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Experience, political connections and efficiency in the financial sector

Experiencia, conexiones políticas y eficiencia en el sector financiero

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Abstract

Purpose – The purpose of this paper is to analyze the influence of political presence on profitability in Spanish savings banks. Together with political connections, the paper analyzes the effects of chairmen's banking experience on the efficiency of the savings banks.

Design/methodology/approach – Information was collected from all the savings banks in the sample for the period 2002-2009. The database used combines time series with cross-section data to give a panel of data to be estimated with this methodology.

Findings – After differentiating between municipal and regional participation, the results show that regional participation causes lower efficiency in a savings bank. There is no evidence that the financial experience of the chairman is an aspect that improves savings banks' profitability.

Originality/value – The analyses undertaken in this paper help to detect whether certain corporate governance practices affect stakeholders' interests and the economy as a whole, through their effects on economic and financial interests, like the efficiency of savings banks. The paper lends support to the recent legal reforms aimed at reducing political presence on the boards of savings banks.

Keywords Corporate governance, Boards of directors, Saving banks, Spain

Paper type Research paper

Resumen

Objetivos – El principal objetivo de este trabajo es analizar la influencia de la presencia política en la rentabilidad de las cajas de ahorro españolas. También se estudia el efecto de la experiencia bancaria del presidente en la eficiencia de las cajas.

Diseño/metodologia – La información se ha obtenido de las cajas de ahorro españolas durante el periodo 2002-2009. La base de datos utiliza datos temporales con información cross-seccional, permitiendo el uso de datos de panel como metodología principal.

Resultados – Tras diferenciar entre participación política municipal y regional, los resultados muestran que es la presencia regional la que causa menor eficiencia en las cajas. No hay evidencia de influencia de la experiencia bancaria del presidente.

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Originalidad/valor – Los análisis realizados en el trabajo ayudan a detector si ciertas prácticas de gobierno afectan los intereses de los stakeholders y la economía como un todo, analizando sus efectos es aspectos económicos, como la eficiencia de las cajas. El documento apoya las recientes reformas legales, tendentes a reducir la presencia política en los consejos de las cajas de ahorro.
Palavras-chave gobierno corporativo, consejo de administración, cajas de ahorro, España
Tipo de papel Trabajo de investigación

1. Introduction

The importance of financial intermediation by banks in an economy and the need to protect depositors' funds means that corporate governance in bank organizations is of huge importance for the international financial system. Following the Basel Committee Agreement on Banking Supervision, efficient corporate governance practices are essential to gain and maintain public confidence in the banking system and for the appropriate functioning of the banking sector and the economy as a whole. Corporate governance shortcomings may mean higher costs and significant effects on the public sphere because of their potential impact, the deposit insurance schemes applicable and the possible macroeconomic implications, such as the risk of contagion or the impact on payment systems.

In this sense, the High Level Working Group on Financial Supervision in the EU and the OECD concluded in 2009 that the shortcomings in the functioning of banking governance mechanisms had been responsible in part for the financial crisis and its consequences. For its part, the Basel Committee Agreement on Banking Supervision has highlighted the need to study, understand and improve corporate governance in banks. In 2010, the committee issued the final version of a document containing a series of principles to improve good practices in corporate governance in banking organizations (Principles for enhancing corporate *governance,* Basel Committee on Banking Supervision (BCBS), 2010). These principles refer to aspects regarding boards of directors and their composition.

Although the recent scandals surrounding financial entities in the USA and Europe (Lehman Brothers in the USA, HBOS in the UK, Fortis in Belgium and IKB in Germany) have sparked more research interest in the corporate governance of financial entities, few papers have addressed the issue and most of those which have focus on the USA (e.g. Cornett *et al.*, 2003, 2010). However, Haggendorf *et al.* (2010) show that the findings of these studies may not be applicable in other countries with different institutional and regulatory norms, so pointing to the need to increase research outside the USA.

In relation to the above, the intervention of the various levels of administration on the boards of directors of Spanish savings banks has generated an intense debate in recent years. Act 31/1985 of August 2 on the Regulation of the Basic Rules of the Governing Bodies of Savings Banks (LORCA), established that the General Assembly, the main governance body of the savings banks, was to be represented by the following groups: depositors, local corporations, founder entities and staff of the entity. A later sentence from the Spanish Constitutional Court enabled the Autonomous Communities to adjust the percentages established for each representation, so paving the way for higher participation by local and regional powers. The Finance Act passed at the end of 2002 reduced the political influence on the running of the savings banks to some extent by limiting the representation of political parties in governing bodies (board and assembly) to 50 percent. Even so, the past remains very present in the financial sector. The boards of the savings banks perform important work in terms of administration, financial management and social work.

