Can Managers' Short-Sightedness Be Reversed Through Close and Clean Business-government Relationships?

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Abstracts: This research uses a sample of Chinese listed firms from 2017 to 2020 to empirically evaluate, based on institutional theory, the influence of close and clean government-business relationships on managers' shortsighted conduct. Close and clean government-business relationship can effectively inhibit managers' short-sighted behavior, and both close government-business relationship and clean government-business relationship can effectively inhibit managers' short-sighted behavior. Government services are mostly employed in the closeness aspect to encourage managers to create long-term goals, and in the cleanness aspect to restrain managers' opportunistic behavior through government integrity and transparency. Managers' shortsighted behavior is inhibited by close and clean government-business relationships, and this effect is especially pronounced in state-owned firms where institutional investors own a significant number of the shares.

***Keywords*:** business-government relationships, close and clean business-government relationships, managers' short-sightedness

1. Introduction

When business managers decide to forego the long-term growth of the company in favor of immediate, short-term gains, this is known as managerially shortsighted behavior[1]. The main way that managers' myopic behavior is manifested is that they manipulate R&D expenditures, appropriately cut R&D expenditures to achieve short-term performance goals when firms are facing short-term performance pressures[2]. Studies on the reasons behind corporate managers' shortsighted behavior have been conducted. From the internal perspective of the business, on the one hand,the ownership structure theory[3]; the extortionist theory[4]; the theory that states that managers are under pressure from shareholders, and that shareholders' shortsightedness will cause managers to be shortsighted; on the other hand, managers start acting in a shortsighted way out of self-interest, according to the merger hypothesis[5], the managerial defense hypothesis[6], and the pay distortion hypothesis[7]. From the external perspective of the business, managers make irrational investments to satisfy the investment preferences of external investors based on the irrational expectations of external investors[8]. Whatever the underlying cause, it is essentially the self-serving behavior of the manager to achieve some purpose.

The close and clean business-government relationship might lessen managers' self-serving actions. In 2016, General Secretary Xi Jinping initially suggested a new kind of "closeness" and "cleanness"-focused government-business interaction. At the Party's 20th National Congress in 2022, he re-emphasize the necessity of creating a close and clean government-business relationship. The literature on close and clean government-business relations has substantiated the beneficial effects of this relationship on corporate innovation[9], corporate performance[10], corporate competitive advantage[11], social responsibility[12], and public resource allocation[13] for the company. However, the strategic level of the company is not adequately addressed in the research on the close and clean government-business relationship. The majority of research on the causes of managerial shortsightedness ignores external institutional factors in favor of internal and external stakeholders. There is a dearth of systematic theoretical explanations and empirical evidence regarding the potential benefits or drawbacks of the external institutional environment of the relationship in terms of mitigating managerial shortsightedness. Therefore, this research investigates whether the affinity of close and clean government-business relationship can affect managers to engage in shortsightedness behaviors using data of Chinese listed enterprises from 2017 to 2020.

2. Forming hypotheses and theoretical analysis

The interaction between the government and the market, the government and businesses, and government officials and entrepreneurs is centralized in the government-business relationship[14]. Close and clean government-business relations, "Qin" is the attitude, is the responsibility; "Qing" is the bottom line, is the principle. Regarding the "close" requirements, public servants fulfill their legal obligations to provide forward service, steer the proper development of businesses, and assist them in resolving practical issues; business managers should take the initiative to speak with the appropriate departments and refrain from "playing Taiji" and abdicating their responsibilities. Business managers actively assume social responsibility, speak the truth, tell the truth, and engage in communication with the pertinent departments. Regarding the "clean" requirements, the phenomena of government-enterprise collusion and government-business collusion ought to be eradicated. Business leaders should follow the proper course, act morally, and conduct themselves in an open and honest manner. Government officials should respect the ethics of politics and draw a clear boundary between becoming an official and becoming wealthy.

