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Abstract

This study examines the relationship between firms' political connections and their confidence in achieving enhanced future sales. Using firm-level survey data from selected Middle Eastern and North African (MENA) countries, we apply ordered probit regressions to demonstrate that businesses with board members who have political experience in government show increased confidence in anticipating improved sales. This positive association remains robust even after controlling for various determinants of managers' sentiment. Quantitatively, our results indicate that having a politician on the board increases the predicted probability of a positive change in firm sales expectations by approximately 10 percentage points, while also reducing the predicted probability of no change or a decrease in sales expectations. Furthermore, we identify that membership in business associations serves as an important mediator, facilitating access to information, markets, credit, and lobbying opportunities. The findings also highlight the significance of a well-defined business strategy and firm size as key factors mediating the relationship between firms' political connections and their confidence in future sales.

Keywords: Business confidence; Middle East; Political connection; Sentiment; Survey Data

1. Introduction

In broad terms, a firm is considered politically connected "if one of its large shareholders or top officers is a member of parliament, a minister, or is closely related to a top politician or party" (Faccio, 2006, p.384). Political connections offer several advantages for firms such as receiving preferential access to credit, preferential treatment from the government, enjoying lighter tax burdens, gaining an edge in competing for government contracts, experiencing more lenient regulatory oversight for the firm itself, and potentially creating stricter regulatory scrutiny for its competitors (Faccio, 2006; Faccio, 2010).

The majority of studies exploring the impact of political connections on firm performance indicate that these affiliations tend to have positive impacts on various financial performance indicators (e.g., Akcigit et al., 2023; Amore & Bennedsen, 2013; Burt & Opper, 2020; Dang et al., 2018; Diwan et al., 2015; Fisman, 2001; Li et al., 2006). This positive effect holds true if the advantages gained from the political connection outweigh the associated costs, such as potential rent extraction by politicians from the businesses they oversee.

Beyond financial performance, extensive literature examines the impact of political connections on various facets of firms' activities and behavior. This includes innovation (e.g., Akcigit et al., 2023; Krammer & Jiménez, 2020; Ren et al., 2022), environmental activities (e.g., Florackis et al., 2023; Long et al., 2024), pollution emissions (Xie et al., 2023), employment (Bartlett, 2023; Diwan et al., 2015; Diwan & Haidar, 2021), labor investment efficiency (Zhou et al., 2023), worker fatalities (Fisman & Wang, 2015), allocation of government contracts (Schoenherr, 2019), firms' cost of debt (e.g., Chkir, 2020), productivity and survival (Akcigit et al., 2023), mergers and acquisitions performance (e.g., Brahma et al., 2023), corporate bailouts (Faccio et al., 2006), firm's future stock price crash risk (Luo et al., 2016), stock returns (Faraji et al., 2020; Goldman et al., 2009), and export performance (Sharma et al., 2020).

In this study, we broaden our understanding of the interplay between political connections and business activities by investigating the relationship between these connections and business sentiment, measured by sales expectations for the upcoming year. Additionally, we aim to identify possible mechanisms, such as memberships in associations, that mediate the relationship by facilitating lobbying efforts and providing access to information, markets, and credit. Using the recent World Bank Enterprise Surveys data collected from the selected Middle East and North Africa (MENA) countries, we find that politically connected firms tend to have more optimistic expectations about their future sales. Our results also identify memberships in associations as key mediators, as they facilitate access to information, markets, credits, and lobbying opportunities.

Our research, investigating the link between political affiliations and a psychological outcome (business confidence in upcoming sales), distinguishes itself from existing studies that predominantly concentrate on the tangible outcomes of politically connected firms, such as profit, capital structure, and innovation. Moreover, the focus of our study is on business sentiment (business optimism/pessimism or business confidence), which can offer crucial insights into future economic activities (e.g., Bartels et al., 1988; Dasgupta & Lahiri, 1993; Khan & Upadhayaya, 2020; OECD, 2024; Taylor & McNabb, 2007) and can also be an important driver of economic growth (Guo & He, 2020), business travels (Gholipour & Foroughi, 2020), and firms' investment (Janada & Teodoru, 2020).