In addition, specific regional laws introduced greater heterogeneity across regions (e.g. Carbó Valverde *et al.*, 2004). Some of these laws permitted the allocation of voting rights to not-for-profit organizations, such as universities or chambers of commerce, and in many cases they allocated a substantial percentage of voting rights to the regional governments. This means that regional governments exercise a decisive power in the renewal of the governing bodies and the establishment of savings banks' strategies. Moreover, board members appointed by regional governments are more likely to be connected to the Spanish federal administration, to the leaders of their political party, and more involved in general policy decisions than local politicians. Thus, regional governments are typically more powerful than local politicians (e.g. Sapienza, 2004).

Today, Act 26/2013 has led to important changes in the composition of the governance bodies in savings banks. First, these bodies are more professional, since all the board members must have specific knowledge and experience in the functions they carry out. The composition of the General Assembly has also been modified, with the participation of public administration reduced to 25 percent.

The new act aims to give more importance to depositors and to prevent savings banks' board members from holding elected political positions or administrative posts, and so "depoliticize financial management" and favor "free market actions" in Spain, which in times of crisis is fundamental.

The insecurity of the financial markets, with their economic uncertainty and changeability has driven this study in its attempt to ascertain the influence of politicians sitting on the boards of Spanish savings banks on profitability, with an analysis of whether different percentages of participation by politicians supposes significant differences in levels of efficiency. The presence of representatives from municipal councils and public administration is examined.

Along with the political connections, the paper analyzes the financial background of the chairmen and the consequences this has for efficiency, as well as whether their greater or lesser training has affected this efficiency in recent years. The analyses employed here show whether certain corporate governance practices affect the interests of stakeholders and the economy as a whole by examining their effects on economic and financial indicators such as efficiency.

2. Corporate governance and efficiency in banking

Within agency theory, an increasingly important line of research in recent years has involved corporate governance, defined by Shleifer and Vishny (1997) as a set of mechanisms through which investors protect themselves from insider expropriation, thus, minimizing agency costs. Although research into corporate governance is one of the most fertile and ongoing areas of economic research, corporate governance has received little attention so far (Macey and O'Hara, 2001). However, High Level Working Group on Financial Supervision in the EU and the OECD concluded in 2009 that the shortcomings in the functioning of banking governance mechanisms had been responsible in part for the financial crisis and its consequences.

Good corporate governance should offer proper initiatives for the board and management to be able to select the most profitable goals for the company and its shareholders and should provide proper follow up (Caravaca *et al.*, 2012). Effective corporate governance in each company, and in the economy as a whole, helps to provide the necessary level of confidence for the correct functioning of a market economy. From the perspective of the banking sector, corporate governance is the way

in which the board of directors and top management direct the bank activities and business. This influences the way in which corporate objectives are fixed, how managers carry out day to day banking operations, how they assume their responsibilities toward shareholders and take into consideration the interests of other parties, how they ensure that bank activities and behavior meet the safety and solidity levels required and comply with existing rules and regulations and, finally, how they protect depositors' interests (Basel Committee on Banking Supervision).

The banks' good corporate governance is bound by different parameters to those generally applied to non-financial companies (Macey and O'Hara, 2003; Mülbert, 2009). Adams and Mehran (2012), of the Federal Reserve, examined data on banks' profitability covering 40 years (1959-1999) and advocated caution when translating results of empirical studies of non-financial companies to banks. According to Ciancanelli and Reyes (2001), the agency problem of commercial banks is structurally different from that of quoted companies, mainly because of regulations that cause additional information asymmetries and, therefore, added agency problems (Levine, 2004). Hence, Crespí and García-Cestona (2004) report that the model of governance in banks means that the duties and responsibilities of the directors go beyond their shareholders and include creditors, depositors and the regulator, as well as the rest of the banking system. In banking, the premise of the regulator is to safeguard depositors' rights, and the regulator is seen as an important corporate governance mechanism (Diamond, 1984).

