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RESEARCH ARTICLE

Managerial political power and the reallocation of resources in the internal capital market

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Abstract

Research Summary: We examine how managers' political power reallocates resources in the internal capital market. By shifting the focus from financial to firm-specific, non-financial resources that are difficult to evaluate and zero-sum in nature, we revise the prevailing view that managers' political power plays a significant yet contingent role under financial constraint and weak governance. We instead characterize managerial political power as an intrinsic, inescapable determinant of internal competition and resource allocation. Our research design links sentence-by-sentence, qualitative analyses of the legal opinion delivered as breaking news during the corruption trials involving a key executive at Samsung group with minute-level shifts in share prices. This study presents a politics-based theory of the internal capital market and highlights the methodological potential of quantitative case studies.

Managerial Summary: Managerial politics presents a vexing yet persistent reality of organizational life and the inter-divisional competition for resources. We attribute its pervasiveness to the contest over non-financial resources with fuzzy ownership and significant yet uncertain value, such as bargaining power over internal transfer pricing, managerial attention, and control over new business opportunities. Because of the zero-sum dynamics of these non-financial resources and their constant scarcity, political contests cannot be suppressed through the provision of financial slack or agency controls and even extend to family members.

Appointing rival managers along clearly separated lines of businesses may curb, but not eliminate, managerial politics. We show that investors are acutely aware of the value of managers' political power and make investment decisions based on them.

KEYWORDS

business groups, case study, internal capital market, managerial politics, tunneling

1 | INTRODUCTION

Within-firm transactions are roughly equal in value to those of external markets (Hall, Lovallo, & Musters, 2012; Lafontaine & Slade, 2007), and distortions in a firm's internal capital market have "enormous real-world consequences" (Siegel & Choudhury, 2012, p. 1764). Relative to the external capital market, which chiefly deals with financial resources (e.g., bank lending) (Gertner, Scharfstein, & Stein, 1994), the internal capital market centers on the (re)allocation of idiosyncratic, firm-specific resources that are difficult to buy or sell externally (e.g., Feldman & Sakhartov, 2021; Kogut & Zander, 1992; Maritan & Lee, 2017a; Sengul, Costa, & Gimeno, 2019). Because of the significant uncertainty around how to value and best allocate these scarce resources as well as whose opinion should prevail, resource allocation in the internal capital market is ultimately a contentious political process that reflects the preferences of politically powerful managers at the top (Allison, 1971; Cyert & March, 1963; Eisenhardt & Bourgeois III, 1988; March, 1962; Milgrom & Roberts, 1988). We examine managers' political power and the scope of its influence in the internal capital market of business groups (e.g., Bertrand, Mehta, & Mullainathan, 2002; Chang & Hong, 2000; Khanna & Yafeh, 2007).

Despite the historical attention to managerial politics, very few studies link the changes in managers' political power to the inter-divisional (or inter-affiliate) reallocation of resources in the internal capital market, leaving managerial politics as a lost theoretical pillar of management research (Gavetti, Levinthal, & Ocasio, 2007). In the few studies that do link a manager's political power to resource allocation, it plays a significant yet highly contingent role. Managerial political power affects the allocation of slack financial resources under the restrictive conditions of internal financial constraint, a poorly developed external capital market, weak corporate governance, or economic uncertainty that limits prioritization based on net present value (NPV) projections (e.g., Buchuk, Larrain, Muñoz, & Urzúa, 2014; Duchin & Sosyura, 2013; Lee, Park, & Shin, 2009). However, the highly limited characterization of a manager's political power conflicts with the qualitative accounts of the incessant struggle for political power and the day-to-day experiences of most people (Eisenhardt & Zbaracki, 1992). Moreover, it presents an overly objective and orderly view of the internal competition and capital allocation process.[1]

[1]In contrast, Cyert and March note that (1963, pp. 205–206): "Just as [a manager] needs to predict and attempt to manipulate the 'external' environment, he must predict and attempt to manipulate his own firm. Indeed, our impression is that most actual managers devote *much more time and energy* to the problems of managing their [political] coalition than they do to the problems of dealing with the outside world (emphasis added)."

We propose that managers' political power is an inescapable determinant of how resources are allocated in the internal capital market of multi-divisional organizations. Looking beyond the earlier focus on cash flows, research on the internal capital market has increasingly attributed greater importance to unique non-financial resources (Sengul et al., 2019). However, in examining how managerial politics affect internal competition and capital allocation, extant research focuses singularly on financial resources that are transparent in value and can be better accessed and expanded in the external financial market, even though political power likely wields the greatest influence in situations of economic uncertainty and strict opportunity cost.

We shift the analytical focus from financial resources to firm-specific, non-financial resources (Chang & Hong, 2000; Lamin, 2013; Manikandan & Ramachandran, 2015), arguing that their oversight has led to a highly contingent and incomplete view of managerial politics. In addition to lacking clear objective value, these idiosyncratic resources, such as access to shared intangible resources and greater bargaining power on internal transfer pricing, are subject to constant scarcity due to the lack of well-functioning external factor markets. As a result, their use by one division requires withdrawal from another (Levinthal, 2017; Levinthal & Wu, 2010).[2] Their allocation takes a zero-sum political process whereby a negative shock to a manager and their diminished political power benefit other managers by enhancing access to scarce resources in the internal capital market.

To test the proposed zero-sum dynamics of managerial power and its pervasiveness, we adopt a qualitative case study approach, which is commonly used in the study of political power and business groups (e.g., Bower, 1970; Eisenhardt & Bourgeois III, 1988; Ghemawat & Khanna, 1998; Glaser, Lopez-De-Silanes, & Sautner, 2013; Joseph & Wilson, 2018), but combine it with an event-study design that has been used to quantitatively estimate the market value of external political connections (e.g., Acemoglu, Johnson, Kermani, Kwak, & Mitton, 2016; Fisman, 2001). Our empirical context is the Samsung business group, where a key executive JY Lee undergoes a series of high-profile corruption trials. By parsing each sentence of the legal opinion delivered during these trials, we identify a series of quasi-exogenous shocks on his standing within the group that unfolds over the course of minutes. We then trace the minute-by-minute reactions of the stock market as key parts of the verdict were being read and conveyed to the public as breaking headlines and show that the loss of one manager's political power indeed transfers value to other divisions. We complement this share price-based evidence with analyses of the "unusual" changes in actual inter-affiliate transactions around JY's trial, reported as notes in the 10Q and 10K filings.

This study presents a politics-based theory of internal competition and resource allocation with several implications. First, we show that managerial political power is an intrinsic part of the internal capital market and highlight as its basis firm-specific, zero-sum resources (Levinthal & Wu, 2010) that are subject to constant scarcity. Our study reintroduces managerial politics into the analysis of the internal capital market and provides a behaviorally sensible and richer foundation for understanding intra-organizational conflict and decision-making (Bardolet, Fox, & Lovallo, 2011; Cyert & March, 1963; Gavetti et al., 2007) as well as the limits of financial slack in smoothing political conflicts. Second, our case analysis highlights the subtle resource transfers that, despite carrying significant value, do not entail a visible or immediate extraction and reallocation. Looking only at tangible and realized resource allocation (e.g., capital expenditure) overlooks the contest over non-financial resources with fuzzy

[2]Levinthal and Wu (2010) refer to zero-sum resources with strict opportunity cost as being "rivalrous," "non-scale free," and "congestible."

ownership and their subtle transfers that withstand external scrutiny. Third, we inform the research on inter-divisional relations, sometimes summarized as "coopetition" (Baumann, Eggers, & Stieglitz, 2019; Poppo, 1995; Tsai, 2002). In addition to the cooperative cross-subsidization of financial resources emphasized in prior research (e.g., Arrfelt, Wiseman, McNamara, & Hult, 2015; Joe & Oh, 2018), divisions compete for zero-sum non-financial resources. As a result, competition and cooperation can simultaneously occur as they unfold over distinct domains of financial and non-financial resources, each emphasizing financial and political winner-picking. The competitive zero-sum dynamics extend to family managers, qualifying the assumption that they are a homogenous group with shared interests (e.g., Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007; Jeong & Siegel, 2018; Jonsson, Greve, & Fujiwara-Greve, 2009). Finally, we discuss implications to multiplex relations in family firms and tunneling research in the Conclusion section.

From a methodological standpoint, this study highlights the potential for using high-frequency data as a tool for generating and testing new theories. The lack of sufficiently long panel data often serves as a roadblock to testing new theories, especially if their predictions conflict with existing ones that have found quantitative support (Eisenhardt & Graebner, 2007). When combined with detailed qualitative analysis, high-frequency data can reveal novel insights even from a short time frame, in some cases spanning less than an hour. Our research design should generalize to congressional debates, testimonies, and tweets by influential figures within a compressed time context. It promises to be an important analytical tool as such data becomes increasingly prevalent and accessible at lower costs.

2 | RELATED LITERATURE AND HYPOTHESIS DEVELOPMENT

2.1 | Opportunity cost and the tournament model of internal resource allocation

One critical feature of the internal capital market is that a central authority can increase overall firm value by extracting resources from one division and reallocating them to more promising ones, for example, in the descending order of expected financial returns (e.g., Feldman, 2021; Hu, He, Blettner, & Bettis, 2017; Khanna & Tice, 2001). As a result, "the extent to which any given project gets funded in an internal capital market will depend not only on that project's own absolute merits but also on its merits relative to other projects in the company's overall portfolio" (Stein, 1997, p. 112).[3] Extant research on this tournament-like model of internal "winner-picking" and "loser-sticking" has focused on financial resources that permit active withdrawal and redistribution. However, the internal capital market also reallocates firm-specific, non-financial resources with critical implications to the scope of managerial political power.

First, financial resources are certainly not scale-free, but business groups and firms can more readily access additional financial resources in the external capital market and reduce the zero-sum dynamics of having to invest in one division at the opportunity cost of others,

[3]There is also an important body of agency and behavioral research that documents the "dark" side of the internal capital market, such as empire building, subsidization of weak divisions, and the naïve socialistic allocation based on 1/n rule (Bardolet et al., 2011; Scharfstein & Stein, 2000).

especially in the presence of a well-developed financial market (Lee et al., 2009). In contrast, firm-specific, non-financial resources are subject to stricter scarcity, in some cases due to the immaturity of the external factor market or an "institutional void" (Guillen, 2000; Khanna & Yafeh, 2007), but more fundamentally, due to the non-tradable and non-substitutable nature of strategic resources (e.g., Barney, 1991; Dierickx & Cool, 1989; Guillen, 2000). Second, the lack of price signals from the external factor market leaves the value of firm-specific non-financial resources more ambiguous. This greatly complicates forecasting the net present value (NPV), creating room for inflated projections, lobbying, and other influence activities. As a result, financial and non-financial resources differ markedly in their potential for inter-divisional conflict and the importance of managers' political power for a favorable resolution. We examine managerial politicking as a fundamental and constant determinant of how firms manage resource scarcity and uncertainty in the optimal allocation of non-financial resources in the internal capital market.

We define political power as managers' ability to impose their preferences in the strategic decision-making process by exercising influence through observable actions within their formal authority as well as more covert actions using informal power (Eisenhardt & Bourgeois III, 1988).[4,5] There is an influential body of research that examines the value of external political power, for example, based on managers' social connections to the ruling political party, in competing against product market competitors (e.g., Acemoglu et al., 2016; Fisman, 2001; Jia, Zhao, Zheng, & Lu, 2022; Siegel, 2007). In stark contrast, analyses of how managers' political power influences internal resource allocation are exceedingly rare (Ganz & Schiff, 2020). In their review of internal capital market literature, Busenbark, Wiseman, Arrfelt, & Woo (2017, table 1) find just five studies, all of which come from finance journals. Our own bibliometric search also reveals five. Managerial political power is such a pervasive and closely experienced part of organizational life that its features are often taken for granted, yet a closer inspection reveals two fundamentally divergent views on when and how it affects the internal capital market.

2.2 | Financial resources and the contingent importance of managers' political power

Prior empirical studies on managers' political power focus predominantly on cash flows (or capital expenditure funded by the cash flow) as their dependent variable. They provide a "contingent view," whereby managers' political power distorts resource allocation and helps to fund additional investment but only under conditions of internal financing constraint, external financing constraint, or weak corporate governance, which all severely limit its scope and strategic importance.[6]

[4]There are several overlapping definitions of political power. Mayes and Allen (1977, p. 675) define it negatively as "the management of influence to obtain ends not sanctioned by the organization." Gandz and Murray (1980, pp. 237–238) compare narrow and broad definitions, spanning "any conflict over the allocation of scarce resources as a political process" to "conflict over any decision" and "the use of *any* power or influence as political." We adopt their narrow definition.

[5]Managerial political power is related to but distinct from *organizational* power examined in resource dependence research (e.g., Kim, Hoskisson, & Wan, 2004; Pfeffer & Salancik, 1974). For example, Bardolet, Brown, and Lovallo (2017) use a division's size relative to the firm as a proxy for its influence and find that the largest divisions are allocated a larger share of resources. We consider this to be organizational power that exists independent of its managers at the top.

[6]Some of these studies also assume that political power is slow to change, further limiting its strategic value. Refer to Joseph, Ocasio, and McDonnell (2014) for detailed examinations of the circulation of power.

While acknowledging that centralization invariably leads to politicking and lobbying for resources, these studies suggest that the demand for economic efficiency effectively disciplines managerial politics and keeps the internal capital market reasonably objective.

In their survey of CEOs and CFOs, Graham, Harvey, and Puri (2015) find that internal resource allocation is largely an objective process where politics play a limited role: the two most important factors are "NPV rank" and "manager reputation" based on past performance. "Corporate politics" and "balanced allocation" rank last of the 10 survey items with greater yet still bottom-ranked importance in European and Asian firms relative to US firms. Glaser et al. (2013) examine a large European conglomerate and find that, following a cash windfall, divisions headed by managers with a longer tenure at the firm are allocated larger than planned capital. Duchin and Sosyura (2013) examine S&P 500 firms and show that divisional managers with social connections to the CEO are allocated more capital relative to the imputed Tobin's Q, especially under weak governance. In contrast, Xuan (2009) finds evidence of reverse favoritism whereby recently appointed CEOs allocate more capital to out-group divisions in efforts to "build a bridge" and elicit cooperation. In these studies, political power helps to secure "extra" capital but does not take away from the economically justified share of resources for politically weak managers. In other words, managerial political power leads to increased allocation but little *re*-allocation.[7]

The research on the internal allocation of financial resources in diversified conglomerates and business groups ascribes a similarly contingent role to the internal capital market itself. The reallocation of capital from less to more productive divisions occurs in financially constrained firms and in the absence of a well-functioning external capital market (Chang & Hong, 2000; Giroud & Mueller, 2015; Granovetter, 2005). As financial markets and intermediaries develop, firms increasingly substitute the internal capital market with public debt (e.g., Carney, Gedajlovic, Heugens, Van Essen, & Van Oosterhout, 2011; Khanna & Palepu, 2000) to the effect of weakening internal financial winner-picking and the zero-sum dynamics (Lee et al., 2009). Within management research, March (1962) and Cyert and March (1963) take a similar stance, suggesting that inter-divisional conflicts and coalitional politics can be reduced through slack resources that permit more generous (financial) side payments and the accommodation of competing goals.

