaf.

Sources:
1: Official website of the National Assembly of Pakistan. <http://www.na.gov.pk/en/index.php>
2: Official website of the Punjab Assembly of Pakistan. <http://www.pap.gov.pk/index.php/home/en>
3: Official website of Sindh Asembly of Pakistan. <http://www.pas.gov.pk/index.php/home/en>
4: Official website of Balochistan Assembly of Pakistan <http://www.pabalochistan.gov.pk/index.php/home/en>
5: Official website of Khayber Pakhtunkhwah Assembly of Pakistan <http://www.pakp.gov.pk/2013>
6: Official website of the Associated Press of Pakistan. <http://app.com.pk/en_/index.php?option=com_content&task=view&id=51833>

Table 17: List of the Governor Generals and the Presidents of Pakistan

Sr.	Name	From	To	Affiliation	Comments
1	Muhammad Ali Jinnah	15-08-1947	11-09-1948	Pakistan Muslim League	Died in office
2	Khwaja Nazimuddin	14-09-1948	16-10-1951	Pakistan Muslim League	Became Prime Minister
3	Malik Ghulam Muhammad	19-10-1951	05-10-1955	Civil service	Dismissed on account
4	Maj. General Iskander Mirza	06-10-1955	22-03-1956	Army/Civil service	Assumed office of the President
5	Maj. General Iskander Mirza	23-03-1956	27-10-1958	Army/Civil service	Dismissed by military
6	General Ayub Khan	27-10-1958	25-03-1969	Army	Handed over power to another army general
7	General Yahya Khan	25-03-1969	20-12-1971	Army	Handed over power to civilian martial law administrator
8	Zulfiqar Ali Bhutto	20-12-1971	14-08-1973	Pakistan People’s Party	Acting
9	Fazal Elahi Chaudhry	14-08-1973	16-09-1978	Pakistan People’s Party	Dismissed by military

Table 17: Continued...

Sr.	Name	From	To	Affiliation	Comments
10	General Mohammed Zia ul Haq	16-09-1978	17-08-1988	Army	Died in plain crash
11	Ghulam Ishaq Khan	17-08-1988	08-07-1993	Civil Service	Resigned
12	Wasim Sajjad	18-07-1993	14-11-1993	Technocrat	Acting
13	Sardar Farooq Ahmed Leghari	14-11-1993	02-12-1997	Pakistan People's Party	Resigned.
14	Wasim Sajjad	02-12-1997	01-01-1998	Technocrat	Acting
15	Muhammad Rafiq Tarar	01-01-1998	20-06-2001	Pakistan Muslim League	Dismissed by military
16	General Pervez Musharraf	20-06-2001	15-10-2007	Army	Assumed office of President
17	General (Retired) Pervez Musharraf	29-11-2007	18-08-2008	Army	Resigned
18	Mohammed Mian Somro	18-08-2008	09-09-2008		Acting
19	Asif Ali Zardari	09-09-2008	09-09-2013	Pakistan People's Party	Completed tenure
20	Mamnoon Hussain	09-09-2013	To date	Pakistan Muslim League	

Sources: 1) Official website of the National Assembly of Pakistan.<http://www.na.gov.pk/en/presidents.php>
2) Official website of the Associated Press of Pakistan.<http://app.com.pk/en_/index.php?option=com_content&task=view&id=51833>

Table 18: List of the Parliaments, the Prime Ministers and the Chief Executives of Pakistan

Parliament	Parliament tenure		Prime Minister	Prime Ministers' tenure	Affiliation	Comments
	From	To				
1st	10-08-1947	24-10-1954	Liaqat Ali Khan	15-08-1947 to 16-10-1951	Pakistan Muslim League	Assassinated
			Khawaja Nazimuddin	17-10-1951 to 17-04-1953	Pakistan Muslim League	Dismissed by the Governor General
			Muhammad Ali Bogra	17-04-1953 to 11-08-1955	Pakistan Muslim League	Resigned
2nd	28-05-1955	07-10-1958	Ch. Muhammad Ali	11-08-1955 to 12-09-1956	Civil service/ Pakistan Muslim League	Resigned
			Hussain Shaheed Suharwardi	12-09-1956 to 18-10-1957	United front	Resigned
			I. I. Chundrigar	18-10-1957 to 16-12-1957	United front	Resigned
			Malik Feroz Khan Noon	16-12-1957 to 07-10-1958	United front	Dismissed as a result of Martial Law
No parliament	08-10-1958	07-06-1962	Martial law under General Muhammad Ayub Khan			
3rd	08-06-1962	07-06-1965	General Ayub Khan President		Army	Presidential system
4th	12-06-1965	25-03-1969	General Ayub Khan President		Army	Presidential system

Table 18: Continued...

