Do board connections between product market peers impede competition?

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**Motivation**

- Board connections between product market peers have the potential to impede competition and hurt consumer welfare.
- In the US, the Clayton Antitrust Act of 1914 prohibits a person's presence on the boards of two rival companies.
- Identifying direct rivals is increasingly difficult, so Clayton might have left some room for board connections that can impede competition.
- Information can flow across competitors not only through a common director but also through a broader director network.
- We ask the following research questions:
  - How prevalent are board connections between competing firms?
  - Do board connections between product market peers impede competition?

**Main Results**

- Gross margin, operating margin, and ROA of treated firms increase relative to control in the three years post treatment.
  - Effects are in the range of 0.8%-1.4% after direct board connections and 0.4%-0.8% after indirect board connections.
  - Using third-party initiated changes yields similar results.

**Methodology**

- Main outcome variables: gross margin, operating margin, ROA.
- Treatments:
  - A firm forming a new direct board connection to a product market peer.
  - A firm forming a new indirect board connection to a product market peer.
- We identify 1,493 instances of new direct connections and 4,085 instances of a new indirect connection to a product market peer.
- Controls:
  - Firms in the same industry as the treated firm and closest in terms of size, gross margin, and Tobin’s Q.
- We stack cohorts of treated and control firms with a 7-year window.
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  Y_{ij,t} = \alpha_0 + \alpha_1 \times \text{Post}_t + \alpha_2 \times \text{Direct Treated}_t + \alpha_3 \times \text{Indirect Treated}_t + \beta_1 \times \text{Direct Treated}_t \times \text{Post}_t + \beta_2 \times \text{Indirect Treated}_t \times \text{Post}_t + \theta_1 + \theta_{2,t} + \epsilon_{ij,t,}\]
- Challenge to identification: Endogeneity of board connections.
  - We tackle this with third-party initiated changes, which we argue to be unrelated to the future prospects of the focal firm.

**Mechanism**

The effects are stronger when:

- Firms share major corporate customers.
- Firms have more similar business descriptions.
- Firms are located closer to each other.
- Firms are in more concentrated industries.
- The connections involve directors who are also executives.

There is no evidence of reduction in SG&A costs or increase in R&D or CAPEX.

Board connections have positive spillover effects on the closest common rivals of newly connected peers.

**Discussion & Conclusions**

- We acknowledge the possibility of a wide variety of anti-competitive practices such as price fixing or market segmentation.
- Information exchange or building of trust.
- Our results are consistent with the anti-competitive rather than the efficiency-enhancing mechanism (Bouwman, 2011).
- The effects of board connections are robust to controlling for within-industry common ownership, suggesting that it is a stand-alone channel (Aazar et al., 2018; Gilje et al., 2020).
- We estimate the effects of incremental board connections to product market peers rather than effects of the stock of board connections, which can be much greater.
- Our results provide support for the current ban of interlocking directorates between competing firms.

**References**