Although financial entities have, because of their special nature, traditionally been subject to intense regulations, the basic dimensions of corporate governance have not changed, except for the inclusion of the depositors as the main risk holders (Caprio *et al.*, 2007) and a banking opacity related to increasing information asymmetries and growing supervision problems (Caprio and Levine, 2002; Salas Fumás, 2003; de Andrés and Vallelado, 2008). From an internal perspective, the boards, the incentives contracts and the general shareholders' meetings are great mechanisms to handle stakeholder conflicts.

Shareholders delegate the responsibility for monitoring, compensating and replacing directors and top management, and approving large strategic projects to the board. The board members, in this case of the savings banks, should take charge of administration, financial running and social benefit work. Independent board members are considered key figures in enhancing the effectiveness of the board. The theory holds that independence increases profitability, on the basis that the first function of the board is to monitor management, and unless independent of management, any such monitoring will be weak (Fama and Jensen, 1983). Other important features are that board members and management should be subject to periodic renewal, meetings should be held regularly, there should be committees to select and remunerate directors and to enhance transparent information. Most studies analyzing the effect of the board on profitability are on non-financial firms, and mainly study aspects related to board independence and size, without obtaining conclusive findings (Hermalin and Weisbach, 2003).

As for research into the role of boards of directors in banks, the evidence is scarce and inconclusive. In the USA, Adams and Mehran (2012) show that the relationship between board size, board composition and bank profitability disappears when endogeneity is controlled for, with non-significant results Zulkafli and Samad (2007) for 107 Asian banks. Agoraki *et al.* (2010) showed a negative relation for European banks between board size and profitability, while de Andrés and Vallelado (2008) found for an international sample of 60 boards that size (up to 19 board members) increases

profitability, after which it starts to fall. As regards board independence, the findings are again varied, with some studies claiming that independence in general favors profitability (Sierra *et al.*, 2006) and the outcomes of complex decisions such as mergers (Cornett *et al.*, 2003). Other studies report the opposite, however, (Staikouras *et al.*, 2007) with non-linear relations (Agoraki *et al.*, 2010; de Andrés and Vallelado, 2008) or non-significant results (Griffith *et al.*, 2002).

Worth highlighting are the findings of Cornett *et al.* (2010), who undertook a more ambitious study and analyzed various measures of efficiency (profitability, operative efficiency, composition of loans, etc.) and contemplated various corporate governance mechanisms. Their findings showed that corporate governance variables had a strong impact on the efficiency of large banks in 2008, which showed weaknesses in their corporate governance mechanisms just before the crisis.

Although the literature has studied general aspects of the boards of directors (size, independence) and their effect on banking efficiency, few papers have analyzed the influence of political presence on these boards. However, there has been a wealth of literature recently on the effect of political connections, but mainly in financial sectors (Goldman *et al.*, 2009; You and Du, 2012; Bona *et al.*, 2013, 2014).

These papers show that politically connected firms are not limited to Spain. The financial and institutional crisis affecting European countries like Greece, Italy, Ireland, Portugal and Spain since mid-2007 has led to increased interest in the study of political and business ties as well as their effect on firm behavior (Bona *et al.*, 2014).

Regarding the results of these papers, several prior studies suggest that political connections can have positive effects. Agrawal and Knoeber (2001) and Goldman *et al.* (2009) argue that political connections can provide expertise on legislative and bureaucratic procedures. Faccio (2006) argues that political connections can lead to increased access to bank financing, lower tax rates, preference in the award of government contracts and less regulatory oversight. Moreover, Khwaja and Mian (2005) argue that politically connected firms enjoy increased access to capital from financial institutions.

In addition, according to Fama and Jensen (1983), political participation in savings banks may be useful, since it reduces risk by guaranteeing their continuity. Agency theory holds that politicians are necessary to reduce savings banks' problems by better control of management. Following this theory, Altunbas *et al.* (2001) determined that German savings banks with high political representation were more efficient than commercial banks.

On the other hand, political connections can increase the information asymmetry arising from the separation of ownership and control (Chen *et al.*, 2011). Thus, especially in environments where external shareholders' interests are poorly protected, political ties can increase dominant owners' incentives to expropriate minority shareholders' wealth (Bona *et al.*, 2014). A negative relationship between the presence of political connections and performance could, therefore, also arise as a result of an information effect whereby politicians provide as little information to the market as possible to prevent the transmission of proprietary information to competitors and to protect political ties from public scrutiny (Riahi-Belkaoui, 2004).