Parliament	Parliament tenure		Prime Minister	Prime Ministers'	Affiliation	Comments
	From	To				
No parliament	25-03-1969	14-04-1972		25-03-1969 to 20-12-1971		Martial law under General Muhammad Yahya Khan
			Mr. Noor-ul-Amin	07-12-1971 to 20-12-1971	Pakistan Muslim League	Assumed office of the Vice-President
			Zulfiqar Ali Bhutto	20-12-1971 to 14-08-1973	Pakistan People's Party	President and Civilian Chief Martial Law Administrator
5th	14-04-1972	10-01-1977	Zulfiqar Ali Bhutto	14-08-1973 to 05-07-1977	Pakistan People's Party	General elections held on 07-03-1977
6th	26-03-1977	05-07-1977	Zulfiqar Ali Bhutto		Pakistan People's Party	Dismissed as a result of Martial Law
No parliament	06-07-1977	19-03-1985	Martial Law under General Zia ul Haq			
7th	20-03-1985	29-05-1988	Muhammad Khan Junejo	23-03-1985 to 29-05-1988	Independent/Pakistan Muslim League	Dismissed by the President
No parliament	30-05-1988	29-11-1988	Martial Law under General Zia ul Haq			
8th	30-11-1988	06-08-1990	Benazir Bhutto	02-12-1988 to 06-08-1990	Pakistan People's Party	Dismissed by the President
No parliament	06-08-1990	02-11-1990	Ghulam Mustafa Jatoi	06-08-1990 to 06-11-1990		Caretaker/Acting

Table 18: Continued...

Parliament	Parliament tenure		Prime Minister	Prime Ministers' tenure	Affiliation	Comments
	From	To				
9th	03-11-1990	18-07-1993	Muhammad Nawaz Sharif	06-11-1990 to 18-04-1993	Coalition	Dismissed by the President
			Mir Balakh Sher Mazari	18-04-1993 to 26-05-1993		Caretaker/Acting
			Muhammad Nawaz Sharif	26-05-1993 to 18-07-1993	Coalition	Reinstated by the Supreme Court but later resigned
No parliament	19-07-1993	14-10-1993	Moin Qureshi	18-07-1993 to 19-10-1993		Caretaker/Acting
10th	15-10-1993	05-11-1996	Benazir Bhutto	19-10-1993 to 05-11-1996	Pakistan People's Party	Dismissed by the President
No parliament	06-11-1996	14-02-1996	Malik Meraj Khalid	06-10-1996 to 17-02-1997		Caretaker/Acting
11th	15-02-1997	12-10-1999	Muhammad Nawaz Sharif	17-02-1997 to 12-10-1999	Pakistan Muslim League (Nawaz)	Dismissed as a result of Martial Law
No parliament	13-10-1999	15-11-2002	Military rule under General Pervaiz Musharraf			

Table 18: Continued...

Parliament	Parliament tenure		Prime Minister	Prime Ministers' tenure	Affiliation	Comments
	From	To				
12th	16-11-2002	26-10-2007	Mir Zafarullah Khan Jamali	23-11-2002 to 26-06-2004	Pakistan Muslim League (Qaid e Azam)	Resigned
			Chaudhry Shujat Hussain	30-06-2004 to 26-08-2004	Pakistan Muslim League (Qaid e Azam)	Resigned
			Shaukat Aziz	28-08-2004 to 15-11-2007	Pakistan Muslim League (Qaid e Azam)	Parliament completed its tenure
No parliament	27-10-2007	16-03-2008	Muhammad Mian Soomro	16-11-2007 to 24-03-2008		Caretaker/Acting
13th	17-03-2008	16-03-2013	Yousaf Raza Gillani	25-03-2008 to 25-04-2012	Coalition	Disqualified by the Supreme Court
			Raja Pervez Ashraf	22-06-2012 to 24-03-2013	Coalition	Parliament completed its tenure
No parliament	17-03-2013	30-05-2013	Mir Hazar Khan Khoso	25-03-2013 to 05-06-2013		Caretaker/Acting
14th	01-06-2013	To date	Muhammad Nawaz Sharif	05-06-2013 to date	Pakistan Muslim League (Nawaz)	