Additionally, the majority of current research on politically connected firms has focused on the Chinese economy, where state-owned enterprises have significant influence. In contrast, there is a scarcity of studies focusing on the MENA countries. In this study, our focus is directed towards the MENA countries, motivated by the accelerating trend of privatizing public assets and the notable presence of politicians on the boards of privatized firms. This presence is indicative of a potential crony capitalist environment, as discussed by Diwan et al. (2019). The scholarly debates about politically connected firms and crony capitalism surged after the Arab

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Spring in 2011. In the context of Morocco, Saadi (2019) demonstrates that connected firms receive political privileges, including preferential access to finance, protection from foreign competition, and discriminatory enforcement of rules and regulations. Diwan and Haidar (2019) use firm-level census data from Lebanon and show that politically connected firms create more jobs than otherwise similar unconnected firms. Their results for Lebanon indicate a reciprocal relationship between firms and politicians, where firms gain regulatory advantages and, in return, partially compensate politicians by hiring some of their supporters. Arouri et al. (2019) analyze the situation in Tunisia during the Ben-Ali government, offering evidence of politically connected firms abusing investment regulations, privatization processes, and engaging in tax evasion. Sabry (2018) examines the formal and informal state-business relationships in Egypt, Tunisia and Morocco and their effects on innovation. Sabry's results indicate that although cronyism and crony-based informal small business regulations may initially seem to provide a functional allocation mechanism that addresses specific institutional deficiencies, it is crucial to recognize that cronyism has a detrimental impact on innovation, ultimately outweighing any potential benefits. Existing debates on the performance of politically connected firms in MENA have yielded varying perspectives, but the literature remains relatively sparse, especially regarding the effects on business sentiments at firm-level and possible channels of effects.

Finally, our study makes a valuable contribution to the literature on the determinants of business confidence. While several studies explore macro determinants such as inflation rates, unemployment rates, current economic activities, institutional instability, monetary policy credibility, economic policy uncertainty, and political uncertainty (e.g., Adekoya & Oliyide, 2021; de Mendonça & Almeida, 2019; Konstantinou & Tagkalakis, 2011; Montes & Nogueira, 2022), there is a gap in the examination of micro drivers of business confidence. To the best of our knowledge, very few studies examine the internal and external characteristics of firms that influence firm owners' and managers' expectations for future sales. In addition to the main

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explanatory variable of interest (political connection), our research explores the role of other factors in shaping these future sale expectations.

The remainder of this article is organized as follows: Section 2 briefly reviews relevant theories, proposes hypotheses, and explains the data and methodology. Section 3 presents the estimation results, and Section 4 concludes the study.

2. Hypothesis, Data and Methodology

Although our study is not closely related to Chen et al. (2010), who worked on financial analysts' earnings forecasts of politically and non-politically connected firms, their theoretical arguments provide clear explanations on the alternative views concerning the role of political connection on the managers'/owners' financial performance forecasts (sale forecast in our study). Chen et al. (2010) note that analysts' earnings forecasts should be more accurate for firms with political connections than for firms without such connections because politicians can use their influence to help connected firms smooth their earnings by transferring political favors when earnings are low, thus making their earnings more predictable. They call this as the "*income-smoothing hypothesis*". Alternatively, they proposed another perspective and call it the "*analyst task difficulty hypothesis*" which argues that analyst earnings forecasts are less accurate for firms with political connections. More specifically, political connections complicate the analyst's task, because political favoritism is usually granted covertly, and often comes in a windfall fashion that distorts the time-series pattern of reported earnings.

In the context of our study, generally the literature indicates that politically connected firms may possess access to insider information, enhancing their ability to steer regulatory challenges, particularly in economies characterized by weak institutional quality, such as those in the MENA region (Sahnoun et al., 2014). This advantageous position may positively influence the business confidence of connected firms. In addition, managers and owners of firms with political connections may have a more optimistic outlook on potential sale growth

opportunities because these firms have better access to favorable regulations, government contracts, subsidies, finance, and networking opportunities. This argument also aligns with the "*helping hand*" theory, which suggests that government intervention such as changing policies to favor specific firms and providing subsidies can enhance firm performance (Brahma et al., 2023).

