



Supply Chain Industrial Policy, Local Entry, and Stock Returns

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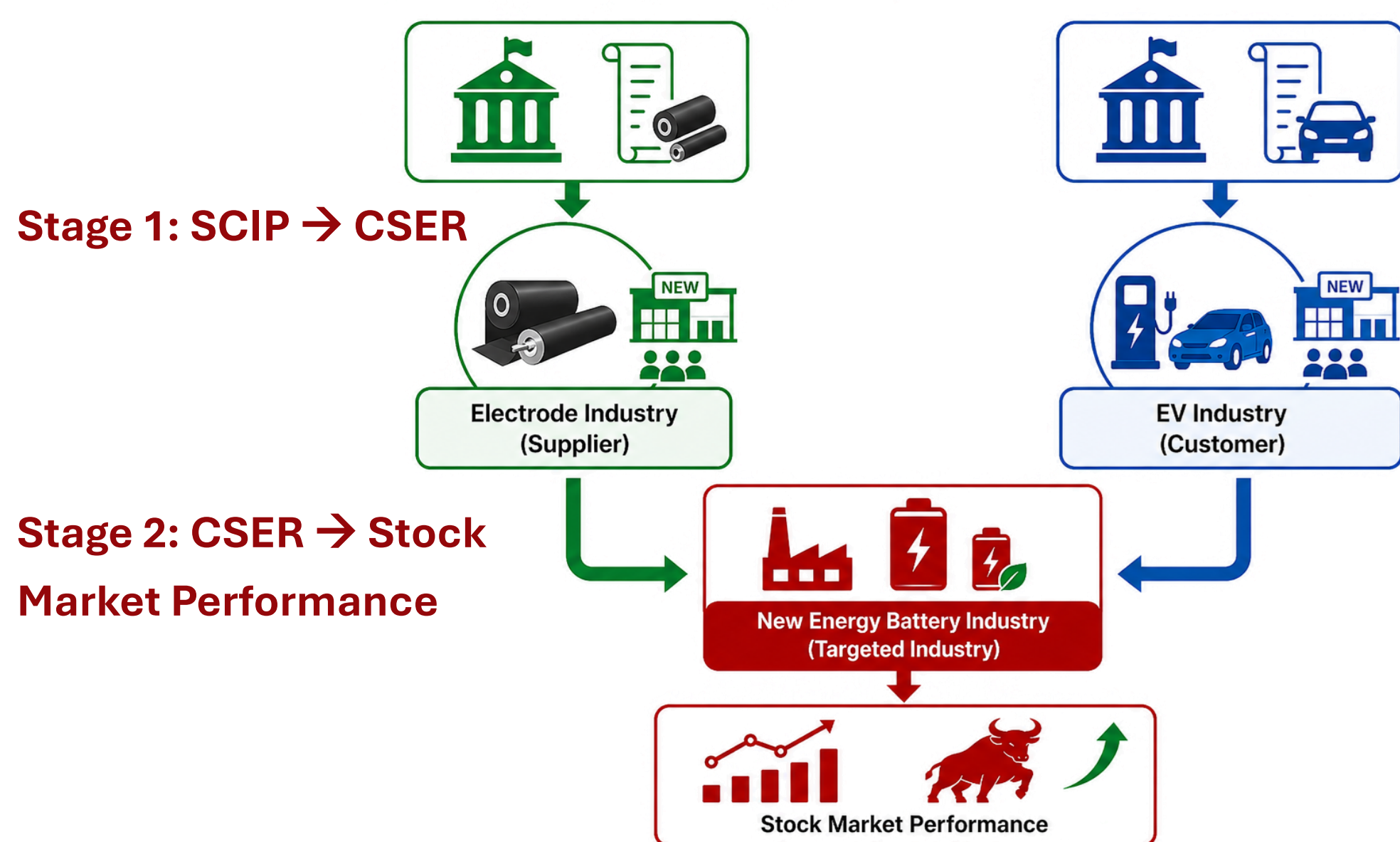
1. Motivation

- **Industrial policy** has gained significant attention in recent years, yet its effectiveness remains highly debated.
- **One key rationale:** industrial policy may address **coordination failures** and generate **agglomeration benefits**.
- Even when policy objectives are achieved, **the implications for shareholder value are unclear**.

2. Research Question

- How does industrial policy affect stock returns of firms in targeted industries through the agglomeration channel?

