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CEO political orientation and loan contract

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Abstract

Banks rely on soft information when assessing loan applications, making it crucial to evaluate the trustworthiness of potential borrowers in order to set loan conditions, even in a legal environment where contractual rights are straightforwardly enforced. Given the common belief that certain personality traits—such as trustworthiness, reliability, loyalty, thriftiness, and stinginess—are more often linked to conservatives (Republicans) than to liberals (Democrats), we investigate whether companies with conservative chief executive officers (CEOs) secure more advantageous loan terms compared to others. Our findings indicate that firms with conservative CEOs are able to negotiate bank loans with lower interest spreads and upfront fees. While we do not observe a direct impact of CEO overconfidence on loan pricing, we reveal that the combined influence of CEO conservatism and overconfidence contributes to our primary findings. Additionally, we discovered that conservative CEOs tend to receive more favorable non-price conditions (fewer covenants) and are less inclined to offer collateral.

Keywords: CEO characteristics, Conservative CEO, Trustworthiness, Loan contract

Introduction

Recent studies suggest that individuals' political affiliations significantly impact their business decision-making processes. For instance, managers who identify with conservative political ideologies are inclined to utilize lower levels of debt (Hutton et al. 2014) and exhibit a reduced propensity to engage in tax avoidance strategies (Christensen et al. 2015). Additionally, analysts with conservative political beliefs tend to produce more cautious financial forecasts (Jiang et al. 2016). This phenomenon can be attributed to the correlation between political orientation and specific personality traits that shape behavior. When parties involved in a contract recognize particular personality traits, such as political orientation, they may take these characteristics into account when negotiating or establishing contract terms. Thus, the perceptions of the traits of the transacting parties can significantly influence business interactions and decisions.

Furthermore, sociological research indicates that trustworthiness—a trait characterized by the ability to inspire trust in others—is more closely associated with a conservative (Republican) political orientation than with a liberal (Democratic) one (Carney et al. 2008).¹ Commercial transactions inherently involve an element of trust (Arrow 1972), and the perceived trustworthiness of the parties involved can lead to more favorable transaction terms. Within the realm of commercial transactions, financial contracts are often considered the "ultimate trust-intensive contract" (Guiso et al. 2004). This study aims to assess the significance of the contracting party's trustworthiness in trust-based financial contracts, specifically focusing on loan agreements between corporations and banks. Trust plays a critical role in corporate lending, as banks engage in due diligence, design and renegotiate contract terms, and monitor borrower behavior throughout the loan process.

The study emphasizes the influence of a CEO's political orientation, as managerial political ideology is indicative of corporate trustworthiness. Prior anecdotal evidence and research have suggested that the political conservatism of borrowers can inform their perceived trustworthiness, which is utilized in credit screening and offerings (Barney & Hansen 1994; Berger et al. 2005; Stein 2002). However, the impact of such political and managerial characteristics on bank loan contract terms has received limited attention in the existing literature. This research investigates whether firms led by conservative (Republican) CEOs receive different loan contract terms compared to those with liberal (Democratic) or politically ambiguous CEOs.

We hypothesize that CEO political conservatism influences bank loan terms, as banks prioritize the trustworthiness of borrowers. Literature in sociology and psychology posits that political orientation shapes individuals' attitudes and values (e.g., Carney et al. 2008). Politically conservative individuals are often associated with specific traits, such as trustworthiness, and are more likely to adhere to their values. This trustworthiness, derived from political ideology, serves as valuable soft information for lenders. If a bank perceives a borrower as trustworthy, it can reduce monitoring costs and offer more favorable loan pricing (Hasan et al. 2017). Furthermore, banks anticipate that trustworthy (conservative) borrowers will honor their loan commitments and exhibit less opportunistic behavior, fostering long-term lending relationships. Consequently, certain CEO characteristics may lead banks to extend more favorable loan contract terms.

Additionally, we argue that conservative corporate policies affect banks' risk assessments. Existing literature indicates that politically conservative CEOs tend to maintain lower levels of debt, reduced R&D expenditures, fewer high-risk investments, and a diminished likelihood of engaging in mergers and acquisitions (M&As) (Hutton et al. 2014; Elnahas & Kim 2017). These findings suggest that Republican-leaning CEOs implement safer and more predictable strategies, resulting in lower default risk for their firms. Given that credit risk is a crucial factor in bank lending decisions, banks may exhibit a preference for CEOs with conservative orientations, leading to the expectation that firms with conservative CEOs will secure more advantageous loan terms.

¹ Other traits include loyalty, reliability, faithfulness, thriftiness, and stinginess.

To empirically test our hypothesis, we assessed CEO political conservatism based on their political contributions to the Republican Party, a widely accepted measure in the literature (e.g., Christensen et al. 2015; Hong & Kostovetsky 2012; Hutton et al. 2014). After controlling for commonly recognized determinants of loan spreads, our analysis reveals that bank loans to firms with conservative CEOs are associated with significantly lower spreads, specifically 9% lower than those of other firms. This reduction in loan spread corresponds to an annual interest cost savings of approximately \$258,000, which is economically significant. Furthermore, we observe that the upfront fees for conservative CEOs are 27.5% lower than those for other firms, indicating that banks perceive loans to these firms as easier to evaluate and monitor.

We anticipate that trustworthiness will significantly influence non-priced loan terms. When lenders perceive a borrower as having a higher level of residual asymmetric information, they may opt for non-priced loan terms rather than adjusting loan rates (Strahan 1999; Dell'Ariccia & Marquez, 2006; Lown & Morgan 2006; Stiglitz & Weiss 1981). Thus, if a borrower's trustworthiness alleviates concerns regarding information asymmetry, banks are likely to offer more favorable non-price terms. Our findings indicate that firms with conservative CEOs receive more advantageous non-priced loan terms, including fewer financial, general, and total covenants, and are less likely to be required to pledge collateral.

To ensure the robustness of our results, we conducted additional tests to address potential confounding factors not explicitly accounted for in our baseline models. First, in low-trust environments, firms and banks may have a greater incentive to mitigate counterparty risk by fostering close borrower-lender relationships (Johnson et al. 2002). While it remains unclear why evolving lending relationships might favor CEOs with specific political values, we controlled for the intensity of borrower-lender relationships, and our results remained largely unchanged. Further analysis suggests that conservative CEOs with established bank relationships tend to secure higher loan spreads, potentially due to banks' assumptions regarding the loyalty and reliability of conservative borrowers (Carney et al. 2008), in addition to the well-documented hold-up effect associated with relationship lending (e.g., Sharpe 1990).

Second, we considered other CEO personality traits, such as overconfidence, which may influence our findings (Malmendier & Tate 2005, 2008). The relationship between CEO overconfidence and bank loan pricing is complex; banks may interpret overconfidence as a signal of positive firm prospects or exploit it to extract higher rents from overly optimistic CEOs. Our analysis indicates that CEO overconfidence does not significantly affect loan terms or materially alter our results. However, firms led by conservative and overconfident CEOs do secure significantly lower spreads, resulting in annual interest savings of \$473,000. These findings suggest that banks place trust in conservative CEOs' assessments of future firm performance. Moreover, our empirical evidence indicates that banks do not impose a risk premium for overconfidence in loan spreads, contrasting with the negative correlation between overconfidence and credit ratings (Hribar et al. 2013).

Third, a CEO's personality may serve as a proxy for their firm's political geography and orientation (Hutton et al. 2014) or religiosity (Hilary & Hui 2009). Our results demonstrate robustness when accounting for these factors.

This study contributes to the literature examining the influence of CEOs' and other key personnel's personality traits and backgrounds on firm policy, including overconfidence (Malmendier and Tate 2005), religiosity (Hilary and Hui 2009), and military and other life experiences (Benmelech and Frydman 2015; Malmendier et al. 2011; Benmelech & Frydman 2015). Closely related to our work, previous studies have established that CEOs' political orientation affects their actions in various contexts (e.g., Lassoued et al. 2023). However, our research is distinct in that it does not focus on the actions of conservative managers per se; rather, it investigates the effects of external perceptions of conservative managers on credit allocation. Thus, our study aligns with the expanding body of literature on political orientation, which remains relatively limited (Hutton et al. 2014; Jiang et al. 2016; Elnahas & Kim 2017; Bhandari & Golden 2021). Unlike other studies that explore the impact of CEO traits on shareholder wealth, analyst forecasts, and credit ratings, we contribute to the literature by emphasizing creditors' evaluations of CEO trustworthiness and documenting that banks consider the trustworthiness of key firm personnel when assessing loan contracts.

Furthermore, our findings have implications for empirical research on the role of information in loan decision-making. This study highlights the significance of soft information in loan issuance decisions. While existing literature emphasizes banks' reliance on hard information to evaluate borrowers' trustworthiness (Ball et al. 2015), our research diverges by focusing on the role of soft information in loan contracts, a topic of increasing interest in related literature (Agarwal & Ben-David 2018; Bozanic et al. 2018; Liberti & Mian 2009; Lin et al. 2011; Ye et al. 2022). By demonstrating that borrower trustworthiness, as proxied by CEOs' political preferences, mitigates the agency cost of debt, our empirical evidence supports the literature linking borrower trustworthiness to lending decisions (Wang et al. 2015; Hasan et al. 2017; Tang et al. 2018).

Two studies have directly examined the impact of borrower trustworthiness on loan outcomes based on borrowers' facial appearance (Duarte et al. 2012; Li et al. 2023). While Duarte et al. (2012) investigate individual lending behavior, our study focuses on financial transactions between banks and corporations. Banks are particularly motivated to monitor firms due to the significant consequences of corporate loan defaults. Consequently, banks must refine their skills by incorporating borrowers' soft information (i.e., trustworthiness). This contrasts with an individual's decision to assess a borrower's image and judge their trustworthiness. Li et al. (2023) find that a CFO's facial trustworthiness correlates with reduced loan spreads, which aligns with our conclusions. However, trustworthiness may vary based on the CEO's political orientation and appearance. While facial trustworthiness typically influences a bank's decisions through interpersonal interactions, its impact is somewhat limited prior to face-to-face meetings between the borrower and the bank.

In contrast, political orientation can be pre-assessed and utilized to gauge the borrower's reliability during the loan process. Li et al. (2023) contend that facial trustworthiness exerts an incremental influence on one aspect of trustworthiness, such as initial impressions, provided that other dimensions, like reputation, have attained specific thresholds.

We propose that a CEO's political orientation is associated with overall trustworthiness, encompassing both reputation and initial impressions.²

The remainder of this paper is organized as follows: Sect. "Related literature and hypotheses development" discusses related literature and develops the hypotheses. Sect. "Data" describes the data, and Sect. "Results" presents the results. Finally, Sect. "Summary and conclusions" presents the summary and conclusions.

Related literature and hypotheses development

Trustworthiness and lending

Recent scholarly investigations and anecdotal observations substantiate the assertion that trustworthiness plays a critical role for contracting parties within the credit market. It has been suggested that lenders are inclined to offer more favorable loan contract terms to politically conservative chief executive officers (CEOs), as they are perceived to be more trustworthy. For example, during a Congressional hearing in 1912, when J.P. Morgan was queried about the possibility of obtaining credit based solely on an individual's "face or character," he responded affirmatively, stating, "Yes; he obtains it on his character... because a man I do not trust could not get money from me on account of the bonds in Christendom... I believe that is the fundamental basis of business." This commentary indicates that trustworthiness is a pivotal factor in determining credit terms and the likelihood of a potential borrower securing credit. This anecdote is consistent with contemporary academic findings that highlight the significance of trust among contracting parties. The trustworthiness of economic entities has been shown to substantially impact various economic indicators, including gross domestic product (GDP) growth (Knack & Keefer 1997), firm expansion (La Porta et al. 1997), financial development (Guiso et al. 2004), stock market engagement (Guiso et al. 2008), diversification of investment portfolios (Cohen 2009), and cross-border investments (Guiso et al. 2009). In an international framework, Slemrod and Katuščák (2005) demonstrate that trustworthiness yields positive outcomes in nations characterized by high levels of aggregate trust. Furthermore, Raiser et al. (2008) provide evidence that trust remains significant even in jurisdictions with robust creditor rights and effective judicial enforcement.

