

The Impact of Tax Administration on Corporate Financialization

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Abstract

In recent years, the tendency of non-financial enterprises to “shift from real to virtual,” characterized by increasing engagement in financial assets and activities, has drawn growing attention. Against this backdrop, how to curb excessive corporate financialization and encourage the reallocation of capital toward the real economy has become an important issue in both academic research and policy practice. Using a sample of non-financial listed firms from China’s Shanghai and Shenzhen A-share markets over the period 2012–2024, this study constructs an index of regional tax administration intensity and examines its relationship with corporate financialization. The empirical results suggest that stronger tax administration is associated with a noticeable reduction in the degree of corporate financialization. Further analysis shows that this inhibitory effect is not uniform across firms. It is more evident among non-state-owned enterprises, firms with a higher share of executives with financial backgrounds, and those facing relatively higher agency costs. From the perspective of external governance, particularly the role of tax administration, the study extends existing discussions on the determinants of corporate financialization. It also offers evidence that may be relevant for policymakers seeking to design more differentiated regulatory approaches, with the aim of encouraging firms to reorient resources from financial activities back to productive investment in the real economy.

Keywords

tax administration, corporate financialization, shifting from real to virtual, agency costs, external governance

1. Introduction

The real economy serves as the foundation of national economic development. In recent years, however, there has been a growing tendency among non-financial firms to allocate increasing resources to financial assets, accompanied by a noticeable decline in their willingness to invest in core business activities. Data from the National Bureau of Statistics show that the value added of China’s financial industry as a share of GDP increased from 6.24% in 2010 to 7.86% in 2021. Alongside this shift, the phenomenon of corporate “shifting from real to virtual” has attracted sustained attention from both policymakers and researchers. Concerns mainly lie in the fact that excessive financialization may crowd out R&D expenditure and real investment, weaken firms’ long-term competitiveness, and potentially amplify financial risks, thereby increasing systemic

vulnerability. Against this background, how to effectively restrain corporate financialization and redirect capital toward the real economy has become an increasingly pressing issue.

As an institutional instrument of economic governance, tax administration has undergone substantial upgrading in recent years, particularly with the advancement of informatization systems such as the “Golden Tax Phase III.” This transformation has not only reshaped the way tax is collected and managed, but has also strengthened firms’ tax compliance environment and altered financing conditions to some extent. Through these channels, tax administration may further influence corporate asset allocation decisions, offering a useful perspective for understanding the external governance mechanisms behind corporate financialization.

The existing literature has extensively examined both the determinants of corporate financialization and the broader economic effects of tax administration. In terms of motivation, two main explanations have been proposed: the “precautionary savings” hypothesis and the “investment substitution” hypothesis (Cai Mingrong and Ren Shichi, 2014) [1]. Hu Yiming et al. (2017) [2] show that Chinese firms are generally driven by liquidity reserve motives, although non-cash financial assets already exhibit substitution effects. From a property-rights perspective, Cao Wei et al. (2023) [3] document significant differences in financialization behavior between state-owned and private enterprises. In addition, Du Yong et al. (2019) [1] find that CEOs with financial backgrounds tend to significantly promote corporate financialization.

Regarding the consequences of tax administration, existing studies suggest a dual effect. On the one hand, strengthened tax enforcement reduces tax avoidance space but may also intensify financing constraints, reflecting a “tax collection effect” (Yu Wenchao et al., 2018 [2]; Zhang Kezhong et al., 2020) [1]. On the other hand, it may improve information transparency and alleviate agency problems, generating a “governance effect” (Ye Kangtao and Liu Hang, 2011 [2]; Wen Wukang and Wang Yutao, 2021 [3]). More recently, attention has shifted toward the direct link between tax administration and corporate financialization. Most studies report that stronger enforcement suppresses corporate financialization (Li Xiaoyan et al., 2022 [1]; Liu Shan et al., 2024 [2]; Du Jian et al., 2021 [3]), although some evidence suggests that, from a precautionary savings perspective, it may also encourage the holding of short-term financial assets (Wang Yifeng and Wei Xingkai, 2024 [4]). Overall, while the inhibitory effect of tax administration has been widely supported, there remains scope for further refinement in heterogeneity analysis and endogeneity identification.

