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UNVEILING THE IMPACT OF POLITICAL CONNECTIONS ON CASH FLOW IN INDONESIAN FIRMS

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Abstract:

One of the critical resources in business, particularly in Indonesia, is political connections. Political power and corporate entities have a mutualistic symbiotic relationship encapsulated in a particular political cost transaction model. There is an inevitable consequence in the form of financial resource sacrifices to establish and preserve that relationship. According to current standards, cash flow reporting cannot satisfactorily account for this outcome. This study aims to test the premise that political connections positively impact aberrant cash outflow by detecting expenditures that do not fall under the purview of regular corporate operations. Eighty-nine organizations listed on the IDX have their financial reports for the years 2016 through 2020, and this research uses panel data from those reports to do a linear regression analysis. According to this research, a company's extracurricular spending is positively impacted by its political connections, even in finance.

Keywords:

Cash Outflow, RBV, Political Connection

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Introduction

Cash as a medium of exchange occupies a very vital position in the business activities of a company entity. The management and performance of a company's cash, as reflected in cash flow statements (investment, financing, and operating activities), will heavily depend on the availability of cash resources. Cash is paramount as a strategic resource within the company (Bates, Kahle, & Stulz, 2009; Faulkender et al., 2006; Jensen, 1986). Cash not only serves as liquidity but also as a tool that provides flexibility in decision-making manages risk, and supports investments that contribute to the success and long-term growth of the company (Bates et al., 2009; Chen et al., 2020; Dittmar & Mahrt-Smith, 2007; Guo, 2018). Effective cash management ensures a company can survive and thrive in a dynamic business environment. With its inherent flexibility, cash is a versatile tool in business strategy. Its easily transferable nature and usability for mobilization or transactions make it a strategic instrument in developing a company's business strategy, including in building or maintaining political relationships with those in power.

Literature documents that political connections are a valuable resource for a company and influence the determination of the company's strategic choices (Goldman, Rocholl, & So, 2009; Wu, et al., 2018 and Kim & Lee 2021) Political connections are considered valuable because they can provide benefits, such as preferential access to credit (Wu, et al., 2012), preferences in obtaining government assistance during financial difficulties (Faccio, Masulis, & Mcconnell, 2006; Tsai, Zhang, & Zhao, 2019), opportunities for access to legislation, and reducing market pressure for public transparency (Kim & Zhang, 2016), a high tendency to receive financial assistance/corporate bailouts (Elkaria, Mahanani, & Sidik, 2024; Faccio, 2006), preferences in obtaining import licenses, and even the possibility of leniency in tax audits, as well as reductions in tax penalties (Ghifary & Lastati, 2024; Mobarak & Purbasari, 2005; Wicaksono, 2017). Political connections provide advantages to companies by offering more significant opportunities to strengthen the bargaining power of directors and commissioners in influencing regulations and tax policies, including advantages in legal risk mitigation against potential risks.

This research views that both factors can apply to companies with effective political connections, namely companies that actively engage in political support activities through various contributions (donations) to political parties and lobbying legislative bodies. The political relationships of companies built and maintained through lobbying activities, which incur significant expenditures, along with contributions or donations to campaigns in the years following elections, reveal extensive impacts and implications for the companies.

Political connections often occur in developing countries with weak property rights protection, including Indonesia (Fisman, 2001). In Indonesia, political connections have become a common practice. Generally, it involves placing individuals with close ties to the government within the company's organizational structure, whether as commissioners or directors.

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common practice. Generally, it involves placing individuals with close ties to the government within the company's organizational structure, whether as commissioners or directors. This often occurs in private companies affiliated with the parties that support the regime. The appointment of several commissioners of state-owned enterprises with political connections to the government has been evident since the presidency of Susilo Bambang Yudhoyono, which lasted from 2004 to 2014. This tendency has also become increasingly pronounced during the administration of President Joko Widodo, with the appointment of commissioners from supporting companies, especially in state-owned enterprises (SOEs) that come from political parties or volunteers to hold positions as commissioners in SOEs. This indicates that political connections are standard within the organizational structure of state-owned enterprises in Indonesia.