Scholars have posited that bank loan managers often rely on qualitative information in their decision-making processes (e.g., Berger et al. 2005; Liberti & Mian 2009). We argue that a borrower's perceived trustworthiness is of considerable importance to banks. If banks are confident that borrowers will manage entrusted resources responsibly and fulfill their obligations, they are more inclined to extend credit under favorable conditions, even in the absence of strong legal and contractual safeguards. Several studies have directly investigated the relationship between a borrower's trustworthiness and lending decisions, particularly in relation to the borrower's physical appearance. For instance, Duarte et al. (2012) found that borrowers who exhibit a more trustworthy appearance

² Similar to our study, Francis et al. (2012) examine the relationship between CEOs' political orientation and loan contract terms. Our empirical evidence is largely consistent with their findings. However, we elaborate on the positive association between politically conservative CEOs and loan contract terms by linking conservatism to borrower trustworthiness and credit risk. To corroborate our argument, we benefit from concurrent studies on corporate political orientation (e.g., Bhandari & Golden 2021; Christensen et al. 2015; Elnahas and Kim 2017; Jiang et al. 2016). We also conduct several robustness tests to rule out potential explanations. Particularly, we document the cross-sectional variations in borrower-lender relationships, firm political orientation, and regional political orientation. Thus, we believe our study complements an in-depth understanding of the loan outcomes of managerial political orientation.

are more likely to secure funding in peer-to-peer lending environments. Similarly, Li et al. (2023) demonstrated that banks tend to offer more advantageous loan terms to firms led by trustworthy chief financial officers (CFOs). Consequently, trustworthiness emerges as a vital source of information that influences lending practices.

Political orientation and corporate policies

The extant literature within the social sciences indicates that individual political characteristics can significantly influence behavior. For instance, individuals with conservative ideologies typically exhibit risk-averse tendencies, often steering clear of uncertainty and ambiguity, prioritizing financial stability, and expressing concerns about the potential loss of their assets (Kish et al. 1973; Wilson 1973; Glasgow & Cartier 1985; Jost et al. 2003). Such personal orientations shape an individual's beliefs and attitudes towards various societal dimensions, including social norms. Numerous studies have illustrated that conservatives or Republicans place a high value on the preservation of traditions, fiscal conservatism, national defense, and trade protections (Carney et al. 2008; Bhandari & Golden 2021).

Political traits are also pivotal in economic contexts. An emerging body of literature has concentrated on the political traits of Chief Executive Officers (CEOs), as these traits can influence organizational behavior and corporate policies. Hutton et al. (2014) found that firms led by Republican CEOs tend to utilize less debt, allocate fewer resources to research and development, and invest less in high-risk projects. Elnahas and Kim (2017) explored the correlation between CEO political ideology and mergers and acquisitions (M&A) decisions, revealing that Republican CEOs are less inclined to pursue M&As, favor public firms as targets, and prefer cash transactions. Christensen et al. (2015) examined the impact of executives' political orientations on aggressive tax planning, a significant operational risk for firms. Their findings indicated that companies with Republican-leaning top managers engage in less tax avoidance, suggesting that conservative CEOs are more motivated to uphold the status quo and eschew excessive risk-taking. Additionally, Jiang et al. (2016) investigated the political traits of financial analysts, determining that analysts who predominantly contribute to the Republican party exhibit a more conservative forecasting style. This observation implies that political orientation serves as a personal characteristic that influences economic decision-making.

Furthermore, the political preferences of CEOs also shape their assessments of external stakeholders. Bhandari and Golden (2021) discovered that credit rating agencies take into account the political ideologies and conservatism of managers, leading to a perception of reduced financial risk; consequently, these agencies assign higher credit ratings to firms with Republican CEOs. While the aforementioned literature elucidates the influence of CEO political orientation on various corporate policies and credit rating evaluations, it offers limited insights into whether banks consider CEO political preferences in their lending practices.

Hypothesis development

The relationship between a conservative CEO's political orientation and bank loan contracts is influenced by the interaction between the perceived trustworthiness of borrowers and their associated credit risk. Existing banking literature indicates that financial

institutions can obtain private information regarding a firm's credit risk (Fama 1985; Rajan 1992). However, in order to maintain this advantageous position, lenders must invest in information-gathering efforts to accurately assess the creditworthiness of borrowers (Bharath et al. 2011). For instance, borrowers may be motivated to undertake high-risk projects at the expense of debt holders' wealth (Jensen & Meckling 1976). Some research posits that trust between borrowers and lenders can alleviate moral hazard issues faced by borrowers (Chen et al. 2016; Hasan et al. 2017; Chung et al. 2022). This body of literature suggests that if a lender perceives a borrower as trustworthy, it can lead to reduced monitoring costs.

When a CEO's political orientation is evident, banks may leverage their understanding of the typical characteristics associated with political conservatism to infer the CEO's political traits as a broader indicator of trustworthiness (Carney et al. 2008). Prior studies have demonstrated that banks exhibit a preference for conservative firms due to their reliable adherence to loan agreements (e.g., Barney & Hansen 1994). Stein (2002) and Berger et al. (2005) further illustrate that a conservative CEO may represent an ideal candidate for a 'character loan.'

Given the nature of financial transactions, banks tend to favor a 'strong-form' of trust (Barney & Hansen 1994). Although banks may possess vulnerabilities that could be exploited, they operate under the assumption that conservative borrowers are less inclined to act opportunistically, as these borrowers are perceived to uphold their "values, principles, and standards of behavior that have been internalized" (Barney & Hansen 1994). For example, banks may expect that conservative CEOs are less likely to neglect their responsibilities, engage in excessive personal consumption, employ deceptive practices, or pursue high-risk strategies. Furthermore, conservative CEOs are likely to experience remorse if they default on their debt obligations (Jiang et al. 2016) and exhibit heightened sensitivity to potential losses (Wilson 1973). Consequently, there is diminished necessity for banks to invest in mechanisms for monitoring and intervening in the actions of borrowers (Barney & Hansen 1994). This dynamic allows contracting parties to allocate resources more efficiently.³

Moreover, a reliable borrower contributes to the establishment of a robust lending relationship, thereby enabling banks to sustain future lending activities, as the information pertaining to the borrower is characterized by specificity, durability, and reusability (Boot 2000). In conclusion, reliable borrowers, particularly those led by conservative CEOs, alleviate lenders' apprehensions regarding moral hazard mitigation and consequently offer greater opportunities for future lending. Hence, we posit that politically conservative CEOs may be afforded more favorable loan terms due to the anticipated additional benefits perceived by banks.

Furthermore, given that firms with conservative CEOs exhibit lower credit risk, we hypothesize that political conservatism may lead to a reduction in the stringency of loan terms. These firms tend to exercise caution in their borrowing and debt expenditure (Hutton et al. 2014). Additionally, they strategically manage their investments to maintain a lower risk profile (Hutton et al. 2014; Elnahas & Kim 2017) and discourage

³ By obtaining a lower cost capital, more projects become feasible, and the economic benefits therefrom are shared between the borrower and the creditor. Less trustworthy borrowers might have to pass on some projects.

opportunistic behavior, thereby alleviating lenders' concerns regarding the credit risk associated with borrowers. In summary, conservative CEOs are generally averse to engaging in excessive risk-taking behaviors, which results in more favorable terms in loan contracts.

The aforementioned arguments suggest that lenders view conservative CEOs as more trustworthy, with diminished moral hazard issues and credit risks, which in turn leads to improved loan terms from banks. Consequently, we propose the following hypotheses:

H: Firms with conservative CEOs receive favorable loan terms.

Conservative chief executive officers (CEOs) may incur higher interest rates on loans and encounter less favorable non-price terms due to the exploitation of their perceived trustworthiness. Drawing on the concept of heterogeneity in trustworthiness within society (Ross et al. 1977), the exploitation perspective posits that individuals who are deemed most trustworthy are often subjected to deceit, as they tend to project their own trustworthiness onto others. Research conducted by Butler et al. (2016) utilizing European survey data provides evidence of rent exploitation, indicating that financial institutions are motivated to appropriate the returns of borrowers. Additionally, findings by Slemrod and Katuščák (2005) support this exploitation perspective, revealing a negative correlation between trustworthiness and financial outcomes in low-trust environments.

Moreover, it can be posited that the political orientation of CEOs does not significantly affect the cost of bank debt for their firms, due to the weak correlation between political orientation and the trustworthiness channel. This dynamic may be influenced by the institutional framework in the United States, where contractual rights are readily enforceable, thereby diminishing the importance of trustworthiness among contracting parties. Furthermore, the interplay of various CEO characteristics, including age, gender, and physical appearance, which are associated with perceptions of trustworthiness, may further dilute the impact of political preferences on loan acquisition. Consequently, it is imperative to empirically investigate the relationship between a CEO's political conservatism and the terms of loan contracts.

Data

Data on conservative and overoptimistic CEOs

In this study, we gathered data from multiple sources to analyze the political values of Chief Executive Officers (CEOs). Our initial step involved selecting firms from the Standard and Poor's (S&P) 1500 index, focusing specifically on relatively large corporations. We assessed the political orientations and levels of financial conservatism of corporate executives by examining their political contributions. To infer the political affiliations of CEOs, we utilized the political contribution data reported by the Federal Election Commission (FEC). The political orientations of these executives were determined based on their financial contributions to candidates and committees associated with the Republican and Democratic parties, including those for the Senate, House of Representatives, and presidential campaigns. Political candidates and parties have established committees to collect and manage campaign funds, with the FEC overseeing the financing of federal elections. For contributions exceeding \$200, the FEC discloses the identities of donors, the amounts contributed, the recipients of these contributions (including party affiliation), and aggregated statistical data, which can be accessed at <http://www.fec.gov>.

Corporate executives may contribute either directly through personal donations to candidates or party committees or indirectly via their companies' political action committees (PACs). However, only direct contributions allow for the identification of executives' political orientations, as PACs typically distribute funds to multiple parties simultaneously. The FEC's individual contribution data includes the donor's name, address, occupation, contribution amount, and date.

We developed two metrics to measure CEO conservatism. The first metric, termed Conservative CEO (Forward-looking), is a binary variable that assumes a value of "1" if the CEO allocates all political contributions during their tenure to the Republican party, and "0" otherwise. The second metric, Conservative CEO (Contemporaneous), is also a binary variable that takes the value of "1" if the CEO makes political contributions to the Republican party prior to securing a loan, and "0" otherwise. These metrics serve as standard proxies for identifying conservative CEOs, as utilized by Hutton et al. (2014) and other researchers in the field.⁴

To proxy for over-optimistic CEOs, we use the CEO overconfidence measure from Malmendier and Tate (2005, 2008) and utilize the number of unexercised exercisable options the CEO has in their firm (Campbell et al. 2011). Malmendier and Tate (2005) contend that if a CEO does not exercise options at least 67% deep in the money, they are overconfident because their portfolio is not diversified.

