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# Estimating the value of connections to Vice-President Cheney

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*Abstract*

We estimate the value of personal ties to Richard Cheney through three distinct approaches that have been used recently to measure the value of political connections. Our proxies for personal ties are based on corporate board linkages that are prevalent in the network sociology literature. We measure the value of these ties using three event studies: (a) market reaction of connected companies to news of Cheney's heart attacks; (b) correlation of the value of connected companies with probability of Bush victory in 2000; and (c) correlation of the value of connected companies with the probability of war in Iraq. In all cases, the value of ties to Cheney is precisely estimated as zero. We interpret this as evidence that U.S. institutions are effective in controlling rent-seeking through personal ties with high-level government officials.

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Recent research has documented the value to firms of personal political ties across a range of countries and circumstances. Utilizing event study methodologies, these studies find that the market valuations of firms with political connections are affected by events such as unexpected electoral outcomes (Faccio, 2005) and sudden changes in a leader's health status (Fisman, 2001) thus demonstrating that firms, on average, benefit from these personal ties. Obviously, there are two ways of limiting the value that firms may extract through political connections – placing constraints on those who may take public office, or finding ways of limiting the extraction through connected individuals after they have taken office. The former may not be desirable, since it can significantly narrows the pool of competent managers that seek public office. If we wish instead to curtail the rent-seeking behaviors of connected politicians, a crucial question is whether there exist circumstances where favor-giving by such politicians is effectively constrained.

In this paper, we report the results of a set of event studies that exactly parallel the approaches of earlier work on valuing political connections to examine the market valuation of firms with personal connections to U.S. Vice-President Richard Cheney. This case has a number of features that make it a potentially useful test of limitations of personal favor-giving by government agents. First, since Vice-President Cheney is a very senior government official, a company's personal connections to him should constitute a substantial proportion of its total stock of political connections, and hence company valuation should be affected by Cheney's fortunes. Additionally, media accounts and conventional wisdom strongly suggest that companies with ties to Vice-President Cheney have materially benefited from their relations with the Vice-President. A February 2004 article published in the New Yorker discussing the fortunes of select military contractors under the Bush administration summarizes this point: "[Cheney] has been both an architect and a beneficiary of the increasingly close relationship between the Department of Defense and an élite group of private military contractors—a relationship that has allowed companies such as Halliburton to profit enormously." On the other hand, the United States has precisely those institutions, such as a relatively free press and active democracy, which should attenuate the role of personal ties in business-government relations. Narrowly, we wish to evaluate the frequent media allegations of corporate favoritism by Vice-President Richard Cheney, i.e., has Cheney been pronounced guilty based on past associations, or do companies really benefit from their relations with him? More broadly, we view this as a case study of the larger question of whether institutional constraints might reduce the ability of high-ranking officials to provide benefits to personally connected businesses.

Following the network sociology literature (see, for example,Mizruchi, 1992; Useem, 1984), we define personal connections to Vice-President Cheney based on board linkages. We examine four types of connected firms: (i) Halliburton, the company where Cheney served as CEO 1995-1999; (ii) companies where Vice-President Cheney sat on the board during 1995-1999; (iii) companies where their CEOs sat on Halliburton's board during 1995-1999; and (iv) companies where at least one board member sat on Halliburton's board during 1995-1999.

We study the effect on market valuation of these connected companies based on three sets of events that potentially affected Cheney's ability to provide favors (i) Cheney's three cardiac episodes while in office; (ii) Tradesports probability of Bush victory in 2000 (Knight, 2005); and (iii) for infrastructure service and military firms, probability of war in Iraq as proxied by the Tradesports probability of the capture of Saddam Hussein (Leigh, Wolfers, and Zitzewitz, 2005).In all cases and for all subgroups of connected companies, we fine zero effect (precisely estimated) of connections: Connected companies do not have negative abnormal returns in response to adverse news about Cheney's health, and returns of connected companies are uncorrelated with the probability of Bush victory as well as (where relevant for the particular industry) probability of war in Iraq.