Under the close government-business relations: First, a close government-business relationship strengthens government-business communication, and the alliance between the local government and enterprises can help the government to tailor its policies to the enterprises, accurately connect with them, and provide them with targeted and forward-looking services. Secondly, it strengthens enterprises' sense of social responsibility and encourages management to assume social responsibility. Close political and business relationships play a cultural role in enlightening and moisturizing the heart, subconsciously enhancing the management's sense of social responsibility, prompting the "pro and measured, clear and productive" values deeply rooted in the heart, prompting the management to subconsciously form a "can be done" and "should be done" and "should be done". The value judgment of "can do" and "should do", the value choice of "can't" and "shouldn't" manipulate the information[15], reduce the opportunistic behavior of the management, and reduce the self-interested short-sighted behavior.

Under the clean government-business relations: First, cut off the chain of collusion between government and business and transfer of benefits between government and enterprises. A clean government-business relationship demonstrates the government's firm determination and thunderous means of zero tolerance for corruption, effectively curbing the phenomenon of collusion between government and business. Rent-seeking is the result of the game between government officials and enterprise managers, with a certain degree of secrecy, and there is uncertainty as to whether enterprises can obtain external resources based on rent-seeking agreements[16]. With the high-pressure anti-corruption, rational economic people realize that rent-seeking behavior is irrational economic behavior. Second, reduce market incentives for short-term investment behavior. Both the market's overreaction to declining unmanaged earnings and its underreaction to decreasing valuable R&D indirectly lead to an overestimation of the benefits of short-term investment[17]. In a fair and transparent market environment, the government and outside investors can effectively collect information about the quality of R&D in order to covertly monitor managers' investment behavior, thereby reducing the opportunity for managerial short-termism and lowering market incentives for short-term investment. Accordingly, it is proposed that:

H1: The close clean government-business relationship can mitigate managers' short-sighted behavior.

One of the main contributors to managers' shortsightedness is the capital market participants' fixation with short-sighted performance, which is a result of institutional investors' significant participation in China's capital market. According to the efficient market hypothesis, institutional investors rely on their advantages over general investors in terms of professional skills and information. They are also better able and willing to monitor a company's business operations and can prevent shortsightedness within the organization by participating in corporate governance[17], which helps to stabilize the capital market[18]. However, as the share of institutional investors increases, this could have negative effects on the firms, including performance pressure and excessive supervision[19]. Conversely, managers' welfare benefits are positively correlated with stock market performance. Managers will reduce research and development costs to satisfy the short-term surplus demand of investors with short sight in order to raise the short-term stock price. The stronger the positive correlation between institutional investors' shortsightedness and managers' catering behavior on stock price overvaluation[20]. The signaling theory states that institutional investors' behavior has a stronger signaling and orienting function the more shares they hold. It also suggests that institutional investors who invest in shortsightedness are more likely to induce managers to be shortsighted. Accordingly, it is proposed that:

H2: The association between managers' shortsighted behavior and close and clean government-business relationships is positively regulated by institutional investors' holdings.

3. Design of research

3.1 Data sources and sample selection

The sample is from companies listed between 2017 and 2020. The data are from CSMAR database, China Statistical Yearbook, and National Academy of Development and Strategy, Renmin University of China. This paper excludes ST, *ST type companies, data missing companies, and financial companies. Eventually, a total of 9,188 observations were obtained.

3.2 Measurement variability

3.2.1 Implicit variable

Based on prior research on managers' myopic behavior, specifically Qiang Cheng's (2015)[21] studies, which use the possibility of R&D cuts as a variable measure of managerial myopic behavior,.When a management reduces research and development spending in the current year relative to the prior year, that reduction is recorded as 1, and 0 otherwise.

3.2.2 Independent variable

This study uses the government-business relationship index from the 2017–2020 China City Government–Business Relationship Ranking (Data source: Nie Huihua, Han Donglin, Ma Liang and Zhang Nandi Yang, Ranking of Government-Business Relations in Chinese Cities (2017,2018,2019,2020), National Academy of Development and Strategy, Renmin University of China.), from Renmin University of China's National Institute of Development and Strategy. The degree of close and clean government-business relationships in that region increases with the health index of government-business relationships score. Furthermore, the percentage of 100 in the index is employed as an explanatory variable because it is not at the same level as the managers' short-sightedness scale.