However, a negative or insignificant relationship between political connections and firms' confidence may also be expected. The benefits of political connections, often arising from political favoritism, tend to be uncertain and irregular, as noted by Chen et al. (2010), and can quickly diminish. Consequently, politically connected firms are aware of the potential for sudden changes in political landscape within MENA countries and may not always anticipate a positive change in their future sales. In addition, managers and owners of politically connected firms in most MENA countries may be pessimistic about their future sales if they perceive their connections to unpopular ruling governments as corrupt or unfair.

Given that most of previous studies support a positive link between political connections and the sentiment of firm managers and owners, we hypothesize that:

Hypothesis: The managers and owners of politically connected firms tend to have higher levels of confidence in the development of their future sales, *ceteris paribus*.

2.1. Data

Firm-level data for nine MENA countries are obtained from the latest Enterprise Surveys of the World Bank (2024). The sample MENA countries which have data for variables of interest are Egypt, Iraq, Jordan, Lebanon, Malta, Morocco, Palestine (West Bank and Gaza), Saudi Arabia, and Tunisia. Data for Saudi Arabia and Iraq were collected in 2022, data for Tunisia and Egypt were collected in 2020 and the rest in 2019. Our data set is cross-sectional but not longitudinal.

The survey asked a wide range of questions from respondents (who are firm representatives) about the firms' general information, sales and supplies, management practices, market competition, production capacity, financing and obstacles[1].

Dependent variable: Business confidence in future sales

The dependent variable of this study is firm managers'/owners' expectation about the next year sales. In the Enterprise Surveys, respondents were asked to indicate "Considering the next year, are this establishment's total sales expected to increase, decrease, or stay the same?" The possible options are Increase, Decrease, Stay the same, and Don't know (Spontaneous). For regression analyses, we assign 1 to "Increase", 0 to "Stay the same" and -1 to "Decrease" and remove those cases who responded as Don't know or did not answer this question. In the overall sample of 5,658 firms, 49% expect an increase in the firm's sales, while 24.7% and 26% anticipate a decrease and no change in the firm's sales, respectively.

Explanatory variable of interest: Political connection

The main explanatory variable of interest is firms' political connection. We use the following question in the survey as a proxy for firms' political connection: "Has the owner, CEO, top manager, or any of the board members of this firm ever been elected or appointed to a political position in this country?" The question is slightly different for Saudi Arabia: "Has the owner, CEO, top manager, or any of the board members of this firm ever been appointed as a deputy minister or higher position in the government?" The possible answers were Yes, No and Don't Know. For our regression analyses, we create a dummy for the political connection variable (1 for Yes and 0 for No) and we remove those respondents who either did not answer this question

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[1] For more details about the survey and its methodology, see: https://www.enterprisesurveys.org/en/data

or responded as Do not know. In the sample of 5,641 firms, for which data on sales confidence is also available, 7.75% of firms have a politician on the board, while 92% do not.

Control variables

In addition to having a politician on the board, various factors may influence expectations about future sales at the firm level. We have categorized these drivers into internal and external factors.

Among the internal factors, we consider the firm's spending on research and development (R&D) activities, firm age, managers' years of experience, quality certifications, gender of the top manager, knowledge acquisition, government contracts, and innovation.

Turning to external factors, we consider the number of competitors in the market, location in the capital city, operation in a business hub, business losses due to weather or pollution, the average impact of various business obstacles, and country-specific characteristics. Table A1 in the Appendix A provides more detailed descriptions of the control variables, data sources, and their expected signs. Table A2 in the Appendix A presents the descriptive statistics for all variables.