2.3 | Non-financial resources and the constant importance of managers' political power

We propose a "constant view" that accords a more central and unqualified role to managerial political power. The departure from the contingent view rests critically on our broader interpretation of "capital" in the internal capital market to include firm-specific non-financial resources. While there is a tendency to view politicking within firms as "the inescapable internal-organization analog of haggling between firms (Gibbons, 2005, p. 222)," the internal capital market differs fundamentally from the external factor market, allocating unique resources that

[7]Research on executive compensation documents a similarly contingent influence: divisional managers' social connections to the CEO lead to higher pay but only when there is excess cash and in the absence of strong governance mechanisms, such as external boards of directors and large shareholders (Duchin, Goldberg, & Sosyura, 2017). Acemoglu, Hassan, and Tahoun (2018) find similar non zero-sum dynamics with respect to the value of external political connections and power.

cannot be bought or sold in the external factor market (e.g., Barney, 1991; Dierickx & Cool, 1989; Guillen, 2000).[8] In fact, firms internalize transactions and replace the price mechanism with managerial authority precisely when the resources are difficult to price and contract, even at the increased risk of moral hazards and managerial politics (Grossman & Hart, 1986; Maritan & Lee, 2017b; Milgrom & Roberts, 1988; Poppo, 1995)

While recognizing that there are valuable non-financial resources that take on the characteristics of non-exclusionary public goods, such as brand value, reputation, and scale-free technologies, we highlight four zero-sum resources with significant yet uncertain value. These intangible resources do not fit neatly into existing resource categories, are difficult to contract and transfer outside firm boundaries, and often show fuzzy ownership and contestability by other managers and divisions. It is precisely these characteristics that expose them to political influence.[9]

First, a politically powerful manager can spend an unfair share of shared intangible resources, such as managerial attention (Feldman, 2016; Joseph & Wilson, 2018) and external bargaining power (Jeong & Siegel, 2018), that often belong to the broader firm as a quasi-public good without a clear formal owner. For example, as a response to J.P. Morgan's refusal to support the digital payment system in Samsung smartphones, there was a group-level embargo on working with J.P. Morgan, mainly targeted at punishing its lucrative and internally influential investment banking division. The coordinated pressure eventually resulted in J.P. Morgan conceding and supporting Samsung Pay. This outcome asymmetrically benefited Samsung Electronics at "unknown costs and disruptions to other Samsung affiliates," some of which had active ongoing engagements with J.P. Morgan at the time, according to a Samsung executive.

Second, a politically powerful manager benefits from higher status in the corporate hierarchy and, in turn, greater internal bargaining power (Magee & Galinsky, 2008). Suppose there is an electronics company that operates two divisions: displays and mobile phones. A powerful manager in charge of the mobile phone division can facilitate its growth by pressuring the displays division to prioritize internal orders from its own division even at the cost of foregoing more profitable external orders. Divisions and affiliates in M-form organizations are often vertically related to capture synergy (e.g., Natividad & Rawley, 2015) and act as major buyers and sellers to each other, rendering bargaining against each other a recurring feature of interdivisional relations (Eccles & White, 1988).

Third, a division with a powerful manager can reset firm and divisional boundaries to its advantage. In addition to external competitors, divisions often face internal competition against other divisions due to overlaps in technologies, customers, and products (Birkinshaw & Lingblad, 2005; Eggers, 2016). Also, firms constantly renegotiate their charter through acquisitions and divestitures (Bennett & Feldman, 2017; Feldman & Sakhartov, 2021; Meyer, Milgrom, & Roberts, 1992; Vidal & Mitchell, 2015), spin-offs and equity carve-outs (Feldman, 2016), and new product launches that can cannibalize existing products. These adjustments in firm and divisional boundaries will likely be gerrymandered to favor politically powerful managers (Albert, 2018; Bidwell, 2012; Guler, 2007), who can first select the most promising new growth opportunities while blocking other divisions from entering overlapping

[8]This is not to say that financial resources are completely scale-free and carry no uncertainty, especially as they can be used to develop new idiosyncratic resources and capabilities, as discussed in depth by Kim and Bettis (2014). However, in relative terms, non-financial resources show far greater ambiguity in their value and allocative uncertainty.

[9]During our field work, in response to the question "what resources and benefits can political power bring," executives repeatedly began their response with some variation of "I am not sure how to describe it…," but then went onto detail concrete instances of both how they lost or won internal competition for resources due to political power.

markets. If divisions are organized as independent firms, more powerful managers can increase their ownership share in other affiliates at unfairly discounted rates (i.e., tunneling) (Bertrand et al., 2002; Siegel & Choudhury, 2012). This was precisely the accusation that American activist fund Elliott Management used to sue the Samsung group.

Fourth and perhaps most elusively, politically powerful managers benefit from the mere expectation of future financial and business support. The expectation that the broader group will prioritize bailing out politically powerful managers functions effectively as an informal loan guarantee (Belenzon, Berkovitz, & Rios, 2013; Hann, Ogneva, & Ozbas, 2013; Jia, Shi, & Wang, 2013). In April 2020, during the peak of the pandemic, Samsung affiliate Hotel Shilla was able to issue new debt "in overwhelming response" even as other Korean firms struggled.[10] This ready access to the external financial market partly reflects a co-insurance effect whereby affiliate firms in a business group mutually support each other to the benefit of lowering the cost of capital (Gopalan, Nanda, & Seru, 2007). However, we also expect affiliates with powerful managers to receive prioritized and larger assistance relative to their contribution, especially in a dire zero-sum situation when not all affiliates can be saved or supported. As a case in point, an analyst at the Korea Investors Service (Moody's equivalent of Korea) justified Hotel Shilla's high credit rating despite the industry downturn from Covid-19 by noting that: "Because Hotel Shilla is directly managed by a member of the Lee family, we expect a strong willingness to provide financial support by the Samsung group... its credit rating is therefore raised by one notch by taking into consideration *the likelihood of financial support in case of financial distress* (emphasis added)."[11] As a result, managerial political power can drive down the cost of capital and support more aggressive investment, even without any direct transfer of financial resources until the actual instance of financial distress.

The pervasiveness of these zero-sum resources serves as a theoretical basis for why a manager's political power is a constant, inescapable feature of internal resource allocation rather than being a selective and opportunistic component.[12] Corporate governance and business group research view the politics-based reallocation of resources with great suspicion and as a potential "theft device" against minority shareholders (Siegel & Choudhury, 2012, p. 1764) that should and can be disciplined through shareholder oversight. However, the idiosyncratic nature of firm-specific resources subjects their value to significant uncertainty and makes it almost impossible to evaluate optimal and unbiased allocation (Bettis, 2017). We view this lack of reliable NPV projections and the resulting allocative uncertainty as an irreducible feature of non-financial resources and their allocation in the internal capital market (Levinthal, 2017; Maritan & Lee, 2017a) rather than an occasional exception due to the high cost of information acquisition (Milgrom & Roberts, 1988; Wulf, 2009). Accordingly, we expect the politics-based reallocation of non-financial resources to be a robust phenomenon that persists under financial slack and the scrutiny of external stakeholders.

At first glance, the proposed pervasive scope of managerial politics conflicts with findings from influential and rigorously executed prior studies that track changes in capital expenditure (e.g., Buchuk et al., 2014; Duchin & Sosyura, 2013). However, a manager can benefit at the cost of the others without the visible extraction and reallocation of resources. In particular, tracking

[10]https://pulsenews.co.kr/view.php?year=2020&no=404982

[11]From the 31st Survey of Credit Ratings conducted in November 2020.

[12]There are important others not discussed here. Formal positions, such as a seat on the board of directors or CEO appointment to a promising affiliate, and human resources are other example of a zero-sum, non-financial resource (Ocasio & Kim, 1999). Our interviewees also indicate control over agendas during executive meetings as a critical zero-sum resource.

visible changes in capital expenditure provides an important yet incomplete analysis of the scope of managers' political power and the internal capital market, which has contributed to the current dominance of the contingent view.[13] Our theory of managerial political power based on non-financial zero-sum resources is summarized in the following two propositions:

Proposition 1. *Politically powerful managers transfer resources to their division in the internal capital market at the cost of other divisions.*

Proposition 2. *The zero-sum dynamics of managerial political power exist even under the scrutiny of external stakeholders and financial slack.*

Testing the two propositions poses daunting empirical challenges. This requires looking inside the firm, collecting personnel records and institutional details of multiple divisions and their managers, and tracking their investment and value over time (Ganz & Schiff, 2020). We need to rule out financial winner-picking that also produces a zero-sum relation where a negative economic shock on one division benefits another by increasing its priority based on economic grounds. Powerful managers prefer to be appointed to a fast-growing division (e.g., Jeong, Kim, & Kim, 2022), and an isolated and exogenous shock that only affects a single manager while leaving the investment opportunities of his/her division and the broader firm unaffected is challenging to find. The recent legal turmoil at the Samsung group provides a suitable empirical context.

3 | EMPIRICAL CONTEXT: SAMSUNG BUSINESS GROUP

Business groups, as a specific type of multi-divisional organization, offer an important context to test our theory whereby divisional (or affiliate) level effects can be observed, which is rarely the case with typical multi-business firms. We examine Samsung, the largest Korean business group (or chaebol) with 16 public and 47 private affiliate firms that maintains an active internal capital market in a multi-divisional (or -affiliate) governance structure.[14] The affiliates vary in the extent of economic interdependence, managerial characteristics (e.g., owner-manager versus professional manager), the divergence in control and cashflow rights, and the intensity of external scrutiny, which provide a rich empirical context to test Proposition 2 that managerial political power plays a robust and constant role.

Appendix Figure A1 lists all public affiliates of Samsung along with their primary cross-ownership structure. Since its controversial merger with Cheil Industries in 2015, Samsung C&T (Construction and Trading Corporation) serves as the de-facto parent company that sits at the top of a pyramidal ownership structure by owning shares in the two most valuable affiliates:

[13]Drawing a close parallel to the proposed expansive scope of internal managerial political power, recent studies on the value of a firm's external political connections revise the view that political connections are valuable only in developing countries with weak institutions, such as Indonesia (Fisman, 2001), China (Jia et al., 2022), or developing economies. Acemoglu et al. (2016) find in the United States that share prices of financial firms with prior connections to Timothy Geithner showed a 6 % abnormal return upon his announcement as the nominee for Treasury Secretary. Amore and Bennedsen (2013) show that family connections to local politicians create significant value for a firm even in Denmark, which scores the lowest in the Corruption Perceptions Index (CPI).

[14]More formally, we define a business group as a set of formally independent firms managed by a common group of insiders.

Samsung Life Insurance and Samsung Electronics. The founder's son, Kun-Hee Lee (hereafter KH Lee), has been the chairman since 1987. However, the low ownership share in Samsung Electronics and the broader Samsung group by the Lee family has been persistently problematized from a political, legal, and governance standpoint and has exposed the family's control to the threat of hostile takeovers.

While the Samsung group represents a case of a single business group, it carries significant economic and theoretical relevance. Its combined market capitalization of 0.4 trillion dollars accounts for over 30% of the entire Korean stock market (KOSPI) and surpasses whole industries in revenue and value generated. Samsung was ranked the fourth most valuable brand globally in 2018, behind Amazon, Apple, and Google. As a research context, business groups and family firms are ubiquitous in Asia, Europe, Latin America, the Middle East (Khanna & Yafeh, 2007), and the United States (Villalonga & Amit, 2006) and have been central to the research on the internal capital market.

3.1 | Managerial political power: JY Lee, BJ Lee, and other managers

We first demonstrate the zero-sum dynamics (Proposition 1) in the context of two family managers and then generalize the findings to the broader top management team. Chairman KH Lee has three children with his wife Ra-Hee Hong: his eldest son JY Lee, first daughter BJ Lee, and second daughter SH Lee. JY and BJ have taken on separate managerial positions along the business line: JY attended Harvard Business School for a DBA degree but was called back to help manage Samsung group's recovery following the 1997 Asian Financial crisis before completing his degree. He became the president of Samsung Electronics in 2009 and vice chairman in 2013. BJ was educated in Korea and has managed the retail and distribution side of the group's businesses. She is currently the CEO of Hotel Shilla, one of the largest hotel chains in Korea and duty-free retailers in the world, and has served as an advisor for the trading division of Samsung C&T.[15]

In 2014, KH Lee suffered a heart attack and fell into a coma, leaving JY as "the presumed heir apparent" to the Samsung group until his passing on October 25, 2020.[16] In the years leading up to KH's hospitalization, JY was in the process of being installed as the day-to-day controlling owner-manager of the group, but KH Lee's sudden absence resulted in significant uncertainty about the final details of succession. BJ was also considered to be a potential successor, but several industry analysts questioned the seriousness of her candidacy because succession to a daughter is unusual in Korea, as in most countries around the world (Bennedsen, Nielsen, Pérez-González, & Wolfenzon, 2007). However, BJ has experience managing the broader portfolio of Samsung subsidiaries, and numerous media outlets have speculated on BJ being a potential replacement for her brother in response to the criminal indictments of JY.[17]

There are several interrelated yet distinct bases of BJ's and JY's political power that position them as the first and second most politically influential managers within the Samsung group, including their equity share and managerial positions, status and legitimacy rooted in their

[15]Refer to Appendix H for an in-depth discussion on the third child SH Lee.

[16]https://www.bloomberg.com/news/articles/2017-01-09/an-830-000-horse-a-presidential-scandal-and-samsung-succession.

[17]Her Forbes profile (https://www.forbes.com/profile/lee-boo-jin/#a2936824a16b) states that "with her brother embroiled in a bribery scandal, there has been speculation about Boo-Jin as a possible successor to the family empire." There is no such mention for her younger sister SH.

family lineage to the founder, and the loyalty of key executives.[18] JY's greater influence relative to BJ, aside from his position at the core affiliate Samsung Electronics, is partly based on his primogeniture and gender as the eldest son (Calabrò, Minichilli, Amore, & Brogi, 2018). There is no change in JY's and BJ's ownership and managerial positions throughout our sample period, and the loss of JY's political power stems from a negative shock to his informal bases of political power, especially status and legitimacy as the head of the Lee family and the heir to the group.