The contribution of this paper can be understood along three interconnected lines. First, in terms of heterogeneity, the analysis focuses on property rights, executives’ financial backgrounds, and agency costs, aiming to capture the boundary conditions of the effect of tax administration. The results suggest that the inhibitory effect is more pronounced in non-state-owned enterprises, firms with a higher proportion of executives with financial backgrounds, and firms facing higher agency costs, which provides micro-level evidence for differentiated regulatory design. Second, regarding identification, local government fiscal pressure is introduced as an instrumental variable for tax administration intensity. By exploiting exogenous variation arising from fiscal revenue–expenditure imbalances, this approach helps mitigate potential endogeneity between tax enforcement and corporate financialization, thereby strengthening causal interpretation. Third, from a theoretical perspective, the heterogeneity results align with the underlying mechanisms in a structured way: differences in ownership correspond to the financing constraint channel of the “tax collection effect,” variations in agency costs reflect the governance improvement channel, and the role of executives’ financial backgrounds highlights how financial expertise may shift from arbitrage-oriented behavior toward compliance-sensitive responses under stronger external regulation.

2. Theoretical Analysis and Research Hypotheses

In the existing literature, the motivations behind firms’ allocation of financial assets are generally explained through two competing but not mutually exclusive perspectives: the “precautionary savings” hypothesis and the “investment substitution” hypothesis (Cai Mingrong and Ren Shichi, 2014 [1]). The precautionary savings view suggests that firms hold financial assets primarily as a buffer against future cash flow uncertainty (Keynes, 1936 [2]), functioning as a liquidity reserve (Hu Yiming et al., 2017 [2]). Under conditions of heightened uncertainty in the operating environment, firms tend to increase their allocation to financial assets as a form of risk management (Demir, 2009 [1]). By contrast, the investment substitution hypothesis emphasizes return differentials across asset types. When financial assets yield higher returns than real investment, capital tends to shift away from productive activities toward financial markets (Orhangazi, 2008 [1]; Zhang Chengsi and

Zheng Ning, 2020 [2]). These two mechanisms are not fixed; rather, they tend to alternate depending on firms' operating conditions. When operating returns are relatively weak, substitution incentives dominate, whereas when internal cash flow is sufficient, precautionary motives become more prominent (Song Jun and Lu Yang, 2015 [1]).

Differences in ownership structure further shape these underlying motivations. State-owned enterprises, due to principal-agent problems and the absence of a clearly defined residual claimant, tend to exhibit financialization driven more by managerial opportunism and substitution incentives. In contrast, private firms, facing tighter credit constraints and resource allocation disadvantages, are more likely to hold financial assets for precautionary purposes (Cao Wei et al., 2023 [3]). Managerial characteristics also play an important role. CEOs with financial backgrounds are more likely to engage in financialization, as such experience may enhance sensitivity to financial returns and, in some cases, strengthen overconfidence or ease financing constraints (Du Yong et al., 2019 [4]). Beyond ownership and managerial traits, agency costs provide another important lens. Dittmar et al. (2003) [1] show that in environments with weaker shareholder protection, firms tend to hold higher levels of cash and liquid assets, implying that agency frictions can encourage the accumulation of discretionary resources. Taken together, these studies suggest that corporate financialization is jointly shaped by external financing constraints that generate precautionary demand and internal agency conflicts that generate substitution-driven behavior.

Against this background, tax administration introduces two distinct but interconnected channels: the "tax collection effect" and the "governance effect" (Ye Kangtao and Liu Hang, 2011 [7]; Yu Wenchao et al., 2018 [5]). From the perspective of tax collection, stronger enforcement directly reduces the pool of internal funds available for discretionary allocation within firms (Desai et al., 2007 [1]). By limiting tax avoidance activities and increasing compliance costs, tax audits intensify financing constraints (Yu Wenchao, 2018 [5]). In response, firms may rely more heavily on trade credit to smooth liquidity shortages, which in turn weakens their capacity to engage in financial asset allocation for speculative purposes (Liu Hang et al., 2017 [1]).