There are two possible conclusions that one might draw from these results. First, it may be that business-politics connections are unimportant in America. Given prior evidence, this seems implausible. For example, Jayachandran (2005) finds that companies that were heavy contributors to the Republican party suffered negative returns when Senator Jim Jeffords unexpectedly crossed over to the Democratic party in 2001. Knight (2005) similarly finds that the probability of Bush victory in 2000 is correlated with the returns of companies that contributed heavily to the Republicans.[2] Alternatively, there may be well-organized institutions (such as political action committees and campaign contributions) for facilitating these relations that differ from the deeply personalized favor exchange that seems to characterize business-politics relations in so much of the world. This distinction is important in practice, since influence-peddling through PACs or donations may be more carefully controlled through legal mechanisms and more closely monitored by the media.

The rest of this paper is structured as follows. In Section 1, we describe our data, including a detailed discussion of our board-based measure of Cheney's connections and an overview of the events we study. Section 2 presents our event study results, and Section 3 concludes.

# 1. Data

*1.1 Cheney Connections*

Because our analysis hinges on the credibility of our measure of Cheney's personal business ties, in this section we discuss why the use of corporate board ties, particularly as they pertain to Vice-President Cheney, are the appropriate measure of personal networks.

The social and economic meaning of relations among board members has been the source of extensive research as well as public concern in the United States ever since the Pujo Committee identified certain board overlapping board memberships as harmful to the public and market early in the 20th century. Board ties have been shown to affect the process of information flow and the diffusion of practices among large corporations, including the adoption of poison pills (Davis, 1991), corporate acquisition activity (Haunschild, 1993), and CEO compensation (Khurana, 2002).

Central to our study, sociologists and organizational scholars have also found board ties to be the most effective means of operationalizing personal ties among the business elite (see Mizruchi, 1996 for a review). The cliché that relationships among

[2] Knight also documents the related result – that the returns of companies favored by Bush party platforms had returns that were correlated with probability of Bush victory.

board members are better characterized as intense, affect-laden, social relations – more a social club than an arms-length economic relations – is, in fact, surprisingly true. Mace (1971) found that directors often describe their relations with fellow directors not in professional terms, but terms more closely associated with describing friends, confidantes and close colleagues. More recently, in an article titled "Just a Friendly Group of Independent Directors", Pulitzer Prize winning financial and investigative journalist Gretchen Morgenstern has documented the comradely and casual character of most public boards, even in the post-Enron era. One possible contributing factor to the sociable atmosphere is the reality that most board nominations do not emanate from shareholders, but the existing board itself. That is, most boards are self-perpetuating entities in which existing board members have significant influence on choosing new board members (Bebchuk and Fried, 2005). Thus, researchers have found that most directors have some prior social connection to, or are even close friends with, existing board members. In the course of their lifetimes, patterns of shared affiliations with respect to educational background, social club memberships, business associations, overlapping board memberships, highlight that these individuals mingle in overlapping social spheres, where in which they easily renew old friendships and draw upon them in an effort to facilitate action. Useem (1984) found that among the largest U.S. corporations, boards of directors have a prior history of personal contact and professional relationships with newly appointed directors, often sharing membership in elite social clubs and educational backgrounds. Moreover, even in those conditions in which directors may not have shared a prior relationship with existing directors, such as when an academic is appointed to a board, these unaffiliated new directors often begin their service with a sense of positive affect toward the inviting board members. Such friendship ties are further reinforced by the general boardroom culture where collegiality and friendship are not only emphasized, but a direct avoidance of conflict and confrontation are the norm (Khurana, 2002).