3.2 | The corruption charge against JY Lee

In November 2016, a special prosecutor was appointed to investigate a corruption scandal involving South Korea's President Geun-Hye Park. Among the multiple charges, one of the most serious allegations was that JY's donation to Park's sports foundation constituted a bribe in exchange for government support for the merger of Samsung C&T and Cheil Industries in 2015. Before the merger, NPS whose head is appointed by the president owned 11.61% of Samsung C&T, 5.04% of Cheil Industries, and 9.03% of Samsung Electronics, surpassing the combined shares of the Lee family as the single largest shareholder of Samsung group. Among others, American activist fund Elliott Management challenged the merger that positioned Samsung C&T as the group's holding company, arguing that the conversion ratio used for exchanging C&T and Cheil shares was unfair and expropriated Cheil's shareholders to benefit the Lee family, who held larger shares in Samsung C&T.[19]

At 13:00 on January 16, 2017 (Monday), the prosecution filed a corruption charge and petitioned for the arrest of JY. The charge eventually led to eight legal events, providing a series of negative and positive shocks on JY's standing as the de-facto heir of the Samsung group. A warrant judge typically reviews a petition for an arrest within 2–3 days of its filing. After its review, the petition was dismissed for lacking compelling need at around 02:00, January 19 (Thursday). The prosecution reapplied for an arrest warrant at 18:00, February 14 (Tuesday), which was approved at 05:00, February 17 (Friday). The first sentencing trial began at 14:30 on August 25 (Friday), and JY was sentenced to 5 years in prison. At the appeals court that opened at 14:00, February 5, 2018 (Monday), his sentence was reduced and replaced with 4 years of probation, effectively releasing him 353 days into his prison sentence at Seoul Detention Center. The prosecutor immediately appealed the case to the Supreme Court, which ruled that the case should be sent back to the appeals court on August 29, 2019 (Thursday). The appeals court sentenced JY to 2 years and 6 months on January 18, 2021 (Monday), and the case was closed as JY decided not to appeal.

Table 1 summarizes the sequence of legal events. Throughout the eight legal events, the direction of the court's rulings remained largely uncertain, and each legal event was highly anticipated and monitored by both domestic and foreign investors. For example, following the

[18]Finkelstein (1992) puts forth four bases of managerial power: structural (or positional), ownership, expert, and prestige. In our empirical analysis, the first three remain constant. With respect to the limited effect on formal positional power, we note that owner-managers in Korean business groups have engaged in "managing from prison" and returned to their management positions shortly after serving their sentences. Even in the case of his imprisonment, it was expected that JY would maintain operational control for Samsung Electronics, especially the appointment of key executives.

[19]Bloomberg reported: "...Elliott claims the government unfairly meddled in the deal, which led to a massive corruption scandal in the country." https://www.bloomberg.com/news/articles/2018-07-13/elliott-seeks-770-million-from-south-korea-in-samsung-fight.

TABLE 1 Dates of key legal events

Event		Direction of the shock to JY	Date	Time
1.	1st Petition for Warrant	Negative	January 16, 2017	Announced at 2:00 p.m.
2.	1st Warrant Hearing	Positive: Warrant denied	January 19, 2017	Announced at 2:00 a.m.
3.	2nd Petition for Warrant	Negative	February 14, 2017	Filed at 6:00 p.m.
4.	2nd Warrant Hearing	Negative: Warrant issued	February 17, 2017	Announced at 5:00 a.m.
5.	1st Sentencing Trial	Negative: Sentenced to 5 years in prison	August 25, 2017	Court opens at 2:30 p.m.
6.	Appeals Court	Positive: Reduced and suspended sentence	February 5, 2018	Court opens at 2:00 p.m.
7.	Supreme Court	Neutral: Case remanded and sent back to appeals court	August 29, 2019	Court opens at 2:01 p.m.
8.	Appeals Court	Negative: Sentenced to 2.5 years in prison	January 18, 2021	Court opens at 2:05 p.m.

issue of the arrest warrant on February 17, *Forbes* published an article titled: "Shocking Arrest Warrant Issued for Billionaire Samsung Head Jay Y. Lee."

We focus our analysis on the first six events that unfold over the 13 months between January 2017 and February 2018. This is due to the unusually long interval between the sixth and seventh events (18 months), which introduced several confounding shocks (e.g., Covid-19 pandemic). In addition, while JY firmly held onto his official position during the first six events, it was speculated and eventually decided that he would not renew his seat on Samsung Electronics' board of directors after the appeals court hearing (sixth event).

3.3 | Key affiliates

Samsung's sixteen public affiliates can be divided into four categories: (a) an affiliate managed by JY—Samsung Electronics, (b) an affiliate managed by BJ Lee—Hotel Shilla, (c) affiliates that are vertically related to Samsung Electronics, and (d) affiliates with limited managerial and economic ties to both JY and BJ. Affiliates in the (c) category include Samsung SDI, Samsung SDS, Samsung Engineering, and Samsung Electro-mechanics. Among other things, SDI manufactures batteries used in cell phones; SDS provides IT solutions and services; Electro-mechanics manufactures electronic components used in mobile phones and semiconductors.

3.4 | Hypotheses

In the context of the Samsung business group, the proposed zero-sum dynamics of managers' political power (Proposition 1) and its pervasive scope (Proposition 2) yield the following two hypotheses:

Hypothesis (H1). *A negative (positive) ruling on JY decreases (increases) the share price of Samsung Electronics.*

Hypothesis (H2). *A negative (positive) ruling on JY increases (decreases) the share price of Hotel Shilla.*

H1 tests whether JY's political power is sufficiently valuable to Samsung Electronics that its erosion from legal shocks will decrease Samsung Electronics' share prices. H2, which hypothesizes a negative coupling between JY and BJ and the benefits to Hotel Shilla from JY's loss of political power, is the central test of our theory that extends existing streams of research that predict a null or positive coupling.

Against Proposition 1, research on business groups and family firms suggests an opposite negative effect on Hotel Shilla from a negative ruling on JY. Affiliates share intangible and financial resources and cross-subsidize each other, which leads to a positive coupling in affiliates' share prices (Bae, Cheon, & Kang, 2008; Joe & Oh, 2018).[20] Research on family firms emphasizes solidarity and shared interests among family members (e.g., Jeong & Siegel, 2018). A negative shock on JY risks delegitimizing control by the Lee family altogether (Jonsson et al., 2009). This suggests that a negative shock on JY should have a null or negative effect on Hotel Shilla. Research on tunneling indicates that owner-managers of Korean business groups tunnel profits out of affiliate firms with low cash flow rights to those with high cash flow rights, expropriating outside investors for their private financial gain (Baek, Kang, & Lee, 2006). BJ's financial interest prioritizes the interest of Samsung Electronics through her equity share in its parent company (Samsung C&T) over Hotel Shilla, where her equity ownership is diluted to nearly zero after passing through layers of cross-ownership (see Appendix Figure A2).

Against Proposition 2, prior research on corporate governance and managerial politics suggests a null effect because internal financial slack and performance pressure from activist investors effectively suppress managerial politics. Samsung business group has been under extreme scrutiny by analysts, shareholders, and regulatory agencies, especially during JY's legal proceedings. Approximately 55% and 20% of Samsung Electronics's and Hotel Shilla's shares are held by foreign institutional investors. Also, both Samsung Electronics and Hotel Shilla enjoy ready access to the external capital market with excellent credit ratings that rival Korea's and China's national credit ratings (refer to Section A.1.2). In addition, the lack of direct cross-ownership and the long distance between Samsung Electronics and Hotel Shilla in the overall pyramidal structure makes it difficult to reallocate financial resources between them and suppresses financial winner-picking, which should lead to a null effect.

In contrast, our theory emphasizes the zero-sum dynamics and the potential upside to BJ that has received little attention. The diminished presence of her brother allows BJ to capture a larger share of the Samsung group's zero-sum resources and transfer value from the broader Samsung group to Hotel Shilla at the cost of Samsung Electronics.

[20]In our empirical context of Korean conglomerates, Bae et al. (2008) and Joe and Oh (2018) find a strong asymmetrical negative spillover where a negative event (e.g., credit rating downgrade) of an affiliate firm negatively affects the share prices of other affiliate firms, especially if it is driven by a leading firm of a business group (e.g., Samsung Electronics).

3.5 | Empirical strategy

In our baseline analysis, we track changes in share prices of Samsung Electronics and Hotel Shilla in response to the latest breaking news at a minute interval as well as a daily interval in a standard event-study design. The high-frequency analysis at the minute interval provides a rigorous empirical test, eliminating influence from any slower-moving macro-economic trends, such as the geo-political conflict with China in 2017 that negatively affected the entire Korean leisure and service sector and the boom in the electronics industry during our sample period (see Appendix I).

As a forward-looking measure, share prices are uniquely advantageous to tracking fluctuations in managerial political power and its value that do not involve immediate or visible resource reallocation and instead center on more favorable future allocations.[21] At the same time, a high-frequency analysis requires that events take place while the market is open to permit tracking reactions in share prices in real-time. It also requires that an event is monitored by at least a few investors. Beyond changes in share price, we further examine below if there are actual changes in inter-affiliate transactions consistent with shifts in BJ's managerial political power.

3.5.1 | Minute-level analysis

Of the six legal events, three took place while the stock market was open, allowing for minute-by-minute observations of market reactions to the latest legal developments released as breaking news.[22] The presiding judges forbade the public broadcasting of both trials, accepting JY's argument that the potential benefit to the public does not outweigh the potential damage to the accused. However, it was still an open trial as mandated by the Korean constitution, and journalists from several media outlets were physically present in the courtroom. They texted each sentence of the judge's opinion as it was being read out in the courtroom, some of which were then broadcasted as breaking news. The transcript was published afterward and scrutinized by liberal and conservative media that advocated for and against a heavier sentence, respectively.

Instead of using the final verdict from the trial as a binary shock (guilty vs. not guilty), we parse each sentence of the opinion delivered during the trial and identify a series of high-frequency shocks on JY and his eligibility as the perceived heir to the Samsung group. Most of the opinion does not contain new or meaningful information. For example, the opening sentence simply states the case number. It is followed by several sentences that summarize the key charges against JY already known to the public. However, some passages contain new information that hints at the direction and severity of the verdict. For example, the judge at the lower court delivered his first legal judgment on his 17th sentence, stating that "Jay-Yong Lee did not explicitly solicit former President Park for special favors during their private meeting." This positive development for JY is then followed by a series of less important sentences, whereby the judge elaborates on his reasoning behind the rejection of the specific charge for 5 min.

[21]Acemoglu et al. (2016) use share prices in assessing the value of external political connections. They document the increase in share prices of financial firms with prior connections to Timothy Geithner from his announcement as nominee for Treasury Secretary based on expectations of more favorable policy discretion in the future.

[22]Korea Exchange, where all of Samsung's public affiliates are listed, opens at 09:00 and closes at 15:30 (Korean local time).

We go through the entire transcript of the two trials and identify key passages that constitute a positive or negative shock through triangulation: (a) parsing the opinion sentence-by-sentence ourselves, (b) looking at the headlines of the breaking news, and (c) monitoring the coverage of the court's ruling by the media the following day. Our approach must yield objective identification of key sentences in the judge's ruling and not an ad-hoc selection that coincides with significant fluctuations in share prices. We find that the sentences we identify as critical were consistently covered as breaking news headlines across news channels (Yonhap News, Bloomberg, YTN, and JTBC) and discussed in the print media the next day.

Next, we identify when a specific sentence is disclosed to the market. Several news outlets provided real-time coverage of the three legal events that occurred during trading hours, and we establish a timeline by looking through multiple TV news channels, their headlines, and timestamps. We use 3-min intervals to balance the benefits of high-frequency analysis and the ability to ascertain the precise interval during which a specific legal passage is delivered to the public. Appendix B details the procedure.

3.5.2 | Daily returns

We follow the standard procedure in calculating daily abnormal returns, as outlined in Acemoglu et al. (2016) and detailed in Appendix C.

3.6 | Data

The intraday share prices are obtained from Bloomberg. To identify the minute at which specific negative and positive news on JY is disclosed to the market, we rely on breaking news from the Yonhap News channel (Reuters equivalent of South Korea), typically first displayed as news alerts on the bottom of the screen and verbalized by the anchor shortly afterward. We rely on Yonhap News as the primary source because it displays the time of the day on the lower-left corner of the screen, providing a clear timestamp for each headline. The major developments from the appeals court hearing were also tweeted approximately in real-time on Bloomberg's Twitter feed with multiple updates every minute, providing an alternative source for establishing the timeline. Appendix D provides specific examples that illustrate the methods used for identifying the time of the news.

4 | EMPIRICAL RESULTS

4.1 | Market response to breaking news

4.1.1 | The lower court (August 25, 2017)

According to the filing, the special prosecutor sought 12 years of jail time for JY on five counts: bribing President Park, embezzling, wrongfully transferring assets overseas, hiding the proceeds of a crime, and committing perjury (Figure 1a). The court opened at 14:30. The sentencing consisted of three parts. From 14:30–14:34, the judge read through the case number and specific charges filed against JY. Consistent with the lack of meaningful new information, both SEC

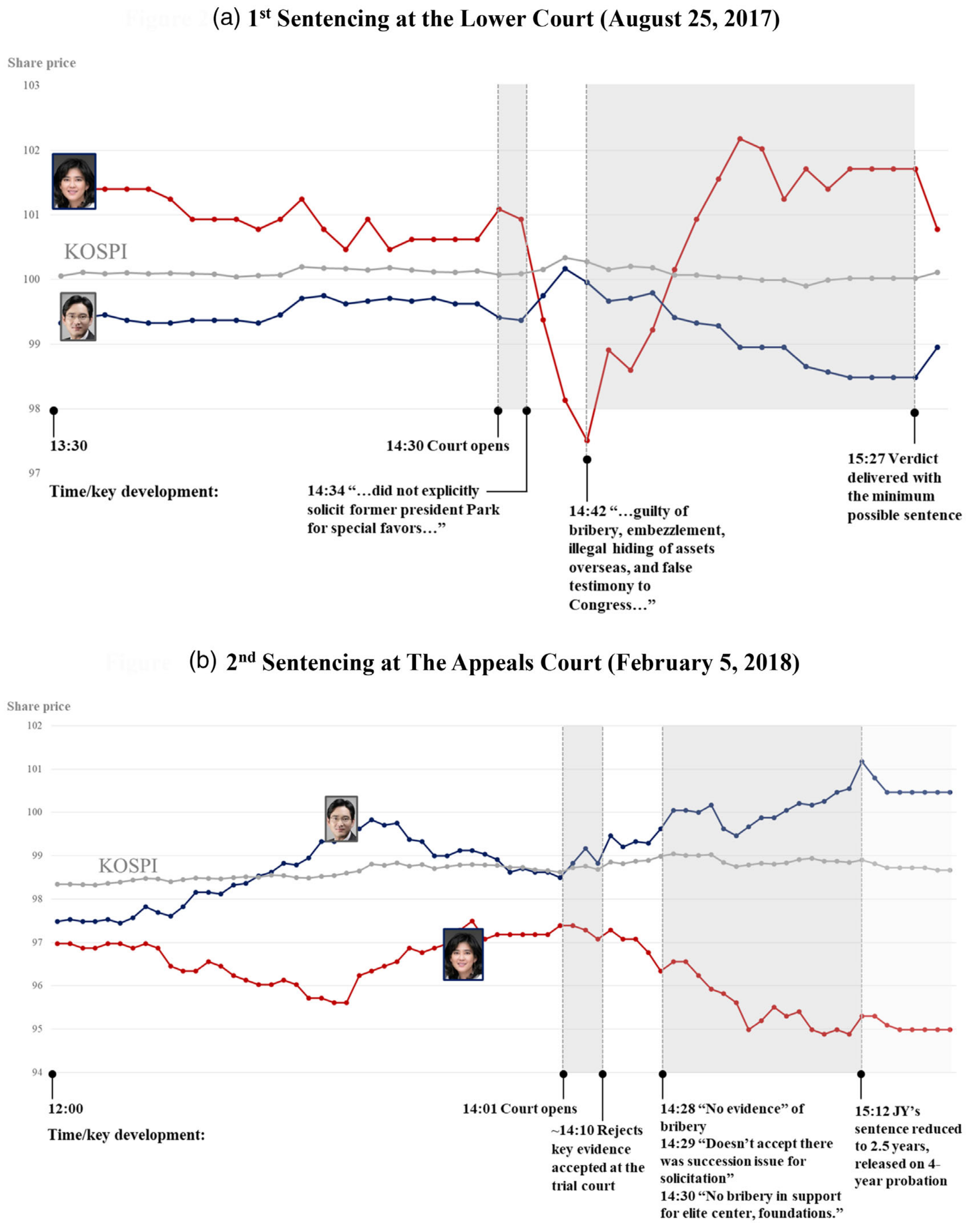

FIGURE 1 We parse the verdict delivered during the trial and link each sentence to 3 minute-level shifts in share prices of Samsung Electronics, Hotel Shilla, and the Korea Composite Stock Price Index (KOSPI). This high-frequency analysis, combined with unexpected shocks opposite in direction, isolates managerial political power as the underlying mechanism.

and HTS showed little movement. At 14:34, the judge ruled that "the court did not find that Jay-Yong Lee explicitly solicited former President Park for special favors during their private meeting," and "from a legal standpoint, it is difficult to ascertain whether there was even an implicit or indirect request." The market immediately reacted to the positive development for JY, driving down HTS by 3.4% while driving SEC up by 0.6% (vs. 0.18% gain in the KOSPI) between 14:34 and 14:42. Starting at 14:42; however, there was a dramatic reversal in the direction of the ruling. The judge then stated that JY was guilty of bribery, embezzlement, illegal hiding of assets overseas, and false testimony to Congress in a series of short sentences detailing each charge. While the actual sentencing had not yet been delivered, the court's acceptance of these charges already implied minimum sentencing of 5 years and indicated that JY would face actual jail time. In response to this sudden reversal, between 14:42 and 15:06, HTS and SEC experienced a gain and loss of 4.5% and 1.0%, respectively (vs. a loss of −0.28% for KOSPI).