Bank loan data and firm characteristics

The data utilized in this study is sourced from the LPC DealScan database, which encompasses historical bank loan information derived from SEC filings and self-reported data from banks. DealScan provides an extensive repository of loans issued to corporations, featuring over 110,000 global loans, high-yield bonds, and private placements dating back to the mid-1980s. The compilation of loan data is achieved through SEC filings, public documents, loan syndicators, and various internal sources, with new transactions being incorporated into the database on a weekly basis. DealScan is accessible via LoanConnector, an LPC Internet-based product distribution platform, and is recognized as a leading source of comprehensive and reliable information regarding the global commercial loan market. The database includes detailed historical data on loan pricing, contractual terms and conditions, as well as information on high-yield bonds, private placements, and hybrid financial structures.

To investigate the impact of CEO conservatism on bank loan pricing, we controlled for several variables that may influence both the price and non-price terms of bank loans. A brief overview of these variables is provided, with additional details available in the Appendix. The sample variables encompass borrower and loan characteristics, prevailing

⁴ There may be a concern that political contributions cannot perfectly capture managerial political preferences. However, previous related literature addresses this with validation tests. Hutton et al. (2014) examine the relation between a manager's self-reported party affiliation and the conservative CEO measure, finding that the conservative CEO measure from political donations and the self-reported political orientation measure are highly correlated (correlation: 0.44). They further test whether political donations correlate with managerial demography, finding that the correlation between the conservative CEO measure and gender, age, and ethnicity is low (0.085, 0.050, and -0.067, respectively), suggesting that a conservative CEO measure captures a manager's political orientation. Furthermore, Jiang et al. (2016) show that 86.33% of analysts contribute to only one party during the entire sample period, implying that political donations represent individual preferences rather than strategic choices. We appraise our conservative CEO measure as valid and less subjective based on the validation results in the related studies.

business conditions, industry-specific factors, and temporal effects. Borrower-specific data is obtained from the COMPUSTAT database.

At the firm level, we identified six control variables: (i) Total assets, measured in millions of US dollars as of 1984, with larger firms generally exhibiting less conservatism (Khan & Watts 2009); (ii) Market-to-book ratio, calculated as the market value of equity plus the book value of debt divided by total assets, where an increase in this ratio indicates a decrease in financial leverage (Duong et al., 2021); (iii) Leverage, defined as the sum of long- and short-term debt divided by total assets, with higher debt financing leading to increased financial constraints (Coles et al. 2006); (iv) Profitability, represented as EBITDA divided by total assets, where firms with higher profitability tend to maintain lower leverage to mitigate debt (Rajan & Zingales 1995); (v) Tangibility, calculated as the value of net assets, plants, and equipment divided by total assets, with firms possessing a higher proportion of tangible assets often having greater collateral and access to credit (Flannery & Rangan 2006); and (vi) Z-score, a modified Altman Z-score, which assesses whether conservative CEOs reduce the likelihood of default through lower-risk behaviors (Han & Jung 2023).

Our regression models incorporate four loan-specific variables: (i) Loan maturity, defined as the duration of a loan in months; (ii) Loan size, quantified as the facility amount in millions of USD from 1984; (iii) Loan performance, a binary variable indicating whether the loan employs performance pricing; and (iv) Collateral, a binary variable indicating whether the loan is secured by collateral. Additionally, we include two macroeconomic variables that capture business cycle effects (Fama & French 1993), which may influence loan terms: the credit spread, defined as the yield differential between BAA- and AAA-rated corporate bonds, and the term spread, defined as the yield difference between ten-year and two-year Treasury securities one month prior to the loan's initiation date. This data is sourced from the Federal Reserve database. Given that the LPC DealScan database utilizes a ticker as its sole identifier, we employed Michael R. Roberts's linking table to connect the COMPUSTAT and LPC DealScan databases. After excluding observations with missing variables, our final sample consisted of 6,144 loan facility-level observations.

The selection of control variables in this study is informed by existing literature on bank loans (e.g., Graham et al. 2008). We controlled for the logarithm of total assets, as larger firms typically have enhanced access to external financing, reduced information asymmetry, and lower monitoring costs. The market-to-book ratio was included to account for a firm's growth opportunities, as firms with superior growth prospects may experience lower loan spreads. Leverage was incorporated to address the heightened default risk associated with highly leveraged firms, which are expected to face increased borrowing costs. Profitability was also controlled for, as profitable firms generally exhibit lower default risk. Tangibility serves as a proxy for recovery levels in the event of default, with firms possessing more tangible assets anticipated to incur lower bank debt costs. The Altman Z-score is utilized as an additional measure of default risk. Furthermore, we accounted for borrowers' credit ratings in relation to default risk. Several loan characteristics that influence loan spreads were also included in our analysis. Loan maturity was considered, as lenders typically demand higher premiums for long-term debt. Loan size was included, as we hypothesize that banks may offer advantages for larger loans while

Table 1 Summary statistics

Variable	N	Mean	Median	Q1	Q3
Conservative CEO (Forward-looking) (dummy)	7331	0.206	0.000	0.000	0.000
Conservative CEO (Contemporaneous) (dummy)	7331	0.211	0.000	0.000	0.000
Overconfident CEO (Holder67) (dummy)	7325	0.452	0.000	0.000	1.000
Log (loan spread)	6144	4.106	4.001	3.401	4.787
Spread (basis points)	6144	90.123	55.000	30.000	120.000
Loan maturity (months)	6650	41.067	36.000	12.000	60.000
Log (loan maturity)	6685	3.372	3.584	2.397	4.088
Log (loan size)	7329	5.826	5.857	5.075	6.620
Number of lenders	7318	11.317	9.000	3.000	16.000
Total number of covenants	7331	2.968	1.000	0.000	5.000
Collateral (dummy)	3350	0.352	0.000	0.000	1.000
Upfront fee (basis point)	861	38.207	20.000	10.000	50.000
Annual fee (basis point)	3645	12.258	10.000	7.000	15.000
Log (asset)	7331	7.714	8.606	7.615	9.667
Leverage	7321	0.285	0.275	0.165	0.383
Tangibility	7203	0.335	0.288	0.151	0.511
Profitability	7247	0.142	0.133	0.090	0.183
Market-to-book	7325	1.942	1.493	1.186	2.143
Z-score	6371	1.813	1.770	1.001	2.524
Asset maturity	7370	11.085	8.605	4.958	14.741
Relationship loan (dummy)	7331	0.615	1.000	0.000	1.000
Tech industry (dummy)	7331	0.128	0.000	0.000	0.000

Tables 1–3 The Tables presents the summary statistics of CEOs' political characteristics and loan contract terms for the sample loans. The Table presents the full sample's summary statistics

perceiving smaller loans as riskier. The performance pricing dummy variable was incorporated due to the impact of additional pricing clauses on loan pricing decisions. Additionally, we considered two macroeconomic variables in our regression model, as credit and term spreads serve as effective indicators of macroeconomic conditions. We also included fixed effects for loan type and purpose, as these factors present varying risks that can influence loan pricing. Finally, industry and year-fixed effects were included to control for time-invariant characteristics of borrower industries and temporal trends.⁵

Table 1 provides summary statistics for the variables under consideration. The analysis encompasses a sample period from 2010 to 2020, comprising 7,331 observations derived from an initial cohort of 771 firms listed in the S&P 1500 index. The mean loan spread within this sample is approximately 90 basis points, which is notably lower than the spreads reported in several prior studies utilizing the same database. This discrepancy can be attributed to the highly specific nature of loan spreads within different samples. For example, Graham et al. (2008) reported an average spread of 173 basis points in their analysis; however, their sample was significantly smaller, consisting of fewer than 2,000 firms, which are likely to exhibit larger spreads compared to the larger, typically higher-quality firms represented in our study.

⁵ For detailed discussions on selecting control variables, please refer to Graham et al. (2008).

Table 2 presents univariate evidence indicating that firms led by conservative CEOs tend to have lower loan spreads than their counterparts. Nevertheless, the observed difference—ranging from two to seven basis points—appears to be economically trivial, suggesting that the influence of soft information, such as the perceived trustworthiness of conservative CEOs, is not particularly pronounced in univariate analyses prior to the incorporation of hard information. The hard information variables exhibit variability between firms with conservative and non-conservative CEOs, indicating that certain factors may enable conservative CEOs to secure more favorable loan terms, while others may adversely impact those terms. For instance, firms with conservative CEOs tend to possess fewer valuable assets, which could lead to higher loan spreads; conversely, these firms also exhibit lower leverage, higher Z-scores, and greater profitability, which may contribute to lower average spreads.

Table 3 displays the Pearson correlation coefficients for the three CEO characteristics employed to explore the interrelationships among the variables. It is not surprising that the two measures of CEO political conservatism are highly correlated, with a coefficient of 0.859. This indicates that a CEO's recent political orientation is largely consistent with their prior orientation, suggesting minimal fluctuations in their political stance. Additionally, the correlation between CEO political conservatism and overconfidence is both negative and small, implying that politically conservative CEOs do not exhibit excessive optimism in their corporate decision-making processes.

Results

The impact of conservative CEOs on loan cost

In our study, we categorized CEO conservatism metrics into two distinct dimensions: consistent political preference (forward-looking) and temporal political orientation (contemporaneous). This approach mitigates concerns related to political contributions, which are often strategic decisions aimed at alleviating financing constraints. The robustness of both measures substantiates the validity of our primary metric. Furthermore, consistent and robust evidence indicating a correlation between political contributions to the Republican Party and conservative corporate policies implies that our measure effectively reflects the political orientation of the CEO. Our analysis commenced with the estimation of the following foundational model:

$$\begin{aligned} \ln \text{ loan spread}_i &= b_0 + b_1 \text{ conservativeCEO}_i + b_2 \ln \text{ assests}_i + b_3 \text{ leverage}_i + b_4 \text{ tangibility}_i + b_5 \text{ profitability}_i \\ &+ b_6 \text{ MB}_i + b_7 \text{ Zscore}_i + b_8 \text{ creditrating}_i + b_9 \text{ assetmaturity}_i + b_{10} \ln \text{ loanmaturity}_i \\ &+ b_{11} \text{ performancepricing}_i + b_{12} \text{ relationship}_i + b_{13} \ln \text{ loansize}_i + b_{14} \text{ creditspread}_i \\ &+ b_{15} \text{ termspread} + B_{16} \text{ loantype} + B_{17} \text{ loanpurpose} + B_{18} \text{ industry} + B_{19} \text{ year} + \varepsilon_i \end{aligned} \quad (1)$$

In this model, we conduct a regression analysis of the natural logarithm of the all-in-spread ($\ln \text{ loanspread}$) against a proxy for conservative CEOs (conservativeCEO), alongside various firm characteristics, loan characteristics, macroeconomic variables, loan type information, the purpose of proceeds, and fixed effects for both industry and year. Definitions for all variables utilized in the analysis are provided in the Appendix. Given that each firm may have multiple loans included in the sample, we employ clustering of standard errors at the firm level.

Table 3 Summary statistics—correlation among CEO characteristics

	Conservative CEO (FL)	Conservative CEO (CT)	Holder67
Conservative CEO (Forward-looking)	1		
Conservative CEO (Contemporaneous)	0.859	1	
Holder67	−0.011	−0.0233	1

The Table presents the Pearson correlation coefficients of CEO characteristics. The definitions of all variables are in the Appendix

*, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively

Table 4 presents the effect of conservative CEOs on loan spreads.⁶ In Model (1), which employs the Forward-looking proxy, the coefficient is found to be negative and statistically significant, suggesting that conservative CEOs secure loan spreads that are 8% lower than those of their non-conservative counterparts. Similarly, in Model (2), which utilizes the Contemporaneous proxy for conservative CEOs, the coefficient associated with conservative CEOs is also significantly negative, resulting in a reduction of the loan spread by approximately 9.15%. The average loan size for firms led by conservative CEOs in our sample is \$318,300,000, with an average loan spread of 90 basis points. Consequently, the interest savings attributable to a CEO's political orientation range from \$258,000 to \$262,000.