Thus, to summarize, board membership in general creates a context for a kind of reciprocal attraction and friendship among a fraternity of individuals. In its strongest form, it creates a sense of deep obligations and shared obligations among a group of similar individuals. This broad theme of reciprocal relations among board members may be applied directly to Vice-President Cheney's many board associations. Further bolstering this view is the role that the vice-president played in transforming Halliburton's board after becoming CEO – his tenure was marked by high turnover, with many of the new appointments going, according to many reports, to those with pre-existing ties to Cheney (see xx, xx). Thus, the Halliburton board under Cheney was marked by both strong prior personal associations to Cheney, and a set of board members with a deep sense of reciprocal relations with Cheney, given that they owed their board position to his influence.

Based on the above motivation, we define an individual to be *Cheney-connected* if he served on Halliburton's board of directors during 1995-1999, the period during which Cheney served as the company's CEO. We then define *Cheney-connected companies* to be those with Cheney-connected individuals (or Cheney himself) on their boards during the period 2000-2003. We further distinguish between companies where the connected individual was a board member of the company, and those where the connected individual served as CEO. We argue that the latter group of companies is more strongly connected, since the connected individual within the firm is more strongly incentivized to use any connections to benefit the company. We thus have four groups of connected companies for the years 2000-2003, in increasing order of connectedness:

(i) Cheney-connected individual is on the company's board of directors.
(ii) Cheney-connected individual is the company CEO
(iii) Cheney as board member 1995-1999
(iv) Cheney as CEO during 1995-1999 (i.e., Halliburton)

We generate a variable *CONNECTION* that takes on values from one to four that is increasing in the extent of connectedness. To generate *CONNECTION*, we use data from Compustat's Execucomp database. It is straightforward to extract companies with *CONNECTION*=3 or *CONNECTION*=4. To identify firms with lesser Cheney connections, we begin by creating a list of all Halliburton board members during 1995-1999, which generates a list of identifiers for all Cheney-connected individuals. To generate the list of companies with *CONNECTION*=2, we search for all company-year observations where the connected individual served as CEO of a company in

COMPUSTAT during 2000-2003; to generate the list of *CONNECTION*=1 companies, we search for all company-year observations where the connected individual served on the board of directors during 2000-2003. In a number of cases, firms had multiple Cheney connections. For example, Cheney sat on the board of EDS, and a board member of EDS during 2000-2003 also sat on Halliburton's board during Cheney's tenure as CEO. In such cases, we assign the higher connection value to the company. The number of firms with Cheney connections of one through four is 21, 4, 3, and 1 respectively.

*1.2 Events affecting the value of Cheney connections*

Paralleling the earlier literature that uses the health status of leaders (Fisman, 2001; Faccio, 2005) as a shock to connections, we examine unexpected changes in Cheney's health as a shock to the value of connections. We first identified all relevant dates through an open-ended search of the *New York Times* and *Wall Street Journal* during 2000-2004 with the keywords CHENEY and HEALTH. This yielded a number of stories, including health check-ups, the Vice-President's two heart attacks and the when doctors implanted a pacemaker in the chest of the Vice-President to control for an irregular heartbeat. We exclude the health check-ups as relatively minor events, which generally stated that the Vice-President was in reasonable health; the pacemaker installation, announced on a late Friday afternoon (likely timed by the White House to minimize public attention) and because information about the procedure may have been leaked prior to the announcement, (see Della Vigna and Pollet, 2005 for an extended analysis about the timing of release of bad news).

Not surprisingly, the White House played down the seriousness of both heart attacks. However, media reports surrounding these events reflected genuine concern. After Cheney's third heart attack, on November 22, 2000, the New York Daily News noted that his " 'very slight heart attack' prompted speculation yesterday about his ability to withstand the rigors of the vice presidency,"[3] and after his fourth heart attack, on

[3] "CHENEY HAS A HEART ATTACK HIS 4TH SPARKS FEARS OF ABILITY TO DO VEEP JOB." Daily News (New York), November 23, 2000.