The actual sentence for JY was delivered at 15:26, just 4 min before the closing of the stock market. The 5-year sentence, significantly lower than the 12 years sought by the prosecution and the most lenient possible given the charges accepted just 40 min earlier, actually sent a positive signal to the market. In Korea, sentencing for powerful business executives has historically followed the so-called 3–5 rule. They are first sentenced to 5 years at the lower court, but the sentence is subsequently reduced to 3 years at the appeals court. A sentence of up to 3 years can be replaced with probation without actual jail time, allowing for an immediate release. Reflecting this positive signal and the expectation that JY's legal fate would follow the 3–5 rule, SEC recorded a gain of 0.46%, while HTS saw a loss of 0.93% in the last 3 min of the market. Overall, the court's ruling was negative for JY, and the market closed with HTS trading 0.78% higher, SEC 1.05% lower, and the overall market 0.11% higher.

These empirical patterns provide highly nuanced and robust support for H1 and H2. The opinion comprises a series of positive and negative shocks that were introduced over the course of 57 min. The contents of the opinion dramatically oscillated between being positive and negative to JY and generated rapid shifts in his perceived standing at the Samsung group. The unusual swings and reversals in the share prices provide concrete evidence for the proposed zero-sum dynamics while ruling out alternative explanations; it is implausible that Samsung Electronics and Hotel Shilla experienced a series of directionally opposite economic shocks that coincide with minute-by-minute developments in JY's trial. It is also equally unlikely that there were changes in Samsung's ownership structure, governance, top management team, and any other institutional environment that affected SEC and HTS in the opposite direction, leaving shifts in political power as the most viable explanation for these unusual swings in share prices.

4.1.2 | The appeals court (February 5, 2018)

The court opened at 14:01. The early part of the trial again focused on summarizing the charges against JY with little to no new information (Figure 1b). Around 14:10, however, the judge rejected the validity of key evidence (a memo taken by Geun-Hye Park's assistant on her conversation with JY) that had been accepted at the lower court. At 14:28, Bloomberg tweeted: the judge ruled that "there is 'no evidence' Lee's alleged bribes were for the purpose of succession" (14:28:55); "it doesn't accept there was succession issue for solicitation" (14:29:18); and "there is 'no bribery in support for the elite center, foundations'" (14:30:52). While the verdict was not delivered for another 42 min, the rejection of these charges that had been accepted at the lower court already made clear that JY's sentence would be significantly reduced. The final verdict was delivered at 15:12. JY's sentence was reduced from 5 years to 2.5 years and replaced with 4 years of probation. This ruling immediately released JY from the prison and was heavily criticized by the liberal media and political pundits for adding another precedent to the "3–5 rule." Overall, unlike the previous hearing at the lower court, the legal opinion did not contain any dramatic reversals and consisted of a series of positive shocks for JY.

Both HTS and SEC remained relatively stable during the first customary part of the hearing (14:00–14:09), with HTS losing 0.31% and SEC gaining 0.33%.[23] Starting at 14:12, however, the market quickly incorporated the judge's rejection of key evidence against JY with gains for SEC and loss of HTS. Following the series of positive rulings between 14:28 and 14:30, there was a loss of 1.57% for HTS between 14:30 and 14:45. In direct contrast, SEC experienced a gradual gain until the market closed. Overall, the day closed with Hotel Shilla trading 5.01% lower, Samsung Electronics 0.46% higher, and the overall KOSPI 1.33% lower.

4.1.3 | Four other events

We provide an analysis of the first petition for an arrest warrant and three other legal events that occurred during off-hours in Appendix E to conserve space. These events show a highly consistent pattern in support of H1 and H2.

4.2 | Daily returns

Next, we examine 1-day abnormal returns in a single-firm event study design (e.g., Gelbach, Helland, & Klick, 2013; Lys & Vincent, 1995).[24] When the nominal returns are adjusted for industry or market returns, this pooled OLS regression provides a difference-in-differences estimation where the first difference compares within-firm differences in days with and without a shock, and the second difference comes from subtracting simultaneous changes in the relevant benchmark indexes.[25]

In Table 2, Columns 1–3, we find a negative (positive) effect on SEC's share price from negative (positive) legal shocks on JY. In Column 3 with market-adjusted abnormal returns as the dependent variable, SEC drops by 0.9% in response to the negative news but increases by 1.9% in response to the positive news. The loss of 3.6% (from four negative shocks) and recovery of 3.8% (from two positive shocks) are consistent with JY's neutral legal position at the end of our sample period when he awaited the Supreme Court hearing. Hotel Shilla's share price shows an opposite pattern but with movements that are approximately twice in magnitude, consistent with its smaller market capitalization. In Column 6 with market-adjusted abnormal returns as

[23]KOSPI was relatively volatile leading up to the trial. The S&P 500 had closed with a loss of 2.1% earlier on Friday due to the fear of an interest rate hike. The Korean stock market opened on Monday with a loss of 3.48, 1.25, and 1.75% for SEC, HTS, and KOSPI in the first 3 min, respectively. SEC's greater loss is consistent with its greater exposure to the US market, which provides approximately 30% of its revenue.

[24]It is customary to check robustness to using a 3-day window, but this is not feasible in our empirical context because some of the events occur within 2 days of each other. We find consistent results using [−1,1] as the alternative event window and using market or sector-adjusted returns (Appendix C).

[25]Because the returns may be correlated over time and distributed non-normally, we use a non-parametric bootstrapping approach (with 10,000 repetitions) to estimate the probability that the abnormal returns differ from zero (Hein & Westfall, 2004).

TABLE 2 Market reactions to legal shocks to JY

	Samsung electronics			Hotel Shilla			
DV: Stock returns	**Nominal (1)**	**Industry adjusted (2)**	**Market adjusted (3)**	**Nominal (4)**	**Industry adjusted (5)**	**Market adjusted (6)**	**SEC adjusted (7)**
Positive shock on JY (1.19/2.25 = 1)	0.008 [0.004]	0.015 [0.002]	0.019 [0.005]	−0.051 [0.001]	−0.049 [0.002]	−0.049 [0.002]	−0.051 [0.001]
Negative shock on JY (1.16/2.14/2.17/8.25 = 1)	−0.009 [0.005]	−0.009 [0.003]	−0.009 [0.003]	0.017 [0.007]	0.022 [0.004]	0.020 [0.005]	0.018 [0.007]
Constant	0.001 [0.001]	0.001 [0.001]	0.001 [0.000]	0.001 [0.001]	0.001 [0.001]	0.001 [0.001]	0.001 [0.001]
R-squared	.003	.007	.010	.018	.022	.021	.018
Obs.	606	606	606	610	610	610	606

Note: Bootstrapped standard errors are provided in brackets.

TABLE 3 Extension beyond JY-BJ to other executives

	Market adjusted returns			
	Larger than SEC	Smaller than SEC		
DV: JY's share	SDS (1)	Electro-mechanics (2)	SDI (3)	Engineering (4)
Positive shock on JY (1.19/2.25 = 1)	0.020 [0.012]	−0.015 [0.001]	−0.045 [0.019]	−0.028 [0.002]
Negative shock on JY (1.16/2.14/2.17/8.25 = 1)	−0.006 [0.002]	0.007 [0.004]	−0.002 [0.008]	−0.006 [0.018]
Constant	0.000 [0.001]	0.001 [0.001]	0.001 [0.001]	0.000 [0.001]
R-squared	.004	.003	.013	.004
Obs.	610	610	610	599

Note: Bootstrapped standard errors are provided in brackets.

the dependent variable, HTS on average gains 2.0% on days of negative legal shocks to JY and loses 4.9% on days of positive legal shocks. The overall loss of 8.0% and gain of 9.8% are again close to each other in magnitude. Column 7 uses the SEC as the benchmark. This controls for any systematic correlation in the share prices of the two firms and yields consistent results.

In Appendix G, as alternative control groups, we repeat the analysis but with respect to Samsung affiliates with minimal managerial involvement or ownership by JY and BJ as well as Samsung Electronics' two primary domestic rivals, LG Electronics and SK Hynix. To the extent that the negative coupling between SEC and HTS (H2) is driven by the manager-specific reallocation of political power within the Samsung group, we should observe a weak or null effect on them. We find consistently small and statistically null results, which help to rule out economic considerations affecting Korea or Samsung group at large as driving our results.

4.3 | Extension to non-family managers and other affiliates

Next, we examine whether the zero-sum political dynamics generalize beyond BJ and HTS to other affiliates managed by non-family executives. Table 3 examines 1-day abnormal returns of four affiliates that are vertically related to Samsung Electronics: Samsung SDS, Samsung Electro-Mechanics, Samsung SDI, and Samsung Engineering. These affiliates maintain close business relations with SEC. Supplying components and services to Samsung Electronics represents 20–50% of their overall revenue, and their performance depends critically on negotiating a higher supplier price against SEC.

Our research design takes advantage of the varying degrees of financial ownership by JY and the Lee family in the four affiliates. Relative to their share in SEC (5.8%), the direct equity ownership of JY and the Lee family is significantly lower in Electro-Mechanics (0.0%), SDI (0.0%), and Engineering (1.54%) but higher in SDS (17.0%). As a result, SDS negotiates with SEC with JY's financial and managerial interest on its side and has most likely benefited from JY's political power within the group, whereas the three other affiliates negotiate with SEC against JY. The CEOs of Samsung SDS, SDI, and Engineering are professional managers with no familial ties to JY but had been divisional CEOs at Samsung Electronics before their promotion to the affiliate CEO position—almost certainly with JY's approval. To the extent that JY's involvement in SEC is reduced and permits the affiliate CEOs to negotiate with someone lower in political power, we expect the negative shocks on JY to benefit the three affiliates. In contrast, we expect JY's decreased presence to hurt SDS, which has benefited from JY's political power in negotiating against SEC and its various divisions.

We find support for the predicted contrasting effects, which provide highly nuanced support for H2. Even though the four affiliates are closely related in their business and interactions with Samsung Electronics, the share prices of SDS gain on the positive shocks to JY by 2.0%, whereas the share prices of the three other affiliates drop by 1.5–4.5%. The response to the negative shocks shows a consistent but weaker pattern. There is a loss of 0.6% for SDS and a gain of 0.7% for Electro-Mechanics but no significant effect on SDI and Engineering. These divergent market reactions cannot be explained without considering the influence of JY's political power in the internal capital market. In other words, the zero-sum dynamics of political power provide a unique explanation for these otherwise puzzling patterns. We provide another instance of reallocation across the four affiliates from a shift in JY's political power based on an earlier non-judicial event in Section E.1.3.

These results also help to rule out two important alternative explanations that could lead to H2: (a) there could be fear that a successor to JY will be of significantly lower quality, increasing relative economic prospects for other Samsung affiliates (H2); (b) BJ could consider splitting off Hotel Shilla from the broader Samsung group for increased autonomy even at a financial cost, but JY's absence decreases its likelihood. The divergent pattern with respect to SDS helps to rule out these alternative explanations. If this were the case, we should observe a positive or null effect on SDS from negative shocks on JY rather than the observed negative effect.

4.4 | Analysis of inter-affiliate transactions

Beyond changes in share prices, we next examine whether there is an actual *re*-allocation of internal resources that coincides with the timing of JY's trial and fluctuations in his political power. We look at inter-affiliate transactions reported in the Notes section of quarterly 10Q and annual 10K filings and conduct a "forensic" analysis that uncovers behaviors that managers would rather conceal (Zitzewitz, 2012).

Comparing the yearly growth rates in revenue from non-affiliates and affiliates in Figure 2a, we find that Hotel Shilla's revenue from Samsung affiliates shows a discontinuous increase following the negative legal shocks to JY in 2017. The growth rate is higher for non-affiliates prior to the legal turmoil in 2016. However, the pattern reverses in 2017. The affiliate growth shows a drastic jump from 1.8 to 19.0% in 2017, even as non-affiliate growth declines from 11.7 to 5.4%. To strengthen the circumstantial evidence, we next look at the quarterly growth rates in Figure 2b. The drastic growth in 2017 commences during the second quarter of 2017, immediately after the timing of JY's first arrest (February 17, 2017).