Upon initial examination, the economic significance of our findings appears modest when considering the overall interest cost of the average loan. However, we contend that the impact of a conservative CEO on loan pricing is considerable for three primary reasons: First, our sample comprises large firms and banks within the S&P 500, which tend to rely more heavily on hard information as opposed to soft information (Berger et al. 2005), suggesting that our findings may be underestimated.⁷ Second, the coefficients for conservative CEOs indicate incremental interest savings arising exclusively from banks utilizing a specific type of soft information after assessing the quantifiable information from firms, loans, and macroeconomic characteristics. Third, the significance of our results should be considered in the specific context of the United States, where a strong legal and institutional environment facilitates the enforcement of contracts; consequently, CEO trustworthiness, proxied by political contributions, influences loan pricing. This explanation is consistent with that of Slemrod and Katuščák (2005), who find

⁶ We use the variance inflation factor (VIF) to assess multicollinearity in our regression models. VIF identifies correlations between independent variables and correlation strength, starting at 1 with no upper limit. A value of 1 indicates no correlation between this independent variable and others. VIFs between 1 and 5 suggest a moderate correlation, but not severe enough to warrant corrective measures. VIFs greater than 5 represent critical levels of multicollinearity where the coefficients are poorly estimated, and the p-values are questionable. We find that the VIFs from Tables four to nine are between 1 and 5 (mostly less than 3). Thus, we believe that our regression results are not necessarily disturbed by the multicollinearity issue.

⁷ Stein (2002) suggests that if banks' capital allocations are "decentralized," which might prevail in multi-bank holding companies, then there is greater incentive for the bank's local agents to gather and use soft information. Liberti and Mian (2009) use data from a large multinational bank in Argentina and find that the bank uses soft information in its decisions to lend to large firms. They also find that the negative impact of hierarchical distance, e.g., between the agent collecting the soft information and the manager responsible for the loan approval, on the use of soft information is mitigated by a closer geographic relationship between the two and the manager's personal experience with the agent's information collecting skills.

Table 4 Effect of CEO conservatism on the cost of bank debt

	(1)	(2)
Conservative CEO (Forward-looking)	− 0.0801** (− 2.08)	
Conservative CEO (Contemporaneous)		− 0.0915** (− 2.52)
<i>Firm characteristics</i>		
Log (assets)	− 0.1241*** (− 6.13)	− 0.1235*** (− 6.14)
Leverage	1.3466*** (8.83)	1.3495*** (8.89)
Tangibility	0.0948 (0.69)	0.0988 (0.72)
Profitability	− 1.7425*** (− 4.98)	− 1.7430*** (− 4.99)
Market-to-book	− 0.0321*** (− 3.14)	− 0.0325*** (− 3.16)
Z-score	− 0.0233 (− 1.34)	− 0.0227 (− 1.32)
Rating	− 0.0523*** (− 6.61)	− 0.0517*** (− 6.49)
Asset maturity	− 0.0088* (− 1.86)	− 0.0089* (− 1.90)
<i>Loan characteristics</i>		
Log (loan maturity)	− 0.0438 (− 1.19)	− 0.0430 (− 1.16)
Performance pricing	0.0794*** (2.69)	0.0795*** (2.69)
Log (loan size)	− 0.0788*** (− 4.79)	− 0.0791*** (− 4.82)
<i>Macroeconomics factors</i>		
Credit spread	0.1079 (0.72)	0.0974 (0.65)
Term spread	0.0540 (1.29)	0.0557 (1.34)
Constant	5.6056*** (20.98)	5.5898*** (21.05)
<i>Controls</i>		
Loan type	Yes	Yes
Loan purpose	Yes	Yes
Industry effect	Yes	Yes
Year effect	Yes	Yes
Observations	5,209	5,209
Adjusted R-squared	0.547	0.548

This table presents the regression results for the effect of CEO conservatism on the cost of bank debt. The dependent variable is Log (loan spread). Clustered-robust t-statistics are reported in parentheses in Models (1) and (2). The definitions of all variables are in the Appendix

*, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively

trustworthiness earns a positive payoff in countries where the aggregate amount of trust is high.⁸

The results for the control variables demonstrated the expected signs with statistical significance. For instance, loan spreads are significantly lower for firms with more valuable assets, greater profitability, higher market-to-book value, higher Z-scores, greater asset maturity, and better credit ratings. By contrast, highly leveraged firms have higher loan spreads. These findings align with those of other studies, such as Graham et al. (2008) and Houston et al. (2014).

However, small and medium companies that do not have the same financial and governance characteristics may not be able to apply it directly. Further research is required to explore whether these findings hold for other business types.

The impact of conservative CEOs on non-price loan terms

Next, we consider the effects of conservative CEOs on several non-priced terms in loan contracts. The basic model resembles that of (1).

$$\begin{aligned} \text{nonpriceterm}_i &= b_0 + b_1 \text{conservativeCEO}_i + b_2 \ln \text{assets}_i + b_3 \text{leverage}_i + b_4 \text{tangibility}_i + b_5 \text{profitability}_i \\ &+ b_6 \text{MB}_i + b_7 \text{Zscore}_i + b_8 \text{creditrating}_i + b_9 \text{assetmaturity}_i + b_{10} \ln \text{loanmaturity}_i \\ &+ b_{11} \text{performancepricing}_i + b_{12} \text{relationship}_i + b_{13} \ln \text{loansize}_i + b_{14} \text{creditspread}_i \\ &+ b_{15} \text{termspread} + B_{16} \text{loantype} + B_{17} \text{loanpurpose} + B_{18} \text{industry} + B_{19} \text{year} + \varepsilon_i \end{aligned} \quad (2)$$

Table 5 delineates the findings of the study. In Models 1 and 2, Probit models are employed, with the dependent variable coded as "1" if the loan necessitates collateral and "0" otherwise. The analysis utilizing a contemporaneous measure reveals that firms led by conservative CEOs exhibit a diminished likelihood of requiring collateral when securing loans. Specifically, a coefficient of -0.1825 corresponds to a marginal effect of 6.4% within the Probit framework, while controlling for other variables at their mean values. These findings are particularly significant given the critical function of collateral in loan security, the mitigation of asymmetric information, the fulfillment of incomplete contracts, and the reduction of agency issues between lenders and borrowers. Furthermore, the results substantiate the notion that conservative CEOs alleviate lender apprehensions regarding potential opportunistic behavior by borrowers post-loan acquisition.

Several control variables demonstrated statistical significance and aligned with anticipated outcomes. These variables generally mirrored the patterns observed in the loan pricing analysis. Smaller firms characterized by higher leverage, lower profitability,

⁸ Previous studies have shown that CFOs typically have a more direct impact on financial policies and strategies due to their specialized financial knowledge (Gore et al. 2011; Ge et al. 2011; Li et al. 2023). To consider, we re-estimate Table 2 to see the effect of CFOs' conservatism on the cost of bank debt. The results still find negative relationships between CFOs' conservatism and the cost of bank debt. However, their economic and statistical significance are weaker than those based on CEOs' conservatism. Hence, we conclude that though the conservatism of CEOs and CFOs is important in loan contracts, the role of CEOs and their characteristics as top managers are more critical. We focus on firms in which a transition from a non-conservative to a conservative CEO has occurred and investigate the impact of such a CEO change on borrowing costs. As a further robustness test for the causal inference of our study, we construct a dummy variable classifying a firm in which a CEO's non-conservatism has been changed to conservatism in a given year and include the dummy variable in the regression models in Table 2. The results show a negative relationship between the dummy variable and loan spread, implying that conservative CEOs reduce loan pricing. The results are available upon request.

Table 5 Effects of CEO conservatism on non-spread contract terms

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
FConservative CEO	−0.1277 (−1.21)		−0.0612* (−1.67)		−0.0589 (−1.38)		−0.0640* (−1.72)		0.0168 (1.00)	
CConservative CEO		−0.1825* (−1.72)		−0.1057*** (−3.06)		−0.1223*** (−3.01)		−0.0657* (−1.85)		0.0162 (1.02)
<i>Firm characteristics</i>										
Log (assets)	−0.1881*** (−3.42)	−0.1876*** (−3.41)	−0.1636*** (−7.12)	−0.1634*** (−7.13)	−0.1440*** (−5.65)	−0.1439*** (−5.68)	−0.2120*** (−8.19)	−0.2115*** (−8.17)	−0.0392*** (−3.77)	−0.0394*** (−3.79)
Leverage	2.3602*** (6.57)	2.3675*** (6.60)	0.6903*** (5.37)	0.6967*** (5.42)	0.6428*** (4.35)	0.6502*** (4.41)	0.8261*** (5.65)	0.8296*** (5.66)	0.1052 (1.43)	0.1049 (1.43)
Tangibility	−0.1458 (−0.37)	−0.1376 (−0.35)	0.0682 (0.50)	0.0744 (0.55)	0.0762 (0.49)	0.0871 (0.57)	0.0435 (0.28)	0.0403 (0.26)	0.0761 (1.10)	0.0764 (1.11)
Profitability	−2.9335*** (−3.27)	−2.9241*** (−3.27)	−0.3630 (−1.17)	−0.3549 (−1.15)	−0.4012 (−1.11)	−0.3918 (−1.08)	−0.2870 (−0.86)	−0.2819 (−0.85)	−0.1934* (−1.75)	−0.1943* (−1.76)
Market-to-book	−0.0333** (−2.02)	−0.0348** (−2.07)	−0.0222 (−1.43)	−0.0231 (−1.47)	−0.0216 (−1.18)	−0.0228 (−1.22)	−0.0241 (−1.57)	−0.0245 (−1.60)	−0.0024 (−0.53)	−0.0023 (−0.51)
Z-score	−0.0582 (−1.00)	−0.0561 (−0.96)	−0.0033 (−0.16)	−0.0024 (−0.12)	−0.0164 (−0.79)	−0.0154 (−0.74)	0.0269 (1.07)	0.0275 (1.08)	0.0105 (1.42)	0.0104 (1.40)
Rating	−0.0927*** (−4.96)	−0.0922*** (−4.92)	−0.0077*** (−1.98)	−0.0079** (−2.05)	−0.0086** (−2.09)	−0.0090** (−2.19)	−0.0055 (−1.22)	−0.0056 (−1.22)	0.0044 (1.31)	0.0043 (1.28)
Asset maturity	−0.0199* (−1.80)	−0.0204* (−1.85)	−0.0251*** (−3.62)	−0.0251*** (−3.62)	−0.0249*** (−3.05)	−0.0249*** (−3.07)	−0.0235*** (−3.27)	−0.0232*** (−3.23)	0.0022 (1.13)	0.0022 (1.13)
<i>Loan characteristics</i>										
Log (loan maturity)	0.0570 (0.69)	0.0558 (0.67)	−0.0836** (−2.18)	−0.0833** (−2.17)	−0.0906** (−2.18)	−0.0901** (−2.17)	−0.0669 (−1.60)	−0.0671 (−1.61)		
Performance pricing	−0.3245*** (−3.90)	−0.3222*** (−3.86)	1.1174*** (19.90)	1.1174*** (19.93)	1.1106*** (18.82)	1.1104*** (18.85)	1.1350*** (18.87)	1.1351*** (18.88)	0.0162 (1.17)	0.0162 (1.17)

