



Political Supports and Financial Distress of Companies in Indonesia

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Abstract

The current study was underlain by the background that many entrepreneurs came into politics and many politicians established companies after having political positions. This study aimed at examining the theory that companies' finance is influenced by political supports. The problem proposed was how political supports affected the companies' financial distress in Indonesia. The data of the current study referred to the ratios of finance reported by each company listed in the period of 2010-2019. The samples were purposively solicited by incorporating 63 companies indicated to have political supports for ten years. For testing hypotheses, the analysis technique used simple regression. The results revealed that political supports (PS1, PS2, and PS3) did not significantly affect financial distress (FD). Subsequently, political supports (PS1, PS2, and PS3) also did not significantly affect companies' performance. The foregoing was caused that the board of directors carried out the companies' operations independently without political pressure.

INTRODUCTION

The current study is conducted to address various issues related to political supports towards companies' financial distress in Indonesia. Some empirical findings exhibit that there are direct effects of political supports from the government and the government supporting parties on the capital structure (Kamaludin, 2010). Blanchard (2006) and Gregory (2006) stated that economic activities of a country cannot be separated from the role of political factors. A safe and conducive political situation has a positive impact on the economy. Furthermore, Blanchard (2006) added that a country plays an important role in maintaining political stability so that it will have an impact on the country's economic growth. More broadly, various indicators exist to measure how political factors affect the economic conditions of a country. Jadevicius and Huston (2014) mentioned that these indicators consist of property rights, redistribution pressure, and dictatorial leadership.

The entrepreneurs that are powerful and closed to the authorities can impose their will and work in collusion with the authorities and decision makers at every governmental level at both central and regional levels in order that the authorities issue effective rules and policies which limit competition and create artificial market power beneficial to their business. Every negotiation always has a cost. Such an activity is only carried out if the revenue obtained from the negotiation is greater than the lobbying cost per se. Faccio and Lang (2002) stated that stemming from business-politic correlations in economic activities of a country, the term politics-connected companies further appear. To see whether a company is considered politically connected, it can be viewed from some indications, for instance, the company's largest shareholders (these can be anyone directly or indirectly connected with the board of directors with the minimum numbers of 10%) are the members of parliament, president, minister, or anyone closely related to top politicians.

Companies that have political supports and do transactions or make connections with particular parties and get banks' loans will have their values increased (Habib et al., 2017). Subsequently, Nys, Tarazi, and Trinugroho (2015) stated that the banks which have political supports will more easily receive funds' supply such as deposit withdrawals from the government. In their operations, the banks politically supported will impose formal insurance for deposit products, so when the banks fail in their management, the return of the depositors' funds will be guaranteed. Banerji, Duygun, and Shaban (2018) mentioned that the bailout makes some loans safe, and the companies' political "capital" functions as unreal collateral for bank loans. As a result, the banks will have no incentives to elicit information vis-a-vis possible bad circumstances. Therefore, trade-offs emerge in the equilibrium wherein the companies' profits from the bailout are partially balanced by less information generated. Thus, it is a political connection although it assists the company in giving a hedge against possible unexpected cash flow.

Fu, Shimamoto, and Todo (2017) said that financial access due to political affiliation tends to be more protuberant in the micro, small, and medium enterprise (MSME) companies compared to the large companies that have gone public. In this regard, political connections between the company owners and politicians tend to be more personal. In the meantime, formal connections viewed from stock ownership or institutional connections such as politicians' involvement in the board of directors do not seem prominent. Subsequently, Fu et al. (2017) elucidated that with politics, there are two ways the companies in Indonesia can get banks' treatments. First, they can more easily borrow finances from the banks owned by the government. Second, they can more easily get the complete loans as requested. The advantage of getting political encouragement such as easy access to banks seems significant for small and medium enterprise. However, this is not for larger companies.

Various studies which have been conducted regarding political supports illustrate that there is possible financial distress for the politically supported companies although this premise is not absolute. Friedman (1999) explains the pattern of banking leverage for companies but does not explain how much influence on the companies' performance. Furthermore, Wong (2010) also stated that the financial performance of the companies with political connections in Hong Kong outperforms those with political connections. The financial performance adopted by Wong (2010) is Return on Equity (ROE) and Ratio Market to Book (market ratio). Kamaludin (2010) in his study revealed that the politically supported companies more or less will face financial distress situations. The credibility of this conclusion certainly needs to be tested because in a different way other studies show a better performance.