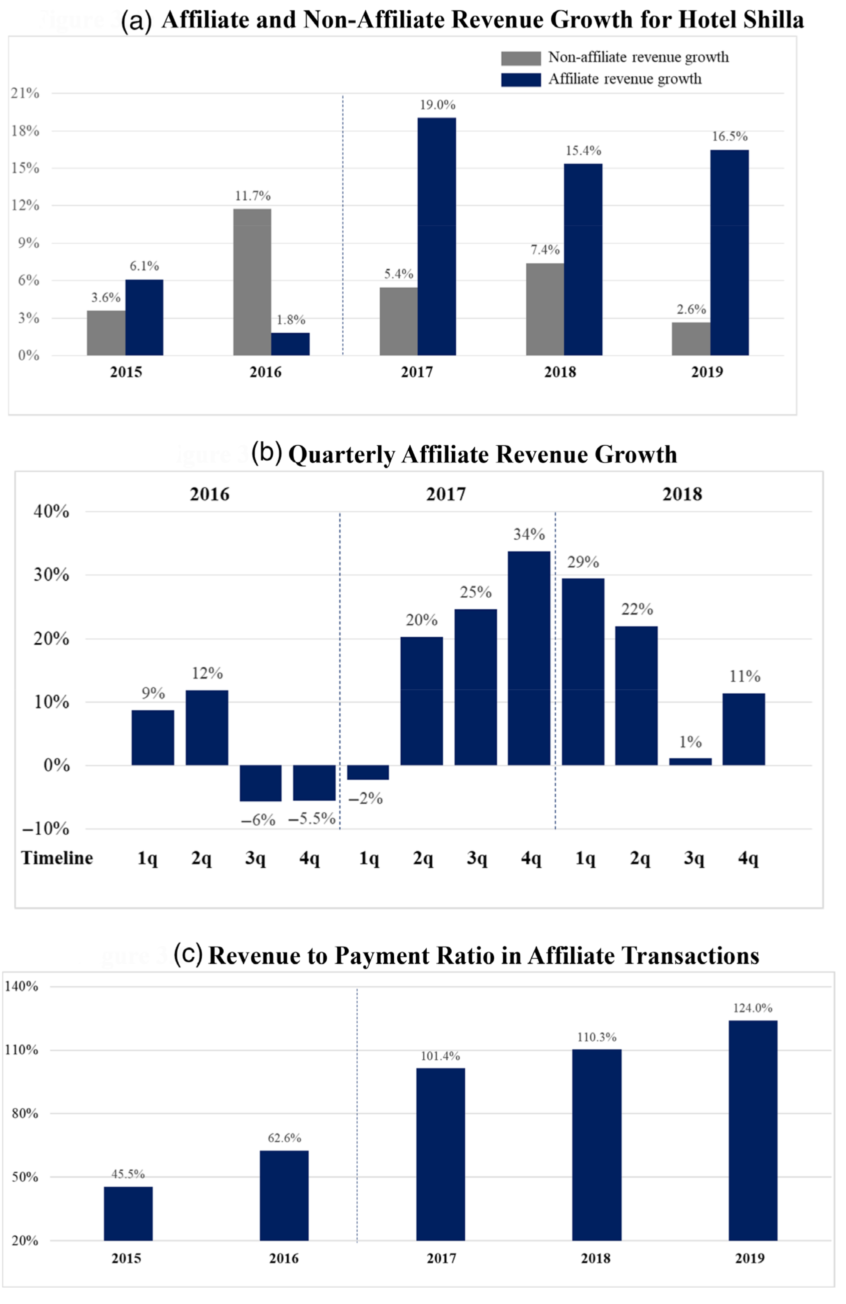

FIGURE 2 We examine the Notes section of annual and quarterly reports (10k, 10q filings) and uncover unusual changes in inter-affiliate transactions that favor BJ and Hotel Shilla around JY's trial dates.

Lastly, we show in Figure 2c that there is a significant jump in the affiliate revenue to payment ratio, akin to the export–import ratio used to track trade flows. Negotiating more favorable trade terms (or transfer pricing) redistributes revenues and profits without affecting (short-term) investments. The ratio jumps to 101.4% in 2017 from 45.5 and 62.6% in 2015 and 2016, indicating more favorable trade terms for Hotel Shilla. The unusual and discontinuous changes provide evidence of internal reallocation in resources consistent with BJ's increased political power at the cost of other paying affiliates and complement our earlier analysis based on share prices.

4.5 | Long-term investment

In Section A.1.3, we detail the timeline of SEC's major investments and the effects of JY's absence by interviewing former Samsung employees and working through media reports and biographies of former Samsung executives. It becomes apparent that Samsung Electronics' investment decisions, especially those that require cross-affiliate coordination, were put on hold or resumed based on JY's legal developments. We detail the timeline of Hotel Shilla's investment and media reports on BY's role in Section A.1.4.

4.6 | Frequency analysis of textual posts in stock market forums

Finally, in Appendix F, we examine the frequency of textual posts on the largest stock market online discussion forum in Korea (Naver Finance) and show that investors of HTS and SEC pay attention to BJ on the dates of JY's trial, even though JY and BJ do not play any formal role in the management of each other's firm. We find that investors are acutely aware of the zero-sum political dynamics between JY and BJ, carefully monitor the latest developments in JY's trial, and make buy and sell decisions based on JY's legal (mis)fortunes.

4.7 | Limitations

Our empirical setting, along with its unique strengths, has important limitations. Despite its quantitative components and analyses across multiple affiliates and managers, this is essentially a case study of a single business group. Samsung presents a "revelatory" case (Eisenhardt & Graebner, 2007; Yin, 2003) that reveals contra-evidence to revisit and extend prior theories. Generalizing our findings to business groups operating in different institutional contexts requires much caution (Yiu, Lu, Bruton, & Hoskisson, 2007).

5 | DISCUSSION AND CONCLUSION

Managerial politics present one of the most vexing yet persistent reality of organizational life. It is often experienced daily, for example, in requesting a larger budget, advocating and rejecting investment projects, and negotiating with other divisions for less work or a greater share of rewards. This study proposes that managerial politics is an intrinsic and constant feature of the internal capital market characterized by resource scarcity and allocative uncertainty.

The zero-sum dynamics in the allocation of firm-specific resources provide a theoretical basis for understanding why the demand for economic efficiency and objectivity cannot fully discipline and substitute managerial politics in the internal capital market. The premise that the internal competition for resources unfolds across two distinct domains—the economic domain of financial resources based on financial winner-picking (Stein, 1997) and the political domain of non-financial resources based on political winner-picking—has important implications to several streams of research.

5.1 | Contribution, implications, and extensions

5.1.1 | Efficiency of internal capital market

The advantages and disadvantages of the internal capital market have been a subject of intense and continued interest (e.g., Chandler, 1962; Feldman, 2021; Khanna & Yafeh, 2007; Stein, 1997; Williamson, 1975). We caution against viewing managerial politics as inserting a clear net negative effect on firm value based on short-term investment patterns, in particular over- or under-investment relative to Tobin's Q that reflects not only growth potential but also the value of managerial political power. Moreover, managerial politics often centers on non-financial resources and their investments into new business development with uncertain returns and counter-factual allocation (Bettis, 2017).

According to one Samsung executive, "JY's political power lubricates moving group resources around and supports fast and aggressive investments." This positive assessment is in line with Pfeffer's view (1992) that politics is necessary for effective change and adaptation. While we formulate managerial politics as being focused on distributing existing resources and their opportunity cost (i.e., splitting the pie), managerial politics may also help firms create new resources and opportunities (i.e., increasing the pie).[26] The continued success of business groups against the earlier prediction that the development of external factor markets would diminish their significance (Carney et al., 2011) has raised questions about the sources of their strategic advantages. The potential upsides of managerial politics as an allocation and coordination device remain an important yet little examined area of research.

5.1.2 | Inter-divisional relations

In acquiring resources to survive and grow, managers must consider not only external product market competitors but also the internal competition against other divisions. In the economic domain based on financial winner-picking, the destructive aspects of internal competition, for example, the incentive to withhold cooperation and information, are checked by business complementarity and the risk of negative spillover. In contrast, in the domain of managerial political power, the incentive for unmitigated rivalry may intensify with economic relatedness, as managers increasingly compete for the same set of zero-sum resources (e.g., transfer pricing). We expect a "frenemy" relation (Tsai, 2002), emphasizing the competitive relation with respect to zero-sum non-financial resources and the cooperative relation with respect to financial and other non-exclusionary resources.

We also expect political and financial winner-picking to differ in their target of competitive interactions. Consider a business group with five affiliates—*A*, *B*, *C*, *D*, and *E*—in the descending order of NPV and also managerial power. A positive *economic* shock that improves the productivity

[26]In a similar vein, research on external political connections has long explored the "greasing-the-wheel" hypothesis (e.g., Méon & Sekkat, 2005) that politics lower coordination costs and facilitate access to shared resources.

of *B* above *A* should have the least effect on *A*, as the increased investment for *A* is funded by diverting resources away from the lowest NPV affiliate *E*. In contrast, a positive *political* shock to *B* should primarily affect *A* or the counterpart to a transaction with limited consequences for *D* and *E*. In other words, financial winner-picking induces affiliates to compete against the lowest funding threshold, whereas political winner-picking creates an upward rivalry.

5.1.3 | Business groups and family businesses

With respect to family-owned firms and business groups, our findings revise the prevailing assumption that family members comprise a homogeneous group with shared status, identity, and financial interests and reveal a more complex relation. The kinship likely both intensifies and lessens the political competition. On the one hand, family members, especially siblings, are close substitutes with respect to legitimacy and status based on their lineage, which can intensify rivalry. On the other hand, they share reputation and other intangible resources with a significant potential for negative spillover. We expect that appointing siblings along clearly separated lines of businesses creates an organizational and managerial distance that can curb intra-family competition and the potential for negative spillover. We expect a more intense rivalry had BJ been managing Samsung SDS or other electronics-related affiliates.

5.1.4 | Tunneling and corporate governance

The negative assessment of managerial politics stems in significant part from the suspicion that it tunnels value away from minority shareholders to controlling stakeholders. Our findings reveal a more nuanced and complex nature of tunneling that trades off different components of owner-managers' interests. Looking at financial interest reveals only a partial picture. BJ is the CEO of Hotel Shilla but holds close to zero equity, whereas she holds equity in Samsung Electronics (through Samsung C&T) but no managerial position. In her dual roles as a manager and an owner, the stock market expected BJ to prioritize her managerial interest and transfer value to Hotel Shilla against her own financial and familial interests, presenting a case of "reverse" financial tunneling.

The reverse tunneling is consistent with socioemotional wealth (SEW) research showing that family managers sometimes pursue SEW even at financial cost (e.g., Gómez-Mejía et al., 2007; Jeong et al., 2022). One unique aspect of our findings is that zero-sum resources create the potential for conflict even among managers with close kinship. How family owner-managers balance the divergence in their multiplex interests as manager, owner, and a family member promises to be an interesting area of future research (Ingram & Zou, 2008; Kuwabara, Luo, & Sheldon, 2010).

6 | CONCLUSION

Much remains to be done to understand the influence of managers' political power in the internal capital market. Despite its pervasiveness and daily encounters, managerial political power remains little examined in terms of its basic characteristics and effects on firm performance with "too few facts" (Glaser et al., 2013, p. 1578). The recent resurgence of research on the internal capital market provides fertile ground to make theoretical and empirical inroads. We offer this study as an early step and hope that its shortcomings will stimulate future research.

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APPENDIX A

A.1 | KEY BACKGROUND INFORMATION

A.1.1. | Samsung business group

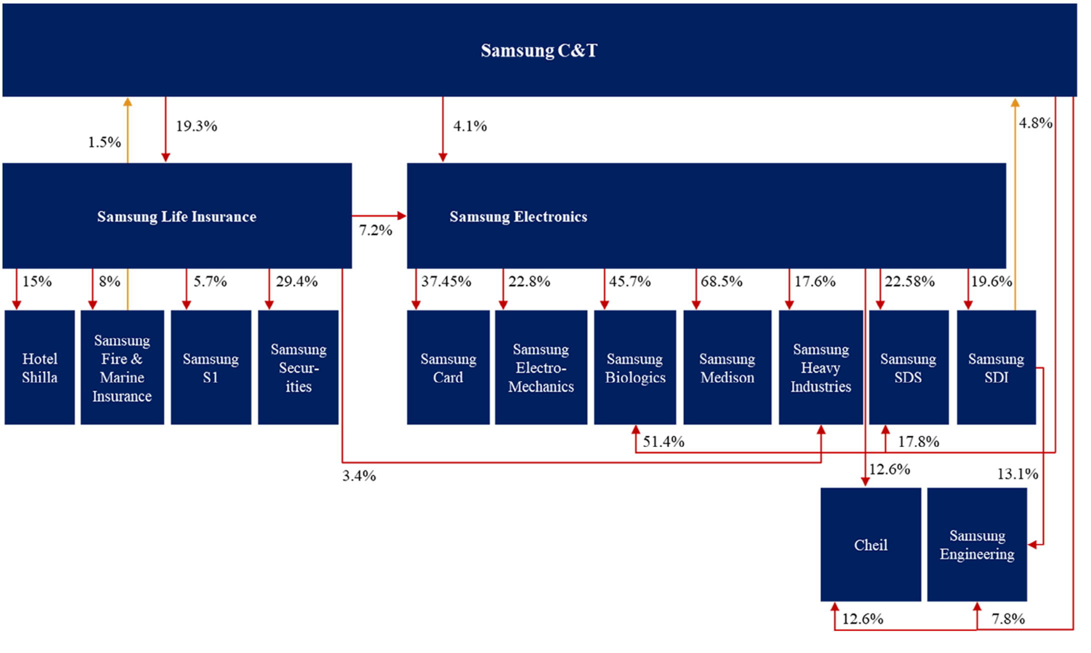


FIGURE A1 Samsung group's primary cross-ownership structure (2017)

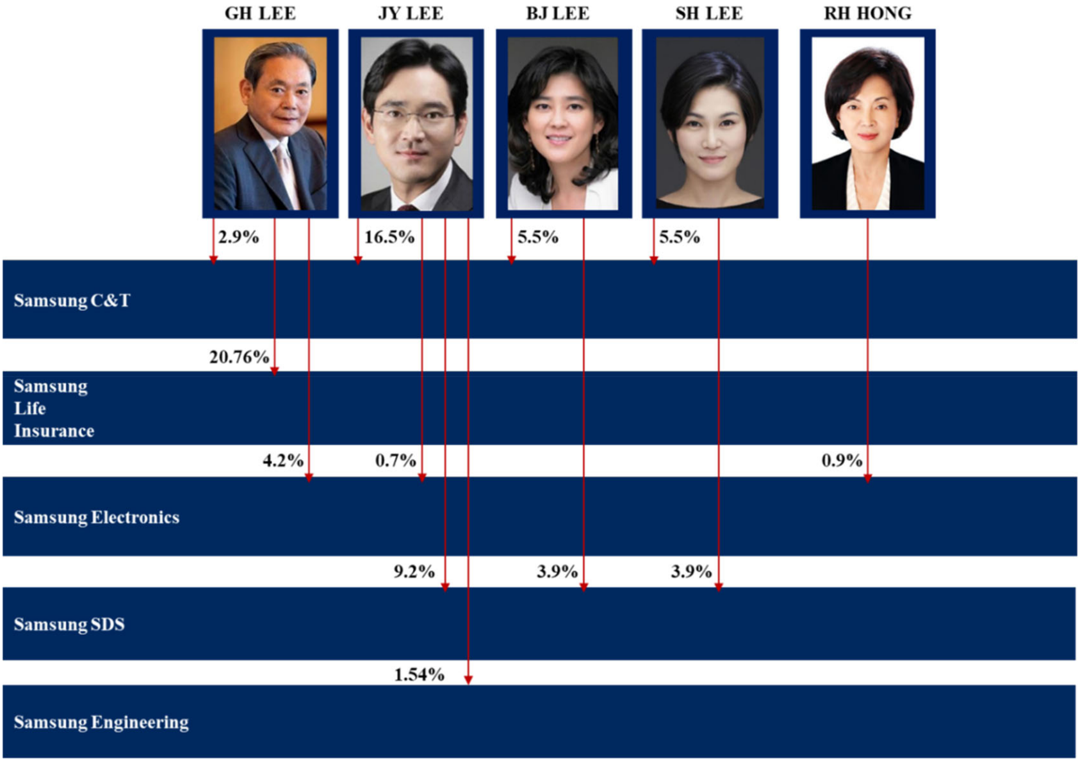


FIGURE A2 Lee family ownership share (2017)

A.1.2. | Samsung business group financial slack (2017–2019)

We here provide more detailed information showing that Samsung Electronics and Hotel Shilla are not capital constrained.

