Political Power and Market Power

Bo Cowgill, Andrea Prat, Tommaso Valletti

The Political Power of Corporations

- Mergers may be detrimental because they increase monopoly power
- ...or because they increase monopsony power

- Another channel first discussed in Brandeis (1914) ("curse of bigness")
- Larger firms may have more incentives or resources to get favorable regulation

Market Power Begets Political Power?

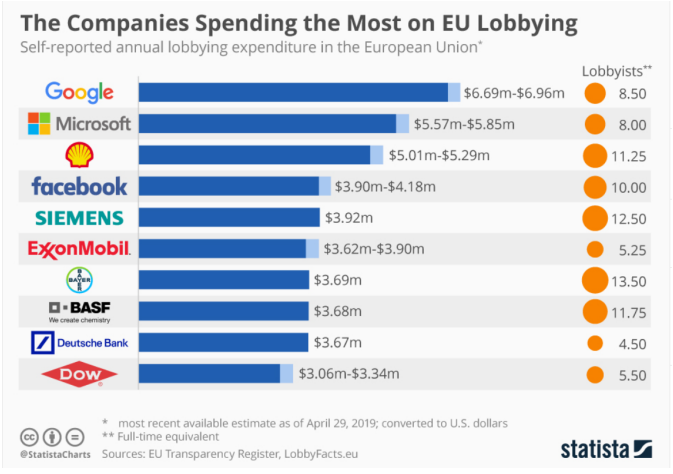
- Rajan-Zingales, Saving Capitalism from the Capitalists, 2003
- Callander-Foarta-Sugaya (2021)
- Incumbents have an incentive to enlist policy-makers to erect barriers to entry so they can maintain oligopoly/monopoly rents.
- Mergers may cause that incentive to go up (Zingales 2017)
- Antitrust policy should look at the effect of concentration on political influence (Wu 2018)

Lobbying Spending in the US by Source in 2019 (Opensecrets)

Business, Labor & Ideological Split, 2019

Business	$2,968,251,096	86.54%
Other	$260,281,617	7.59%
Ideological Groups	$152,310,046	4.44%
Labor	$48,964,316	1.42%

Largest Spenders in EU Lobbying



This Paper

- **Question:** Do firms whose size increase because of a merger increase their political influence activity?
- **Theory:** combine Grossman-Helpman (1994) with IO merger model
- **Data:**
  - Mergers + company info: Compustat firms (25k) from 1999 to 2017
  - Two influence activities: lobbying spend and campaign donations
- **Empirical Approach:**
  - Panel event study: Freyaldenhoven et al 2019
  - Bartik instruments

Theory

Model: Idea

- Combine two ingredients:

1. Standard oligopoly model with the addition of regulatory variables ("augmented Cournot model").
2. Standard lobbying model where firms try to influence regulatory variables.

- Characterize lobbying and oligopoly equilibria
- Study effect of merger on lobbying activity, quantities/prices, and firm profits

Model: Lobbying

- Lobbying model of Grossman-Helpman (1994), building on Bernheim-Whinston's (1986) menu auctions.
- Two stage game:
  1. All lobbies offer transfers;
  2. The policy maker chooses policy

Two Cases

- Recall the demand function

$$p_i = A - Q + bF_i + aR.$$

- Two scenarios:

1. **Pure public-good lobbying**: $b = 0$
2. **Pure private-good lobbying**: $a = 0$

Merger Analysis: Public-Good Case

- If the two firms merge, both the total transfer $t_1^* + t_2^*$ and the amount of regulation R go up.
- Intuition: in duopoly, firms dissipate part of the potential benefit of R through lower prices. With a merger, they benefit from it fully and hence they invest more in lobbying.

Theory: Conclusions

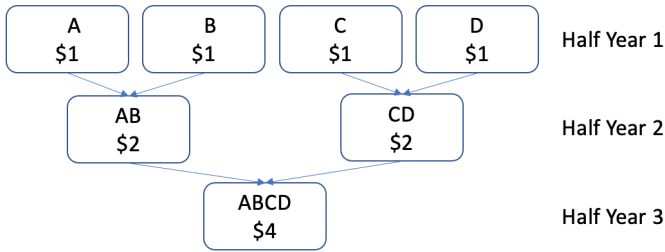
- Depending on the nature of regulatory policy, increased industry concentration can increase or decrease total lobbying activity
- As both kinds of policies are present in the US, need for empirical analysis
- Extension with (heterogeneous) fixed costs: extensive & intensive margin
- Extension to industry associations

Empirical Analysis

Overview

- Research question: *Do lobbying and campaign contribution activities increase or decrease after mergers?*
- Do firms spend more together, vs the sum of when they were separate?
- Composite firms + two identification strategies

Example: Graphical Representation of Composite Firm "ABCD"



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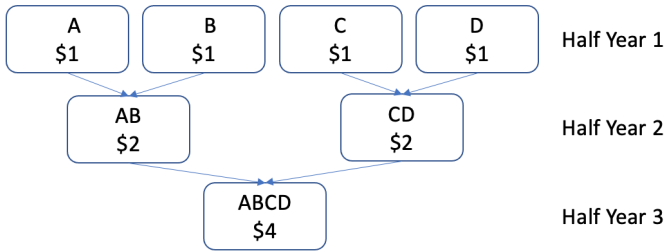