Actually, the connections between politics and companies are indeed established. Both parties have their own interests and advantages. From the political or governmental side, such connections can help the formulation of public policies including the policies on business interests, and companies' activities also help the political objectives of the government. From the companies' side, such connections are beneficial in the cases of tax relief, getting governmental projects, getting assisted in monopoly, and other aids supporting the companies' activities. Furthermore, the companies' activities originated from the greater use of debt cause a greater interest expense (Murniati, 2016). If the companies' operating expenses are greater than the operating profits, there will be problems of financial difficulties leading to decline of the performance. However, debt interest expense is also a tax deduction which can increase the companies' values. In this sense, it can be said that debt can improve performance, whereas if the companies use equity, there will not be tax savings because the burden of equity does not reduce taxes.

A number of previous studies have demonstrated a significant relationship of political supports and companies' performance, especially in the financial sector. However, it seems that it also needs to be further investigated how much urgency of political supports is to a company's financial performance. In certain periods, a politically connected company will experience a lot of financial distress because it is urged by political institutions (including political parties and politicians) to be able to provide financial supports in achieving political goals (Kamaludin, 2010). Therefore, the current study formulates the following research questions: 1) Do political supports affect financial distress? 2) Do political supports affect companies' performance?

RESEARCH METHODS

The current study is an empirical quantitative research that examines the theories of political supports, capital structure, financial distress, and their effects on the performance of companies going public in the Indonesia Stock Exchange in the 2010-2019 period. The research paradigm drew upon empirical positivists viewing that science including the science of companies' financial management can be developed by testing hypotheses. The hypotheses were formulated based on the propositions from various literature studies. The approach used was the deductive hypothesis method (Greener, 2015).

The following table 1 presents the variable definitions as well as the indicators used in this study.

Table 1. Operational Definitions of Each Variable and Indicator.

Variable	Operational Definition	Scale Measurement Formula	Sources
Political support	Political support is the incorporation of political parties and power in companies; in this study what is meant by political support is the supports politically given to companies or also the people involved in politics towards the companies.	<ol style="list-style-type: none"> 1. The minimum of 10% of share ownership by the President or Vice President, Ministers or members of the People's Representative Council, or; 2. The companies' top managers have connections with authorities (executive) or politicians, both friendship, family relations, and business organizations; 3. Among the companies' top managers (Board of Directors and or Board of Commissioners), there are the leaders of political parties, the former or active bureaucrats, or officers or the former officers of the TNI-POLRI, having a relationship with companies' operations 	(Bliss & Gul, 2012; Faccio, 2006; Fraser et al., 2006; Johnson & Mitton, 2003)
Financial Distress	Comparison of total current assets to current liabilities	Current Ratio	(Faccio et al., 2006; Platt & Platt, 2002; Winters & Benjamin., 2009)
Company's performance	Company's performance is a portrait of the company's financial condition analyzed by financial analysis tools.	$ROA = \text{Gross profit} / \text{The average of total assets} \times 100\%$ $ROE = \text{Net income} / \text{Capital}$	(Chantrataragul, 2007; Fan et al., 2007; Kamaludin & Pribadi, 2011)

The data concerning political supports were the ranking data exhibiting their respective levels and ratios. The data as regards political supports were converted to the ratio as presented in the following table 2

The secondary data directly related to the study and sourced from the companies listed

on the Indonesia Stock Exchange (BEI) were the annual reports of the 2010-2019 period. The resources in the form of articles, journals, and the results of previous studies were used as comparative resources to the present study conducted.

Table 2. The Score of Response Scale of Each Variable

No	Criteria	Category	Scale	Score
	Political Support (PS1)	Stock Ownership 20 %	Ranking	1
		Stock Ownership 40 %	Ranking	2
		Stock Ownership 60 %	Ranking	3
		Stock Ownership 80 %	Ranking	4
		Stock Ownership 100 %	Ranking	5
	Political Support (PS2)	President/ vice President /DPR RI	Ranking	5
		Governor/ Deputy Governor /DPRD	Ranking	4
		Regent/Vice-Regent/DPRD	Ranking	3
		Officials of TNI /POLRI	Ranking	2
		Political Party Leader	Ranking	1
	Political Support (PS3)	President Commissioner	Ranking	5
		President Director	Ranking	4
		Commissioner	Ranking	3
		Director	Ranking	2
		Others	Ranking	1
	<i>Financial Distress</i>	Current Asset / Current Liability	Ratio	

The secondary data directly related to the study and sourced from the companies listed on the Indonesia Stock Exchange (BEI) were the annual reports of the 2010-2019 period. The resources in the form of articles, journals, and the results of previous studies were used as comparative resources to the present study conducted.