So far, many studies and research have examined the influence and impact of political connections on policies, actions, and corporate performance. However, there still needs to be more evidence that provides insight into how the patterns and the extent of cash resource sacrifices made by politically connected companies are revealed. Therefore, this study further investigates the cash resource expenditures in the company's cash flow statement, including standard business activities for investments, financing, and operational expenditures.

About the hypothesis of this research, the researcher proposes the measurement of abnormal cash outflow. This measure was developed based on the consideration that sacrificing economic resources for developing and maintaining political connections is separate from the company's normal business activities. Therefore, the company's expenditures to support this activity will create an abnormal spending pattern. Political activities do not always occur with the same intensity over time. Corporate spending based on political connections is likely to increase in line with the political cycle (general elections and regional elections) that takes place. The fluctuating intensity can create abnormal patterns in the company's expenditures.

This study provides essential benefits and contributions to the literature. First, the effort to prove the direct relationship between the existence of political connections and the company's cash flow activities, including identifying how the pattern of abnormal cash outflow occurs. Furthermore, this study proves that direct relationships can encourage further analysis of various management performance, market performance, and the company's policies and strategies.

Literature Review and Hypotheses Development

Transaction Cost Politics

The transaction cost theory was first introduced by Ronald Coase in 1937 and later further developed by Oliver E. Williamson. (Bylund, 2014). This theory explains that transaction costs arise from the need to create, manage, and enforce contracts under conditions of uncertainty and imperfect information. In a political context, transaction costs include the efforts expended by companies to influence policies and regulations for their own benefit. These efforts can range from lobbying activities to legal costs incurred in challenging or complying with regulations.

The basic assumption in transaction-cost politics is very similar to transaction-cost economics. The main difference lies in the nature of the contracts of the two types of transactions and their

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completeness. Political contracts tend to be incomplete compared to economic contracts. There is uncertainty regarding the fulfillment of a political contract. In other words, there is only sometimes a guarantee that the sacrifices made by political actors will yield benefits as initially hoped by the contract.

On the other hand, political actors have limitations in assessing and considering future conditions. The bounded rationality experienced by actors in political contracts is greater than that of the parties involved in economic contracts. The agency relationship patterns in political contracts are more complex compared to those in economic contracts. Agency costs, as explained in agency theory(Jensen, 1986), are not the main concern in the explanation of transaction-cost politics. However, it's important to note that bonding costs, which are the costs associated with creating trust between the principal and the agent, and monitoring costs, which are the costs of overseeing the actions of the agent, do not represent effective mechanisms for controlling agency problems among the actors involved in the contract.

Political contracts have a different nature from economic contracts. Uncertainty is an inherent characteristic of that political contract. The benefits expected from each sacrifice made to carry out a political contract are only sometimes attainable. The main implication of the transaction-cost politics approach is maximizing economic benefits at every political transaction cost in each political process and decision, aimed at fulfilling political interests rather than the interests of efficient economic activities.

Economic inefficiency in policies and political decisions occurs when economic benefits shift from the public interest to the interests of certain political groups. Favoritism in economic regulation is a phenomenon that is likely to occur as an implication of maximizing political transaction costs. The sacrifice of economic resources for political interests requires compensation. Legislative arrangements and the structuring of public administration that favor the interests of certain political groups can serve as a means for that compensation.

Resource-Based View

Referring to the Resource-Based Theory by Barney and Clark (2007), the concept of Resource-Based View (RBV) in the discipline of strategic management was first introduced by Wernefelt (1984) as a strategically valuable resource(Barney & Clark, 2007). The RBV study was further developed and popularized by Barney (1986, 1991, 1997), viewing organizations as a collection of resources. (bundles of resources). The development of further studies is primarily oriented toward answering questions about how organizations can look inside for competitive advantage, why firms are different, and how firms achieve and sustain competitive advantage. The concept creates an organization's dependence on optimizing its resources compared to its competitors. An organization is considered successful and capable of maintaining its existence if it possesses unique resources that surpass its competitors.