Fan *et al.* (2007) showed that political interference in the management of firms and the weak managerial skills of politicians could be harmful to firms' performance, and Bertrand *et al.* (2007) found that the profitability of French firms managed by politically connected chief executive officers declines because of higher wage bills as employment in politically contested areas increases. Politically connected banks also increase their

lending in election years (Dinc, 2005) and charge lower interest rates (Sapienza, 2004), which could have negative effects on their performance.

According to this idea, in Spanish savings banks, it is the regional governments that bring political projects to the savings banks. These are sometimes of low profitability and they increase risk for the savings banks (García-Marco and Robles-Fernández, 2008). Similarly, Fonseca Díaz and González (2005) found that changes in regional legislation between 1984 and 1999 increased the risk of savings banks, especially of those with high political representation.

Most research has adopted an international perspective, which makes interpretation of the results difficult, as they may be affected by differences in legal, judicial and cultural factors that make it hard to disentangle firm-level effects from country level ones. Indeed, Faccio (2010) shows that differences between politically connected and unconnected firms are greater in weak institutional environments, and that the costs and benefits of political connections vary across countries. In addition, they mostly focus on non-financial firms. However, government ownership of banks is very common outside the USA. In any discussion of financial systems in countries with government ownership of banks, it is, therefore, imperative to take into account the government's control of financial resources and their role in boards.

The present study aims to fill a gap in the literature by examining the performance of politically connected savings banks in one country – Spain. With regard to the above, we believe that political presence in the governance bodies of Spanish savings banks may negatively affect their efficiency, and we put forward the following hypothesis:

H1. Politicization of a savings bank's governance bodies has a negative effect on its efficiency.

At the same time, one must recognize the importance of experience and knowledge for efficiency, which is currently an area of great interest. The ability of a chairman to make correct decisions is largely determined by his experience (Rindova, 1999). In banking, experience in the financial sector may favor better decision making and enhance the efficiency of the bank or savings bank. Cuñat and Garicano (2010) found that Spanish savings banks whose chairman had postgraduate studies gave 7 percent more loans to individuals and between 5 and 7 percent less loans to the real estate sector. Consistent with this, in July 2009, these savings banks had a significantly lower non-performing loan rate, at around 1 percent less. Fields *et al.* (2012) also reported that experience is an attribute that defines the quality of the board, showing that lenders whose boards are larger, more independent and have greater experience are able to grant loans at lower interest rates. So experience is a key factor in the future of savings banks. Experience cannot be delegated and it feeds on knowledge, so non-experienced chairmen will run into more difficulties. We assume that experienced savings bank chairmen will make more efficient decisions than inexperienced ones, so we propose the following hypothesis:

H2. The banking experience of a savings bank's chairman positively affects its efficiency.

3. Empirical study

The sample data were taken from three sources: financial information on savings banks was taken from the CECA (Spanish Confederation of Savings Banks);

information on corporate governance in savings banks came from the CNMV (National Stock Market Commission); and information regarding the banking experience of savings banks' chairmen was taken from their curricula vitae.

Information on 32 savings banks was collected for the 2002-2009 period (217 observations). This allowed us to work with data dating back to before the banking reform of 2010, when important changes were made such as the majority of savings banks being converted to commercial or other banks, while Bankia and Banca Cívica were floated on the Madrid stock market. There was also an important consolidation in the savings bank sector through mergers and other types of integration. In 2010, the reform of the Savings Banks Act came in under Spanish Royal Decree 11/2010, which sought to reduce the political power of public administrations. The sample represents over 80 percent of all assets of Spanish savings banks.

With regard to the variables selected, the efficiency of savings banks was measured following Cornett *et al.* (2010) as the profitability over assets, the result of the quotient of the pre-tax earnings and mean total assets.

The independent variables are:

- *Presence of municipal and regional politicians on the board of directors (Politics)*: the percentage of municipal and regional politicians on the board. Following García-Meca and Sánchez-Ballesta (2013), this variable is the sum of the variables municipal councillors and regional government members, which measures their presence separately. According to Illueca *et al.* (2014), regional governments have different incentives to local ones, so it is reasonable to expect them to differ in their priorities and their decisions, and therefore affect efficiency.
- *Presence of municipal councillors on the board (Municipal)*: this variable measured the percentage of municipal councillors on the board.
- *Presence of regional politicians on the board (Regional)*: this variable measured the percentage of board members representing public administrations within the group of "others" on the board.
- *Banking experience of the chairman in the savings bank (Experience)*: a dummy variable that takes the value one if the chairman of the savings bank has banking experience prior to occupying the post and 0 otherwise.