Table 5 (continued)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Log (loan size)	−0.1394*** (−3.35)	−0.1389*** (−3.35)	0.0645*** (3.45)	0.0640*** (3.43)	0.0874*** (4.28)	0.0868*** (4.27)	0.0095 (0.40)	0.0093 (0.40)	0.0428*** (3.69)	0.0428*** (3.70)
<i>Macroeconomics factors</i>										
Credit spread	0.4558 (0.91)	0.4296 (0.86)	0.4692** (2.50)	0.4552** (2.44)	0.5031** (2.38)	0.4878** (2.32)	0.4104** (2.13)	0.4005** (2.08)	−0.0170 (−0.20)	−0.0156 (−0.18)
Term spread	−0.1243 (−0.85)	−0.1168 (−0.80)	−0.0549 (−1.14)	−0.0526 (−1.10)	−0.0257 (−0.45)	−0.0238 (−0.42)	−0.1193** (−2.46)	−0.1169** (−2.41)	0.0222 (0.94)	0.0218 (0.93)
Constant	2.7863*** (3.44)	2.7533*** (3.41)	1.5240*** (4.71)	1.5099*** (4.69)	1.0694*** (3.17)	1.0585*** (3.16)	0.3015 (0.70)	0.2842 (0.66)	3.8973*** (32.22)	3.9008*** (32.25)
<i>Controls</i>										
Loan type	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Loan purpose	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	2981	2981	5796	5796	5796	5796	5796	5796	5796	5796
Adj. R-squared	0.314	0.315	—	—	—	—	—	—	0.753	0.753

This table presents the regression results for the effect of CEO conservatism on non-spread contract terms. Models (1) and (2) are Probit regressions, with the collateral dummy variable as the dependent variable. Models (3) to (8) are Poisson regressions with the total, general, and financial covariates as dependent variables. Models (9) and (10) are OLS regressions with Log (loan maturity) as the dependent variable. Clustered-robust t-statistics for OLS regressions and clustered-robust z-statistics for Probit and Poisson regressions are reported in parentheses. The definitions of all variables are in the Appendix

***, ** and * indicate significance at the 10%, 5%, and 1% levels, respectively

limited growth opportunities, inferior credit ratings, and shorter asset maturities are more inclined to face collateral requirements.

Models 3 and 4 investigate the impact of conservative CEOs on covenant intensity through a Poisson model. The findings suggest that contracts involving conservative CEOs mitigate banks' concerns regarding borrowers' moral hazards. Although negative and statistically significant coefficients for FConservative CEO and CConservative CEO were identified, the economic implications are minimal, given that the average total number of covenants is three.

In Models 5 and 6, we differentiate between the number of financial covenants and the overall covenant count, assessing the influence of conservative CEOs on financial covenant intensity. As anticipated, the evidence indicates that loans secured by conservative CEOs impose between 6 and 12% fewer restrictions on accounting ratios and financial metrics. Similarly, Models 7 and 8 evaluate the effect of CEO political conservatism on general covenants, revealing that banks impose approximately 6% fewer general covenants on loans obtained from conservative CEOs. These loans tend to impose fewer constraints on management discretion concerning dividend distributions, repayment sources, and regulations governing post-agreement modifications to loan terms. Such findings suggest that conservative CEOs enjoy greater latitude in their loan agreements, which may enhance performance.

Consistent results for control variables were observed across various models. For instance, as indicated in other loan pricing studies, the number of covenants is negatively correlated with a firm's assets, profitability, asset maturity, credit ratings, and market-to-book value (Graham et al. 2008; Houston et al. 2014). Additionally, the number of covenants diminishes in relation to market-to-book value, suggesting that growth-oriented firms with elevated market-to-book ratios favor the financial flexibility associated with fewer covenants (Nash et al. 2003). Conversely, firms with higher leverage tend to encounter more restrictions, likely reflecting banks' concerns regarding default risks and agency dilemmas.

The number of covenants is associated with various loan characteristics. Our findings indicate that loans with extended maturities typically have fewer covenants, potentially due to the superior quality of the sample firms. Moreover, larger loans are more likely to entail additional covenants, indicative of the heightened monitoring necessitated by substantial financial stakes in a firm (Sufi 2007). Furthermore, loans incorporating performance-pricing clauses tend to have more covenants, which is expected as banks are increasingly inclined to implement performance-based pricing strategies when covenants are in place. However, covenants are less effective in safeguarding against moral hazard and adverse selection (e.g., Asquith et al. 2005). The evidence suggests that covenants and performance-pricing clauses function synergistically to mitigate the risk of default.

We also explored the potential influence of conservative CEOs on loan maturity. Models 9 and 10 indicate that, on average, conservative CEOs secure longer loan maturities; however, this effect does not reach conventional levels of significance, suggesting that the soft information derived from political values does not drive extended loan maturities. Instead, several hard information variables, including asset size, leverage, firm profitability, and loan size, were found to impact maturity.

In conclusion, the results presented in Table 5 substantiate the assertion that the political inclinations of CEOs significantly affect the nonfinancial terms of loans, particularly those sourced from large banking institutions. Banks perceive firms led by conservative CEOs as more reliable and predictable, thereby reducing the intensity of monitoring necessitated by the residual information asymmetry between borrowers and lenders.

The impact of conservative CEOs on loan structure

The number of lenders

Assuming all other variables remain constant, the lead underwriter may opt to engage fewer syndicate members when assessing a loan application from a conservative CEO. This is predicated on the premise that firms led by conservative CEOs present a lower loan risk compared to those with non-conservative leadership. Consequently, extending credit to a conservative firm necessitates less diversification through extensive syndicate arrangements. However, this hypothesis is not corroborated by the findings presented in Models 1–4 of Table 6, which reveal that conservative CEOs do not significantly influence the number of lenders within the syndicate. As anticipated, various firm-specific factors, such as asset size, leverage, and profitability, do impact the lender count. Nevertheless, the Altman Z-scores exhibited unexpected results. Additionally, loans characterized by larger amounts, extended maturities, and superior performance pricing tend to attract a greater number of lenders in the syndicate. Therefore, there is inadequate evidence to ascertain whether conservative CEOs have a positive or negative effect on the lender count. In contrast to the findings of Erkens et al. (2014), the authors observe a reduction in the number of lenders associated with conservative companies. Guay (2008) suggests that lenders favor conservative firms due to the provision of timely information regarding adverse developments and mechanisms that mitigate errors in loan agreements.

Upfront and annual fees

Upfront and annual fees are indicative of the risk and complexity associated with loans, as these fees necessitate ongoing monitoring by lenders following the execution of a loan agreement. It is plausible to assert that financial institutions impose lower fees on reliable borrowers due to the reduced costs associated with their oversight. Consequently, it is anticipated that loans issued to firms led by conservative CEOs will incur lower fees.

The analysis presented in Models 5–12 reveals a negative correlation between the conservative CEO variables and both upfront and annual fees. For example, the coefficient in Model 7 of Table 6, which utilizes the contemporaneous proxy for conservative CEOs, demonstrates that firms with conservative CEOs experience a 27.5% reduction in upfront fees compared to those with liberal or undisclosed CEOs. Furthermore, Model 11 indicates that conservative CEOs are associated with a 4.6% decrease in annual fees. These findings, in conjunction with the results from the loan spread analysis, underscore the impact of qualitative information on loan pricing strategies. As leverage increases, there is a corresponding decline in fees, attributable to factors such as asset size, profitability, market-to-book ratios, Z-scores, and asset maturity. Additionally, the evidence suggests that credit ratings exert a variable influence depending on the type of fee

Table 6 Effects of CEO conservatism on lender structure

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
FConservative CEO	0.0126 (0.55)	0.0126 (0.36)			−0.1823** (−2.11)	−0.1823 (−1.61)			−0.0603*** (−3.20)	−0.0603* (−1.91)		
CConservative CEO			0.0080 (0.36)	0.0080 (0.25)			−0.2747*** (−3.15)	−0.2747** (−2.41)			−0.0463** (−2.57)	−0.0463 (−1.58)
<i>Firm characteristics</i>												
Log (assets)	0.0699*** (5.61)	0.0699*** (3.87)	0.0696*** (5.60)	0.0696*** (3.87)	−0.0518 (−1.11)	−0.0518 (−0.95)	−0.0541 (−1.17)	−0.0541 (−0.99)	−0.0795*** (−5.95)	−0.0795*** (−3.54)	−0.0783*** (−5.85)	−0.0783*** (−3.48)
Leverage	0.5849*** (7.19)	0.5849*** (4.49)	0.5850*** (7.19)	0.5850*** (4.49)	0.3320 (1.09)	0.3320 (0.83)	0.3518 (1.17)	0.3518 (0.90)	0.7197*** (8.45)	0.7197*** (4.67)	0.7194*** (8.42)	0.7194*** (4.64)
Tangibility	−0.0887 (−1.23)	−0.0887 (−0.86)	−0.0876 (−1.22)	−0.0876 (−0.85)	−0.7185** (−2.26)	−0.7185* (−1.91)	−0.6614** (−2.12)	−0.6614* (−1.81)	−0.0386 (−0.52)	−0.0386 (−0.29)	−0.0431 (−0.58)	−0.0431 (−0.32)
Profitability	−0.3604** (−2.22)	−0.3604 (−1.49)	−0.3597** (−2.22)	−0.3597 (−1.49)	−0.6255 (−1.05)	−0.6255 (−0.90)	−0.6724 (−1.12)	−0.6724 (−0.96)	−0.9165*** (−3.76)	−0.9165** (−2.01)	−0.8988*** (−3.69)	−0.8988*** (−1.98)
Market-to-book	−0.0016 (−0.20)	−0.0016 (−0.14)	−0.0017 (−0.21)	−0.0017 (−0.14)	−0.0106 (−0.87)	−0.0106 (−0.80)	−0.0105 (−0.85)	−0.0105 (−0.79)	−0.0793*** (−6.38)	−0.0793*** (−4.25)	−0.0800*** (−6.42)	−0.0800*** (−4.27)
Z-score	0.0347*** (2.82)	0.0347 (1.64)	0.0346*** (2.81)	0.0346 (1.64)	−0.0653* (−1.77)	−0.0653* (−1.69)	−0.0642* (−1.72)	−0.0642 (−1.65)	−0.0186 (−1.42)	−0.0186 (−0.80)	−0.0183 (−1.38)	−0.0183 (−0.78)
Rating	−0.0013 (−0.63)	−0.0013 (−0.48)	−0.0013 (−0.63)	−0.0013 (−0.48)	0.0175* (1.94)	0.0175 (1.61)	0.0164* (1.85)	0.0164 (1.55)	−0.0331*** (−7.22)	−0.0331*** (−3.85)	−0.0325*** (−7.07)	−0.0325*** (−3.75)
Asset maturity	0.0012 (0.28)	0.0012 (0.17)	0.0011 (0.26)	0.0011 (0.16)	−0.0192 (−1.03)	−0.0192 (−0.88)	−0.0202 (−1.08)	−0.0202 (−0.93)	−0.0038* (−1.79)	−0.0038 (−1.02)	−0.0037* (−1.76)	−0.0037 (−0.99)
<i>Loan characteristics</i>												
Log (loan maturity)	0.0684** (2.32)	0.0684* (1.95)	0.0684** (2.32)	0.0684* (1.95)	−0.0428 (−0.44)	−0.0428 (−0.38)	−0.0372 (−0.38)	−0.0372 (−0.33)	−0.1575*** (−3.70)	−0.1575*** (−3.48)	−0.1574*** (−3.70)	−0.1574*** (−3.48)