March 5, 2001, USA Today worried that "In a worst-case scenario, Cheney himself could die… In Cheney's case, that's not a far-fetched consideration."[4]

We date each cardiac episode to the day when the event was announced by the White House. We provide a timeline of both episodes as well as interpretations of the seriousness of each heart attack in Appendix 1.[5]

An additional, in some sense broader, test of the value of Cheney connections is to examine the effect of the fortunes of the Bush Administration in general on the value of Cheney connected companies. This may be a more rigorous test, since it may be expected that a company with personal ties to Cheney may have cultivated personal ties throughout the Republican administration. We use the Tradesports contract on the probability of Bush victory in 2000 to proxy for the probability of the Republican ticket taking office, as in Knight (2005).

Finally, there have been many allegations, including those quoted in the introduction, that companies with ties to Cheney were disproportionately awarded contracts in Iraqi reconstruction. To examine whether government contracting was expected to favor Cheney's friends, we examine the relationship between the probability of war in Iraq and the value of companies with Cheney connections in affected industries (military, oil, oil/gas services, and construction). Following Leigh, Wolfers, and Zitzewitz (2005), we proxy for the probability of war using the Tradesports contract on the probability that Saddam Hussein would be captured by June 2003.

### *1.3 Company Data*

Data on the risk adjusted daily returns are from CRSP for each company. Since we wish to focus on personal connections (as distinct from industry-wide effects), we also calculate returns for all COMPUSTAT firms in a company's 4-digit SIC code. We

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[4] "Cheney gets physicians' OK, but concerns remain." USA Today, March 7, 2001.

[5] It is difficult to come up with real measures of the extent of these concerns – one possibility is the change in the Tradesports probability of Cheney receiving the Republican nomination for president in 2008. In each of our events, this probability did decline by a large percentage. However, this is a very thinly traded security, and is over very small probabilities. An additional possibility would be to look at the differential insurance premia or actuarial tables for an individual with Cheney's pre- and post-heart attack health profile. Unfortunately, someone with Cheney's health profile is not insurable. Further, while academic studies on the mortality effects of cardiac episodes do show a significant increase in short-term mortality rates (see, for example, Skinner et al, 2005), Cheney's health characteristics are too different from the subject pool to infer changes in survival probabilities based on such studies.

additionally obtained basic firm characteristics (such as sales and assets) through COMPUSTAT.

# 2. Results

*2.1 Effect of Cheney's Cardiac Episodes*

As outlined in the preceding section, Richard Cheney has a history of heart trouble that may be the source of plausible exogenous shocks to the value of Cheney connections. This parallels the analysis of Fisman (2001), Roberts (1990), and Faccio and Parsley (2005). We report the risk-adjusted excess returns of connected firms on the two trading days that Cheney had heart attacks after taking office. Table 1 lists both the basic returns, as well as the returns relative to median industry returns. In all cases, the point estimates are actually positive, but very close to zero. Longer event horizons only increase the standard deviations of returns. If all companies are pooled in a regression with fixed effects for level of connection (effectively eliminating the effect of Halliburton), the constant term, which reflects excess returns, takes on a value of 0.0026 with a standard error (clustered at the firm level) of 0.026. Thus, we obtain a precisely measured zero effect of Cheney's health status on companies with ties to him.

*2.2 Probability of Bush Victory*

Under the hypothesis that companies with Cheney connections are affected by the political fortunes of the Bush administration more broadly, returns of connected companies should be correlated with the probability of Bush's electoral victory. We follow the approach of Knight (2005), who studies the correlation of the returns of firms favored by Bush or Gore policies with the Tradesports probability of Bush victory. In our case, we consider regressions of the following form:

$$(1) \qquad R_{it} = \alpha_i + \beta * \Delta Bush_t + \varepsilon_{it}$$

where $\Delta Bush_t$ is the change in Tradesports probability of Bush victory on date t and $R_{it}$ is the excess returns of company i on date t. Results based on specification (1) are listed in

Table 2, columns (1) – (4). In no case is there a significant correlation between firm returns and changes in the probability of Bush victory. Columns (5) – (8) show similarly insignificant point estimates on after netting out median industry returns. This is perhaps not surprising, since the Cheney-connected firms are not concentrated in the industries that Knight identifies as being sensitive to Bush victory.