Control variables:

- *Board size (Board size)*: the number of members on each board.
- *Risk (Z)*: measured by the *Z*-score (Hannan and Hanweck, 1988; Sullivan and Spong, 1998). This control variable was calculated by the sum of the *ROA* plus the ratio of capital divided by the typical deviation of the *ROA*. The variable reflects the inverse probability of bankruptcy, so a high *Z*-score implies less risk. Recently, Laeven and Levine (2009) and Hadad *et al.* (2011), among others, have also used this measure as a proxy for bank insolvency.

Apart from insolvency risk, we also considered credit risk. Thus, following Fernández Alvarez *et al.* (2006), we used the *Loan Loss* reserve to assets (*Loan Loss*) variable. The issue of risk provisioning is particularly important for banks because there is an inter-temporal relationship between a bank's lending standards, its loan growth and

its loan losses (Illueca *et al.*, 2014). Nier and Baumann (2006) have also used this proxy of risk:

- *Leverage (lev)*: the result of the quotient between liabilities and the entity's own funds.
- *Size of the savings bank (size)*: a control variable resulting from the logarithm of total assets presented by the savings bank which allows us to control for its size.
- *Crisis*: a dummy variable that takes the value of one for the years 2008 and 2009 (crisis).

Two regression models were used in this study. The first model checked for the influence on the *ROA* of all politicians on the board, i.e. municipal politicians and those designated under "others," who usually represent public administration. It also checked for the influence of the banking experience of the savings bank's chairman. The second model sought to ascertain which politicians, municipal or regional, affect the efficiency of the savings bank most:

$$ROA_{it} = \beta_0 + \beta_1(Experience_{it}) + \beta_2(Politics_{it}) + \beta_3(Boardsize_{it}) + \beta_4(Lev_{it}) + \beta_5(Z_{it}) + \beta_6(LoanLoss_{it}) + \beta_7(Size_{it}) + \beta_8(Crisis) + \eta i + \eta t + \varepsilon it \quad (1)$$

$$ROA_{it} = \beta_0 + \beta_1(Experience_{it}) + \beta_2(Municipal_{it}) + \beta_3(Regional_{it}) + \beta_4(Lev_{it}) + \beta_5(Boardsize_{it}) + \beta_6(Z_{it}) + \beta_7(LoanLoss_{it}) + \beta_8(Size_{it}) + \beta_9(Crisis) + \eta i + \eta t + \varepsilon it \quad (2)$$

The relations previously proposed in the hypotheses of this study are materialized in the following panel data models. Panel data enabled us to assess savings banks' performance in the sample over time by analyzing observations from several consecutive years for the same savings banks. Our database combines time series with cross-sectional data, allowing the formation of panel data, which we estimated with the appropriate panel data methodology. Constant and unobservable heterogeneity refers to specific characteristics of each firm that remain constant over time as represented by the fixed-effects term η_i.

We treated endogeneity by providing efficient estimates whose consistency depends critically on the absence of second order serial autocorrelation in the residuals and on the validity of the instruments (Arellano and Bond, 1991). Accordingly, we report the m_2 test. With this estimator, we can control the endogeneity problems that may appear in the models. To test the validity of the instruments, we used the Hansen test of overidentifying restrictions, which allowed us to test the absence of a correlation between the instruments and the error term and, therefore, to check the validity of the selected instruments.

4. Results

4.1 Descriptive statistics

Table I shows the descriptive statistics for all the continuous variables used in the models analyzed. The average number of municipal councillors sitting on boards is very high, at almost 21 percent, while regional politicians are some distance behind with just 9 percent. In total 77.6 percent of Spanish savings banks' chairmen had no experience prior to taking on the chairmanship. Table II records that efficiency of the

Variable	Mean	SD	Min.	Max.
ROA	0.8973	0.7192	−3.1429	5.6739
Politic	32.7695	11.7068	14.00	58.81
Municipal	20.9622	5.6074	10.00	33.33
Regional	9.1689	9.6377	0.00	37.5
Z	13.6385	19.6598	−1.53	122.26
Lev	17.05	6.32	7.04	77.01
Size	16.2435	1.1876	13.2100	19.4200
Board size	17.23	3.699	7	30
LoanLoss	0.1007	0.224	0	3.972
	No experience	Experience		
Experience	77.6%	22.4%		