The population of the current study referred to the companies listed on the Indonesia Stock Exchange (go public) in 2010-2019. The samples were determined by firstly identifying the political connections to the board of commissioners and the board of directors of the companies. Identification was carried out by matching the positions of the board of commissioners and the board of directors with the positions of the government cabinet and the members of the House of Representatives of the Republic of Indonesia. In addition, it was also used some information elicited from the mass media with respect to political interests and the closeness of the companies to the governmentally made economic policies. Based on the results of

identification, the samples of this study referred to the companies having political supports. The sampling criteria are as follows: the companies were listed on the Indonesia Stock Exchange in 2010-2019; the companies were not delisted on the Indonesia Stock Exchange in 2010-2019; the companies had the data concerning EBIT, the positions of the Board of Commissioners and Board of Directors, total Assets, Leverage, and total capital; the value of ROA might not be negative; the companies had the structure of stock ownership; the companies were not the financial sector companies

The samples were selected using a purposive sampling method by assigning certain criteria (Notoatmojo, 2010). From a total of 481 companies, after being selected, there were found 63 companies indicated to have political connections from 2010-2019.

Data analysis method employed in this study was a statistical analysis method using simple regression equations and multiple regressions. The data analysis was undertaken with the help of SPSS version 20.0. Before testing the hypotheses, the researchers firstly tested the

classical assumptions encompassing tests of normality, multicollinearity, heteroscedasticity, and autocorrelation. The following table 3 presents the results of the classical assumption tests.

Table 3. The Summary of Scores gained from various tests

No	Variable	t test	r test	F test		Watson's Autocorrelation test	
				F test	Sig F		
1	PS1	FD	-1.138	0.049	1.294	0.256	1.975
2	PS2	FD	0.549	0.024	0.302	0.583	1.970
3	PS3	FD	0.821	0.035	0.674	0.412	1.965

Source: Data Processing in 2020

Based on table 3, the autocorrelation values were seen from the Durbin-Watson's values which were all located between -2 and +2, so according to Santoso (2008), the Durbin-Watson's values located at the aforesaid interval indicate that there is no the occurrence of autocorrelation.

RESULTS AND DISCUSSION

According to table 4 below, the Means of PS1, PS2, PS3, and FD were 0.2880, 0.2326, 3.2532, and 214.126. The minimum scores of PS1, PS2, PS3, and FD were 0.00, 0.00, 0.00, and 0.00. The maximum scores of PS1, PS2, PS3, and FD were 5.00, 3.00, 5.00, and 16309.00.

Table 4. Descriptive Statistics

	N	Minimum	Maximum	Sum	Mean	Std. Deviation
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic
Sokongan Politik (SP1)	632	.00	5.00	182.00	.2880	.90042
Sokongan Politik (SP2)	632	.00	3.00	147.00	.2326	.67654
Sokongan Politik (SP3)	632	.00	5.00	2056.00	3.2532	1.20846
Financial Distress (FD)	539	.00	16309.00	115413.96	214.1261	895.79859
Return on Asset (ROA)	611	.01	39.00	4047.99	6.6252	6.52277
Return on Equity (ROE)	611	.01	213.79	9144.24	14.9660	16.60723
Valid N (listwise)	539					

Source: Data processing in 2020

The maximum score of PS1 was 5. It meant that the stock ownership was above 80%. The maximum score of PS2 was 3 which meant there was an element of power in the companies. The maximum score of PS3 was 5 meaning that there was an element of politics in the companies' board of director. The maximum score of

Financial Distress was 16309.00 which meant the comparison of companies' current assets and current liabilities, wherein the companies had the current assets as many as 16309.00 times more than the current liabilities.