3.2.3 Control factors

Regulating variables include Institutional investors' holdings (INST: Ratio of institutional investors' holdings to total shares) and Nature of ownership (Own:Assign a value of 0 to state-owned businesses and 1 to other ownership).

Control variables include Capital expenditures (Capx: If capital expenditures are lower this year than they were last year, this is recorded as 1., otherwise it is recorded as 0), Equity of the CEO (CEO_E: Whether the CEO holds shares or not, holdings are recorded as 1, otherwise 0), Gender of the CEO (CEO_G: CEOs are recorded as 1 for males and 0 for females), Percentage of Independent Director(Outr: Percentage of independent directors on the board of directors), shareholding structure (PT: Shareholding ratio of largest shareholder), Development capacity (EG: Growth rate of operating profit), earning power (ROA: Total assets net profit margin), Tobin's Q(Tobin Q), industrial structure (Str: Share of value added of secondary industry in GDP), and Government interventions (GI: Government fiscal expenditure as a share of regional GDP).

In addition, Year and Industry dummy variables are controlled.

3.2.4 Descriptive statistics

The outcomes of descriptive statistics are displayed in Table 1. The sample firms' managers exhibited evident shortsightedness as 22.8% of them reduced their R&D expenditures in the current year, as indicated by the mean value of De of 0.228. There is a noticeable variation in the government-business relationship index between different regions, as seen by the ZS mean value of 0.580, which ranges from 0 to 1. In contrast, the standard deviation of the ZS2 is 0.195 and that of the ZS1 is 0.240. The latter is more steady and less erratic.

Table 1. Descriptive statistics

Variable	N	Mean	p25	p50	p75	SD	Min	Max
De	9188	0.288	0	0	1	0.453	0	1
ZS	9188	0.580	0.394	0.565	0.793	0.233	0.110	1
ZS1	9188	0.511	0.310	0.474	0.688	0.240	0.0930	1
ZS2	9188	0.685	0.566	0.721	0.823	0.193	0.143	1
Capx	9188	0.156	0	0	0	0.363	0	1
CEO Equity	9188	0.597	0	1	1	0.491	0	1
CEO gender	9188	0.935	1	1	1	0.246	0	1
INST	9188	39.63	17.94	40.58	59.06	24.47	0.116	89.31
Outr	9188	0.377	0.333	0.364	0.429	0.0540	0.333	0.571
PT	9188	32.02	21.14	29.99	40.90	14.04	8.090	70.22
Ownership	9188	0.706	0	1	1	0.456	0	1
EG	9188	0.0980	-0.0260	0.0970	0.224	0.275	-0.802	1.111
ROA	9188	0.0260	0.0120	0.0350	0.0650	0.0930	-0.489	0.208
Tobin Q	9188	2.142	1.331	1.750	2.437	1.318	0.878	8.750
Str	9188	0.425	0.311	0.402	0.468	0.669	0.117	22.68
GI	9188	0.670	0.175	0.365	0.732	1.035	0.00700	36.08

3.2.5 Correlation test

The correlation coefficient between close and clean government-business relationships and whether firms cut R&D expenditures, without taking other control variables into account, is -0.030 and is negatively significant at the 1% level. Due to the length of the article, only the results are reported here.

4. Model design

4.1 Empirical tests

To verify H1 above, the following model is constructed:

$$RD\_De_{i,t} = \beta_0 + \beta_1 ZS_{i,j,t} + \sum \beta_i Controls_{i,t} + Year + Industry + \varepsilon_{i,j,t} \quad (1)$$

In order to test the regulating effect of the shareholding ratio of institutional investors d, the following regression model is constructed:

$$RD\_De_{i,t} = \beta_0 + \beta_1 ZS_{i,j,t} \times INST_{i,t} + \beta_2 ZS_{i,j,t} + \beta_3 INST_{i,t} + \sum \beta_i Controls_{i,t} + Year + Industry + \varepsilon_{ijt} \quad (2)$$

4.2 Model test

The regression results of model(1) are shown in columns (1)-(3) of Table 2. The government-business relationship index, proximity index and innocence index are significant at 5%, 10% and 5% respectively, indicating that there is a negative correlation between close and clean government-business relationship and managers' short-sighted behavior, and close and clean government-business relationship can inhibit enterprises' management behavior of reducing R&D expenditure. H1 is verified.