First, Hotel Shilla has the second-highest credit rating (AA) in Korea's credit market with a "stable" outlook (see table 1 of Joe & Oh, 2018). Samsung has an Aa3 rating from Moody's (note below that France and South Korea's national credit ratings are Aa2, and China's is Aa3). Second, both firms pay dividends, which can be paused in case of financial distress (Deangelo & Deangelo, 1990). Third, in commenting on Shilla's high credit rating, *Korea Ratings* comments that "Hotel Shilla owns a substantive share of Samsung affiliate equity as well as the real estate of significant value." For Samsung Electronics, its net income was 43B and 41B USD in 2018 and 2017, making it one of the most profitable tech firms in the world.[27] Hotel Shilla also remained profitable during our sample window (2016–2019) before making a loss in 2020 due to lost sales from the pandemic.[28] However, Hotel Shilla was also able to issue new debt "in overwhelming response" during the peak of the pandemic even as other Korean firms struggled (Figure A3).[29]

[27]https://www.wsj.com/market-data/quotes/SSNLF/financials/annual/income-statement
[28]https://www.wsj.com/market-data/quotes/KR/008770/financials/annual/income-statement
[29]https://pulsenews.co.kr/view.php?year=2020&no=404982

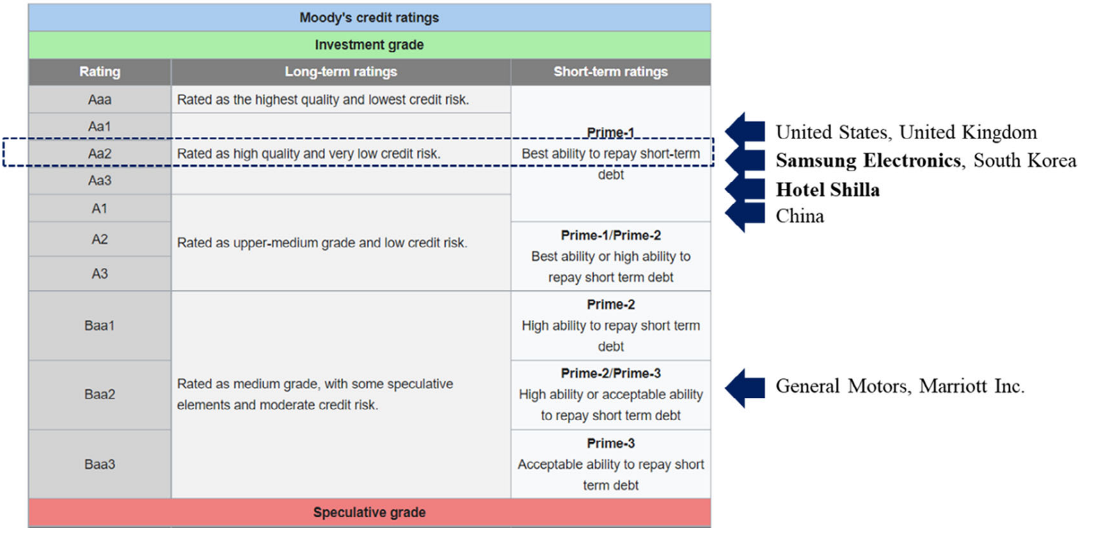


FIGURE A3 Samsung Electronics and Hotel Shilla: Credit rating. * Moody's Credit ratings from https://en.wikipedia.org/wiki/Moody%27s_Investors_Service.

A.1.3. | Timeline of key investments announced by JY

We detail the timeline of SEC's major investments and the effects of JY's absence by interviewing former Samsung employees and working through media reports and biographies of former Samsung executives. It becomes quickly apparent that Samsung Electronics' investments are closely tied to JY's legal fortunes. The events from July 10, 2018, to August 8, 2018, and August 13, 2021, to August 24, 2021, are particularly telling.

2016.11.14	Acquisition of Harman (USD 8B); averages 5 acquisitions per year between 2015-2017; zero 10M+ acquisitions between 2018-2021 due to "uncertainty around JY's future."[1]
2017	Legal shocks / JY in prison (7.25) / CEO promotions delayed from 2016.12 to 2017.3
2018.2.5	Released from the prison
2018.7.10	President Moon meets JY for the first time, asks for domestic investment and job creation
2018.8.8 (**1 month**)	JY announces USD ~150B investment plan in AI, biotechnology, and automotive electric parts
2019.4.24	JY announces Samsung Electronics will invest 110B in non-memory "system" chips by 2030
2021.1.18	2nd imprisonment after appeals court ruling
2021.5.24	Samsung announces USD ~18B (foundry) semiconductor investment in US but does not specify the final investment site
2021.8.13	JY released on a presidential pardon / visits Samsung HQ immediately upon release
2021.8.24 (**11 days**)	JY announces USD ~200B investment plan in semiconductors and biotechnology
2021.11.24	Announces Taylor, Texas as the investment site "based on JY's decision – who directly communicated with the White House."[2]

Attributing these investment decisions to JY requires much caution. In requesting lighter sentencing, Samsung's legal team repeatedly pointed to JY's role in key investment decisions and their positive effects on the broader Korean economy, including job creation. It is plausible that Samsung merely delays the announcements of pre-planned investments for JY to take credit. However, interviews with ex-Samsung employees involved with the strategic planning note that: (regarding August 24, 2021 announcements) "The finance team kept updating the plan. The ~200B announcement was larger than what we had in mind initially."

As another example, Samsung Electronics announced on November 23, 2021, that it will invest $17 billion to open a new plant in Taylor, Texas, over other potential sites in Texas, Arizona, and New York.[30] The announcement was initially supposed to be made in 2020 but delayed several times—which is attributed to JY's absence.[31] Most tellingly, Samsung Electronics has been holding onto USD >100B cash to make acquisitions in new strategic growth areas (AI, biotechnology, and automotive electric parts). However, after the acquisition of Harman (~8B) in 2016, Samsung Electronics has not engaged in any meaningful acquisition (>10M) between 2017 and 2021 due to "uncertainty around JY's future."[32] With the release of JY in August 2021, Samsung Electronics has announced a series of plans for multiple large-scale acquisitions. According to one Samsung executive, "JY's political power lubricates moving group resources around and supports fast and aggressive investments."

An autobiography by Chang-Gyu Hwang, a former CEO of Samsung Electronics, also provides an interesting anecdote. In December 2004, Steve Jobs demanded that Samsung supply NAND-flash for iPods at close to zero profit margin. Hwang believed it would be worthwhile in the long run but had to seek JY's approval, who was merely a vice-president at the time.[33]

A.1.4. | Timeline of key investments announced by BJ

A senior manager at Hotel Shilla commented that Hotel Shilla continued to invest through the THAAD and Covid-19 crises (Appendix I) that forced peer firms to pause almost all investments. This confidence stems in part from the belief that "there is a close to zero chance that Hotel Shilla goes bankrupt," partly due to BJ's personal wealth (~5B) but also the expectation that "the Samsung group will not let BJ look bad."

As a case in point, an analyst at the Korea Investors Service (Moody's equivalent of Korea) justified Hotel Shilla's high credit rating despite industry downturn from Covid-19 by noting that: "Because Hotel Shilla is directly managed by a member of the Lee family, we expect a strong willingness to provide financial support by the Samsung group... its credit rating is therefore raised by one notch by taking into consideration *the likelihood of financial support in case of financial distress* (emphasis added)."[34]

[30]https://www.nytimes.com/2021/11/23/technology/samsung-chip-plant-texas.html

[31]https://mobile.newsis.com/view.html?ar_id=NISX20210614_0001475188#_enliple

[32]https://www.sedaily.com/NewsVIew/22HAYK8QJ8

[33]JY was one of the few "business associates" that was invited to Steve Job's burial ceremony.

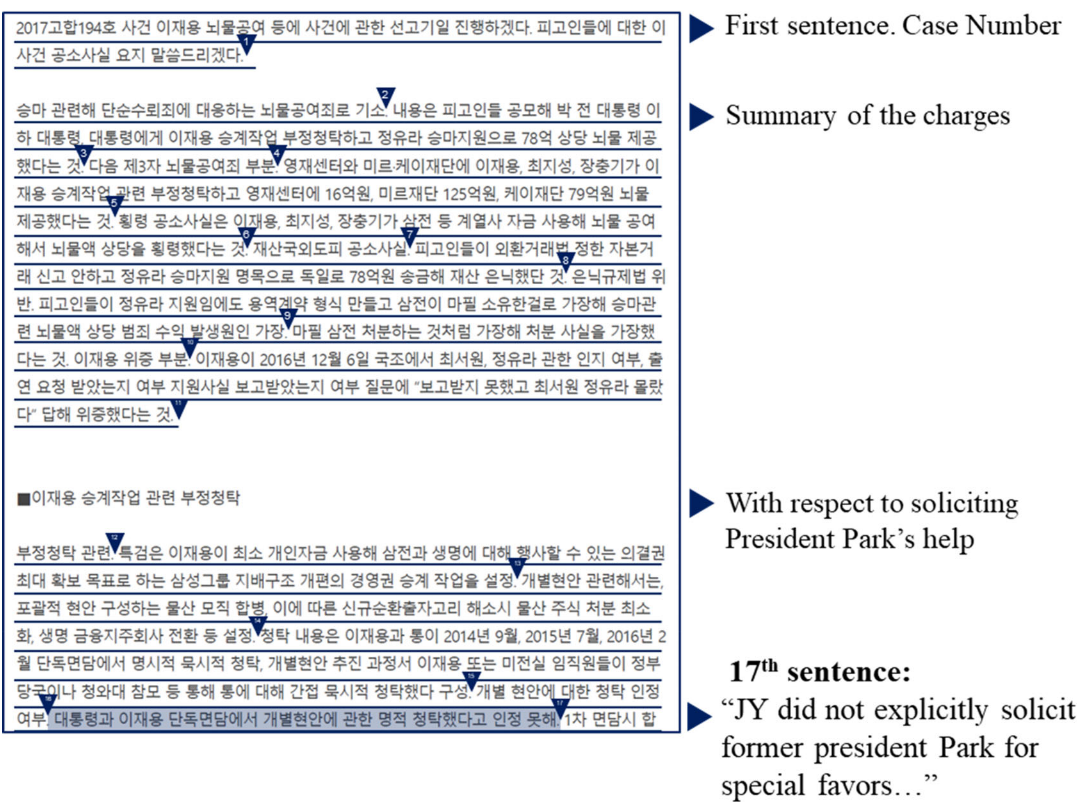
[34]From the 31st Survey of Credit Ratings conducted in November 2020. https://www.edaily.co.kr/news/read?newsId=02850326625966704&mediaCodeNo=257

2010	BJ becomes Hotel Shilla's CEO
2015	BJ announces partnership with rival Hyundai to establish HDC Shilla Duty Free
2016	BJ wins city approval for the first "traditional Korean-style" hotel in Seoul, announces 300M project investment
2017	BJ increases the revenue share of duty-free shops from ~15% to 90+%
2018-2020 2020-2021	Korean hotel and leisure firms pause most new investments due to THAAD crisis Global hotel and leisure firms pause most new investments due to Covid-19
2019	BJ acquires 44% stake in #1 in-flight duty-free firm "3Sixty" for USD ~120M
2020	BJ opens a new hotel in Vietnam (Shilla Monogram Danang) despite deteriorating performance due to Covid

APPENDIX B

B.1 | SENTENCE-BY-SENTENCE PARSING OF THE COURT'S OPINION

Lower Court Manuscript



Choosing an appropriate time-frequency of analysis is critical to tracking market reactions in a short-interval event study (Goodhart & O'Hara, 1997). Market participants carefully monitored each legal event, and we expect the market to incorporate the latest developments in the court rapidly. Busse and Green (2002) track reports about individual stocks on the financial television network CNBC and find that both positive and negative news are incorporated into share prices within 2 min. Earlier studies (e.g., Patell & Wolfson, 1984; Barclay & Litzenberger, 1988) find a slightly slower response, ranging between 5 and 15 min.

Investor overreaction or herding that results in over-shooting requires much caution in using high-frequency data (Schijven & Hitt, 2012). A key strength of our research design is that we combine qualitative and quantitative analyses to obtain a series of positive and negative shocks on the same firms over time, rather than a one-time shock (e.g., "buy" or "sell" recommendation on TV) on a single firm as in prior studies. The multiple treatments on the same set of firms—both within a single day and over months (Table 1, Figure 1)—allow sufficient time for learning to occur, reducing concerns of irrational short-term run-ups as dominating our results. Some degree of overreaction will still be present, but the overreaction relates primarily to the magnitude of changes in the share price, not the direction.[35]

APPENDIX C

C.1 | CALCULATING ABNORMAL RETURNS

In an event study analysis that examines daily returns, we use three different measures of stock returns (Acemoglu et al., 2016). First, we use a nominal return on the day of the event (Day 0) with the closing price from the previous trading day as the baseline. Second, we adjust this nominal return by subtracting the relevant sector return in the Korea Composite Stock Price Index (KOSPI). For example, we use the electronics sector returns (KOSP-ELEC) for Samsung Electro-Mechanics and financial sector returns (KOSP-FIN) for Samsung Life Insurance. In the case of Hotel Shilla, we also test robustness to using Samsung Electronics as the benchmark, which should control for any potential confounding events that affect the entire Samsung group. Given the size of Samsung Electronics, representing approximately 20% of all of KOSPI (vs. Apple that represents approximately 9% of NASDAQ), we use the entire KOSPI as a benchmark in adjusting returns for Samsung Electronics. Third, we take the residual from a market model regression of stock returns against relevant benchmarks. Specifically, we estimate the following model:

$$\mathrm{AR}[0,1]_{it} = R_{it} - \left[\widehat{\alpha}_i + \widehat{\beta}_i R_{mt}\right], \tag{C1}$$

where AR_{it} is the abnormal return for firm i on event day t, R_{it} is the nominal return on firm i for event day t, and R_{mt} is firm i's benchmark return for event day t. α_i and β_i are estimated using the equation:

$$R_{it} = \alpha_i + \beta_i R_{mt} + \varepsilon_{it}, \tag{C2}$$

[35] We refer to Bollerslev, Litvinova, and Tauchen (2006) and Goodhart and O'Hara (1997) for more detailed discussions of potential pitfalls to using high-frequency data.

using the rolling window that starts 250 trading days before and ends 30 days prior to the event day. Using an alternative index for R_{mt}, such as the entire KOSPI, KOSPI 100, or KOSPI 200, which only includes the largest 100 or 200 companies, does not change any of the conclusions. The overall Korean stock market was relatively stable on the days of key legal events and showed movements within 0.6%. February 5, 2018, (Monday) is a single exception with a loss of 1.34% from increasing fears of an interest hike by the US Federal Reserve over the weekend. We start our analysis from January 2016 to the end of June 2018. All of the results are robust to an alternative window that starts from January 2017 or other feasible ranges.