The discussion of political connections from the perspective of the RBV can be based on the assumption that such capabilities are one of the resources. Political connections are a form of resource with characteristics outlined in Barney's initial formulation (1991) regarding the resource-based view. The explanation of the resource-based view tends to assume that organizations operate implicitly in a stable environment. The ability to exploit attributes into competitive resources tends to overlook the assumption that under high uncertainty, these resources may not always provide maximum returns.

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Exploitation's role in forming these resources implicitly assumes the importance of active actions that require the sacrifice of economic resources and the ability to carry out those actions. Besides providing benefits such as the formation of superior resources, that sacrifice can also lead to unfavorable impact. The explanation of the impact of that sacrifice is not sufficiently detailed in Barney's initial formulation of the resource-based view (Barney & Arikan, 2005).

Political Connections

The research on political connections in the interplay between business and politics, a field that has seen significant development over the past two decades, holds immense significance in economics and business studies. Trinugroho's (2017) work, which builds on Schaffer's (1995) concept of categorizing political influence in business into 'micro' and 'macro' levels, is a testament to this. The micro level, often synonymous with the corporate or organizational entity level, is the primary focus of researchers in management, business, and finance. On the other hand, macro-level analysis, which encompasses communities, industries, social classes, and society, is predominantly utilized in political science, public economics, sociology, and related fields.

Political connections are a widespread phenomenon in developing countries, and the effects of their transitions have attracted significant research interest. A company is defined as having political connections if its chairman (CEO) is currently serving or is a former government official (Wu et al., 2012). According to Faccio (2006) an organization is considered to have political connections if at least one of its executives, majority owners, or their kin has held or is presently holding a senior position in the government, is a minister, a member of parliament, or has a close relationship with political figures or parties. Adhikari et al. (2006) added that direct ownership by the government can be seen as a political connection. Thus, political connection can be understood as the close relationship between companies/corporations and the government.

The company's pursuit of political connections has piqued the interest of economic observers due to the potential benefits, such as preferential treatment from the government. This can include expedited bureaucratic processes, access to government contracts, and immunity from specific regulations. (Faccio, 2006, Kim & Lee, 2021)). Companies with political connections can also receive protection from the government, have easy access to capital loans, and face a low risk of tax audits, leading to aggressive tax planning and a lack of financial transparency. Even during a financial crisis, these companies can quickly receive bailout funds from the government (Kim & Zhang, 2016; Rudyanto, Julisar, & Debora, 2023).

Political connections, often considered a valuable resource for many companies (Fisman, 2001), significantly influence the economic performance of both private and state-owned enterprises, be it positive or negative (Adela, Agyei, & Peprah, 2023; Li, Meng, Wang, & Zhou, 2008). The prevalence of political connections in a company is a standard feature in countries with high levels of corruption, transparent systems, and restrictions on foreign investment by residents. Conversely, political connections are less common in countries with regulations that impose stricter limits on political conflicts of interest (Faccio et al., 2006; Ngo & Susnjara, 2020).

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Defining a company as having political connections involves several criteria. A company is said to have political connections if its board of directors and commissioners hold dual positions as politicians affiliated with political parties, government officials, or military officials. Similarly, if the board of directors and commissioners consists of former government or military officials, or if the owners of the company or shareholders are politicians, government officials, or military officials, the company is considered to have political connections (Blau, et all (2022); Vukovic, 2021).

Cash Flow

An essential element of financial reporting objectives is "to assess the amount, timing, and uncertainty of cash flows." (Kieso, Weygandt, & Warfield, 2020). The three formats of financial reports that have developed so far, namely the income statement, statement of changes in equity, and statement of financial position, all present some information about the cash flow of a corporate entity over a period. However, these three reports do not provide a detailed summary of cash inflows and outflows, including the sources of cash acquisition and the specific purposes for which the cash managed by the company is used. Therefore, for this purpose, the statement of cash flows is of utmost importance in financial reporting, as it covers information on cash flows from investing activities, financing activities, and operating activities as a representation of normal business activities.

Hypothesis Development

Political connections are not just incidental relationships, but strategic alliances built on the motivation of business entities to defend business interests. These relationships, forged with political powers in the legislature and to a particular political party, are leveraged by business entities to gain advantages and strengthen their bargaining position in legal and administrative processes within the business.