From the governance perspective, tax administration operates as an external disciplinary mechanism on managerial behavior (Desai et al., 2007 [8]; Ye Kangtao and Liu Hang, 2011 [7]). This influence is reflected in several dimensions. In earnings management, stronger enforcement increases the cost of manipulating reported profits and thereby constrains opportunistic financial behavior (Ye Kangtao and Liu Hang, 2011). In financing channels, improved tax enforcement can reduce debt financing costs, particularly for firms with more severe agency problems (Guedhami and Pittman, 2008 [1]). At the same time, better tax enforcement improves the overall information environment and supports the development of credit markets, including increased lending to SMEs (Gallemore and Jacob, 2020 [1]). In terms of information quality, tax evasion is negatively associated with both local information transparency and judicial intensity (Slemrod, 2007 [2]), while the informational value of tax data becomes more pronounced under stronger enforcement regimes (Kerr, 2019 [3]). At the firm level, tax enforcement also interacts with internal control quality, exerting a stronger governance role in firms with weaker internal monitoring systems (Wen Wukang and Wang Yutao, 2021 [8]).

Although the tax collection effect and governance effect are analytically distinct, they are not independent in practice. Desai and Dharmapala (2006) [1] argue that complex structures used for tax avoidance often overlap with those used to conceal managerial private benefits. In this sense, stronger enforcement not only reduces tax avoidance space but also increases the cost of constructing opaque arrangements, thereby indirectly constraining agency problems. Conversely, in environments with weak supervision, tax avoidance may itself become a vehicle for managerial rent extraction (Lim, 2011 [2]). This suggests that the governance role of tax administration is, to a considerable extent, built upon its effectiveness in tax collection.

When these two channels are considered in the context of corporate financialization, their implications are largely aligned. The tax collection effect reduces the internal liquidity available for speculative financial investment by increasing tax payments and tightening cash flow constraints. The governance effect, in turn, suppresses agency-driven financialization by improving transparency and limiting managerial opportunism. Based on this logic, the following hypothesis is proposed:

H1: The higher the tax administration intensity, the lower the degree of corporate financialization.

However, this effect is unlikely to be uniform across firms. Ownership structure is a key source of variation. Compared with non-state-owned enterprises, state-owned enterprises benefit from implicit guarantees and

easier access to credit, making them less sensitive to the liquidity pressure induced by tax enforcement. Non-state-owned enterprises, by contrast, face tighter budget constraints, which makes the tax collection effect more directly binding (Yu Wenchao et al., 2018 [5]; Cao Wei et al., 2023 [3]). Executive characteristics further moderate this relationship. CEOs with financial backgrounds are not only more capable of identifying financial arbitrage opportunities (Du Yong et al., 2019 [4]), but also tend to possess stronger capabilities in interpreting policy signals and adjusting asset structures. Under stronger regulatory pressure, such firms may reduce speculative financial allocation more proactively in order to mitigate compliance risks (Custódio and Metzger, 2014 [1]). Agency costs represent another important dimension. When agency problems are more severe, managerial incentives to pursue private benefits or conceal poor performance through financialization become stronger (Dittmar et al., 2003 [18]). In this context, tax administration functions as an external governance supplement, partially offsetting weaknesses in internal control systems. Dyck and Zingales (2004) [1] find that higher tax compliance is associated with lower private benefits of control. Moreover, the information-enhancing effect of tax enforcement tends to be more pronounced in regions with weaker traditional governance mechanisms (Gallemore and Jacob, 2020 [22]). Based on these three dimensions, the following heterogeneity hypothesis is proposed:

H2: The inhibitory effect of tax administration on corporate financialization is more significant in non-state-owned enterprises, firms with a higher proportion of executives with financial backgrounds, and firms with higher agency costs.

3. Research Design

3.1 Sample Selection and Data Sources

The empirical analysis is based on A-share listed companies from the Shanghai and Shenzhen stock exchanges over the period 2012–2024. Financial firms are excluded from the sample, along with ST and PT firms and observations with missing key financial information. After applying these filters, the final sample consists of 49,066 firm-year observations. The data used in this study come from multiple sources. Fiscal data on local government general public budget revenues and expenditures are obtained from the official website of the National Bureau of Statistics. Firm-level financial information, along with other macroeconomic variables, is primarily drawn from the CSMAR database. To mitigate the influence of extreme values, all continuous variables are winsorized at the 1% level in both tails.