We also consider the benefits from memberships in different associations as a crucial factor influencing business expectations. Membership in associations may be motivated by various factors, including gaining access to new markets, obtaining credit, accessing government information, and engaging in lobbying efforts. We hypothesize that a main channel explaining the positive influence of having a politician on the board on the optimistic expectations of future sales for firms is the larger and stronger networking facilitated through memberships, along with access to a variety of information. Thus, we anticipate that once we control for the average level of these membership benefits, the positive and significant association between having a politician on the board and firms' sales expectations will diminish.

2.2. Estimation method

Given that the dependent variable (firm's confidence in the next year sale) is an ordinal variable (which is measured on a 3-point scale ranging from -1 to 1), we apply Ordered Probit regressions, with robust standard errors which corrects the standard errors for heteroscedasticity.

The empirical model (1) is specified as follows:

$$\Pr(\text{CONF}_j = i) = \Pr(k_{j-1} < \beta_1 PC_j + \beta_2 Z_j + u_j \leq k_i) \tag{1}$$

where CONF is firm's expectation about the next year sales, PC is a measure of political connection, Z represents the control variables, βs are the coefficients, $k_1, k_2, ..., k_{I-1}$ are the cutpoints, and i is the number of possible outcomes, Pr is the probability, and finally u is an error term which is assumed to be normally distributed. We report marginal effects that illustrate the changes in the predicted probability of various outcomes in the firm's sales expectations resulting from a unit change in the explanatory variable. Our focus is particularly on the presence of a politician on the board of the firm, coded as 1, and otherwise coded as 0.

3. Results

Table 1 presents the estimated marginal effects of a positive change in our key explanatory variable (having a politician on the firm's board) on three outcomes within our dependent variable, business sentiment regarding the next year sale: an increase in the firm's future sales (+1), a decrease in the firm's future sales (-1), and no change in the firm's future sales (0).

In Model 1, shown in Table 1, not controlling for other explanatory variables, it is evident that having a politician on the board raises positive expectations for firm's sales by 11.2 percentage points (pp).

In Models 2-9 in Table 1, we control for other internal drivers of firm's sale expectations including R&D spending within firm, logarithm of firm's age, logarithm of managers' years of experience, firm's possession of quality certification, gender of top manager, spending on

external knowledge acquisitions, government contract, and innovation. The key finding remains robust. Across all models, a positive change in having a politician on the board is consistently associated with an approximately 10 pp increase in the predicted probability of an elevated expectation for firm sales. However, the effect on the other two outcomes, namely no change and a negative change in firm sales, is negative. The estimated marginal effects are statistically significant at the 1% level in all models.

These findings support our hypothesis that there is a significant relationship between political connection and firm owners and managers' expectations on their future sales. Managers and owners of politically connected firms in the MENA countries tend to have a more positive outlook on their future sales. Our results also provide empirical support for the "*income-smoothing hypothesis*" (Chen et al., 2010), which suggests that political connections help financial analysts in predicting connected firms' earnings more accurately because the connection secure and stabilize firms' future earnings. Our findings are also in line with the "*helping hand*" theory, which argues that government intervention in favor of politically connected firms helps them achieve better performance. In addition, we provide further empirical support for the existing literature for the MENA region on the positive impacts of political connections on firm performance (e.g., Saadi, 2019; Diwan & Haidar, 2019; Sabry, 2018).

Table 1. The marginal effect of politician on the board and expected change in firm's sales (controlling for internal factors)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Sales expected to decrease	-0.089***	-0.080***	-0.085***	-0.084***	-0.070***	-0.087***	-0.083***	-0.083***	-0.087***
	(-4.913)	(-4.399)	(-4.679)	(-4.574)	(-3.791)	(-4.743)	(-4.545)	(-4.514)	(-4.766)
Sales expected to not change	-0.023***	-0.021***	-0.022***	-0.021***	-0.018***	-0.022***	-0.021***	-0.021***	-0.022***
	(-4.863)	(-4.363)	(-4.639)	(-4.532)	(-3.773)	(-4.699)	(-4.509)	(-4.479)	(-4.718)
Sales expected to increase	**0.112*****	**0.101*****	**0.108*****	**0.105*****	**0.088*****	**0.109*****	**0.104*****	**0.104*****	**0.110*****
	(4.939)	**(4.418)**	**(4.703)**	**(4.595)**	**(3.804)**	**(4.767)**	**(4.567)**	**(4.535)**	**(4.790)**
Control variables		Firm's R&D spending within firm	Logarithm of firm's age	Logarithm of manager's years of experience	Firm's possession of quality certification	Gender of top manager	Spending on external knowledge acquisitions	Firms' government contract	Firms' innovation
Observations	5,641	5,603	5,552	5,520	5,549	5,624	5,604	5,573	5,608