The relationship between political power and business entities is not one-sided, but a mutualistic symbiosis. In this pattern, both parties benefit from each other. The advantages gained by an entity require sacrificing the economic resources the related political institution needs, creating a fair exchange. Businesses serve as providers of economic resources, while political parties rely on government funding and member contributions and open themselves up to donations from the public. This mutual benefit reassures the fairness of the system.

What and how do companies engage in political activities to build political connections, such as contributing to political campaigns, political action committees, having directors and commissioners with political connections, and various lobbying actions (Kelleher Richter, Samphantharak, & Timmons, 1988; Kim & Zhang, 2016; Kim & Lee, 2021; Meade & Li, 2015), even in illicit forms such as gratification or bribery (Rajwani & Liedong, 2015). The literature review findings by Khelil, Khlif, and Amara (Khelil, Khlif, & Amara, 2022) reveal that an increase in political connections tends to result in favorable opinion outcomes (opinion delays and an increase in going concern opinions) with higher audit costs. Tang (2020) provides evidence that private companies, small businesses, state-owned enterprises (SOEs) with weak political connections, and companies in competitive industries spend more on entertainment and travel expenses to bribe tax officials to reduce their tax burden. This implies that these companies have a more vital need to build political connections to eliminate bureaucratic obstacles and gain a competitive advantage.

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At this stage, cash resources become not just important, but vital in building and supporting the strength of political connections. Cash funding plays a crucial role in establishing and developing political relationships because of its high mobility, easy transferability, and versatility in use for various activities. The urgency and significance of this aspect are clear.
This research suggests that companies or corporations involved in a political connection will sacrifice cash resources to gain benefits from that relationship. However, significant cash expenditures can impact the potential for political scandal if disclosed in financial reports as political contributions. Considering the regulations regarding the limitations on the amount of donations from private entities, as well as the potential for negative sentiment and differing interpretations from stakeholders and the general public regarding the disclosure of such political activities, business entities may report these expenditures within a specific cash flow scheme in the company's business activities. (investasi, pendanaan, dan operasional).

The disclosure of such activities requires techniques that do not directly and openly reveal the political activities of the company or corporation. Considering that expenditures for political activities are not a regular business activity, this will have implications for an abnormal cash outflow pattern, which refers to cash expenditures that are significantly higher than the norm. This study suspects it will lead to abnormal cash expenditures across all these activities. Based on the description, this study proposes the hypothesis: Political connections positively influence abnormal cash outflow.

Research Methodology

Populasi dan Data Sampel

The population of this research consists of companies listed on the Indonesia Stock Exchange (IDX) that published financial statements for the fiscal years 2016-2020. Ideally, this study should be conducted for an observation period up to 2023. However, there are differences in the structure of the independent variable data (political connection) available from 2021 to 2023. Therefore, the selection of the years 2016-2020 is not only for the measurement and analysis of the indicators of the involved variables but also for the consistency of relevant data for analysis in this study.

The following criterion is to select corporate entities detected to have political connections within the board of directors and the board of commissioners. Next is to measure the index of tax avoidance activity in each observation unit using the following criteria:

1. All manufacturing companies listed on the Indonesia Stock Exchange that consistently and thoroughly publish audited financial statements from 2016 to 2020.
2. The company is not among those delisted; it conducted an IPO from 2016 to 2020.
3. The financial reporting period ends on December 31.
4. The company's financial statements are not issued in foreign currency.
5. Having complete financial report documents, namely audited financial statements and the company's annual report, that are published and accessible to the public.

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Variables

Independent Variable – Political Connection

This variable refers to the relationship between business entities and political actors, whether they are members of the legislature or members of a political party. The measurement of political connections, a meticulously designed method, is based on the number of board of directors and board of commissioners identified as having political ties either with political parties or within legislative bodies.

Weighting is done to differentiate the potential strength of each political relationship. The president's commissioner detected to have political connections is assigned a weight of 2. Meanwhile, board members who are found to have political ties are given a weight of 1. The heavier weighting for the president and commissioner is based on considering their higher authority in cash expenditure decisions.