3.2 Variable Definitions

3.2.1 Dependent Variable

Following Du Yong and Wang Ting (2019) [1], corporate financialization in this paper is measured by constructing a broad indicator of financial assets. Specifically, corporate financial assets are defined as the sum of six components: trading financial assets, derivative financial assets, net loans and advances, net available-for-sale financial assets, net held-to-maturity investments, and net investment properties. This definition differs slightly from the standard accounting classification of financial assets. Monetary funds are excluded, as they primarily serve liquidity and day-to-day operational needs rather than capital appreciation purposes. In contrast, investment properties are included in the measure. This adjustment is motivated by the observation that, during the sample period, China's real estate sector experienced rapid expansion, and firms' holdings of real estate assets increasingly shifted from operational use toward value appreciation, exhibiting characteristics more consistent with financial investment behavior. Based on this construction, the degree of corporate financialization is measured as the ratio of total corporate financial assets to total assets.

3.2.2 Explanatory Variable

Following Ye Kangtao and Liu Hang (2011) [7], the intensity of local tax administration is measured using the ratio of actual tax revenue to the region's expected taxable capacity. In this framework, expected tax revenue is first estimated using Model (1), and the ratio between actual and expected revenue is then used to capture the strength of tax enforcement at the local level.

$$T_{i,t}/GDP_{i,t} = \beta_0 + \beta_1 \cdot IND1_{i,t}/GDP_{i,t} + \beta_2 \cdot IND2_{i,t}/GDP_{i,t} + \beta_3 \cdot OPENNESS_{i,t}/GDP_{i,t} + \varepsilon_{i,t} \quad (1)$$

where i denotes the region and t denotes the year. $T_{i,t}$ represents the total tax revenue of each region at the end of the year. $IND1_{i,t}$ and $IND2_{i,t}$ represent the output value of the primary and secondary industries in each region at the end of the year, respectively. $OPENNESS_{i,t}$ represents the total import and export volume of each region at the end of the year. After regressing the model, the predicted value of $T_{i,t}/GDP_{i,t}$ is obtained. The local government's tax administration intensity indicator $TE_{i,t}$ for the year is then calculated as the ratio of actual tax revenue to the predicted value.

3.2.3 Control Variables

Following the methods of Li Xiaoyan et al. (2022) [9] and Wang Yifeng and Wei Xingkai (2024) [12], the following indicators are included as control variables:

Firm size (SIZE): Natural logarithm of total assets.

Leverage (LEV): Total liabilities divided by total assets.

Investment intensity (INVEST): Net fixed assets divided by total assets.

Cash holdings (CASH): Total cash and cash equivalents at the end of the period divided by total assets.

Regional financial development (FIR): Total deposits and loans of financial institutions in the region divided by the region's GDP for the year.

Financing constraints (SA): Calculated according to the Hadlock and Pierce (2010) [1] formula, taken as the negative of the absolute value; a larger value indicates higher financing constraints.

Return on assets (ROA): Net profit divided by total assets.

Real earnings rate (EFF): (Operating profit – fair value gains – investment income + investment income from associates and joint ventures) divided by operating revenue.

Regional economic development (LNGDP): Natural logarithm of the region's GDP for the year.

3.3 Model Construction

To test the hypotheses, the following model is constructed:

$$FI_{i,t} = \beta_0 + \beta_1 \cdot TE_{i,t} + \beta_2 \cdot \text{CONTROLS}_{i,t} + \sum \text{YEAR} + \sum \text{FIRM} + \varepsilon_{i,t} \quad (2)$$

where i denotes the firm, t denotes the year, $FI_{i,t}$ represents the degree of corporate financialization, $TE_{i,t}$ represents the tax administration intensity in the firm's region for the year, $\text{CONTROLS}_{i,t}$ is the vector of control variables, YEAR represents year fixed effects, FIRM represents firm fixed effects, and $\varepsilon_{i,t}$ is the random disturbance term.

4. Empirical Analysis

4.1 Descriptive Statistics

Table 1 presents the descriptive statistics of the main variables.