After conducting t test, the researchers conducted the r test and F test whereby the results obtained are displayed in the following table 5:

Table 5. Political Supports (PS1,2,3) on Companies' Performance (ROA and ROE)

ROE = $\alpha + \beta SP + \epsilon$									
Hypothesis 1= Political supports affect companies' performance (ROA and ROE as the dependent variables)									
Hypothesis 1									
Model	Beta	T	Sig	R	R Square	F	Result	Conclusion	
PS1 ... ROA	-.571	-1.977	.048	0.135	0.018	3.733	Insignificant	Accepted	
PS2 ... ROA	1.184	2.005	.045	0.203	0.021	0.382	Insignificant	Accepted	
PS3 ... ROA	-.330	-1.481	.139	0.155	0.043	1.655	Insignificant	Accepted	
PS1 ... ROE	-1.227	-1.657	.098	0.071	0,005	1.014	Insignificant	Accepted	
PS2 ... ROE	-.784	-.518	.605	0.072	0.009	0.518	Insignificant	Accepted	
PS3 ... ROE	-.312	-.547	.584	0.083	0.036	2.148	Insignificant	Accepted	

Source: Data Processing in 2020

According to the data processing process, the r test was used to find out the contribution of political supports (PS1, PS2, and PS3) to Financial Distress (FD). The analysis result shows the effect of political supports (PS1, PS2, and PS3) on Financial Distress (FD) that can be seen in table 6 below:

Table 6. The effect of political supports (PS1, PS2, and PS3) on Financial Distress (FD)

Hypothesis 2							
FD = $\alpha + \beta SP + \epsilon$							
Hypothesis 6 = Political supports affect financial distress							
Financial Distress (FD) is the dependent variable							
	B Unst	T	B	Sig	F	Conclusion	
PS1 --> FD	-42.049	-1.044	-.045	.297	0.127	Insignificant	Rejected
PS2 --> FD	44.800	.505	.022	.614	0.152	Insignificant	Rejected
PS3 --> FD	27.359	.833	.036	.405	0.152	Insignificant	Rejected

Source: Data Processing in 2020

Political supports 1, 2, and 3 did not contribute to financial distress. However, if compared, political support 2 contributed more to financial distress if compared to political support 1 and political support 3. Table 6 drew the conclusion that political support 1 due to the share ownership in companies, political support 2 due to the involvement of governmental elements, and political support 3 in light of the involvement in company management did not contribute to financial distress (FD), so financial distress was caused by other factors that were not regarded as the objects in this study. The values of PS1, PS2, and PS3 to FD were 0.127, 0.152, and 0.152. If the F value was greater than 0.05, it could be summarized that the data had been distributed normally.

The results of the present study indicated that there were effects and contributions of political supports (PS1, PS2, PS3), capital structure (DAR, DER), and financial distress on and companies' performance (ROA, ROE). Grounded in the results of the current study, it was revealed that political supports (PS1, PS2, and PS3) had no significant effect on companies' ROA. This data refutes the opinions of Johnson, Kochhar, Mitton, and Tamirisa (2007); Khwaja and Mian (2005) stating that differences in loan behaviour from state-owned banks are influenced by the election results of the parties connected with banks. Such an action is a transfer of wealth from consumers to the companies, resulting in an increase in the companies' values.

The results showed that on the companies' ROE, political supports (PS1 and PS2) also had no significant effect. This point is contrary to the result of the study undertaken by Chantrataragul (2007) wherein in his study it was found that political connections had a significant positive effect on the companies' performance such as ROE, Tobin's Q, and market division in Thailand. Wong's (2010) opinion is also refuted by this study, wherein in this study, it was revealed that political connections give an influence on the companies' performance measured by ROE and market ratios. This study result also refutes Faccio's et al. (2006) opinion where they argued that political supports can be seen as one of the situations in which at least one person from a company's top officer, a large shareholder of a company, or the owners' relatives are the holders of high politics or prominent politicians.

Political support due to the involvement in companies' management (PS3) had no significant effect on ROA and ROE of the companies. This result is in line with the study conducted by Wahab et al. (2011) on a number of companies in Malaysia, whereby their study revealed that there was no significant effect between governmental connections with companies' performance. Their data were taken from observations during 2001-2003 period incorporating as many as 1,022 companies. The result of Fadeev's (2008) study in Russia also agreed that there has no significant effect of political connections on company's productivity.

The following discusses the effect of political supports on companies' performance in every aspect, namely PS1, PS2, PS3, ROA and ROE. Political support due to the share ownership in the companies (PS1) did not have a significant effect on the companies' ROA. Political support due to the share ownership in companies (PS1) had a significant effect on the companies' ROE. This result refutes Winanda and Ardiyanto's (2009) opinion stating that the structure of share ownership also has an impact on the company's performance. Nuraeni and Chariri (2010) also agreed that the share

ownership structure has a positive influence on company's performance.