3. Supply Chain Industrial Policy (SCIP) in China



- **SCIP:** A set of industrial policies issued by city-level governments that directly support the **customer** and **supplier** industries of a targeted industry **within the jurisdiction**.
- **Stage 1:** Increases local customer and supplier entry rate (**CSER**) by addressing **coordination failures** → **Agglomeration**
- **Stage 2: How Do Firms in the Targeted Industry Benefit from CSER?**
 - Specialized Suppliers, Economies of Scale, and Reduced Transportation Costs (Krugman, 1991; Holmes, 1999)
 - Knowledge spillovers (Chu et al., 2019; Matray, 2021)
 - Labor pooling (Helsley and Strange, 1990; Dougal et al., 2022)

4. Data (2007-2022)

Supply Chain Industrial Policy (SCIP)

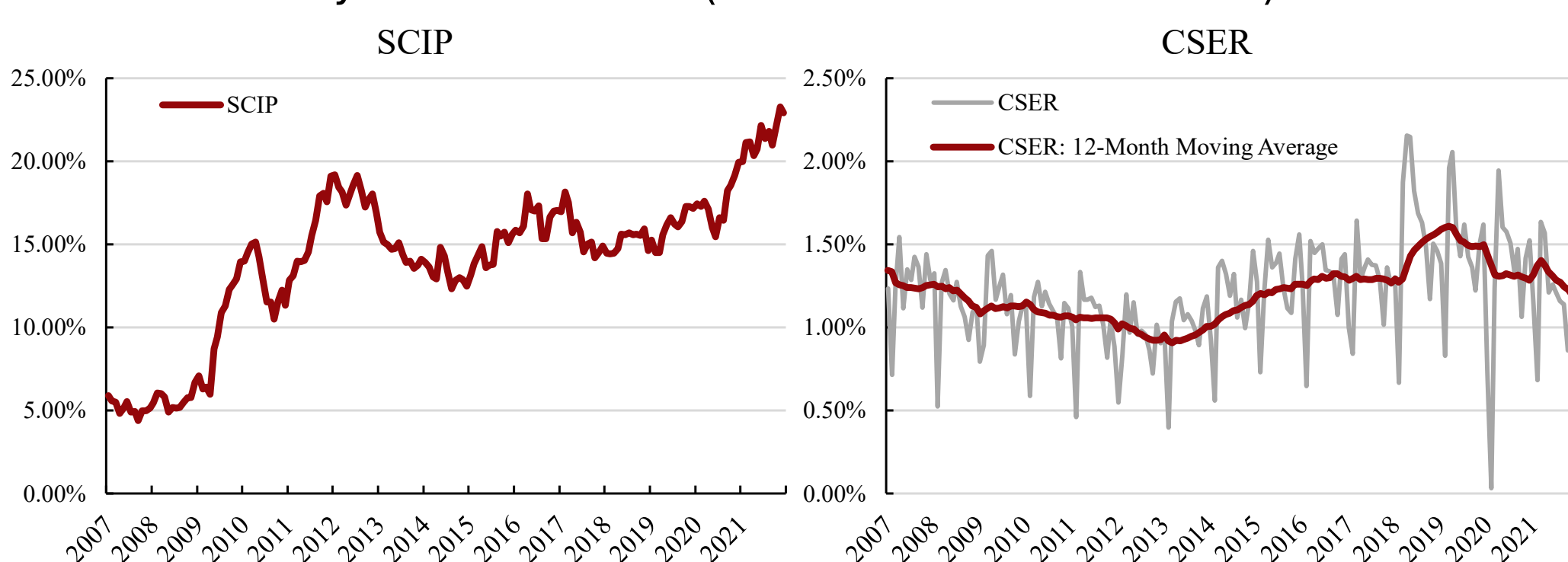
$$SCIP_{i,t-h,t} = \sum_{d=1}^{96} w_{k,d} IP_{c,d,t-h,t}$$

- **Source:** PKULAW (3 million government documents).
- **Analyzed by LLM (DeepSeek):** Identified 15,535 industrial policies with clearly specified issuing authority, issuance date, target industry, and policy instruments.
- **Weights:** National Input-Output Tables.

Customer and Supplier Entry Rate (CSER)

$$CSER_{i,t} = \sum_{d=1}^{96} w_{k,d} IER_{c,d,t}$$

- **Source:** Full-sample Firm Registration Data from State Administration for Industry and Commerce (More than 58 million firms).