Note: Estimation method is ordered probit. Marginal effects are reported. Robust standard errors are used to calculate the z statistics in ().
Asterisks indicate significance at the 10% (*), 5% (**), and 1% (***) levels, respectively.

In Table 2 we revisit our inquiry, incorporating external drivers of business confidence. These include the number of competitors in the market, a firm's location in the capital city or a business city, business losses due to severe weather or pollution in the past, the average burden of various business obstacles, and a country dummy variable.

Once more, a consistent pattern emerges. Having a politician on the board consistently raises the predicted probability of an increase in firm sales expectations by an average of 10 percentage points across seven models. Furthermore, the adverse effects on predicted probabilities for the other two outcomes persist (columns 1-7 of Table 2).

Table 2. The marginal effect of politician on the board and expected change in firm's sale (controlling for external factors)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Sales expected to decrease	-0.075***	-0.073***	-0.068***	-0.087***	-0.088***	-0.096***	-0.061***
	(-3.936)	(-4.083)	(-3.810)	(-4.807)	(-4.833)	(-5.259)	(-3.592)
Sales expected to not change	-0.019***	-0.024***	-0.023***	-0.023***	-0.023***	-0.025***	-0.019***
	(-3.917)	(-4.072)	(-3.802)	(-4.765)	(-4.795)	(-5.168)	(-3.574)
Sales expected to increase	**0.093***	**0.098***	**0.091***	**0.111***	**0.111***	**0.121***	**0.080***
	(3.952)	**(4.102)**	**(3.826)**	**(4.832)**	**(4.860)**	**(5.288)**	**(3.598)**
Control variables	Firm's competitors	Firm's location: Capital city	Firm's location: Business city	Firm's losses due to extreme weather	Firm's losses due to pollution	Average of firm's business obstacles	Country dummy
Observations	5,290	5,058	5,057	5,580	5,587	5,250	5,641

Note: Estimation method is ordered probit. Marginal effects are reported. Robust standard errors are used to calculate the z statistics in (). Asterisks indicate significance at the 10% (*), 5% (**), and 1% (***) levels, respectively.

Table 3 introduces our hypothesized mechanism, which explains the main effect of having a politician on the board on anticipated changes in firm sales. This mechanism is represented by the average level of benefits that firms derive from their memberships in different associations. These memberships hold significance for firms due to their potential for providing access to government information, credit, new markets, and opportunities for lobbying. We use the following question from the Enterprise Survey to measure the benefits of association membership: "Referring to the most important business association that this firm is part of, how useful are the following services provided to this firm?" (1) Information or contacts on international input and product markets, (2) Accrediting standards or quality of products, (3) Information on government regulations and (4) Influencing regulatory decision-making processes or "lobbying". The assigned scores for these benefits range from 1 (Not at all useful) to 4 (Very useful), with higher scores indicating greater importance of the benefits obtained from membership.

The inclusion of the average benefits of membership variable leads to a significant reduction in the sample size because many respondents chose not to answer this question. Model 1 in Table 3 shows results without the inclusion of average benefits of membership variables but utilizes the sample of Model 2, which incorporates both average benefits and all internal controls. Therefore, the only distinction between Model 1 and Model 2 is attributed to the inclusion of average benefits indicators in the latter.

The results show that having a politician on the board increases the predicted probability of a positive change in firms' sales expectations, controlling for all internal factors, in Model 1 by approximately 6 percentage points. In Model 2, this effect diminishes to only 1 percentage point and becomes statistically insignificant. The impact of average benefits on the model outcome is positive and significant (not presented in Table 3). This suggests a mediating role for this factor.