Table 6 (continued)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Performance pricing	0.4269*** (20.34)	0.4269*** (15.02)	0.4267*** (20.34)	0.4267*** (15.04)	0.0587 (0.70)	0.0587 (0.56)	0.0540 (0.64)	0.0540 (0.52)	0.1457*** (8.24)	0.1457*** (5.34)	0.1457*** (8.23)	0.1457*** (5.32)
Log (loan size)	0.2986*** (22.51)	0.2986*** (17.54)	0.2987*** (22.51)	0.2987*** (17.52)	0.0274 (0.62)	0.0274 (0.52)	0.0276 (0.63)	0.0276 (0.53)	−0.0653*** (−4.64)	−0.0653*** (−3.10)	−0.0657*** (−4.65)	−0.0657*** (−3.11)
<i>Macroeconomics factors</i>												
Credit spread	0.1096 (0.86)	0.1096 (0.86)	0.1100 (0.86)	0.1100 (0.64)	0.1439 (0.29)	0.1439 (0.25)	0.1549 (0.32)	0.1549 (0.27)	0.2599* (1.95)	0.2599 (1.48)	0.2499* (1.88)	0.2499 (1.43)
Term spread	−0.0166 (−0.55)	−0.0166 (−0.40)	−0.0169 (−0.56)	−0.0169 (−0.41)	0.0109 (0.08)	0.0109 (0.06)	0.0339 (0.26)	0.0339 (0.20)	0.0130 (0.43)	0.0130 (0.33)	0.0144 (0.47)	0.0144 (0.37)
Constant	−0.5118** (−2.55)	−0.5118** (−2.00)	−0.5081** (−2.53)	−0.5081** (−1.99)	3.0593*** (4.52)	3.0593*** (4.04)	3.0647*** (4.55)	3.0647*** (4.02)	4.2796*** (18.22)	4.2796*** (14.10)	4.2547*** (18.06)	4.2547*** (13.98)
<i>Control</i>												
Loan type	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Loan purpose	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	5792	5792	5792	5792	787	787	787	787	3087	3087	3087	3087
Adj R-squared (Pseudo)	0.259	–	0.26	–	0.31	0.31	0.32	0.32	0.47	0.47	0.47	0.47

This table presents the regression results on the effect of CEO conservatism on lender structure. Models (1)–(4) are OLS (Poisson) regressions, with the number of lenders as the dependent variable. Models (5) to (12) are OLS regressions with Log (upfront fee) and Log (annual fee). Clustered-robust t-statistics for OLS regressions and clustered-robust z-statistics for Poisson regressions are reported in parentheses. The definitions of all variables are in the Appendix

***, **, and * indicate significance at the 10%, 5%, and 1% levels, respectively

assessed. Overall, these results imply that banks are able to lower monitoring expenses for firms led by conservative CEOs, thereby leading to reduced upfront and annual fees.

Robustness tests

Thus far, our evidence is consistent with the conjecture that banks regard conservative CEOs as more trustworthy, consequently granting them more favorable loan contract terms. Our results provide several alternative explanations. We address this issue empirically as follows:

Overconfident CEOs

Various personality traits and attributes of CEOs, such as managerial overconfidence, may influence our findings (Malmendier & Tate 2005, 2008). Generally, the actions of overconfident CEOs tend to have a detrimental impact on firm value. However, in scenarios involving optimal compensation contracts, moderately overconfident yet risk-averse CEOs may enhance firm value by mitigating underinvestment, particularly in comparison to rational and risk-averse managers (Goel & Thakor 2008). Furthermore, the overconfidence exhibited by CEOs could serve as a credible indicator of favorable firm prospects, potentially leading loan managers to offer more advantageous terms. Despite this possibility, we remain skeptical that it accounts for our findings. Hribar et al. (2013) indicate a negative correlation between overconfidence and credit ratings, implying that banks impose risk premiums on loans to firms led by overconfident CEOs.

To investigate this matter, we replace the proxy for overconfidence—specifically, the CEO's unexercised exercisable options—with a conservative CEO proxy within the loan spread model. The results presented in Table 7 (Model 1) reveal that overconfidence appears to positively influence loan spreads, aligning with the perspective that overconfident CEOs operate within a less favorable information environment (Goel & Thakor 2008). However, this coefficient lacks statistical significance. Subsequently, we incorporated overconfidence as a standalone variable in the regression model and conducted a comparative analysis with conservative measures. In Models 2 and 4, the coefficients associated with CEO overconfidence are found to be insignificant, while the coefficients for CEO conservatism maintain both economic and statistical significance. These findings strongly suggest that CEO overconfidence does not affect our results.

To further elucidate the interplay between conservatism and overconfidence, we estimated a model that includes both the overconfidence variable and the conservatism measure, along with their interaction (Models 3 and 5), yielding intriguing results. Our analysis indicates that conservative CEOs who lack overconfidence do not significantly impact loan spreads. Similarly, overconfidence in the absence of a conservative orientation does not substantially affect loan spreads. Notably, the coefficients for the interaction terms in both models are economically substantial and statistically significant. This suggests that conservative CEOs who also exhibit overconfidence—termed "conservatively overconfident"—experience reduced loan spreads, estimated to be approximately 14% to 17% lower. While the weak evidence of overconfidence may reflect either an inherent trait of the CEO or the transient nature of the proxy, these results imply that loan managers assess CEO conservatism favorably, but do not necessarily regard overconfidence positively unless it is coupled with conservatism. In essence, loan managers

Table 7 CEO conservatism versus CEO overconfidence

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
FConservative CEO		−0.0797** (−2.07)	−0.0109 (−0.23)			−0.0802** (−2.08)		−0.0107 (−0.22)		−0.0107 (−0.22)	
CConservative CEO				−0.0909** (−2.51)	−0.0414 (−0.99)		−0.0915** (−2.52)		−0.0151 (−0.32)		−0.0151 (−0.32)
Overconfident CEO (Holder67)	0.0257 (0.76)	0.0246 (0.73)	0.0604 (1.57)	0.0239 (0.71)	0.0544 (1.45)			0.0615 (1.60)	0.0655* (1.70)	0.0615 (1.60)	0.0655* (1.70)
Conservative x Overconfident			−0.1648** (−2.32)		−0.1396** (−2.12)			−0.1654** (−2.33)	−0.1823*** (−2.62)	−0.1654** (−2.33)	−0.1823*** (−2.62)
Log (assets)	−0.1226*** (−6.07)	−0.1243*** (−6.15)	−0.1256*** (−6.26)	−0.1237*** (−6.16)	−0.1255*** (−6.27)	−0.1239*** (−6.13)	−0.1233*** (−6.13)	−0.1254*** (−6.25)	−0.1255*** (−6.28)	−0.1254*** (−6.25)	−0.1255*** (−6.28)
Leverage	1.3449*** (8.76)	1.3505*** (8.85)	1.3482*** (8.84)	1.3533*** (8.91)	1.3508*** (8.87)	1.3498*** (8.85)	1.3527*** (8.91)	1.3520*** (8.86)	1.3610*** (8.95)	1.3520*** (8.86)	1.3610*** (8.95)
Tangibility	0.0777 (0.57)	0.0983 (0.72)	0.1050 (0.77)	0.1021 (0.75)	0.1096 (0.81)	0.0946 (0.69)	0.0987 (0.72)	0.1050 (0.77)	0.1076 (0.79)	0.1050 (0.77)	0.1076 (0.79)
Profitability	−1.7494*** (−4.96)	−1.7593*** (−4.99)	−1.7795*** (−5.09)	−1.7593*** (−5.00)	−1.7783*** (−5.08)	−1.7416*** (−4.97)	−1.7421*** (−4.98)	−1.7792*** (−5.08)	−1.7960*** (−5.12)	−1.7792*** (−5.08)	−1.7960*** (−5.12)
Market-to-book	−0.0328*** (−3.19)	−0.0329*** (−3.19)	−0.0318*** (−3.15)	−0.0332*** (−3.20)	−0.0322*** (−3.16)	−0.0322*** (−3.14)	−0.0326*** (−3.15)	−0.0320*** (−3.14)	−0.0323*** (−3.15)	−0.0320*** (−3.14)	−0.0323*** (−3.15)
Z-score	−0.0227 (−1.30)	−0.0226 (−1.30)	−0.0219 (−1.28)	−0.0221 (−1.28)	−0.0218 (−1.28)	−0.0235 (−1.35)	−0.0230 (−1.33)	−0.0222 (−1.29)	−0.0210 (−1.24)	−0.0222 (−1.29)	−0.0210 (−1.24)
Rating	−0.0520*** (−6.49)	−0.0526*** (−6.61)	−0.0531*** (−6.68)	−0.0520*** (−6.50)	−0.0528*** (−6.62)	−0.0521*** (−6.59)	−0.0515*** (−6.47)	−0.0528*** (−6.66)	−0.0520*** (−6.56)	−0.0528*** (−6.66)	−0.0520*** (−6.56)
Asset maturity	−0.0084* (−1.77)	−0.0088* (−1.88)	−0.0088* (−1.91)	−0.0089* (−1.92)	−0.0089* (−1.95)	−0.0088* (−1.85)	−0.0089* (−1.90)	−0.0088* (−1.91)	−0.0090* (−1.96)	−0.0088* (−1.91)	−0.0090* (−1.96)
Log (loan maturity)	−0.0471 (−1.27)	−0.0440 (−1.19)	−0.0456 (−1.24)	−0.0432 (−1.16)	−0.0444 (−1.20)	−0.0429 (−1.16)	−0.0421 (−1.13)	−0.0446 (−1.21)	−0.0445 (−1.20)	−0.0446 (−1.21)	−0.0445 (−1.20)

Table 7 (continued)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Performance pricing	0.0801*** (2.70)	0.0791*** (2.67)	0.0762*** (2.58)	0.0791*** (2.67)	0.0765*** (2.60)	0.0786*** (2.67)	0.0787*** (2.67)	0.0752** (2.56)	0.0759** (2.57)	0.0752** (2.56)	0.0759** (2.57)
Relationship loan						−0.0168 (−0.65)	−0.0165 (−0.64)	−0.0193 (−0.75)	−0.0193 (−0.74)	−0.0193 (−0.75)	−0.0193 (−0.74)
Log (loan size)	−0.0785*** (−4.77)	−0.0788*** (−4.79)	−0.0789*** (−4.81)	−0.0791*** (−4.82)	−0.0790*** (−4.83)	−0.0778*** (−4.68)	−0.0781*** (−4.71)	−0.0777*** (−4.70)	−0.0773*** (−4.70)	−0.0777*** (−4.70)	−0.0773*** (−4.70)
Credit spread	0.1182 (0.78)	0.1126 (0.75)	0.0802 (0.53)	0.1020 (0.68)	0.0793 (0.53)	0.1087 (0.72)	0.0981 (0.66)	0.0811 (0.54)	0.0687 (0.46)	0.0811 (0.54)	0.0687 (0.46)
Term spread	0.0552 (1.30)	0.0534 (1.27)	0.0550 (1.31)	0.0552 (1.32)	0.0552 (1.32)	0.0545 (1.30)	0.0562 (1.35)	0.0555 (1.32)	0.0568 (1.36)	0.0555 (1.32)	0.0568 (1.36)
Constant	5.5898*** (20.96)	5.6071*** (20.93)	5.5900*** (20.83)	5.5913*** (21.00)	5.5887*** (20.93)	5.6023*** (20.96)	5.5866*** (21.04)	5.5862*** (20.82)	5.5726*** (20.94)	5.5862*** (20.82)	5.5726*** (20.94)
Loan type	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Loan purpose	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	5,209	5,209	5,209	5,209	5,209	5,209	5,209	5,209	5,209	5,209	5,209
Adj. R-squared	0.55	0.55	0.55	0.55	0.55	0.547	0.548	0.55	0.55	0.55	0.55

This table presents the regression results for the effect of CEO personality traits on the loan spread. CEO overconfidence is a dummy variable that equals “1” when CEOs do not exercise their option, which is at least 67% deep in the money, and “0” otherwise. Clustered-robust t-statistics for OLS regressions are reported in parentheses. The definitions of all variables are in the Appendix

*, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively

may harbor doubts regarding a firm's future performance under the leadership of an overconfident CEO. However, when this overconfidence is paired with CEO conservatism, loan managers are more inclined to trust the CEO's capacity to conduct thorough due diligence on loans. This outcome is advantageous for overconfident CEOs.