5. Main Results

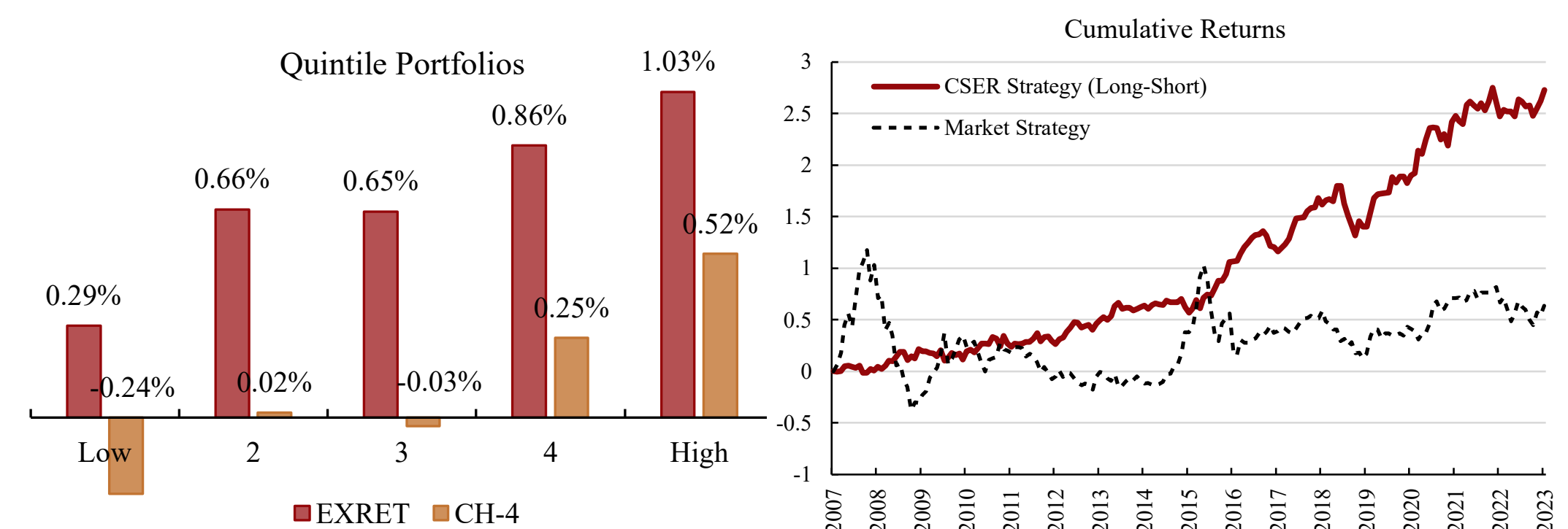
Stage 1: SCIP → CSER

- SCIP is associated with higher CSER over the subsequent 12 months.
- FM Regression: $CSER_{i,t,t+12} = \alpha + \beta SCIP_{i,t-h,t} + \gamma' X_{i,t} + \varepsilon_{i,t}$
- 1-unit increase in SCIP → 1.119pp higher monthly CSER.

Policy Window =	3 months	6 months	12 months
SCIP	1.119*** (4.16)	0.732*** (5.14)	0.546*** (4.94)
Controls	Yes	Yes	Yes
Observations	306,721	306,721	306,721
R-squared	0.264	0.263	0.254

Stage 2: CSER → Stock Returns

- CSER over the past 12 months positively predicts cross-sectional returns:
 - Monthly LS Strategy: EXRET: 0.736% (t=4.5); CH4 Alpha: 0.755% (t=3.1).



- Market underreaction to the fundamental improvement predicted by CSER.
 - CSER → Higher ROA and higher ΔEPS.
 - CSER → Underestimation in consensus analyst forecasts.

6. Further Analysis

Decomposing CSER: SCIP-Driven vs. Prospect-Driven

- **Selection Issue:** Industries with good prospects naturally have higher CSER, and local governments tend to target such industries.
- **SCIP-driven CSER has incremental return predictability.**
- **After 2013:** SCIP is more exogenous to local industry conditions (Fang et al., 2025; Luo et al., 2025).

	Period		
	2007-2022	2007-2013	2013-2022
$r_{i,t+1}$			
$CSER_{i,t}^{SCIP}$	0.537*** (2.70)	0.277 (1.31)	0.739*** (2.75)
$CSER_{i,t}^{GDP}$	1.654*** (3.79)	0.997** (2.08)	2.165*** (4.14)
$CSER_{i,t}^{RCA}$	1.172 (0.67)	-2.237 (-1.13)	3.824*** (3.33)
$CSER_{i,t}^r$	0.237*** (3.55)	0.175 (1.29)	0.285*** (5.11)
Controls	Yes	Yes	Yes
Observations	198,494	58,691	139,803
R-squared	0.287	0.295	0.281

Localized Effect: Within Jurisdiction

- Only CSER within provincial borders has significant return predictability.



SCIP Alone Does Not Positively Predict Returns

- **Offsetting effects:** benefits may accrue to society rather than to shareholders.
 - More employment
 - More investment
- **Our Channel:** SCIP benefits firms in targeted industries by boosting local customer and supplier entry.

	(1)	(2)	(3)	(4)
$r_{i,t+1}$				
SCIP(t-24,t-12)	0.1995 (0.85)	0.1676 (0.85)	-0.0272 (-0.10)	0.0206 (0.10)
CSER(t-12,t)			0.4615*** (4.11)	0.1939*** (2.87)
Controls	No	Yes	No	Yes
Observations	306,217	198,494	306,217	198,494
R-squared	0.064	0.294	0.074	0.298