The trading days are 4 days shorter for SEC and in Column 7 of Table 1 that uses SEC as a control. SEC stopped trading between April 30 and May 3, 2018, due to a stock split, yielding 610 (606) observations. All of the results are robust to varying the start and end periods (e.g., expanding them by 6 months).

In addition to the 1-day abnormal returns used in our baseline analysis, it is customary to show robustness to alternative event-study windows. The alternative windows are not feasible in our empirical context because several events happen within 2 days of each other, leading to an interference (Table 1: events 1 & 2, 3 & 4). [−1, 1] is a natural alternative, and we find robust results.

DV: Stock returns	**Samsung electronics: Market adjusted**	**Hotel Shilla: Market adjusted**
Positive shock on JY (1.19/2.25 = 1)	−0.009* [0.005]	0.014*** [0.004]
Negative shock on JY (1.16/2.14/2.17/8.25 = 1)	0.005*** [0.001]	−0.019*** [0.005]
Constant	0.001** [0.000]	0.001 [0.001]
R-squared	.007	.010
Obs.	605	610

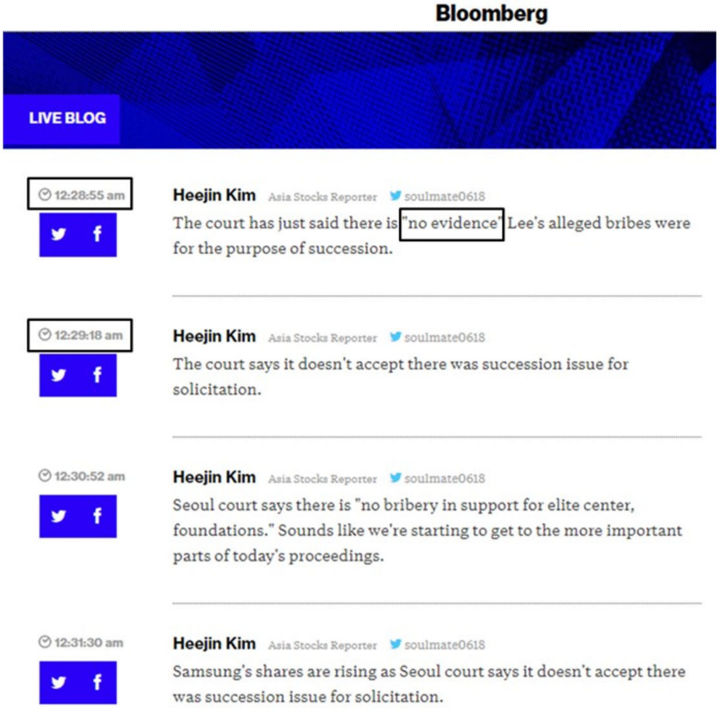
***, **, and * indicate two-tailed statistical significance at the 1%, 5%, and 10% levels, respectively.

As an exception, we find consistent yet weaker results on Samsung Electronics when we do not adjust for market or industry returns: this is because of Event #6 (February 5, 2018, Monday): the fear of the interest rate hike from US Federal Reserve over the weekend caused a significant drop against our predicted direction (SEC's greater loss reflects its exposure to the US market, where approximately 30% of its revenue comes from).

APPENDIX D

D.1 | ESTABLISHING TIMELINE

1. Yonhap News TV, LIVE
2. Time marker
3. Breaking news


Bloomberg

LIVE BLOG

12:28:55 am — Heejin Kim, Asia Stocks Reporter, soulmate0618: The court has just said there is "no evidence" Lee's alleged bribes were for the purpose of succession.

12:29:18 am — Heejin Kim, Asia Stocks Reporter, soulmate0618: The court says it doesn't accept there was succession issue for solicitation.

12:30:52 am — Heejin Kim, Asia Stocks Reporter, soulmate0618: Seoul court says there is "no bribery in support for elite center, foundations." Sounds like we're starting to get to the more important parts of today's proceedings.

12:31:30 am — Heejin Kim, Asia Stocks Reporter, soulmate0618: Samsung's shares are rising as Seoul court says it doesn't accept there was succession issue for solicitation.

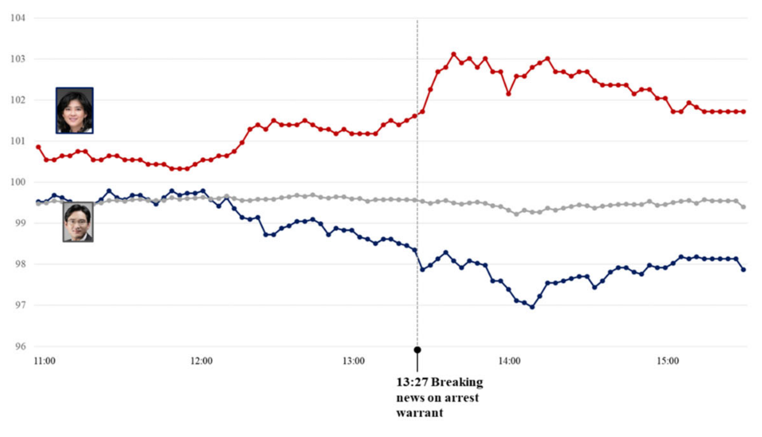
APPENDIX E

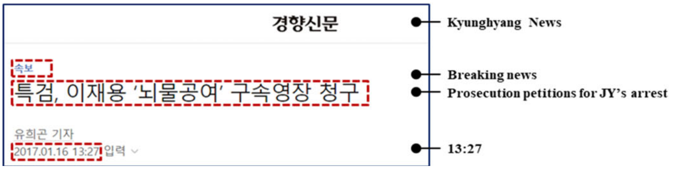
E.1 | OTHER EVENTS

E.1.1. | First petition for JY's arrest warrant (January 16, 2017)

The special prosecutor's office delayed its decision on whether to petition for JY arrest from January 15 to 16, and on the morning of January 16, several media outlets reported that the decision would be announced that afternoon.[36] The first news of the arrest warrant of JY broke out at 13:27.[37] The press briefing by the office took place at 14:00 but did not convey any new information. While the overall Korea Composite Stock Price Index (KOSPI) showed little movement, ranging below 0.53% throughout the day, HTS showed an immediate uptick upon the breaking news at 13:27, followed by a minor correction after 13:51. In contrast, SEC showed a gradual and steady loss during the same time period. The market closed with a gain of 1.72% for HTS, a loss of 2.14% for SEC, and a loss of 0.61% for KOSPI.

It is interesting to note that the downward (upward) trend for SEC (HTS) begins at 12:00, while smaller in magnitude compared to the drop (increase) following the breaking news at 13:27. In accounting for this early trend, interviews with investors and analysts pointed to the possibility of leakage and exploitation of private information. This is consistent with the fact that the media already reported on the specific charges against JY officially disclosed by the prosecution team during the press briefing that began at 14:00. Therefore, we interpret the market response to the January 16 event more tentatively compared to the later court rulings that were much better guarded against leakage.



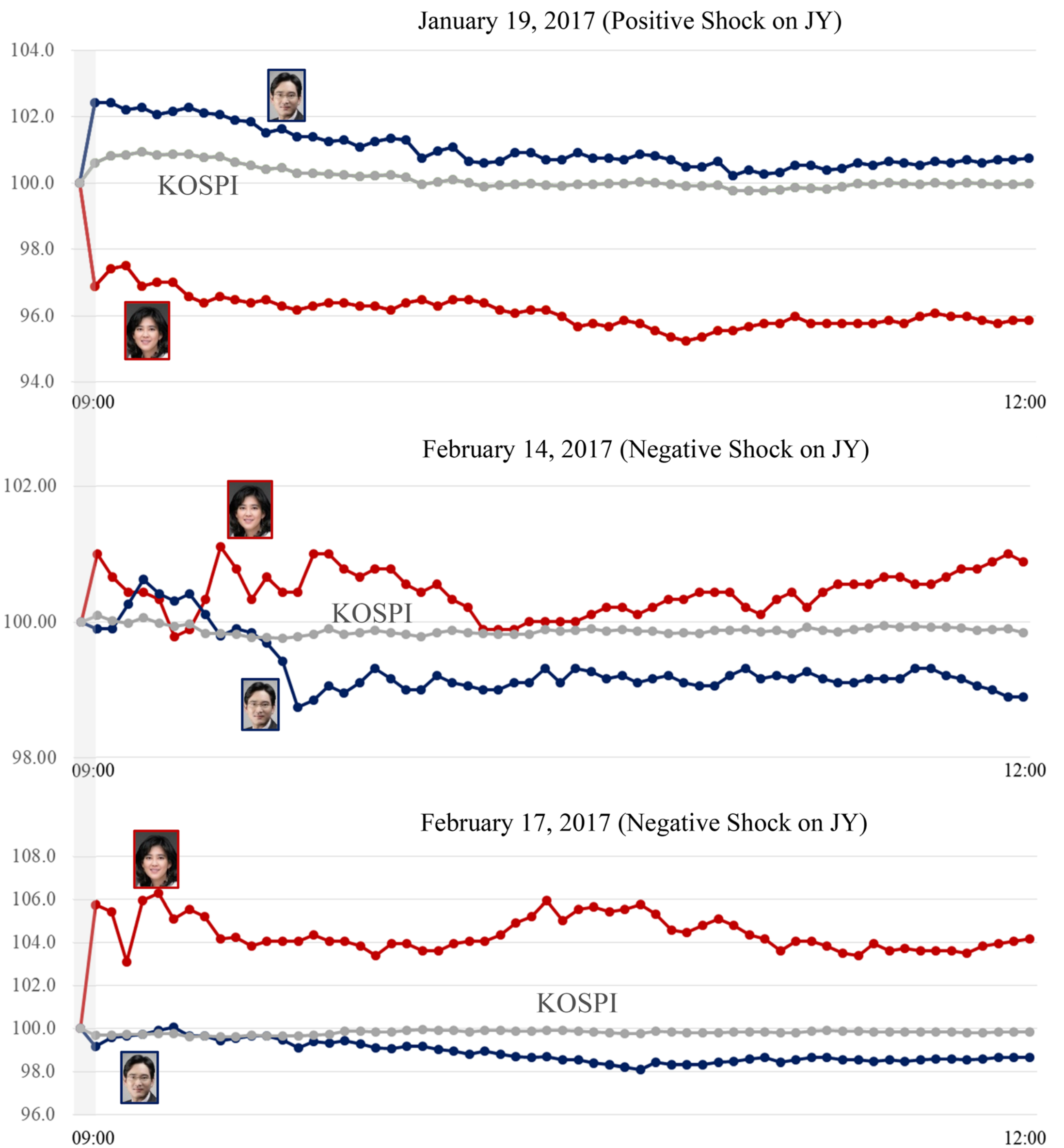


[36]https://m.newspim.com/newsamp/view/20170116000007

[37]https://m.khan.co.kr/national/court-law/article/201701161327001/amp; http://sports.khan.co.kr/bizlife/sk_index.html?art_id=201701161327003&sec_id=560901&pt=nv; https://mnews.jtbc.joins.com/News/Article.aspx?news_id=NB11401575

E.1.2. | Three off-hour events

Three other legal events occurred during off-hours and do not allow for tracking the market's immediate reaction. As an alternative, we examine the first 3 h of the stock market (09:00–12:00) with an added emphasis on the first 3 min of the market opening (09:00–09:03). For all three events, we find market reaction consistent with H1 and H2. In response to the warrant's denial (2 a.m., January 19, 2017), HTS opened with a loss of 3.1% versus a gain of 2.4% for SEC between 9:00 and 9:03. In response to the reapplication for an arrest warrant (6 p.m., February 14, 2017), there was a gain of 1.0% for HTS, but a loss of 0.1% for SEC between 9:00 and 9:03 the following day. The loss for SEC increased in magnitude over time, reaching 1.2% by 12:00. The news on the issue of the arrest warrant (5 a.m., February 17, 2017) generated a gain of 5.8% for HTS. SEC, in contrast, showed a decline of 0.8% in the first 3 min that expanded to 1.1% by 12:00.



E.1.3. | Extension to non-family managers and other affiliates based on a non-judicial event

Beyond the legal shocks on JY examined in Section 4.3, we observe a consistent pattern from another earlier event. On January 28, 2016, when JY reduced his equity share from 11.25 to 9.2% to invest in Samsung Engineering through after-hours block trading, Samsung SDS's share price dropped by 12.4% within the first 30 min of the market opening on the following day. In contrast, the share price of Samsung Engineering shows a 13.9% increase while Samsung SDI and Electro-Mechanics' share price stayed relatively flat, gaining 3.5 and 0.18%, respectively. Share prices of other Samsung affiliates, including Hotel Shilla, show negligible movement. While we cannot claim causality as in our main analysis using exogenous shocks, the opposite effects on the share prices of Samsung SDS and Engineering and the muted effect on SDI and Electro-Mechanics provide additional evidence for the reallocation of value across affiliates based on JY's political power.

E.1.4. | Passing of KH Lee

We stop our main analysis at the sixth event in February 2018—prior to his passing in October 2020. KH Lee's passing was an important event, first covered by the media at 09:53 on October 25, 2020.[38] We decided to focus on the series of judicial shocks based on JY's corruption trials because we are concerned that his passing and other non-judicial shocks contain both economic and political components. In the case of KH Lee's passing, we were concerned with the following two issues:

1. *Conflation with an economic shock*: Prior to October 25, 2020, there had been several false news reports of KH Lee's passing by both major daily newspapers and other channels as well as tabloids (e.g., on June 30, 2016). In each instance, the share prices of Samsung affiliates show an increase. This is because his three children and his wife Ra-Hee Hong were expected to be charged approximately USD 10B as estate tax from inheriting KH Lee's shares in Samsung affiliates. Even the Lees do not have this much liquid assets, and the market expected that they would try to increase dividend payments (which several investors have been calling for) to secure the necessary cash flow.[39] As a result, KH Lee's passing carries an important economic component (i.e., dividend payout and the resulting effects on investments).
2. *Weak political shock*: The information on how KH Lee's shares will be divided among his family, especially between JY and BJ Lee, was not disclosed until much later (it ended up being divided in line with their current shares—having no net effect on their control). As a result, his passing acted as a weak shock politically.