Other CEO characteristics and relationship lending

Financial institutions often engage in various business activities through relational dynamics rather than through traditional arm's-length transactions. There exists a divergence of theoretical perspectives regarding the relationship between the strengthening of bank-borrower relationships and the potential decline in interest rates (Petersen and Rajan 1995; Sharpe 1990). Nevertheless, a segment of the banking literature has identified a correlation between prolonged banking relationships, reduced interest rates, and a diminished likelihood of requiring collateral (Berger and Udell 1995; Bharath et al. 2011). Consequently, it can be posited that our findings illustrate the advantages associated with relationship banking, although the rationale for why such lending relationships would preferentially benefit CEOs with a specific political orientation remains ambiguous.

To account for this possibility, we incorporate a proxy for the borrower-lender relationship. We operationalize the relationship dummy variable as "1" if the borrower has a prior loan history with the bank and "0" otherwise. The results are presented in Table 8—Models 1 and 3 display the foundational models from Table 6, enhanced with the relationship dummy, while Models 2 and 4 illustrate the models that include the interaction term (conservative $\times$ overconfidence) alongside the relationship dummy. In alignment with the findings of Berger and Udell (1995), the coefficient estimate for the relationship lending proxy is significantly negative at the 10% level. Importantly, the influence of conservative CEOs on loan spreads remained largely consistent in both magnitude and significance.⁹

Companies led by conservative CEOs experience loan spreads that are 17% to 18.5% lower for arm's length (non-relationship) loans, contingent upon the specific proxy utilized to identify conservative CEOs (Models 1 and 3). Furthermore, the findings suggest that the advantages of banking relationships are primarily realized in the loan processes of firms with non-conservative CEOs. Specifically, firms with non-conservative CEOs that maintain bank relationships benefit from approximately 5% lower spreads, whereas loans to firms with conservative CEOs and established bank relationships incur spreads that are roughly 14.5% higher. This discrepancy may be attributed to the conservative characteristics of these CEOs, who tend to prioritize loyalty in relationships and maintain the status quo (Carney et al. 2008; Hutton et al. 2014), leading to a reluctance to change banking partners. Consequently, banks may capitalize on their relationships with conservative CEOs.

Additionally, we examine the influence of CEO overconfidence (Models 2 and 4), given the previously documented significant impact of "conservatively overconfident" CEOs

⁹ In untabulated tests, we find that when we account for relationship lending, the magnitude and significance of the impact of conservative CEOs on the probability of pledging collateral, the number of covenants, and the upfront fees remain unchanged.

Table 8 Relationship loans and CEO characteristics

	(1)	(2)	(3)	(4)
FConservative CEO	− 0.1702*** (− 3.24)	− 0.1018* (− 1.76)		
CConservative CEO			− 0.1848*** (− 3.72)	− 0.1366** (− 2.54)
Relationship loan	− 0.0481* (− 1.66)	− 0.0508* (− 1.75)	− 0.0485* (− 1.68)	− 0.0519* (− 1.80)
FConservative CEO × relationship loan	0.1436** (2.50)	0.1431** (2.50)		
CConservative CEO × relationship loan			0.1449*** (2.64)	0.1474*** (2.67)
Overconfident CEO (Holder67)		0.0663 (1.63)		0.0609 (1.53)
Conservative × Overconfident		− 0.1633** (− 2.33)		− 0.1396** (− 2.14)
<i>CEO characteristics</i>				
Age	− 0.2733* (− 1.86)	− 0.2654* (− 1.81)	− 0.2793* (− 1.89)	− 0.2681* (− 1.82)
Tenure	0.0137 (0.79)	0.0088 (0.49)	0.0134 (0.77)	0.0081 (0.45)
Gender	− 0.1099 (− 1.03)	− 0.1264 (− 1.16)	− 0.1042 (− 0.97)	− 0.1225 (− 1.13)
<i>Firm characteristics</i>				
Log (assets)	− 0.1215*** (− 6.00)	− 0.1232*** (− 6.15)	− 0.1203*** (− 5.96)	− 0.1226*** (− 6.12)
Leverage	1.3538*** (8.96)	1.3563*** (8.98)	1.3545*** (8.99)	1.3565*** (8.98)
Tangibility	0.0953 (0.69)	0.1070 (0.79)	0.1012 (0.74)	0.1137 (0.84)
Profitability	− 1.7199*** (− 4.92)	− 1.7611*** (− 5.05)	− 1.7180*** (− 4.92)	− 1.7581*** (− 5.03)
Market-to-book	− 0.0324*** (− 3.13)	− 0.0322*** (− 3.14)	− 0.0334*** (− 3.19)	− 0.0330*** (− 3.18)
Z-score	− 0.0220 (− 1.26)	− 0.0205 (− 1.20)	− 0.0216 (− 1.25)	− 0.0204 (− 1.19)
Rating	− 0.0522*** (− 6.65)	− 0.0531*** (− 6.71)	− 0.0515*** (− 6.53)	− 0.0526*** (− 6.64)
Asset maturity	− 0.0082* (− 1.71)	− 0.0082* (− 1.78)	− 0.0083* (− 1.75)	− 0.0083* (− 1.81)
<i>Loan characteristics</i>				
Log (loan maturity)	− 0.0374 (− 1.01)	− 0.0389 (− 1.06)	− 0.0359 (− 0.97)	− 0.0370 (− 1.01)
Performance pricing	0.0756** (2.57)	0.0723** (2.47)	0.0758** (2.57)	0.0727** (2.49)
Log (loan size)	− 0.0764*** (− 4.68)	− 0.0763*** (− 4.70)	− 0.0773*** (− 4.74)	− 0.0771*** (− 4.74)
<i>Macroeconomics factors</i>				
Credit spread	0.0896 (0.60)	0.0626 (0.42)	0.0738 (0.50)	0.0557 (0.37)

Table 8 (continued)

	(1)	(2)	(3)	(4)
Term spread	0.0503 (1.22)	0.0509 (1.23)	0.0523 (1.28)	0.0515 (1.25)
Constant	6.7516*** (10.98)	6.7303*** (10.93)	6.7406*** (10.91)	6.7233*** (10.89)
<i>Controls</i>				
Loan type	Yes	Yes	Yes	Yes
Loan purpose	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	Yes	Yes
Year effect	Yes	Yes	Yes	Yes
Observations	5209	5209	5209	5209
Adj. R-squared	0.55	0.55	0.55	0.55

Note: This table presents the regression results for the effects of CEO conservatism and relationship loans on loan spread. Clustered-robust *t*-statistics for OLS regressions are reported in parentheses. The definitions of all variables are in the Appendix

*, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively

on loan spreads. To this end, we incorporate an overconfidence variable and its interaction with the conservative dummy variable. Our analysis reveals that conservative CEOs engaging in arm's length loans, who do not exhibit overconfidence, benefit from loan spreads that are 10.18% to 13.66% lower.¹⁰ Consistent with the findings presented in Table 7, our analysis reveals that the coefficients associated with the interaction term Conservative x Overconfident exert a similar influence on loan spreads. Furthermore, the coefficients for the interaction terms FConservative CEO x Relationship loan and CConservative CEO x Relationship loan exhibit similarities to those observed in Models 1 and 3, even after the incorporation of the CEO overconfidence variable. These findings support the hypothesis that conservative CEOs play a significant role in shaping loan contracts. Additionally, it appears that relationship lending and CEO overconfidence do not alter the effect of CEOs' political conservatism on loan spreads.

In our analysis, we also account for other CEO characteristics, including age, firm tenure, and gender. For example, it is posited that older CEOs with longer tenures may secure lower interest rates and more favorable non-price terms due to a reduced propensity to engage in high-risk endeavors. Similarly, female CEOs are often perceived as exhibiting greater financial conservatism (Huang and Kisgen 2013). Our results indicate that older CEOs do indeed achieve lower loan spreads. However, the inclusion of these additional characteristics does not significantly alter our primary findings.

Political geography and orientation of firms

The conservative CEO effect may be misleading, as the political orientation of management could be influenced by the broader political stance or geographical context of the firm. Recent studies indicate that conservative managers are often drawn to firms that align with conservative values and are situated in conservative regions (Hutton et al.

¹⁰ Note that the overall effects of the conservative CEO are – 12.20% and – 12.88% for the two conservative CEO proxies.

2014). To address this potential confounding factor, we incorporate controls for political geography (specifically, the firm's location in a county with a majority of Republican voters) and the Republican firm effect (measured by net donations to the Republican Party through a Political Action Committee, or PAC).

Moreover, religious beliefs may also shape political orientations, potentially impacting our findings. Financial institutions may perceive religious individuals as more trustworthy. To account for this, we include a proxy for religiosity (Hilary & Hui 2009) in our models. Although we are unable to directly measure the religious affiliations of CEOs, we align with existing literature by assuming that the number of religious adherents in a firm's locality correlates strongly with the religious values of the local population. The results are presented in Table 9.

Initially, we incorporate stand-alone variables representing firms with a Republican political orientation or located in Republican-leaning areas, alongside the religiosity of the region. Models 1 and 2 reveal that firms led by conservative CEOs experience loan spreads that are 9% to 12% lower than those of their non-conservative counterparts. This finding reflects a modest increase in magnitude compared to the baseline model outlined in Eq. (1). This enhancement may stem from the consideration of both the firm's and the region's political orientations, which facilitates a clearer, less confounded analysis of the CEO-specific effect.

Furthermore, we observe that the Republican firm effect is statistically significant, resulting in approximately 14% lower loan spreads. This suggests that conservative CEOs do not uniformly represent all Republican firms, thereby supporting the notion that Republican firms possess distinct characteristics that are separate from those of their conservative CEOs. This observation is consistent with the conservative corporate policies typically adopted by such firms, which include lower leverage, higher profitability, and a tendency to engage in less risky investments (Hutton et al. 2014). Notably, we find no evidence to suggest that political geography influences loan spreads. We employed continuous variables as proxies for both firm and regional political orientations and conducted additional tests by varying the indicators. While the impact of conservative CEOs on loan spreads is more pronounced when using dummy variables, the independent effect of the firms' political orientation becomes statistically insignificant.¹¹ Regarding religiosity, the coefficient estimates are negative but not significant. In these models, we also control for CEO age, tenure, gender, relationship banking, and other controls.