Notes: *ROA* is the return on assets; *Z-score* is the natural logarithm of the *Z*-score, where *Z*-score is calculated as the return on assets plus the equity ratio divided by the standard deviation of return on assets; *LoanLoss* is the ratio of loan loss reserves to assets; *Experience* is a variable that takes the value of 1 if the chairman of the saving bank has previous banking experience, and zero otherwise; *Politics* is the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Municip*, *Regional*, represent, respectively, the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Size* is the natural logarithm of total assets; *Board size* is the number of members in the board, *Leverage* is debt divided by equity. All models include control dummy variables

Table I.
Descriptive statistics

	Mean	SD	
Pre-Crisis	1.045	0.324	7.04***
Crisis	0.381	0.708	

Notes: Pre-Crisis period: 2004-2007; Crisis period: 2008 and 2009. ***$p < 0.001$

Table II.
Efficiency
Pre-Crisis/Crisis

savings banks was statistically significantly lower in 2008-2009 (Crisis) than in the previous years ($p < 0.01$).

Table III gives the correlations matrix and shows a negative and significant relation between the savings banks' profitability and the influence of politicians on the board ($p < 0.05$), especially that of town councillors ($p < 0.1$).

4.2 Univariate results

We used a means univariate analysis to get an initial idea of the effect of the representative variables of political influence, experience and women on profitability in savings banks, categorizing the corporate governance variables and taking efficiency as the dependent variable. The aim is to ascertain whether profitability changes according to the level of these variables. With the exception of banking experience, which is dichotomous, the others are categorized in three levels, each representing 33 percent of the sample. Given the lack of normality of the variables, as shown by the Kolmogorov-Smirnov test, we used non-parametric tests: the Mann-Whitney test for the dichotomous variable, and the Kruskal Wallis and median tests for the three-level variables.

The results are given in Table IV, and they show there are significant differences in the *ROA* of the savings banks according to the levels of politicization of the boards, and especially when non-local public administrations are represented.

	ROA	*Politics*	*Municipal*	*Regional*	*Lev*	*Z*	*Board size*	*Size*	*Loan Loss*
ROA	1								
Politics	−0.171**	1							
Municipal	−0.08	0.522**	1						
Regional	−0.146*	0.831**	−0.041	1					
Lev	0.055	−0.084	−0.294**	0.162*	1				
Z	0.320**	−0.05	−0.086	0.006	−0.132	1			
Board size	−0.066	0.129*	0.201**	0.005	0.395**	0.088	1		
Size	−0.056	0.008	−0.012	−0.048	0.308**	0.07	0.567**	1	
LoanLoss	−0.047	−0.022	−0.069	0.008	−0.005	0.007	−0.052	−0.058	1

Notes: *ROA* is the return on assets. *Z-score* is the natural logarithm of the *Z*-score, where *Z*-score is calculated as the return on assets plus the equity ratio divided by the standard deviation of return on assets; *Loan Loss* is the ratio of loan loss reserves to assets; *Experience* is a variable that takes the value of 1 if the chairman of the saving bank has previous banking experience, and zero otherwise; *Politics* is the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Municip*, *Regional*, represent, respectively, the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Size* is the natural logarithm of total assets; *Board size* is the number of members in the board, *Leverag*e is debt divided by equity. All models include control dummy variables. *$p < 0.1$; **$p < 0.05$

Table III.
Correlation matrix

Estatistics	*Politics*	*Municipal*	*Regional*	*Experience*
χ^2 K-W	4.858	1.763	8.429	
Significativity	0.088	0.414	0.015	
χ^2 M	12.790	0.356	12.493	
Significativity	0.002	0.187	0.002	
U Mann-Whitney				4597
W Wilcoxon				6137
Z				−1.029
Significativity				0.303

Table IV.
Mean differences in *ROA*

4.3 Results of the regression

Table V shows the results of the regressions for models one and two. Both models study the profitability of the Spanish savings banks in relation to the political presence in their governing bodies, the experience of the chairman and the gender diversity of the board.