Political supports because of political and governmental elements in companies' management (PS) did not have a significant effect on ROA. This point is aligned with Chang and Wong's (2004) study revealing that political connections provide a greater significance to ROE of 5% and ROI of 5% compared to ROA of 1%. Political support because of the company ownership from governmental elements (PS2) also did not have a significant effect on the companies' ROE. This result refutes Fan's et al. (2007) study result reporting that the companies which have political affiliated CEOs have lower performance compared to those having no political affiliations.

Political support in light of the involvement in companies' management (PS3) also did not have a significant effect on the companies' ROA and ROE. This result aligns with the study undertaken by (Istan, 2018); revealing that there are no relationships among the composition of management, the composition of political connections, and the companies' performance. Entrepreneurs' motivation to enter politics generally aims to improve conditions. There is a positive side if entrepreneurs enter into the political world. With their strong capital, they will certainly be able to finance all parties' interests, so that the parties' political costs no longer rest on the APBN. The initial purpose of entrepreneurs entering into politics is to willingly improve conditions as is often conveyed during campaigns or in debates and dialogues in the media. Indeed, such desires are the ideals of those who have incipiently entered the world of politics, but these ideals may change when they have really been engaged into real conditions.

Political activities in Indonesia cannot be separated from the games of money and power. To get power, not a few of Indonesians use money so what they do after gaining power is hoping to get even more money. From that more money, he will also "buy more power". So, the formula is that M (money) will get power P (power), then from P, MM (more money) will be

got. Furthermore, from MM, MP (more power) will be got, and so on.

The cases as regards the entrepreneurs who break through authorities due to either closeness, collusion, or multiple roles, actually have since been addressed in political economy studies. The theory concerning this issue is commonly known as theory of economic rent-seeking. The theory explains the phenomenon of entrepreneurial behaviour to obtain special licenses, monopolies, and other facilities from the authorities who have power over the field. Armed with a special license, the other parties cannot enter the market. The behaviour of economic rent-seeking is usually anti-competitive or avoiding competition.

Hence, the supports given by politicians to companies do not significantly affect the companies' performance because the entrepreneurs with business-related background, when running the companies' operations and power, do not solely seek rent, but in accordance with their initial goal which is willingly improving conditions with their authorities. Then, political supports are also not the only determinant of companies' performance. Companies' performance is also influenced by many factors falling into both financial and non-financial factors such as capital structure, companies' size, growth, ownership, and economic conditions in a certain period. Future studies will be more interesting if they can integrate financial and non-financial factors.

Political supports (PS1, PS2, and PS3) have no significant impacts on financial distress (FD). The conclusion is that either the political support due to share ownership, the political support because of government elements, or the political support from management does not show a significant effect on the companies. This result is in line with the study conducted by Narayanaswamy (2013) stating that politically connected companies have lower income than those having no political connections. This result also refutes Whitaker (1999) opinion stating that in a stable and normal condition, if there are companies experiencing financial distress, it is a result of management weaknesses. Likewise,

Wijantini's (2007) opinion is refuted from this study result showing that the companies experiencing financial difficulties benefit from political support. Kamaludin and Pribadi (2011) also stated that the Return on Equity (ROE) of a company significantly influences the prediction of a company's financial distress.

The result of this study is also contrary to Hastuti (2014) study finding out that the managerial ownership affects financial distress. Whitaker (1999) also found that most companies experience financial distress as a result of management weaknesses. From the results of this study, stock ownership, governmental involvement, and the companies' management have no effects on financial distress. The political support due to the share ownership in companies (PS1), the political support due to the ownership of companies from government elements (PS2), and the political support because of the involvement in company management (PS3) contribute 0.9% to financial distress (FD), while the other 91.9% is influenced by other factors. Other factors can be caused by the capital structure of DAR and DER (Riyanto, 2010). The politicians' involvement in companies still applies the precautionary principle and consideration of rationality in making decisions. Investment decisions, funding decisions and other decisions made by the companies pay attention to investment risk considerations, possibly not imposing political will and desire.

CONCLUSION

Grounded in the data analysis results resting upon the two research questions, it can be concluded that the political support of share ownership (PS1), the presence of political elements both exclusive, TNI/POLRI elements, and leaders of political parties (PS2), and the involvement of political elements in companies' management (PS3) have no significant effects on companies' performance in terms of the companies' return on assets (ROA) and return on equity (ROE). Political supports (PS1, PS2, and PS3) do not have significant effects on Financial Distress (FD). This condition shows that political

supports due to share ownership, governmental elements, and the involvement in management do not significantly influence the companies' financial distress (FD).

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