To further test the results, we explore proxies for firm and regional political orientation using conservative CEO measures. Models 3 and 4 present these results. We find that firms with Republican political orientation led by conservative CEOs obtain significantly lower spreads, as indicated by the coefficient estimates of -0.4198 (t -statistic = -2.49) and -0.3512 (t -statistic = -2.14). For instance, when a firm only contributes to the Republican Party (the Firm Republican Index is 1), it would obtain 35% to 42% lower loan spreads if its CEO were also politically conservative. These results support the hypothesis that conservative CEOs have lower borrowing costs. Furthermore,

¹¹ Instead of presenting the results of indicator variables, we report the results of the continuous variable because it is consistent with our view that a firm's political orientation affects loan spreads.

Table 9 Geography, firm political contribution, and CEO characteristics

	(1)	(2)	(3)	(4)
FConservative CEO	− 0.1148** (− 2.25)		0.0359 (0.46)	
CConservative CEO		− 0.0951* (− 1.95)		0.0324 (0.44)
Overconfident CEO (Holder67)				
FConservative CEO × Local Republican Index			0.1109 (0.50)	
FConservative CEO × Firm Republican Index			− 0.4198** (− 2.49)	
CConservative CEO × Local Republican Index				0.0872 (0.40)
CConservative CEO × Firm Republican Index				− 0.3512** (− 2.14)
<i>Local and firm political preference</i>				
Local Republican Index	0.0774 (0.58)	0.0805 (0.60)	0.0802 (0.54)	0.0866 (0.59)
Firm Republican Index	− 0.1401* (− 1.85)	− 0.1399* (− 1.84)	− 0.0566 (− 0.68)	− 0.0657 (− 0.80)
Religiosity	− 0.2997 (− 1.21)	− 0.2747 (− 1.11)	− 0.3156 (− 1.28)	− 0.2995 (− 1.21)
Other controls	Yes	Yes	Yes	Yes
Loan type	Yes	Yes	Yes	Yes
Loan purpose	Yes	Yes	Yes	Yes
Industry effect	Yes	Yes	Yes	Yes
Year effect	Yes	Yes	Yes	Yes
Observations	2,450	2,450	2,450	2,450
Adj. R-squared	0.65	0.66	0.65	0.65

This table presents the robustness tests for the effect of CEO conservatism on loan spread with other political measures and regional religiosity. Clustered-robust t-statistics for OLS regressions are in parentheses. The definitions of all variables are in the Appendix

*, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively

the CEO effect is robust to a firm's geographical or political orientation, which magnifies the impact of a conservative CEO.

These findings have broad social, economic, ethical, and practical implications. Socially, employees, customers, and investors may perceive conservative CEOs as more trustworthy because of their stability, increasing stakeholder trust and loyalty and strengthening the company's sustainable development. Economically, conservatism in financial management can help minimize financial risk and improve access to capital. Conservative CEOs tend to use less leverage and enhance profitability, which can attract loans at lower interest rates and improve company competitiveness and financial performance (Hutton et al. 2014).

From an ethical perspective, the fact that conservative CEOs are perceived as more trustworthy raises issues regarding management diversity and inclusivity. Companies must ensure that they are unbiased in selecting CEOs and maintain a balance in their management teams to avoid one-sided decisions and to promote diversity and equality within organizations. Companies must adjust their financial strategies to take advantage

of conservative CEOs. Understanding the advantages and disadvantages of being conservative will help a company adapt its strategy to obtain better loan terms. For example, a company can focus on enhancing its valuable assets and maintaining a reasonable level of leverage to minimize borrowing costs.

Summary and conclusions

Personal characteristics significantly impact individuals' economic choices, with political orientation—specifically conservatism or liberalism—playing a crucial role in shaping these decisions. This research contributes to the existing literature by examining the extent to which the political orientation of corporate executives influences their business decisions. We hypothesize that conservative CEOs facilitate their firms' access to favorable debt financing through two primary mechanisms. Firstly, banks perceive conservative CEOs as more creditworthy, as their political ideologies are likely to mitigate moral hazard risks associated with borrowing, even in the presence of weak legal and contractual safeguards against opportunism. Consequently, banks allocate fewer resources to monitor potential opportunistic behavior when dealing with trustworthy borrowers, thereby optimizing resource allocation between the bank and the borrower. Secondly, the conservative policies adopted by these CEOs inherently lower credit risks. These propositions suggest that conservative CEOs are likely to secure more advantageous credit terms.

Utilizing political contributions to the Republican Party as an indicator of CEO conservatism, our analysis reveals that firms led by conservative CEOs benefit from significantly lower spreads and loan-related fees compared to those managed by non-conservative CEOs. This finding implies that banks find it easier to assess and oversee loans for these firms. Additionally, evidence indicates that conservative CEOs are granted more favorable non-priced loan conditions, such as reduced financial, general, and total covenants, and are less frequently required to provide collateral. We conduct various supplementary tests to ensure that our findings are not confounded by other plausible factors, establishing that the influence of a CEO's political orientation on loan contracting terms is distinct from other CEO attributes, including age, tenure, gender, and overconfidence.

Moreover, our results indicate that "conservatively overconfident" CEOs receive a more substantial discount on loan spreads compared to their conservative counterparts who do not exhibit overconfidence. Our findings remain robust when considering the political orientations of firms, regional political preferences, and the religiosity of locations. We also observe that a firm's political orientation amplifies the effect of a conservative CEO, although it does not significantly influence the political geography of the firm. Notably, we find that relationship lending does not account for the effects of CEO political conservatism; conservative CEOs incur higher spreads on relationship loans than on arm's length loans, potentially due to banks capitalizing on the loyalty and reluctance to change exhibited by conservative borrowers.

Our findings suggest that the perceived trustworthiness of key executives has a substantial impact on firm decisions and performance. In a broader context, our results align with recent studies exploring how the personality traits and backgrounds of CEOs and other executives—such as overconfidence, religiosity, military experience,

and various life experiences—affect firm policy. More specifically, prior research has established that the political orientations of CEOs, particularly their conservative values, influence their decision-making across diverse contexts. This study focuses on how banks assess the political conservatism of CEOs and the implications of these assessments for loan contracts, thereby contributing to the existing body of literature on bank loans by demonstrating the significant role of managerial trustworthiness in shaping financial agreements.

However, our study is not without limitations inherent to empirical analysis. Firstly, our measure of CEO political conservatism does not raise endogeneity concerns. Although we differentiate the CEO conservatism metric into consistent political preference (forward-looking) and temporal political orientation (contemporaneous), there remains a possibility of a reverse causation where CEOs may opportunistically contribute to the Republican Party to lower borrowing costs. We anticipate that future research will address these concerns by examining changes in the exogenous regulation of political donations. Secondly, our empirical findings should not be generalized to all contexts of CEO political orientation and loan contracts, as our sample is limited to loans issued to large public firms within the S&P 1500. This limitation raises further questions regarding the applicability of our findings to smaller or private firms. Future research exploring the influence of CEO political traits on loan contract terms across different types of firms or within varying legal and contractual environments would be beneficial.

Appendix

See Table 10.

Table 10 Variable definitions

Classification	Variable	Definitions
<i>CEO characteristics</i>		
	FConservative CEO (Forward-looking)	A dummy variable that takes the value of “1” if the political contributions of the CEO during their tenure are all directed toward the Republican party, and “0” otherwise
	CConservative CEO (Contemporaneous)	A dummy variable that takes the value of “1” if the political contributions of the CEO during the most recent election cycle before a loan was issued are all directed toward the Republican party and “0” otherwise
	Holder67	A dummy variable that takes the value of “1” if a CEO does not exercise the option that is at least 67% deep in the money and “0” otherwise (Malmendier & Tate 2005; 2008)
	Age	Natural log of CEO age
	Tenure	Natural log of the number of years the CEO has held their current position
	Gender	Dummy variable that equals “1” if the CEO is male and “0” otherwise

Table 10 (continued)

Classification	Variable	Definitions
<i>Firm characteristics</i>		
	Leverage	(Long-term debt + debt in current liabilities)/total assets = (data9 + data34)/data6
	Log (assets)	Natural log of total assets = log(data6)
	Tangibility	Net property, plants, and equipment/total assets = data8/data6
	Profitability	EBITDA/total assets = data13/data6
	Market-to-book	(Market value of equity plus the book value of debt)/total assets = (data25*data199 + data6-data60)/data6
	Z-score	Altman's (1968) Z-score = (1.2working capital + 1.4 retained earnings + 3.3EBIT + 0.999sales)/total assets = (1.2data179 + 1.4data36 + 3.3data170 + 0.999data12)/data6 We use a modified Z-score, which does not include the ratio of the equity market value to the total debt book value because a similar term, market-to-book, enters the regressions as a separate variable
	Asset maturity	Asset maturity is the book value-weighted maturity of long-term assets and current assets, where we compute the maturity of long-term assets as gross property, plant, and equipment divided by depreciation expenses, and the maturity of current assets is calculated by current assets divided by the cost of goods sold (see Barclay & Smith, 1995; Billett, King, & Mauer, 2007) [PPE/(CA + PPE)] [PPE/Depreciation] + [CA/(CA + PPE)] [CA/COGS] = data7/(data4 + data7) [data7/data14] + [data4/(data4 + data7)] [data4/data41], where PPE = gross property, plant, and equipment, CA = current assets, and COGS = cost of goods sold
<i>Loan characteristics</i>		
	Loan spread	All-in spread was drawn in the DealScan database. The all-in spread drawn is the amount the borrower pays in basis points over LIBOR or LIBOR equivalent for each dollar drawn down
	Log (loan maturity)	Natural log of the loan maturity in months
	Log (loan size)	Natural log of the loan facility amounts in millions of dollars
	Collateral	A dummy variable that equals "1" if the collateral secures the loan facility and "0" otherwise
	Performance pricing	A dummy variable that equals "1" if the loan facility uses performance pricing and "0" otherwise
	Number of lenders	Total number of lenders in a single loan facility

Table 10 (continued)

Classification	Variable	Definitions
	Relationship loan (<i>dummy</i>)	A dummy variable that equals “1” if any of the lead arrangers for the current loan facility had been a lead arranger for previous loans for the same borrower and “0” otherwise
	No. Tcon	Total number of covenants in the loan agreement
	No. Gcon	The number of general covenants that are restrictions on prepayments, dividends, and voting rights
	No. Fcon	The number of financial covenants that place limits on accounting variables and ratios during the loan contract period
	Upfront fee	A fee paid by the borrower upon the closing of a loan (measured in basis points)
	Annual fee	An annual charge against the entire loan commitment amount, whether used or unused (measured in basis points), also called a facility fee
	Loan type	Dummy variable for loan types, including term loan, revolver greater than one year, revolver less than one year, and 364-day facility
	Loan purpose	Dummy variable for loan purposes, including corporate purposes, debt repayment, working capital, takeover, etc
<i>Local and firm political characteristics</i>		
	Local Republican index	The county-level margin of victory for a Republican candidate in a presidential election: The difference between voter turnouts earned by a Republican candidate and a Democratic candidate in a presidential election before the loan issuance divided by the total voter turnouts earned by Republican and Democratic candidates
	Firm Republican index	The difference between political contributions made by the firm’s political action committee (PAC) to candidates in the Republican and Democratic parties during an election cycle divided by total political contributions made by the PAC to both parties during the election cycle
	Religiosity	Interpolated total number of religious adherents in the location divided by the total population of that location (American Religion Data Archive [ARDA]) (See Hilary & Hui 2009)
<i>Macroeconomic factors</i>		
	Credit spread	The difference between the monthly AAA corporate bond yield and BAA corporate bond yield
	Term spread	The difference between the monthly 10-year treasury yield and the 2-year treasury yield

Abbreviations

CEO Chief executive officer
GDP Gross domestic product
VIF Variance inflation factor

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