### *2.3 Probability of War in Iraq*

One of the primary allegations against Vice-President Cheney, as alluded to in the introduction, was the preferential treatment of contractors in the wake of the invasion of Iraq. As Leigh, Wolfers, and Zitzewitz (2005) carefully document, there were strong industry-level responses to the Iraq War; below, we assess whether firms experienced particularly strong returns by virtue of their personal connections to Cheney *relative* to industry returns. For this section, we limit the analysis to the relatively select set of connected firms that were in oil, oil/gas services, military, or construction. The rationale for each is relatively straightforward. While oil companies would uniformly benefit from the higher oil prices generated by risk of war, connected oil firms might have preferential access to Iraqi oil fields. Construction and services firms might be favored in provided goods and services to the reconstruction process. Finally, military firms and their suppliers might differentially benefit from access to military contracts (though Leigh et al do not find any industry-wide impact on military firms). The SIC codes and firms in this group are listed in Appendix A2.

In the first column of Table 3, we provide results showing the relationship between connected firms' excess returns and the change in probability of Saddam's capture in June 2003 ($\Delta \text{SaddamJ03}_t$), for the full sample of connected firms. We use the following specification that precisely parallels (1) above:

$$(2) \qquad R_{it} = \alpha_i + \beta^* \Delta \text{SaddamJ03}_t + \varepsilon_{it}$$

We find that the coefficient on ΔSaddamJ03 is positive, and borderline significant. However, as noted previously, there were strong industry-level responses to the probability of war in Iraq, so it is crucial to net out industry effects. The second column shows the industry-level relationship between the probability of Saddam's capture and median industry excess returns for the industries that we identify as being sensitive to probability of war, conditional on there being at least one Cheney-connected company in the industry. We find a significant positive coefficient on ΔSaddamJ03, confirming that the Leigh et al result holds in aggregate the industry categories that we identify as sensitive to war. This emphasizes the importance of netting out industry-wide effects in trying to capture the effects of personal connections as distinct from general industry effects. In the remaining columns, we report returns relative to the industry average, first for all connected firms, then for each level of connections separately. Once again, we obtain precisely estimated zeroes for the coefficient on ΔSaddamJ03 in all regressions.

# 3. Conclusion

In this paper, we document that the returns of firms with political ties to Richard Cheney are unaffected by events that would credibly impact the value of any such connections. This is in contrast to the public perception, reinforced by the media, that Cheney showed special favors to Halliburton and others. Interestingly, as noted above, it may be exactly this type of media scrutiny that prevents highly placed public officials in the United States from favoring those with whom they have personal connections. In that vein, our study's negative finding on the effect of connections is entirely consistent with the recent scandals involving Tom Delay and Randy Cunningham. Such scandals are evidence that blatant violations are uncovered by law enforcement and widely reported in the media, serving as warnings to politicians tempted to engage in favor-giving.

We recognize that there are potential alternative explanations for our zero result – For example, the board ties measure emphasized by the network sociology literature may not be a sufficiently strong proxy for connectedness; Cheney's heart attacks may not have sufficiently impacted his medium-term longevity. However, nearly identical critiques apply to the work of Fisman (2001), Faccio (2005), and others, who do report strong effects in other contexts. We thus interpret our results as highlighting the fact that there may be limits to the value extracted through political connections in the American context. We feel that our case-study approach is a useful starting point, as it allows us to focus carefully the specifics of a particular individual where allegations of favor provision were rife. Obviously, this has also allowed us to concentrate on a particular case that is of significant import in its own right. However, further research will be useful in understanding the factors that limit value extraction through personal connections in general. This is one part of the broader agenda to understand the situations that lead firms to interface with government through personal relations relative to more formal institutionalized mechanisms.