Dependent Variable – Abnomal Cash Outflow

The component of cash expenditures known as the "abnormal cash outflow" cannot be explained by the factors that determine the operations, investments, and financing of a normal business activities. The following formula will be used to calculate the abnormal cash outflow variable:

$$\frac{COF_t}{Asset_{\ t-1}} = \propto + \beta 1 \frac{1}{Asset_{t-1}} + \beta 2 \frac{COGS}{Asset_{t-1}} + \beta 3 \frac{Liability}{Asset_{t-1}} + \varepsilon_1$$

Remark

COF	:	*Cash Outflow*
1/Asset	:	Size
COGS	:	*Cost of goods sold*
Liability	:	Liabilities
t	:	Time indicator of observation year
t_{-1}	:	Time indicator at 1 year before the observation year
α	:	Constanta
$\beta_1 \ldots \beta_3$	:	Regression coefficient
ε_1	:	Epsilon, which is the residual value that represents the presence of abnormal cash outflows

Furthermore, this research employs several control variables to produce more accurate conclusions and a higher percentage of the coefficient of determination. The control variables selected in this study are company size, debt level, and profitability, which are proxied by return on assets. (ROA).

Data Analytic

First, we will conduct a descriptive statistical analysis, a crucial step to gain a comprehensive understanding of the data. This analysis will involve measures of central tendency, such as mode, median, and mean, which are crucial to understanding the typical values in our data. Additionally, we will explore measures of dispersion, particularly the standard deviation, to understand the spread of our data.

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Next, the data analysis method used to test the influence of political connections on the indication of abnormal cash outflow is panel data regression analysis. For this purpose, the following panel data regression model is used:

$$Abn\_COF_{it} = \alpha_1 + \beta_1 PC_{it} + \beta_2 Ctrl_{Var_1} + . \ldots \ldots + \ \beta_n Ctrl\_Var_{n-1} + \ \varepsilon_{it}$$

Remark:

PC	= Political connection
Abn_COF_{it}	= *Abnormal cash outflow*
α_1, α_2	= *Intercept* / constanta
β_1, β_2,	= *Slop* / coefisien variable
i	= *Cross section*
t	= *Time series*

Gujarati and Porter (2009) provide an approach for estimating model parameters using panel data. The testing was conducted by running three different analysis models: the Pooled OLS/Common Effect model, the Fixed Effect model, and the Random Effect model. The first testing model, the standard effect model, assumes that the intercept of the cross-sectional and time series units is fixed. Second, in the fixed effect model, only the intercept of the cross-sectional unit is assumed to be fixed. Meanwhile, the random effect model assumes that the intercept of the time-series data for each group of cross-sectional items is random.

Data Quality Testing

Regression analysis requires data to be normally distributed. The normality test is conducted by performing the Durbin-Watson Test, which involves calculating the Durbin-Watson statistic and comparing it to the critical values. Data is normally distributed if the asymp sig residual value is greater than 0.05. The heteroscedasticity test is aimed at proving whether there is a variance inequality. A good model is one that meets the assumption of homoscedasticity among variables. The test for heteroscedasticity is conducted using the Glejser test procedure by performing i) regression analysis and ii) using the natural logarithm of the squared residuals or $Ln(\varepsilon 1)^2$ as the dependent variable. The symptoms of heteroscedasticity occur in variables with a regression coefficient ≠ of 0 or a significance level < 0.05..

Result and Discussion

Data and Sample

The companies selected as samples for this research are 89 companies spread across 22 subsectors from 7 main sectors. The entire sample is distributed across three industries: the infrastructure industry, the property industry, and the general industry. With a 5-year observation period, the number of observations (n) ready for processing is 445.

Descriptive statistics are used to explain the characteristics of the research variables employed. As shown in Table 1.

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Table 1: Descriptive Statistics

Variables	Min.	Max.	Mean	Median	Std. Deviasi
PC	0	7	1,03146	0,00000	1,42970
Abn_COF	-18,03270	56,31164	0,08605	74,34430	3,33346
Ln_Asset	21,90806	33,25569	29,82631	29,86104	1,61826
ROI	-2,02970	0,67500	0,05021	0,05110	0,17217
DER	-26,03450	55,58333	1,33212	0,75228	4,13819

Source : processed data for this study

The political connection variable (PC), which measures the degree of political influence on a company's operations, has an average value of 1.03146, with a minimum value of zero and a maximum value of 7. Meanwhile, the abnormal cash out-flow variable (Abn_COF), which indicates unexpected cash outflows, has an average value of 0.08605, with a minimum value of -18.03270 and a maximum value of 56.31164, with a median value of 74.34430.