Model 3 in Table 3 controls for all external variables, using the same sample as in Model 4, which includes both external controls and average benefits of membership. The results in Model 3 align with Model 1. However, in Model 4, the positive and significant influence of having a politician on board on firms' sales increase expectation diminishes somewhat, both in its magnitude and statistical significance (it is now only significant at the 10% level). Model 5 includes all internal and external variables, using the same sample as in Model 6, which has all these controls but also includes average benefits variables. In this case, we do not observe a significant marginal effect.

Table 3. The marginal effect of politician on the board and expected change in firm's sale (controlling for internal, external factors and membership benefits)

	(1)	(2)	(3)	(4)	(5)	(6)
Sales expected to decrease	-0.048**	-0.008	-0.042**	-0.036*	-0.025	-0.023
	(-2.216)	(-0.376)	(-2.054)	(-1.739)	(-1.216)	(-1.109)
Sales expected not to change	-0.009**	-0.002	-0.012**	-0.010*	-0.007	-0.007
	(-2.217)	(-0.377)	(-2.053)	(-1.738)	(-1.216)	(-1.108)
Sales expected to increase	**0.058****	**0.010**	**0.053****	**0.046***	**0.032**	**0.030**
	(2.221)	**(0.377)**	**(2.057)**	**(1.741)**	**(1.217)**	**(1.109)**
Control variables	All internals	All internals & Average score of membership benefits	All externals	All externals & Average score of membership benefits	All internals and externals	All internal, externals & Average score of membership benefits
Observations	3,524	3,524	2,994	2,994	2,919	2,919

Note: Estimation method is ordered probit. Marginal effects are reported. Robust standard errors are used to calculate the z statistics in (). The average score for membership benefits is computed by taking the mean of the scores for Information or contacts on international input and product markets, Access to credit, Information on government regulations, and Influencing regulatory decision-making processes or "lobbying". Asterisks indicate significance at the 10% (*), 5% (**), and 1% (***) levels, respectively.

4. Conclusion

While several studies have examined the link between political connection and firms' environmental, economic, financial and social activities, no empirical research has yet explored the relationship between political connection and firms' business sentiment (measured by expectation on future sales) in the MENA region. This gap is significant, as political connection plays a key role in business operations for many firms in this area (Sahnoun et al., 2014). Using firm-level cross-sectional data from the recent Enterprise Surveys of the World Bank (2024) across nine MENA countries, and applying Ordered Probit regressions, we find that politically connected firms tend to have a positive outlook on their future sales. This positive sentiment among politically connected firms stems from their access to greater resources, insider information, extensive networks, and their ability to influence regulations in favor of their businesses and industries.

Our findings have at least three implications for firms operating in these countries, political activists and independent media, and suppliers of intermediate and final goods and services. First, firms may consider appointing ex-politicians to their boards of directors or as managers to facilitate future sales. However, this practice can result in substantial costs for other firms in these countries, such as discriminatory enforcement of rules and regulations. This brings us to our second implication for political activists and independent media. To mitigate the costs imposed by politically connected firms on the broader economy, these groups should advocate for greater transparency in the employment of politicians and their relatives by firms. Finally, from a commercial perspective, business confidence often translates into actual sales growth. Therefore, domestic and international suppliers of goods and services to politically connected firms in the region can benefit from this opportunity by specifically targeting and promoting their products to these firms.

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Appendix A

Table A1. Descriptions of control variables

Variables	Questions in the survey
Firm's R&D spending within firm	"Over the last three years, did this establishment spend on research and development activities within the establishment?"
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's age	"In what year did this establishment begin operations?"
	To calculate the firm's age, we subtract the year of establishment from the year of data collection. We then take the logarithm of the firm's age.
Firm manager's years of experience	"How many years of experience working in this sector does the Top Manager have?"
	We take the logarithm of the manager's years of experience.
Firm's quality certification	"Does this establishment have an internationally-recognized quality certification?"
	The possible responses are Yes, No, Don't Know (Spontaneous) and Still in Process. We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) and Still in Process are excluded from the analysis.
Gender of top manager	"Is the Top Manager female?"
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's acquisition of knowledge	"Over the last three years, did this establishment spend on the acquisition of external knowledge? This includes the purchase or licensing of patents and non-patented inventions, know-how, and other types of knowledge from other businesses or organizations."
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's government contract	"Over the last year, has this establishment secured or attempted to secure a government contract?"