***Table 1. Average excess returns, by connection level, in the two day period after a Cheney heart attack***

Connection represents the level at which the company is connected to Cheney (1= Cheney-connected individual is on the company's board of directors, 2= Cheney-connected individual is the company CEO, 3=Cheney as board member 1995-1999, and 4= Cheney as CEO during 1995-1999 (i.e., Halliburton)).

| (1) | (2) | (3) | (4) |
|---|---|---|---|
| Connection | Risk-adjusted returns | Risk-adjusted returns (relative to industry median) | *N* |
| 1 | .0016<br>(.0174) | .0007<br>(.0151) | 42 |
| 2 | .0095<br>(.0284) | .0022<br>(.0205) | 8 |
| 3 | .0072<br>(.0189) | .0069<br>(.0130) | 6 |
| 4 | .0045<br>(.0140) | .0025<br>(.0023) | 2 |

***Table 2. Relationship between probability of a Bush victory and excess returns, by connection level.***

Values represent coefficients on ΔBush (change in Tradesports probability of Bush victory on date t) in a regression with dependent variable of excess returns (in columns 1-4), and excess returns net of median industry returns (in columns 5-8).

Connection represents the level at which the company is connected to Cheney (1= Cheney-connected individual is on the company's board of directors, 2= Cheney-connected individual is the company CEO, 3=Cheney as board member 1995-1999, and 4= Cheney as CEO during 1995-1999 (i.e., Halliburton)).

| Dependent variable | Risk-adjusted returns | | | | Risk-adjusted returns (relative to industry median) | | | |
|---|---|---|---|---|---|---|---|---|
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) |
| | Connection | | | | Connection | | | |
| | 1 | 2 | 3 | 4 | 1 | 2 | 3 | 4 |
| ΔBush | -0.008 | 0.055 | -0.028 | 0.018 | 0.016 | -0.001 | -0.020 | 0.016 |
| | (0.191) | (0.038) | (0.084) | (0.133) | (0.016) | (0.018) | (0.053) | (0.099) |
| *N* | 2835 | 532 | 399 | 133 | 2835 | 532 | 399 | 133 |
| *R2* | 0.01 | 0.01 | 0.00 | 0.00 | 0.01 | 0.00 | 0.00 | 0.00 |

Robust standard errors in parentheses

* significant at 10%; ** significant at 5%; *** significant at 1%

***Table 3. Relationship between probability of Saddam's capture and returns, across all connected companies in war-related industries and by level of connection.***

Values represent coefficients on ΔSaddam03 (change in Tradesports probability of Saddam Hussein being captured by 2003) in a regression with dependent variable of excess returns (in column 1), median industry excess returns (in column 2), and excess returns net of median industry returns (in columns 3-6).

Regressions in column (2) use industry-level data; all other regressions use firm-level data.

Connection represents the level at which the company is connected to Cheney (1= Cheney-connected individual is on the company's board of directors, 2= Cheney-connected individual is the company CEO, 3=Cheney as board member 1995-1999, and 4= Cheney as CEO during 1995-1999 (i.e., Halliburton)).

(There were no companies connected at level 3 in these industries)

| Dependent variable | Risk-adjusted returns | Median ind. risk-adjusted returns | Risk-adjusted returns (relative to industry median) | | | |
|---|---|---|---|---|---|---|
| | (1) | (2) | (3) | (4) | (5) | (6) |
| | (All connected companies) | | | Connection | | |
| | | | | 1 | 2 | 4 |
| ΔSaddam03 | 0.0004 | 0.0005** | 0.0000 | 0.0000 | -0.0001 | 0.0003 |
| | (0.0002) | (0.0002) | (0.0001) | (0.0002) | (0.0003) | (0.0007) |
| *N* | 1012 | 552 | 1012 | 736 | 92 | 92 |
| *R2* | 0.00 | 0.01 | 0.00 | 0.00 | 0.00 | 0.00 |

Robust standard errors in parentheses, clustered by company where possible.
* significant at 10%; ** significant at 5%; *** significant at 1%

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