Regression Analysis

This research conducts an analysis of the regression equation of panel data to test the hypothesis, namely:

$$Abn\_COF_{it} = \alpha_1 + \beta_1 PC_{it} + \beta_2 Ctrl_{Var_1} + . \dots \dots + \ \beta_n Ctrl\_Var_{n-1} + \ \varepsilon_{it}$$

Abnormal Cash Outflow is symbolized by Abn_COF, derived from the function of abnormal Cash outflow, while PC represents political connections proxied by the natural logarithm of PC. While α_1 is constanta, β_1 is the regression coefficient, then dan ε_1 is residual.

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Table 2: Regression Analysis of Equations -*Transformed Model*

Keterangan		Common Effect		Fixed Effect		Random Effect	
		Abn_COF	**Res_1_Sqr**	**Abn_COF**	**Res_2_Srq**	**Abn_COF**	**Res_3_Sqr**
Const	Coefficient	-0,188402	-8,46829	-0,146529		-0,181402	
	Std. Error	0,492866	21,5093	0,557649		0,500267	
	t-ratio	-0,3823	-0,3937	-0,2628		-0,3626	
	p-value	0,7025	0,6940	0,7929		0,7169	
PC	Coefficient	0,289492	14,2243	0,188163		**0,272443**	
	Std. Error	0,125294	5,46799	0,155026		0,126955	
	t-ratio	2,310	2,601	1,214		2,146	
	p-value	0,0214	**0,0096**	**0,2558**		**0,0319****	
Ln_Asset	Coefficient	-0,00135935	0,263951	0,00199471		-0,00115061	
	Std. Error	0,018070	0,788597	0,0203341		0,0180242	
	t-ratio	-0,07523	0,3347	0,09810		-0,06384	
	p-value	0,9401	**0,7380**	**0,92190**		**0,9491**	
ROI	Coefficient	0,0289847	-3,26959	0,28981		0,0513239	
	Std. Error	0,998855	43,5913	1,28989		1,02103	
	t-ratio	0,02902	-0,7501	0,2247		0,05027	
	p-value	0,9769	**0,94020**	**0,8224**		**0,9599**	
DER	Coefficient	-0,0105593	-0,102079	-0,0427031		-0,0149154	
	Std. Error	0,022981	1,00292	0,0248292		0,0227376	
	t-ratio	-0,45950	-0,1018	-1,720		-0,656	
	p-value	0,64610	**0,91900**	**0,0865**		**0,51128**	

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Keterangan	**Common Effect**		**Fixed Effect**		**Random Effect**	
	Abn_COF	**Res_1_Sqr**	**Abn_COF**	**Res_2_Srq**	**Abn_COF**	**Res_3_Sqr**
Mean dependent var	0,066176		0,066176		0,066176	
Sum squared resid	4831,796		3400,798		4832,534	
R-squared	0,014002					
LSDV R-squared			0,30602			
F(3, 439)	1,377518					
LSDV F(91, 351)			1,437924			
Log-likelihood	-1050,694		-981,6806		-1050,724	
Schwarz criterion	2131,256		2518,926		2131,316	
rho	0,177005		-0,157054		-0,157054	
S.D. dependent var	3,535683		3,535683		3,535683	
S.E. of regression	3,528892		3,366892		3,524623	
Adjusted R-squared	0,003837		0,014591			
P-value(F)	0,241018		0,012282			
Akaike criterion	2111,387		2149,361		2111,447	
Hannan-Quinn	2119,261		2295,815		2119,321	
Durbin-Watson	1,371603		1,92427		1,92427	
N	445		445		445	

Source : processed data for this study

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Normality Test

The normality test of this research produced a Jarque-Bera value with a p-value of 0.000, indicating that the residuals are not normally distributed. However, it's important to note that this study uses a relatively large sample size, exceeding 100 samples. This means that even though the residuals are not normally distributed, the OLS estimator can still be considered unbiased, providing a reliable basis for our analysis (Gujarati & Porter, 2009).