[38]https://www.sedaily.com/NewsVIew/1Z99ON3KVM
[39]https://www.hankyung.com/economy/article/2020112372717

APPENDIX F

F.1 | SAMSUNG ELECTRONICS STOCK DISCUSSION FORUM—NUMBER OF DISCUSSION THREADS MENTIONING BJ AND JY

To verify the reallocation of political power from BJ to JY as underpinning the observed market reactions, we examine textual posts in the largest stock market discussion forum in Korea (Naver Finance). Specifically, we track whether investors of HTS and SEC pay attention to BJ on the dates of JY's trial, even though JY and BJ do not play any formal role in the management of each other's firm. The forum's participants are mostly small retail investors, but institutional investors closely follow its contents. Our analysis starts from June 7, 2017, when Naver Finance first makes its historical data available.

Figure F1a and b plots the number of new discussion threads under Hotel Shilla's stock market forum with references to BJ and JY, respectively. As expected of her position as CEO, BJ is the most frequent discussion topic, averaging 0.44 new threads per day. There are dramatic increases in the number of new threads mentioning BJ on three specific dates, as indicated by the peaks: the day of JY's first trial, the day of the Hotel Shilla's third-quarter earnings announcement (October 30, 2017), and the day of JY's appeals court hearing. Threads mentioning JY also peak on the same two dates: the day of JY's first trial and the appeals court hearing. Several posts express wishes for heavier sentencing for JY. The lack of attention to JY on the day of Hotel Shilla's earnings announcement serves as an effective placebo test

In Figure F2a and b, we repeat the analysis with respect to Samsung Electronics' discussion forum and find a mirroring pattern.[40] Investors of Samsung Electronics pay increased attention to BJ on JY's trial dates even though she does not play any formal role. These patterns indicate that investors are acutely aware of the zero-sum political dynamics between JY and BJ, carefully monitor the latest developments in JY's trial, and consider buying and selling shares based on JY's legal (mis)fortunes.

[40] https://finance.naver.com/item/main.nhn?code=005930f

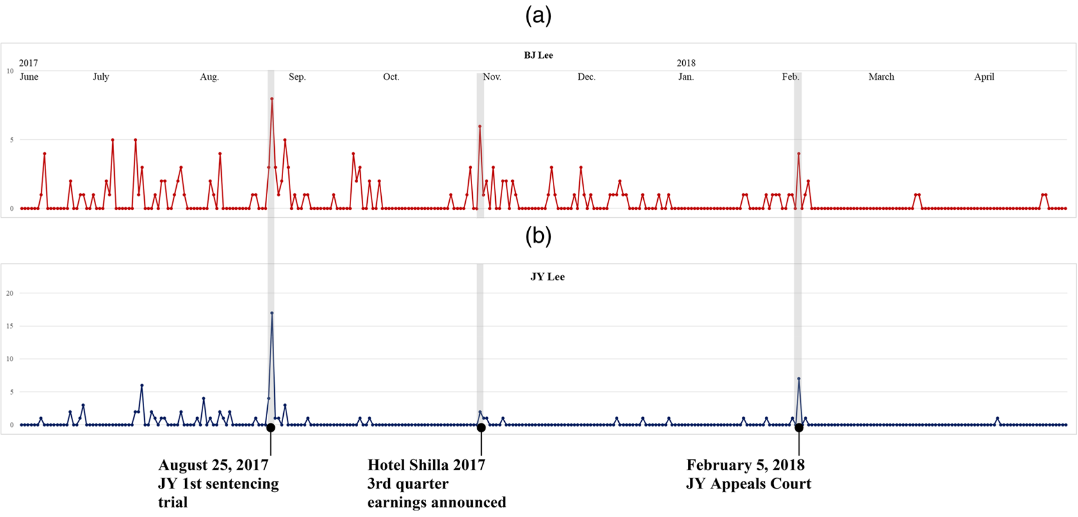


FIGURE F1 Hotel Shilla stock discussion forum—number of discussion threads mentioning BJ and JY. (a) New discussion threads mentioning BJ Lee. (b) New discussion threads mentioning JY Lee.

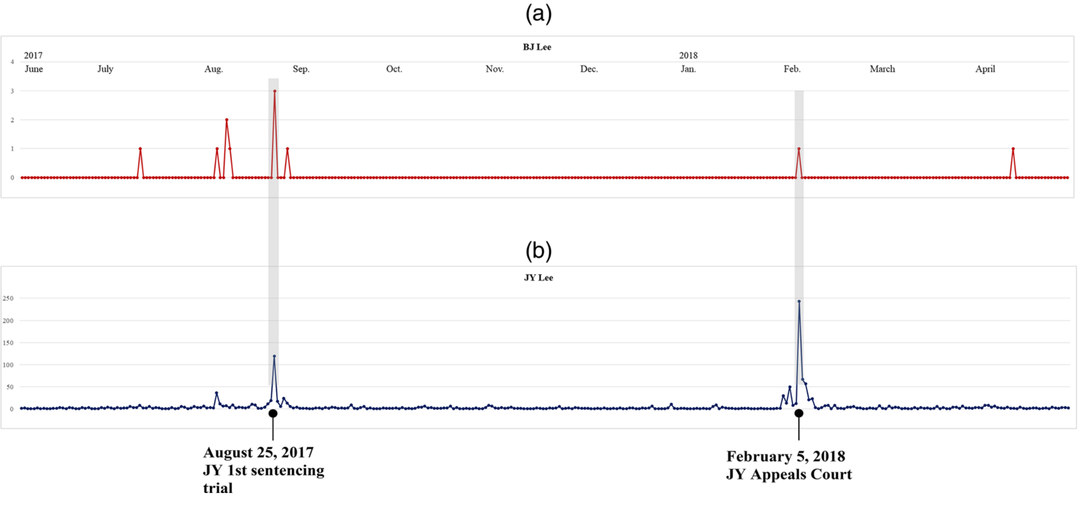


FIGURE F2 Samsung Electronics stock discussion forum—number of discussion threads mentioning BJ and JY. (a) New discussion threads mentioning BJ Lee. (b) New discussion threads mentioning JY Lee.

APPENDIX G

G.1 | MARKET REACTIONS TO UNRELATED FIRMS

Here, we repeat the same analysis as in Tables 2 and 3 but using (a) Samsung affiliates that have weak ties to JY and BJ and (b) Samsung Electronics' domestic product market rivals, LG Electronics and SK Hynix, as alternative control groups.[41] All models use market-adjusted

[41]Samsung Biologics is excluded from the analysis because it went public in November 2016.

abnormal returns as the dependent variable; using nominal or industry-adjusted returns yield similar results.

Samsung affiliates: Across the four financial affiliates—Samsung Life Insurance, Samsung Fire and Marines Insurance, Samsung Card, Samsung Securities—and three other affiliates—Cheil Worldwide (advertising agency), Samsung S-1 (security and safety services), and Samsung Heavy Industries (shipbuilding), there is only a negligible and statistically insignificant response to negative legal shocks on JY, suggesting that they have little to gain from JY's loss of political power. The positive legal shocks have null or small but positive effects, with the exception of Samsung Securities.

External market competitors: As an alternative control group, we next test whether the shocks on JY affect the share prices of Samsung Electronics' two primary domestic rivals, LG Electronics and SK Hynix, which should not be exposed to Samsung's internal politics. We find null results. We interpret this result more tentatively because the null result could be due to (a) Samsung Electronics' extensive financial slack, ranging in >USD 100B during this period, and (b) extensive delegation to professional managers. JY and BJ are not heavily involved in daily decisions and spend most of their time reviewing large-scale investments in new businesses (e.g., acquisitions). Analysts and the media notes that: "the day-to-day decisions are made by the CEO Kinam Kim but key investment decisions [on new businesses] needs JY Lee."[42] At the same time, another media observes that JY is needed for "the resolution of uncertainty on large M&A and investment decisions".[43]

As a result, looking at share prices of existing competitors (i.e., LG and Hynix) may be highly noisy. However, taken together with the null or very weak results on other Samsung affiliates, the null result provides nuanced support for the internal reallocation of value as driving our main results, not industry-specific trends.

[42] https://www.edaily.co.kr/news/read?newsId=01876166629045968&mediaCodeNo=257
[43] https://www.mk.co.kr/news/economy/view/2021/08/773758/

DV:	Market adjusted returns								
	Financial subsidiaries				Others			Competitors	
	Life insurance (1)	Fire & marine (2)	Card (3)	Securities (4)	S-1 (5)	Heavy industries (6)	Cheil (7)	LGE (8)	Hynix (9)
Positive shock on JY (1.19/2.25 = 1)	0.004*** [0.001]	−0.005 [0.006]	0.010 [0.006]	−0.006** [0.003]	0.006 [0.011]	0.004 [0.004]	0.006*** [0.002]	−0.004 [0.013]	0.003 [0.007]
Negative shock on JY (1.16/2.14/2.17/8.25 = 1)	−0.004 [0.007]	0.000 [0.005]	−0.006 [0.005]	−0.005 [0.006]	−0.007 [0.005]	−0.003 [0.008]	0.002 [0.007]	−0.002 [0.006]	−0.004 [0.008]
Constant	0.000 [0.001]	0.000 [0.000]	0.000 [0.001]	0.000 [0.001]	0.000 [0.001]	0.000 [0.001]	0.000 [0.001]	0.000 [0.001]	0.001 [0.001]
R-squared	.001	.001	.002	.002	.001	.000	.000	.000	.000
Obs.	610	610	610	610	610	610	610	610	610

*p < .10; **p < .05; ***p < .01; bootstrapped standard errors are provided in brackets.

APPENDIX H

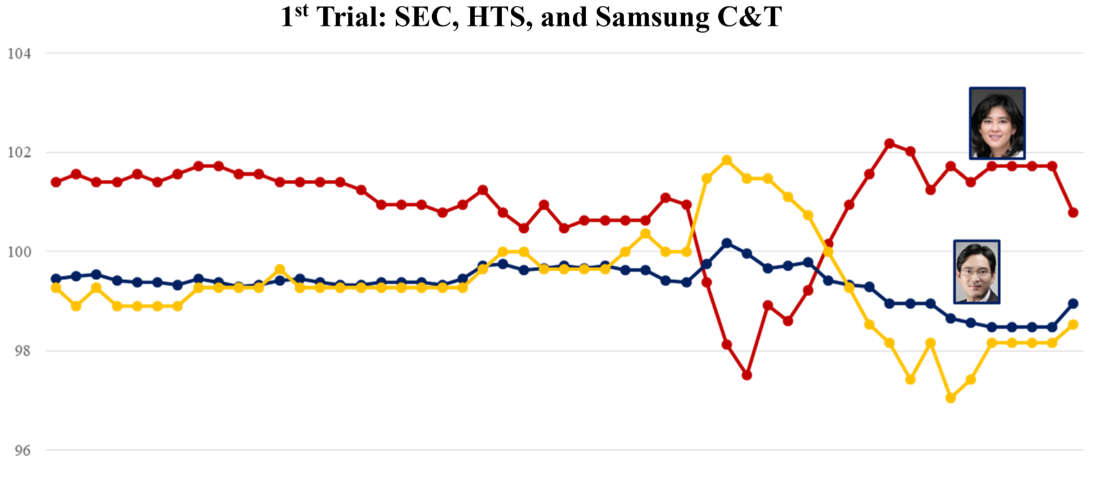
H.1 | SH (SEO-HYUN) LEE

Beyond BJ and JY, the second daughter SH Lee presents a potential opportunity to further examine the managerial political dynamics. SH received her undergraduate degree from Parsons School of Design and was responsible for the fashion arm of Cheil Industries before its merger with Samsung C&T.

We cannot analyze Cheil Industries (where SH Lee served as the head of the fashion division) due to its merger with Samsung C&T in 2015. The legality of this merger, specifically the ratio of equity exchanges, was one of the bases of JY's trial that JY solicited ex-President Park's help in the process and the lawsuit by Elliott Management. As a result, a negative court ruling on JY generated negative, null, and positive effects on Samsung C&T (and Cheil Industries that became a part of C&T).

1. Negative: increases the concern that Samsung C&T might have to unwind the merger or pay a significant fine.
2. Positive: increases the managerial political power of SH Lee.
3. Neutral: JY, BJ, and SH all own shares in C&T (16.5, 5.5, and 5.5%). Hence any gain or loss of political power happens *within* C&T, having a marginal effect on its political power relative to other affiliates.

Because of these multiple channels, it is difficult to isolate changes in the managerial political power with SH Lee as an actor. When we look at the share-price changes during the first trial (marked in yellow), we find that C&T largely tracks SEC but with an even wider swing, indicating that channel (a) dominates (b) and (c) in this case.

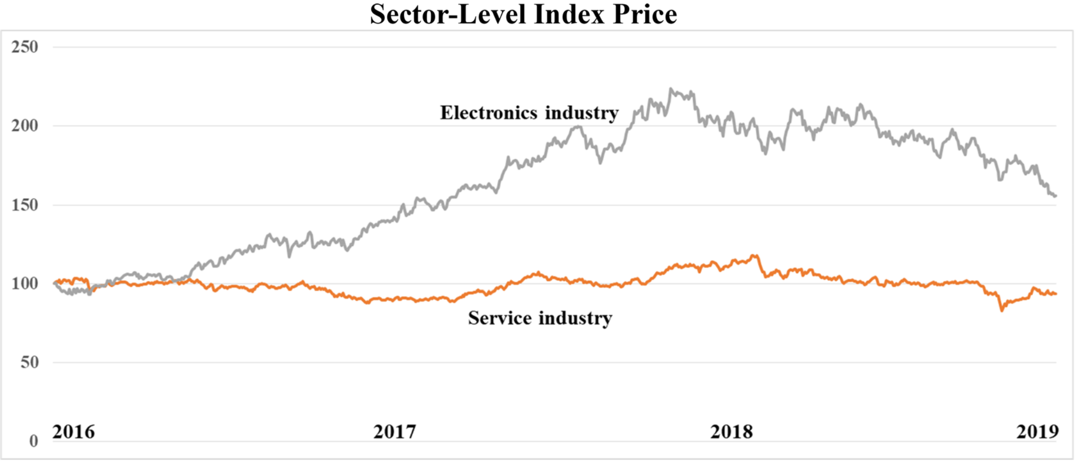


On December 6, 2018, she announced that she will retire from all business-related positions and focus on managing Samsung's charitable foundations and Leeum Museum.

APPENDIX I

I.1 | MACRO-ECONOMIC EVENTS DURING THE SAMPLE WINDOW

The long-term trend in the share prices of SEC and HTS shows a strong divergence to each other. This is in significant part due to three macro-economic events: (a) the THAAD missile crisis, (b) the Covid pandemic, and (c) increasing demand for memory chips. With respect to (a), Hotel Shilla and the entire leisure and service sector in Korea depend very heavily on Chinese tourists. As a protest against installing US THAAD missiles in Korea, the Chinese government effectively banned Chinese tourists from visiting Korea, leading to drastic underperformance at the sector level.[44] In contrast, Samsung Electronics, especially its DS division (responsible for memory chips), has enjoyed a "super-cycle" due to (c).[45] These confounding trends typically complicate a causal inference. However, performed at minute and daily intervals, our analysis effectively holds these broader trends constant and allows us to examine *within*-period variations based on the latest legal developments on JY.



[44]https://www.latimes.com/world-nation/story/2020-11-19/south-korea-china-beijing-economy-thaad-missile-interceptor

[45]https://m.pulsenews.co.kr/view.php?year=2021&no=489942