As for the coefficients of the variables, we can observe in model one how political influence (*Politics*), measured by the sum of the municipal and regional politicians, is significant ($p < 0.1$) and, in line with our expectations, has a negative influence on the profitability of the savings bank. The results therefore suggest that savings banks whose boards have greater politicization return lower levels of efficiency than others, as posited in *H1*. Later, in model two, we broke down this independent variable and observed that what has a negative influence on savings banks' profitability is the presence of regional politicians (Regional) ($p < 0.1$). We can add to these results those already reported by García-Marco and Robles-Fernández (2008), which reflect that the presence of this type of politician decreases the profitability of savings banks, since the

	(1)	(2)	(3)	(4)
Politics	−0.005*			
	(−1.889)			
Municipal		−0.039		
		(−1.419)		
Regional		−0.068**		
		(−2.351)		
Crisis	−0.314***	−0.340***		
	(−5.598)	(−6.145)		
Politics×Crisis			−0.008***	
			(−1.718)	
Municipal×Crisis				−0.010***
				(−4.356)
Regional×Crisis				−0.006*
				(−1.884)
Experience	−0.082	−0.073	−0.061	−0.056
	(−1.294)	(0.255)	(−1.073)	(−0.974)
Leverage	−0.005	−0.006	−0.012**	−0.013***
	(−0.834)	(0.320)	(−2.480)	(−2.628)
Z-score	0.179***	0.177***	0.102***	0.102***
	(11.467)	(11.417)	(5.261)	(5.221)
Firm size	0.023	0.024	0.017	0.018
	(0.833)	(0.874)	(0.672)	(0.717)
Board size	0.025***	0.024***	0.027***	0.027***
	(3.207)	(2.998)	(3.760)	(3.795)
Loan Loss	0.040	−0.054	−0.301	−0.331
	(0.132)	(0.858)	(-1.140)	(0.217)
m_2	0.85	–0.18	0.81	–0.20
Hansen	61.72 (215)	65.39 (207)	60.27 (213)	63.93 (206)
R^2	0.567	0.577	0.648	0.646

Notes: *ROA* is the return on assets. *Z-score* is the natural logarithm of the *Z*-score, where *Z*-score is calculated as the return on assets plus the equity ratio divided by the standard deviation of return on assets; *Loan Loss* is the ratio of loan loss reserves to assets; *Experience* is a variable that takes the value of 1 if the chairman of the saving bank has previous banking experience, and zero otherwise; *Politics* is the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Municip*, *Regional*, represent, respectively, the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks; *Crisis* is a dummy variable that takes the value of one if the years are 2008 and 2009, zero otherwise; *Size* is the natural logarithm of total assets; *Board size* is the number of members in the board, *Leverag*e is debt divided by equity; m_2 is a test of second order serial autocorrelation; Hansen test is a test of overidentifying restrictions, which distributes as χ^2 (degrees of freedom). *$p < 0.1$; **$p < 0.05$; ***$p < 0.001$

Table V.
Results of the regression of models on *ROA*

decisions made by them often relate to not very profitable projects that had already been announced in their manifestos. The findings lead us to reject *H2* regarding the influence of the chairman's banking experience on profitability of Spanish savings banks.

The specification proofs of our model are satisfactory. According to the m_2 test, no second order correlation exists among the residuals, so our estimates are efficient. The Hansen test of overidentifying constraints supports the selection of instruments.

Additionally, we have considered whether the presence of municipal and regional directors on savings banks' boards affects performance depending on the crisis.

We then created new variables as a result of the interaction between Crisis and the different variables representing municipal and regional presence in savings banks (models 3 and 4). The results, interestingly, show that the negative effects of political connections in savings banks, measured by the presence of municipal and regional directors, is higher in the crisis years (2008 and 2009). In model 4, we observe that, when we consider the crisis, the effect of municipal presence is also negative.

Robustness test. In order to check the robustness of our results we recodified the variable *Politics* in two groups (*HvL_Political*), measuring savings banks with high vs low political connections. Similarly, the variables representing municipal and regional presence were recodified to measure high vs low municipal (*HvL_Municipal*) and regional (*HvL_Regional*) presence, respectively.

Table VI presents the robust results obtained for the proposed models. Specifically, we can see that the presence of political directors negatively affects bank profitability. Regarding the presence of municipal and regional directors on boards, again a negative impact produced by the presence of regional directors on bank performance is confirmed ($p < 0.01$). The results are similar for models 3 and 4. The effect of municipal and regional directors is negative for 2008 and 2009.