The normality test for panel data does not become the primary determinant of obtaining the analysis. This is due to the significant influence of the characteristics of panel data, which consists of cross-section and time-series data. These characteristics make the data distribution susceptible to outliers and sharp differences between those outlier values and the average. The varying cross-section characteristics, such as differences in company sizes, play a crucial role in leading to a wide range of variable values (min-max). Thus, with such a broad range of values, it is very likely that outlier values (both min and max) will emerge, causing the data distribution to deviate from the assumption of normality.

Heteroskedasticity Test

This research detects the presence of heteroscedasticity symptoms through the Glesjer test. The regression analysis of the equation model shows that there is a heteroscedasticity phenomenon in the standard effect model. Thus, it is not chosen for hypothesis testing. The symptoms of the test are reflected in the p_value of the effect of political connection (PC) on Residual_12, which is 0.0096. (significant pada 0,01). Similarly, in the Fixed Effect model, there is no need to conduct a heteroskedasticity test, as no independent variables have a significant effect. Therefore, it is not used for hypothesis testing.

The Generalized Least Squares (GLS) model (Random Effect) was developed to eliminate the phenomenon of heteroskedasticity, so there is no need to conduct a heteroskedasticity test on that model (Gujarati, 2008). The hypothesis testing in this study uses the Random Effect model or GLS. Thus, the hypothesis testing based on the equations of this research model employs the Random Effect Model. The analysis results show that PC positively and significantly affects Abn_COF with a regression coefficient of 0.272443 and is significant at the 5% alpha level. (p-value: 0,0319).

Hypothesis Testing

As demonstrated in the test results in Table 2, this study's analysis confirms the significant influence of political connections on Abn_COF, with a β value of 0.23347 and a p-value of 0.0379, below the significance level of $\alpha = 0.05$. These results, which support the hypothesis, suggest a strong and positive effect of political connections on abnormal cash outflow. The implications of these findings are profound, indicating that as political activity increases, so does abnormal cash outflow, which are expenditures caused by factors other than the company's everyday activities.

Result and Discussion

This research hypothesis states that political connections positively influence abnormal cash outflow. This hypothesis is based on the view that companies/corporations involved in political connections are likely to sacrifice cash resources in order to gain benefits from those relationships. The revelation of such activities requires disclosure techniques that cannot all be direct and open as political activities. In addition to the existence of regulations that impose

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limitations, expenditures for political activities are often outside the normal business activities of a corporate entity, which will consequently lead to an abnormal cash outflow pattern, as proposed in this study.

This research can provide analytical support as a justification for studies that reject the conventional view of how political connections influence cash-holding policies by management, such as those of Boubakri et al.,(2013) and Sehyun Park (Park, 2022)). Conventional wisdom suggests that companies with political connections should not need to hold large amounts of cash, either for precautionary reasons or transaction costs, arguing that they have easy access to credit at preferential rates and are even more likely to be bailed out in times of crisis. Boubakri et al. (2013) and Tawfik et al. (2024), through their thesis, argue that companies with political connections tend to hoard cash to finance their political agendas through various legal and illegal activities. Also, because they reduce political extraction, these companies are more likely to hold onto liquidity than their politically unconnected counterparts. In turn, the agency problem tends to be more acute in politically connected companies due to the differing agendas of managers or the board of directors and shareholders, which increases the likelihood of higher cash holdings.

In line with this, Park, (2024) andSehyun Park (2022) argues against the conventional wisdom that companies in more corrupt environments hold less cash to protect their liquid assets from political extraction. Instead, Park finds that corruption reduces corporate cash holdings due to its adverse impact on financial development. Furthermore, Park discovers that companies in more corrupt countries suffer from more severe financial constraints and hold cash beyond their optimal levels.