Sources: 1) Official website of the National Assembly of Pakistan. <http://www.na.gov.pk/en/presidents.php>
2) Official website of the Associated Press of Pakistan. <http://app.com.pk/en_/index.php?option=com_content&task=view&id=51833>

Appendix 2

Regulatory institutions in Pakistan

In Pakistan, public companies are registered and regulated under Companies Ordinance, 1984. For listed organisations, the CCG of Pakistan and listing rules of the relevant stock exchange also apply. SECP is the apex regulatory body that is entrusted with the powers for compliance of Companies Ordinance, 1984 and the CCG.

Companies Ordinance, 1984

Companies Ordinance 1984 is the major statute for corporate governance in Pakistan. The ordinance provides for rules and procedures for incorporation of a company and allotment and transfer of shares. It also sets out rights, duties and liabilities of shareholders, directors and managers. While it contains several provisions for protection of minority shareholders, it also provides procedures to be followed for meetings of shareholders and directors. Further, to ensure transparency and accountability, the ordinance provides certain requirements for financial reporting and requires mandatory external audit of annual financial statements.

Code of Corporate Governance, 2012

Corporate governance in Pakistan is still in a transitory stage. Pakistan adopted its first CCG in 2002 which lacks behind the corporate governance practices in developed and well regulated economies. However, an amended CCG, adopted in 2012 and implemented in 2013, proposes several advancements. For example, amended version of CCG requires at least one independent director on the Board while in previous version, it was not mandatory. Further, new CCG provides a more detailed criterion for the assessment of independence of an independent director. Furthermore, maximum number of executive directors has been reduced from 75% to 33.33%. In addition, several provisions have been amended and included which discourage CEO duality, improve internal audit and encourage transparency and better governance

Pakistan CCG is a hybrid of mandatory and voluntary regimes, whose main purpose is to ensure effective monitoring of the management, to limit the abuse of power by the insiders and to enhance performance. While compliance with CCG is mandatory for all listed companies, some important provisions, like appointment of independent directors, are voluntary to be complied and companies can report about these provisions on “if not, why not’ principle. The CCG is part of the listing requirements of the stock exchanges in Pakistan and is monitored by the SECP.

Stock Exchanges in Pakistan

The capital market of Pakistan comprises three stock exchanges namely KSE, Lahore Stock Exchange (LSE) and Islamabad Stock Exchange (ISE). KSE is the oldest stock exchange in Pakistan that was established in 1947. It is also the largest stock exchange in Pakistan with more than 900 companies currently listed in 36 sectors.

Stock exchanges in Pakistan are incorporated under the Companies Ordinance 1984 and are governed by the SECP. CCG is an important part of listing requirements of all three stock exchanges. The stock exchanges work as regulators to ensure that listed companies comply with listing requirements and the CCG. For instance, KSE takes action against those companies which are not complying with the listing requirements by putting these companies on “default counter”.

Securities and Exchange Commission of Pakistan (SECP)

Formerly known as Corporate Law Authority (CLA) of Pakistan and re-organised under the SECP Act 1997, SECP is the major regulator of corporate activities in Pakistan. It regulates the activities of corporate sector, capital market, insurance companies, non-banking financial institutions and private pensions. The SECP comprises five to seven commissioners, majority of which must be from the private sector. One of the commissioners is appointed as the Chairman. All the commissioners, including the Chairman, are appointed by the Federal Government. The main objective of the SECP is "*to develop a fair, efficient and transparent regulatory framework, based on international legal standards and best practices, for the protection of investors and mitigation of systemic risk aimed at fostering growth of a robust corporate sector and broad based capital market in Pakistan*" (SECP, 2015)