5. Conclusions

Despite the importance of political presence in financial entities, the role of the banks and the current financial crisis, little is known about the municipal and regional politicization of our savings banks. In the current financial crisis, this is a highly relevant issue with important implications. Criticism of politicization of Spanish savings banks and their lack of professionalization are constant features in the national and international press, yet there is scarce empirical evidence of these issues affecting the efficiency.

The purpose of this paper has been to study the influence of certain variables – present in today's social and economic situation – on the efficiency of Spanish savings banks – specifically, whether the presence of politicians and the chairmen's banking experience affect profitability.

Our findings reveal a significant and negative effect produced by the presence of politicians on the profitability of the savings banks analyzed, which coincides with the ongoing social and economic debate on this issue. The findings also show that it is regional more than municipal politicians who seem to account for lower efficiency in the savings banks. This supports recent measures taken by the Spanish Government to depoliticize savings banks as an essential part of the restructuring of the financial sector.

Another important aspect of this analysis is the study of how the financial experience of savings banks' chairmen can influence the entity. However, the findings are not conclusive, with no evidence that this may help to make savings banks more profitable.

This paper seeks to contribute to the debate in the financial and academic spheres about the effects of public administration in the Spanish financial system. The High Level Working Group on Financial Supervision in the EU and the OECD concluded in 2009 that the shortcomings in the functioning of banking governance mechanisms had been responsible in part for the financial crisis and its consequences. The analyses made here show how certain corporate governance practices, especially excessive politicization of the boards of directors of Spanish savings banks, have affected the interests of the economy in terms of economic and financial indicators, such as profitability. This is of special interest in a country like Spain, characterized by a high shareholder concentration and the huge importance of financial entities, which are shareholders in many quoted companies, when funding is required.

	(1)	(2)	(3)	(4)
HvL_Politic	−0.054*			
	(−1.718)			
HvL_Municipal		−0.039		
		(11.419)		
HvL_Regional		−0.068**		
		(−2.351)		
Crisis	−0.314***	−0.340***		
	(−5.598)	(−6.145)		
HvLPolitic×Crisis			−0.123***	
			(−5.467)	
HvLMunicipal×Crisis				−0.099***
				(−4.147)
HvLRegional×Crisis				−0.006**
				(−2.123)
Experience	−0.082	−0.073	−0.063	−0.042
	(−1.294)	(0.255)	(−1.152)	(−0.717)
Leverage	−0.005	−0.006	−0.012**	−0.013**
	(−0.834)	(0.320)	(−2.463)	(−2.464)
Z-score	0.179***	0.177***	0.111***	0.102***
	(11.467)	(11.417)	(5.795)	(5.221)
Firm size	0.023	0.024	0.021	0.015
	(0.833)	(0.874)	(0.853)	(0.599)
Board size	0.025***	0.024***	0.025***	0.027***
	(3.207)	(2.998)	(3.436)	(3.795)
Loan Loss	0.040	−0.054	−0.261	−0.302
	(0.132)	(0.858)	(−0.977)	(−1.131)
m_2	0.27	0.18	0.32	0.37
Hansen	69.2 (215)	56.71 (207)	61.68 (213)	60.34 (204)
R^2	0.567	0.577	0.638	0.641

Notes: *ROA* is the return on assets. *Z-score* is the natural logarithm of the *Z*-score, where *Z*-score is calculated as the return on assets plus the equity ratio divided by the standard deviation of return on assets; *Loan Loss* is the ratio of loan loss reserves to assets; *Experience* is a variable that takes the value of 1 if the chairman of the saving bank has previous banking experience, and zero otherwise; *HvL_Politic* is a dummy variable that takes value of one if the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks is higher than the mean, and zero otherwise; *HvLMunicip, HvLRegional*, represent, respectively, dummy variables that take the value of one if the percentage of power of Municipalities and Regional governments in the General Assembly of saving banks is higher than the mean, and zero otherwise; *Size* is the natural logarithm of total assets; *Board Size* is the number of members in the board, *Leverag*e is debt divided by equity. All models include control dummy variables; m_2 is a test of second order serial autocorrelation; Hansen test is a test of overidentifying restrictions, which distributes as χ^2 (degrees of freedom). *$p < 0.1$; **$p < 0.05$; ***$p < 0.001$

Table VI.
Robustness analysis of models 1 and 2 on *ROA*

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