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Economic Policy Uncertainty and Corporate Financialization

-- A Regulatory Effect Based on Corporate Social Responsibility

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Abstract: The article selects listed companies in the non-financial and non real estate industries of China's A-share market from 2010 to 2020 as research samples to empirically examine the relationship between economic policy uncertainty faced by individual enterprises and their financialization. Research has found that economic policy uncertainty significantly suppresses the level of corporate financialization, and the level of corporate social responsibility plays a negative moderating effect in this process; The results of heterogeneity analysis show that the inhibitory effect of economic policy uncertainty on the level of corporate financialization is more pronounced in the central region and state-owned enterprises. The research conclusion of this article provides reference value for the government to prevent excessive financialization of the real economy.

Keywords: Economic policy uncertainty, Enterprise financialization, Corporate social responsibility.

1. Introduction

The real economy is the foundation of the national economy and the key to maintaining long-term competitiveness of the country. However, in recent years, the phenomenon of China's real economy shifting from real to virtual has become increasingly serious. Due to the profit seeking nature of capital, a large number of non-financial enterprises have used excessive funds for speculative activities, known as "corporate financialization". The enhancement of non-financial enterprise financialization will enhance the linkage between the real economy and the virtual economy, causing excessive expansion of the virtual economy and even leading to financial crises, which is not conducive to the stable development of the macro economy [1].Therefore, it is crucial to explore the influencing factors of enterprise financialization level. At the same time, as China's domestic reform has entered the difficult and deep-water areas, facing various unresolved problems in the economy, economic policies are constantly changing, and economic policy uncertainty is deepening. Therefore, will economic policy uncertainty have an impact on the level of financialization of enterprises? Exploring this issue can enrich the influencing factors of corporate financialization and provide valuable references for high-quality economic development.

2. Theoretical Analysis and Research Hypotheses

At present, there is disagreement in the academic community regarding the impact of economic policy uncertainty on corporate financialization. On the one hand, some scholars believe that economic policy uncertainty can increase the uncertainty of future income, costs, and cash flows for enterprises[2]. In order to reduce the negative impact of future fund chain disruptions on enterprises, enterprises will choose to hold some cash and short-term financial assets. In addition, in order to diversify risks, enterprises may choose to purchase financial derivatives such as options and forwards to hedge, therefore, economic policy uncertainty will increase the proportion of financial assets of enterprises [3]. On the other hand, some scholars have proposed that economic policy uncertainty can lead to increased financial market risks [4]. At this time, banks will choose to shrink credit to resist risks, enhance corporate financing constraints, and ultimately lead to a decrease in corporate financial investment. At the same time, financialized investments have option characteristics, and changes in the market environment can lead to changes in investment decisions by enterprises. When uncertainty increases and the volatility of financial assets increases while liquidity decreases[1], investing funds in the financial market will expose enterprises to significant risks, resulting in a decrease in the level of financialization of enterprises. Given this, the following assumptions are proposed:

H1a: Economic policy uncertainty can promote corporate financialization.

H1b: Economic policy uncertainty can inhibit corporate financialization.

Further consider the potential moderating effect of corporate social responsibility in the relationship between the two. Corporate social responsibility refers to the responsibility that an enterprise bears to other stakeholders in addition to realizing the Profit maximization of shareholders [5]. The social exchange theory proposes that corporate social responsibility comes from the resource exchange between the enterprise itself and other social members. Gu Leilei et al. (2020) [6] found that strong social responsibility can help enterprises obtain financial resources from stakeholders such as banks and investors, and alleviate financing constraints faced by enterprises. Therefore, in the face of increased economic policy uncertainty, enterprises with strong social responsibility may hold more financial assets due to weaker financing constraints. Given this, the following assumptions are proposed:

H2a: Corporate social responsibility plays a positive regulatory role in the process of economic policy uncertainty

promoting corporate financialization.

H2b: Corporate social responsibility plays a negative regulatory role in the process of economic policy uncertainty inhibiting corporate financialization.

3. Research Design

3.1. Sample selection and data sources

The article selects non-financial and non real estate industry listed companies in China's A-share market from 2010 to 2020 as research samples, and excludes ST and PT samples. The financial indicators of the companies are sourced from the CSMAR database, and the corporate social responsibility indicators are sourced from Hexun.com. To eliminate the impact of extreme values, a 1% bilateral tail reduction treatment is applied to continuous variables.