Tabular Panel Representation of "ABCD"

HalfYearID	CompositeFirmID	Total Revenue (Size)	# of Component Firms	Composite HHI Index	
1	"ABCD"	\$4	4	2,500	$=(1/4)^2 \times 4 \times 10K$
2	"ABCD"	\$4	2	5,000	$=(1/2)^2 \times 2 \times 10K$
3	"ABCD"	\$4	1	10,000	$=(1/1)^2 \times 1 \times 10K$

Our composite firm panel

- All Compustat firms (1999-2017)
- Transformed into composite firms using SDC Platinum data.
- $\Longrightarrow \approx$12K composite firms (bundles) composed of 15K component firms (members).
- Joined with political data.
  - LobbyView: Total spent on lobbying by all component firms.
  - OpenSecrets: Total PAC spending of all component firms.

Regression Equation

$$\sum_{f \in \mathcal{F}_{it}} y_{f,t} = \beta_0 + \beta_1 \text{MergerIndex}_{it} + \beta_2 X_{it} + \delta_i + \gamma_t + \epsilon_i. \quad (1)$$

- $y_{f,t}$ = political influence expenditures for firm f at time t.
- $\sum_{f \in \mathcal{F}_{i,t}} y_{f,t}$ = sum of expenditures all firms inside composite firm i.
- MergerIndex_{it} = Main variable of interest.
- X_{it}: $Revenue_{it}$ and additional controls (varied in coordination with identification strategies).
- δ_i = composite firm FEs, γ_t = time period FEs.
- SEs clustered at panel unit i (composite firms).

Panel Event Study

Main Results: Panel Event Study

	(1) Lobby Amount	(2) Lobby Amount	(3) PAC Contribs	(4) PAC Contribs
# Component Firms	-65,384**	-62,393***	-4,470*	-4,290
	(27,069)	(24,160)	(2,382)	(2,839)
Additional Controls		Y		Y
Observations	222,540	222,519	222,540	222,519
R^2	.54	.55	.32	.32

- # Component firms = Number of independent, as-yet-unmerged firms inside composite firm. $\downarrow$ with each merger.
- All regressions include composite firm fixed effects, time period fixed effects, and total size (revenue) controls. "Additional controls" are described in Slide 43.

Large vs Small Firms

- Theory suggests different results for "private good" vs "public good for industry" lobbying.
- One implementation of this: Large vs small firms.

Heterogeneity by Firm Size

	(1) Lobby Amount	(2) Lobby Amount	(3) PAC Contribs	(4) PAC Contribs
# Component Firms	-14,996	-60,468**	-689	-4,201
	(16,417)	(24,512)	(966)	(2,856)
Additional Controls	Y	Y	Y	Y
Sample	Below Median Revenue	Above Median Revenue	Below Median Revenue	Above Median Revenue
Observations	76,352	146,167	76,352	146,167
R^2	.4	.55	.67	.32

- All regressions include composite firm fixed effects, time period fixed effects, and total size (revenue) controls. "Additional controls" are described in Slide 43.

“Close” vs “Distant” Mergers

- Possibly different results when merging firms are in the same industry or in different industries.
- Similarity measure: # of unique NAICS code inside composite firm.
  - Lots of different NAICS codes $\implies$ mergers of different firms.
  - Few $\implies$ competitors merging.

Close vs Distant Mergers

	(1) Lobby Amount	(2) Lobby Amount	(3) PAC Contribs	(4) PAC Contribs
# Component Firms	-69,195**	-69,913**	-3,115	-2,700
	(34,589)	(31,367)	(2,748)	(2,507)
# Component Firms × Unique NAICS3	13,712**	13,761**	230	67
	(5,481)	(5,792)	(357)	(186)
Additional Controls		Y		Y
Observations	222,540	222,519	222,540	222,519
R^2	.54	.55	.32	.33

- Interpretation: When very different firms merge, the lobbying increase isn't as high.
- We need similar firms to merge (horizontal) to get as big of an increase in lobbying.
- Qualitatively same story with PAC, but less precise.

Alternative Mechanism

- "*After* a merger happens, regulators increase scrutiny."

Hassan et al. (2019), "Firm-level political risk."

- "[T]he share of their quarterly earnings conference calls that they devote to political risks."
- We study this variable as an outcome of the merger.
- Measure of higher regulatory scrutiny.

- This is available only for a subset of firms that have regular investor calls.

Hassan et al. (2019), "Firm-level political risk."

	(1) Lobby Amount	(2) PAC Contribs	(3) Political Risk	(4) Political Risk Econ. Policy	(5) Political Sentiment
# Component Firms	-93,960***	-5,698	-.031	-.034	-.002
	(30,584)	(4,448)	(.034)	(.036)	(.035)
Additional Controls	Y	Y	Y	Y	Y
Observations	54,549	54,549	54,549	54,549	54,549
R^2	.63	.38	.36	.31	.44

- Replicated results on main specifications (Col 1 & 2).
- Political risk outcomes normalized.
- Can reject large effects: 95% CI: (-0.1 to $+0.03$ σs).

Conclusions

- Do firms increase or decrease their lobbying activity when they merge?
  - Theory: depends on what they lobby for
  - Evidence for increased lobbying spending
  - Weaker evidence for increased campaign donations
  - All action is in larger firms
- Implications for policy
  - Next round table!

Thank you!