Table 1: Descriptive Statistics

Variable	Observations	Mean	Std. Dev.	Min	Median	Max
FI	49065	0.047	0.085	0.000	0.009	0.473
TE	49066	0.956	0.162	0.647	0.930	1.431
SIZE	49065	22.116	1.390	18.924	21.956	26.246
LEV	49065	0.415	0.208	0.053	0.403	0.929
INVEST	49064	0.202	0.154	0.002	0.170	0.672
CASH	49061	0.164	0.129	0.008	0.127	0.624
FIR	49066	4.018	1.415	2.011	3.645	7.618
SA	40694	-3.857	0.263	-4.544	-3.856	-3.195
ROA	49065	0.033	0.071	-0.304	0.036	0.208
EFF	47080	0.046	0.235	-1.352	0.068	0.491
LNGDP	49066	10.756	0.733	8.229	10.816	11.861

The dependent variable, the degree of corporate financialization (FI), has a mean of 0.047, a minimum of 0.000, and a maximum of 0.473. This indicates substantial variation in financialization levels across non-financial firms. The median is 0.009, suggesting that most non-financial firms have relatively low levels of financialization. The tax administration intensity (TE) ranges from a minimum of 0.643 to a maximum of 1.431, indicating significant differences in the tax administration intensity faced by firms across different years and regions.

4.2 Baseline Regression

Table 2 reports the baseline regression results. Column (1) shows the regression of tax administration on corporate financialization after controlling for firm fixed effects and year fixed effects. The coefficient on tax administration (TE) is -0.015, significant at the 1% level, providing preliminary support for Hypothesis H1. Column (2) adds firm-level and region-level control variables while retaining firm and year fixed effects. The coefficient on tax administration remains significantly negative at -0.013 (1% level). This indicates that stronger regional tax administration encourages local firms to reduce their level of financialization and restrains the tendency of “shifting from real to virtual.”

Table 2: Baseline Regression

	(1)	(2)
	FI	FI
TE	-0.015***	-0.013***
	(0.005)	(0.005)
Constant	0.058***	-0.110
	(0.005)	(0.077)
Control Variables	No	Yes
Year FE	Yes	Yes
Firm FE	Yes	Yes
N	48,947	39,018
R ²	0.618	0.641

Note: ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Standard errors clustered at the firm level are reported in parentheses. The same applies below.

4.3 Heterogeneity Analysis

4.3.1 Heterogeneity Based on Property Rights Nature

Following Li Xiaoyan et al. (2022) [9], the sample is divided into state-owned and non-state-owned enterprises for separate regressions. As shown in Columns (1) and (2) of Table 3, the coefficient of the core explanatory variable is significantly negative in the subsample of non-state-owned enterprises, whereas it is statistically insignificant in the state-owned subsample. This indicates that the inhibitory effect of tax administration on corporate financialization is mainly concentrated in non-state-owned firms. One possible explanation is that non-state-owned enterprises operate under tighter budget constraints and therefore respond more strongly to changes in external tax enforcement and tax burdens. By contrast, state-owned enterprises typically bear broader policy and social responsibilities and benefit from implicit government guarantees. As a result, their asset allocation decisions tend to be less sensitive at the margin to variations in tax administration intensity.

Table 3 Heterogeneity: Property Rights

	(1)	(2)
	State-owned	Non-state-owned
	FI	FI
TE	-0.005	-0.024***
	(0.005)	(0.007)
Constant	0.090	-0.062
	(0.112)	(0.128)
Control Variables	Yes	Yes
Year FE	Yes	Yes
Firm FE	Yes	Yes
N	12,035	26,912
R ²	0.714	0.635

4.3.2 Heterogeneity Based on Executives' Financial Background

Drawing on Du Yong et al. (2019) [4], the sample is split into two groups according to the median proportion of executives with financial backgrounds. As shown in Table 4, the inhibitory effect of tax administration is statistically significant only in the group with a higher share of financial-background executives. This suggests that financial literacy at the managerial level tends to amplify firms' sensitivity to external regulatory pressure. This pattern can be interpreted from two related perspectives. On the one hand, executives with financial training are more attuned to changes in policy signals, including intensified tax administration, and may therefore take earlier action to reduce speculative financial asset holdings in order to manage potential risks. On the other hand, such firms often have relatively stronger capabilities in financial planning and asset allocation, which makes it easier for them to adjust their portfolios and redirect resources toward core business activities when external constraints increase. By contrast, firms without sufficient financial expertise at the managerial level tend to adjust more slowly, partly due to delayed interpretation of policy changes and partly due to established organizational routines that are harder to shift in the short term.

