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Political power, economic freedom and Congress: Effects on bank performance [☆]

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Abstract

This paper studies the linkages between bank performance, connections to powerful politicians, and the degree of economic freedom in a bank's home state. We find that bank performance is positively related to state economic freedom. We also reconfirm the finding of Gropper et al. (2013) that bank performance is improved by political connections. However, the positive effect of political connections appears to be significantly reduced when there is a higher degree of economic freedom in the state, indicating that political connections may matter less to banks when there is more economic freedom. Economic freedom in a state can have a beneficial effect on state economic growth and hence may outweigh any political connection benefits. However, the declines in state economic freedom in recent years could make political connections potentially more valuable to banks.

JEL classification

G21; G18

Keywords

Political effects; Government regulation; Economic freedom; Bank performance

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