3.2. Variable definition

Enterprise financialization (fa):Based on the measurement of the level of corporate financialization in existing literature, the measurement method for corporate financialization in this article is as follows: corporate financialization=(trading financial assets+derivative financial assets+net loans and advances issued+net available for sale financial assets+net held-to-maturity investments+net investment real estate)/total assets

Economic Policy Uncertainty Faced by Enterprises (fepu):Previous literature often used Baker et al. (2016) [7] to construct a national level economic policy uncertainty index based on the text analysis method used by newspapers. However, enterprises in different regions and industries often face varying degrees of economic policy uncertainty. To accurately measure the degree of economic policy uncertainty faced by individual enterprises, this article draws on the research of Nie Huihua et al. (2020) [8], Construct an uncertainty dictionary and an economic policy dictionary, and use Python to conduct text analysis based on the "Management Discussion and Analysis" (MD&A) in enterprise annual reports. Sentences containing both uncertainty words and economic policy words are considered as economic policy uncertainty sentences, Measure the economic policy uncertainty (fepu) faced by individual enterprises by the proportion of the total number of uncertain words in economic policy uncertainty sentences to the total number of MD&A words .

Corporate Social Responsibility (csr):This article selects the total score of the social responsibility report of listed companies on Hexun.com to measure the level of corporate social responsibility commitment. The score is derived from five aspects: shareholder responsibility, employee responsibility, supplier, customer, and consumer rights responsibility, environmental responsibility, and social responsibility, and the weight is changed based on the industry in which the company operates.

Control variables (controls):Referring to relevant research, the control variables selected in this paper include: enterprise size (size, total assets take Natural logarithm), leverage ratio (lev, total liabilities/total assets), equity concentration (shrcr, shareholding ratio of the largest shareholder), book to market ratio (bm, total assets/total market value), profitability (roe, total net profits/owner's equity), enterprise age (age, enterprise establishment years plus 1 take Natural logarithm), Cash flow intensity (cash, balance of cash and cash equivalents at the end of the period/total assets), board size (board, the number of directors takes the Natural logarithm).

3.3. Model design

Build a model (1) to test the impact of economic policy uncertainty on corporate financialization, where the lower corner i represents the individual listed company, t represents the year, controls represents various control variables, and year and industry represent fixed effects for the year and industry, respectively, α_0 represents the constant term coefficient, α_J is the regression coefficient of each control variable, α_1 is the focus of this article. If the value is significantly positive or negative, it indicates that the economic policy uncertainty faced by the enterprise will promote or suppress the financialization of the enterprise. To investigate the moderating effect of corporate social responsibility in the relationship between the two, the interaction term between corporate social responsibility and this variable and the uncertainty of corporate economic policy is introduced into the model, and model (2) is constructed. csr is corporate social responsibility, and the other indicators are the same as model (1). If δ_2 is significant, and the direction of it is the same as δ1, there is a positive regulatory effect, while if the direction is opposite, it is a negative regulatory effect.

$$fa_{it} = \alpha_0 + \alpha_1 fepu_{it-1} + \sum \alpha_j controls_{it-1} + year + industry + \varepsilon_{it} \quad (1)$$

$$fa_{it} = \delta_0 + \delta_1 fepu_{t-1} + \delta_2 fepu_{it-1} * csr_{it-1} + \delta_3 csr_{it-1} + \sum \delta_j controls_{it-1} + year + industry + \varepsilon_{it} \quad (2)$$

4. Empirical Analysis

4.1. Benchmark regression and moderating effect test

The Hausman test results indicate that a fixed effects model should be used in this article. To verify the hypothesis H1 proposed in this article, based on model (1), the regression results are shown in column (1) of Table 1 without introducing control variables, but with fixed effects of year and industry. Furthermore, after introducing various control variables, the regression results are shown in column (2) of Table 1. It can be seen that the economic policy uncertainty faced by enterprises significantly suppresses their level of financialization, This article assumes that H1b holds. Furthermore, based on model (2) to test the moderating effect of corporate social responsibility, the regression results are shown in column (3) of Table 1. It can be seen that corporate social responsibility plays a negative moderating role in the relationship between the two, and the article assumes that H2b is valid.

4.2. Robustness check

4.2.1. Endogenous discussion

Considering the economic policy uncertainty faced by enterprises and the possible reverse causality problem of enterprise financialization, this article lags behind the core explanatory variable and control variable by one period in the empirical process. Considering the problem of missing variables, based on the fixed effect model and the research of Jiang Minxing et al. [9], this paper takes the average economic policy uncertainty index of enterprises in the same

industry, same year and same region as a Instrumental variables estimation. On the one hand, the level of economic policy uncertainty faced by individual enterprises is related to the average value, and on the other hand, the level of enterprise financialization is difficult to affect the average fepu in the same region and industry, The regression results are shown in column (1) of Table 2, indicating that the estimated results are still robust.

Table1. Benchmark regression and moderating effect regression results

	(1)fa	(2)fa	(3) fa
fepu	-0.015**	-0.014**	-0.037***
	(-2.41)	(-2.17)	(-3.32)
csr			-0.001
			(-0.15)
*csr*fepu*			0.108***
			(2.94)
controls	No	Yes	Yes
year fixed effect	Yes	Yes	Yes
industry fixed effects	Yes	Yes	Yes
_cons	0.031*	0.029	0.038
	(1.90)	(0.57)	(0.75)
sample size	19066	19066	19066
R^2	0.138	0.146	0.147

Note: * * *, * * and * represent significance levels of 1%, 5%, and 10%, respectively; The t value in parentheses is the robust consistency estimate of Homoscedasticity and heteroscedasticity adjusted by clustering at the enterprise level, the same as in the following table.