The regression results of model(2) are shown in columns (4)-(7) Table 2. This finding suggests that the institutional investors' shareholding ratio can positively regulate the relationship between the government-business relationship and managers' shortsighted behavior. H2 is tested.

Table 2. Results of basic regression

Variables					H-INST		L-INST
	(1) De	(2) De	(3) De	(4) De	(5) De	(6) De	(7) De
ZS	-0.0539**				-0.1019***	0.0016	0.0414
	(-2.3466)				(-3.0835)	(0.0512)	(1.1190)
		-0.0395*					
		(-1.7744)					
			-0.0604**				
			(-2.3019)				
ZS*INST							-0.0025***
							(-3.3166)
INST				-0.0011***			0.0004
				(-4.6273)			(0.7308)
Control	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry	Yes	Yes	Yes	Yes	Yes	Yes	Yes
_cons	0.4444***	0.4318***	0.4575***	0.4172***	0.4946***	0.3247***	0.3953***
	(7.0217)	(6.8714)	(7.1151)	(6.6975)	(5.2699)	(3.7617)	(6.0777)
N	9188	9188	9188	9188	4594	4594	9188
R2	0.1500	0.1498	0.1500	0.1495	0.1378	0.1699	0.1510

Note: The values in parentheses are t-values. *, **, *** denote that the estimation results are significant at 10%, 5%, and 1% levels, respectively.

4.3 Robustness test

The robustness test of this paper adopts three methods: one-stage lag test, refining the indicators of the relationship between government and business, and replacing the core explanatory variables. Limited by the length of this paper, only the test results are reported here.

Firstly, regression analysis is repeated using the independent variable as the lag one period. The result is still significantly negative. These findings suggest that the close and clean government-business relationship will continue to have a significant inhibitory effect on managers' shortsighted behavior in the years to come.

Second, Based on the composition of the government-business relationship index, the influence on managers' short-sighted behavior is further investigated. The empirical findings indicate that the closeness aspect of the government-business relationship primarily stems from government services that encourage managers to make long-term plans, and the cleanness aspect primarily stems from government integrity and transparency that restrain managers' behavior that is too short-sighted.

Thirdly, on the one hand, The ratio of current R&D investment to current main business revenue is used as a reverse proxy variable for managerial shortsightedness behavior, drawing on Cao(2017)[22] variable definitions of managerial shortsightedness. The results demonstrate that the close and clean government-business relationship an promote the R&D investment of enterprises and restrain the short-sighted behavior of managers, and support H1.On the other hand, this study uses abnormal production costs and abnormal discretionary expenditures as a proxy for managerial myopia[23]. The results indicate that this effect is negatively significant at the 1% level, suggesting that the enterprise's true surplus management behavior is reduced by the close and clean government-business relationship, thereby impeding managers' shortsightedness.

5. Conclusion

Using a sample of Chinese listed businesses from 2017 to 2020, the impact of close and clean government-business relationships on managers' shortsighted conduct is empirically studied based on institutional theory. The empirical study demonstrates that: first, the close and clean government-business relationship can effectively inhibit managers' shortsightedness behavior. In the close and clean aspect, managers are motivated to make long-term plans primarily through government services; in the clean aspect, managers' shortsighted behavior is constrained primarily by government integrity and transparency. Secondly, in companies with a higher number of independent directors, the hindrance that proximity has on managerial myopia is more noticeable. Third, pro-business ties have a stronger stifling influence on managerial myopia in companies where institutional ownership is higher.

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