

When Politics Costs Profits: Firm-Level Political Risk and Firm Performance in the U.S.

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Abstract

Understanding how political uncertainty affects firm outcomes is crucial for strategic planning and environmental adaptability in a rapidly shifting institutional landscape. This paper examines the relationship between firm-level political risk (FLPR) and firm performance. While prior research has largely emphasized macro-level political uncertainty, recent studies underscore the importance of firm-specific exposure, shaped by how individual firms perceive and respond to political developments affecting operations and profitability. Using a novel text-based measure of political risk derived from earnings calls, we analyze 21,307 U.S. firm-year observations and, consistent with our expectation, find a significant negative relationship between FLPR and firm performance. We address potential endogeneity by implementing a comprehensive identification strategy that includes placebo tests, propensity score matching technique, instrumental variable estimation, firm fixed effects and dynamic panel estimation via a system generalized method of moments. We also find the effect to be prominent after accounting for crisis and non-crisis periods. Our robust results contribute to the business strategy literature by emphasizing the negative performance implications of political risk, which should be considered in strategic planning and environmental adaptability to support organizational resilience.

Index Terms

Firm-Level Political Risk; Political Uncertainty; Strategic Resilience; Business Strategy; Corporate Performance