4.2.2. Replace the dependent variable with the core explanatory variable

Change the calculation method for corporate financialization to: corporate financial assets/(total assets - corporate financial assets), and re calculate the regression results as shown in column (2) of Table 2; Change the measurement method of enterprise economic policy uncertainty to the ratio of the number of sentences with economic policy uncertainty in MD&A to the total number of sentences in MD&A for regression. The regression results are shown in column (3) of Table 2, indicating that the estimated results are still robust.

Table 2. Robustness test regression results

	(1)*fa*	(2)*fa*	(3)*fa*
fepu	-0.040*	-0.021**	-0.001*
	(-1.66)	(-2.29)	(-1.53)
controls	Yes	Yes	Yes
year fixed effect	Yes	Yes	Yes
industry fixed effects	Yes	Yes	Yes
_cons	0.033	0.052	0.028
	(0.66)	(0.72)	(0.55)
sample size	19066	19066	19066
R^2	0.145	0.117	0.146

4.3. Heterogeneity analysis

The Chinese economy has been in a state of long-term regional development imbalance. In view of this, in order to examine whether there is heterogeneity in the impact of economic policy uncertainty on the financialization of enterprises in different regions, the sample was divided into three parts: eastern, central, and western for regression [10]. The results are shown in columns (1) - (3) of Table 3. It can be seen that only enterprises in the central region will significantly reduce the level of financialization due to the enhancement of economic policy uncertainty, and the reasons for this are investigated, As the most developed economic region in China, enterprises in the eastern region will face more financial investment opportunities, and fierce competition among banks will limit their credit contraction, so the regression results are not significant. As a key national development area, China has provided a lot of policy support for its economic development, such as encouraging investment in the eastern region to the western region. Therefore, the impact on enterprises in the western region is not significant, On the one hand, there are fewer financial investment opportunities in the central region, and on the other hand, there is no significant policy support from the country, resulting in a significant decrease in the level of financialization.

Furthermore, based on the nature of enterprises, enterprises were divided into state-owned enterprises and non-state-owned enterprises for examination. The results are shown in columns (4) to (5) of Table 3. It can be seen that although the increase in economic policy uncertainty has a inhibitory effect on the financialization of both types of enterprises, for state-owned enterprises, this inhibitory effect is greater and more significant, because state-owned enterprises shoulder certain government functions, In response to the call of national entity enterprises to "shift from virtual to real", they will reduce their holdings of financial assets. Based on the pressure of maintaining and increasing the value of state-owned assets, when economic policy uncertainty increases and financial asset prices fluctuate, state-owned enterprises are more inclined to reduce their holdings of financial assets.

Table 3. Heterogeneity analysis regression results

	(1) *eastern*	(2) *central*	(3) *southern*	(4) *state*	(5) *Non-state*
fepu	-0.011	-0.030**	0.001	-0.017**	-0.009
	(-1.44)	(-2.00)	(0.12)	(-2.49)	(-0.92)
controls	Yes	Yes	Yes	Yes	Yes
year fixed effect	Yes	Yes	Yes	Yes	Yes
industry fixed effects	Yes	Yes	Yes	Yes	Yes
_cons	0.102	-0.028	-0.068	0.127*	-0.003
	(1.61)	(-0.33)	(-0.65)	(1.65)	(-0.04)
sample size	13130	3385	2532	7206	11697
R^2	0.165	0.179	0.099	0.129	0.174

5. Research Conclusion

The article selects listed companies in the non-financial and non real estate industries of China's A-share market from 2010 to 2020 as research samples, constructs indicators of economic policy uncertainty faced by individual enterprises, and finds that: (1) an increase in economic policy uncertainty will suppress the level of financialization of enterprises; (2) The level of corporate social responsibility plays a negative regulatory effect in this process; (3) During this process, the level of financialization of enterprises and state-owned enterprises in the central region has decreased more significantly.

The research conclusion of this article extends the influencing factors of corporate financialization and indicates that economic policy uncertainty is not a cause of excessive financialization of the real economy, but rather has a inhibitory effect on it. To effectively alleviate the problem of the economy shifting from real to virtual, the government should, on the one hand, reduce enterprise operating costs, improve the profit margin of physical investment, and encourage the development of the real economy in multiple aspects through policies such as tax reduction and fee reduction; On the other hand, the government should deeply promote the structural reform of the financial supply side, alleviate the financing difficulties of private enterprises and small and medium-sized enterprises, and make finance better serve the real economy.

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