This research proves the validity of the RBV theory explained by transaction cost politics as a support for the RBV theory that resource creation requires sacrifice. The RBV explanation focuses on strategy development based on resources to form competitive strategies. Therefore, the RBV does not sufficiently describe that competitive resources have different characteristics, meaning that the advantage may lie in fundamental economic and business strengths or the advantage may be found in other aspects, including political relationship advantages.

While the superiority of resources lies in the fundamental economic aspects of a company's business entity (such as innovation, technology, market dominance, cost leadership, differentiation, and so on), the form of the strategy implemented will differ from advantages in the non-fundamental economic and business scope, such as advantages derived from political connections. Therefore, the explanation regarding RBV as a whole is supported by the discussion of hypotheses, where this research demonstrates that the resource creation process influences the actions of the company/corporation.

Conclusion

In conclusion, this research affirms the hypothesis that political connections positively influence abnormal cash outflow, as politically connected companies often redirect cash resources to sustain and benefit from these relationships. Unlike traditional business expenditures, political-related expenditures frequently fall outside a company’s typical operations and are often less transparent due to regulatory constraints, resulting in irregular cash outflow patterns. This study makes important contributions to the understanding of

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political connections, corporate cash-holding policies, and the Resource-Based View (RBV) theory:

1. Challenging Conventional Wisdom : The research challenges the traditional view that politically connected companies hold less cash due to easier access to credit and bailouts. Instead, it suggests that such firms may experience abnormal cash outflows to sustain their political relationships. This perspective offers an alternative explanation for cash management in politically connected companies, building on the findings of Park, (2024) and Tawfik et al., (2024) who show ed that political ties can lead to increased cash reserves or outflows for political activities.

2. Expanding the RBV Framework: The study broadens the scope of RBV theory by showing that resource advantages are not only derived from economic factors but also from political connections. It presents evidence that resources linked to political relationships can result in abnormal financial behaviors, such as higher cash outflows, highlighting that competitive advantages may come from politically motivated strategies rather than purely economic strengths.

3. Corporate Strategy Insights: By investigating the relationship between political connections and abnormal cash outflows, the research offers insights into how politically connected firms manage resources. It enhances the understanding of how corporate strategies may be influenced by political factors rather than just market-driven forces, providing a more comprehensive view of corporate financial decisions.

4. Agency Problems in Politically Connected Firms : The study also points to agency issues within politically connected companies, where the goals of managers or directors might conflict with those of shareholders. This adds to existing research on governance, suggesting that political connections can worsen agency problems due to differing internal priorities.The business background of politically involved entrepreneurs can serve as a crucial support for their business activities, often becoming a specific advantage as a resource for the company/corporation entity.

This phenomenon has prompted an investigation into the relationship between political connections and the sacrifice of cash resources beyond financing the normal business activities of a company. For further studies could investigate how changes in political regimes, policies, or governance structures affect the cash management strategies of politically connected firms. This would offer a dynamic view of how firms adjust their financial strategies in response to shifting political landscapes.

Research Implications

First, regarding the implications of transaction cost-political theory, which explains that every contract will incur sacrifices. Political connections as a resource are built through contracts. Therefore, political connections also have the potential to require the sacrifice of cash resources. Companies may be driven by further motivation because, in transaction cost-political contracts, there is always uncertainty about the outcomes that will be achieved in the future. Secondly, the Resource-Based View theory can provide a deeper explanation of how resources can give a strategic advantage to companies. This research views political connections as a resource from the perspective of the resource-based view. Politically

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connected companies have various preferences and certain conveniences through their lobbying ability. However, the resource-based view does not provide sufficient explanation regarding the role of the existence of a company's strategic resources (including cash) that triggers motivation for more aggressive and risky decision-making and actions. This research views that transaction cost-political theory can complement the resource-based view in explaining the pattern of that relationship.

Finally, the results of this research offer significant practical contributions to the company's management, investors, and the government. For investors, the research findings provide valuable insights into companies with political connectivity, which tend to exhibit abnormal patterns of cash resource expenditure. For the government, particularly financial authorities, this research serves as a crucial input for understanding and regulating business behavior, including tax obligations and industry regulations. The findings can guide the enforcement of tax laws, especially in situations involving conflicts of interest from parties in political power.

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