	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's innovation	"During the last three years, has this establishment introduced new or improved products or services?"
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's competitors	"In [last] fiscal year, for the main market in which this establishment sold its main product, how many competitors did this establishment's main product face?"
	We categorize them into four groups: 0 for none, 1 for 1-9 competitors, 2 for 10-100 competitors, and 3 for above 300 competitors and "too many to count".
Capital city	"Is this city the official capital city?"
	We create a dummy variable where Yes is coded as 1 and No as 0.
Business city	"Is this city the main business city?"
	We create a dummy variable where Yes is coded as 1 and No as 0.
Firm's losses due to extreme weather	"Over the last three years, did this establishment experience monetary losses due to extreme weather events (such as storms, floods, droughts, or landslides)?"
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's losses due to pollution	Over the last three years, did this establishment experience monetary losses due to pollution not generated by this establishment (that is, independent of this establishment's activity)?
	The possible responses are Yes, No, and Don't Know (Spontaneous). We create a dummy variable where Yes is coded as 1 and No as 0. Responses of Don't Know (Spontaneous) are excluded from the analysis.
Firm's business obstacles	Using the response options on the card; To what degree are each of the following an obstacle to the current operations of this establishment? Corruption, Labor regulation, Tax rates, and Access to finance.
	The possible responses are (0) No obstacle, (1) Minor obstacle, (2) Moderate obstacle, (3) Major obstacle, (4) Very Severe Obstacle, Don't know and Does not apply. Responses of Don't Know (Spontaneous) and Does not apply are excluded from the analysis.

We take the average burden of four business obstacles in the analyses.

Country fixed effects	Country-specific characteristics are captured by a dummy variable for each sample country.
Benefits of being member of business organization	Referring to the most important business association that this firm is part of, how useful are the following services provided to this firm? (1) Information or contacts on international input and product markets, (2) Accrediting standards or quality of products, (3) Information on government regulations and (4) Influencing regulatory decision-making processes or "lobbying". The possible responses are (1) Not at all useful, (2) Not very useful, (3) Somewhat useful and (4) Very useful.

Table A2. Descriptive statistics (before transformation)

Variables	Frequency (%)	Mean	Std. dev
Business confidence in future sales (1 "increase", 0 "Stay the same", -1 to "decrease")	-1 (24.77%)		
	0 (26.09%)		
	1 (49.14%)		
Political connection (Yes=1)	7.75%		
Firm's R&D spending within firm (Yes=1)	9.73%		
Firm's age		22.73	13.88
Firm manager's experience		21.72	11.30
Firm's possession of quality certification (Yes=1)	18.88%		
Gender of top manager (Female=1)	5.55%		
Firm's spending on external knowledge acquisitions (Yes=1)	4.68%		

Firm's government contract (Yes=1)	13.69%	
Firm's innovation (Yes=1)	8.81%	
Firm's competitors	3 (66.85%)	
	2 (4.01%)	
	1 (19.61%)	
	0 (3.32%)	
Firm's location: Capital city (Yes=1)	24.89%	
Firm's location: Business city (Yes=1)	30.79%	
Firm's losses due to extreme weather (Yes=1)	6.13%	
Firm's losses due to pollution (Yes=1)	2.23%	
Firm's business obstacles (average of 4 obstacles: corruption, labor regulation, tax rates, and access to finance) (scores between 0-4)	1.48	0.93
Benefits of being member of business organization (average of 4 benefits: Information or contacts on international input and product markets, access to credit, Information on government regulations, Influencing regulatory decision-making processes or "lobbying"). Scores are between 1 to 4.	2.93	0.88