Table 4: Heterogeneity: Managerial Financial Background

	(1)	(2)
	High Financial Background	Low Financial Background
	FI	FI
TE	-0.014*	-0.007
	(0.007)	(0.006)
Constant	-0.036	-0.099
	(0.120)	(0.116)
Control Variables	Yes	Yes
Year FE	Yes	Yes
Firm FE	Yes	Yes
N	16,346	17,312
R ²	0.673	0.656

4.3.3 Heterogeneity Based on Total Asset Turnover Rate

This paper follows Ang et al. (2000) [1] and uses total asset turnover (operating revenue divided by total assets) as an inverse proxy for agency costs. A lower turnover ratio is interpreted as reflecting weaker asset utilization efficiency under managerial control, and thus higher agency costs. The sample is then split into high and low turnover groups based on the industry-year median. As shown in Table 5, the coefficient on tax administration (TE) is significantly negative at the 1% level in the low-turnover group (i.e., firms with higher agency costs), while it becomes statistically insignificant in the high-turnover group. This pattern suggests that the restraining effect of tax administration on corporate financialization is mainly concentrated in firms with weaker internal governance. In other words, tax administration appears to play a more pronounced external governance role when internal monitoring mechanisms are relatively ineffective, partially substituting for deficiencies in firm-level governance structures.

Table 5: Heterogeneity: Asset Turnover Rate

	(1)	(2)
	High Turnover	Low Turnover
	FI	FI
TE	-0.007	-0.018***
	(0.007)	(0.007)
Constant	-0.041	-0.108
	(0.100)	(0.119)
Control Variables	Yes	Yes
Year FE	Yes	Yes
Firm FE	Yes	Yes
N	15,450	22,716
R ²	0.622	0.690

4.3.4 Instrumental Variable Test

For robustness, following Tan Yanzhi and Shi Weiqi (2023) [1], this paper uses fiscal pressure (FP) as an instrumental variable, defined as local government general public budget expenditure divided by general public budget revenue. The underlying logic is that greater fiscal deficits tend to induce local governments to strengthen tax administration in order to alleviate budget constraints. At the same time, budgeted fiscal revenue and expenditure are largely determined at the beginning of the fiscal year and are unlikely to directly affect firms' financial asset allocation decisions through channels other than tax enforcement. The two-stage least squares (2SLS) results indicate that the first-stage F-statistic is 342.9, suggesting that the instrumental variable is not weak. In the second stage, the coefficient on tax administration remains significantly negative at the 10% level, consistent with the baseline findings.

Table 6: Instrumental Variable Regression

	(1)	(2)
	First Stage	Second Stage
	TE	FI
FP	0.699***	
	(0.038)	
TE		-0.042*
		(0.023)
Control Variables	Yes	Yes
Year FE	Yes	Yes
Firm FE	Yes	Yes
N	39018	39018
F	342.9	53.52

4.3.5 Robustness Tests

To enhance the reliability of the baseline results, a series of robustness checks are conducted. First, the dependent variable is redefined. Following Yao Dequan and Fu Xiaofei (2022) [1], corporate financialization is alternatively measured by the growth rate of financial assets, calculated as the first difference of financial assets scaled by lagged total assets. The results remain broadly consistent with the baseline estimates. Second, municipalities directly under the central government—Beijing, Shanghai, Tianjin, and Chongqing—are excluded from the sample. As noted by Tang Song et al. (2020) [2], these cities differ markedly from other provinces in terms of economic scale, fiscal autonomy, concentration of financial resources, and policy responsiveness. Re-estimating the model after their exclusion yields results that are still consistent with the baseline findings. Finally, a sub-period analysis is conducted by excluding the earlier sample period (2012–2016). The inhibitory effect of tax administration on corporate financialization remains statistically significant, suggesting that the main conclusion is robust even in a more recent institutional context characterized by more digitalized tax administration and stricter regulatory enforcement.

Table 7: Robustness Tests

	(1)	(2)	(3)
	Replace Dep. Var.	Shorter Period	Exclude Municipalities
	FI2	FI	FI
TE	-0.008*	-0.020***	-0.012**
	(0.005)	(0.006)	(0.005)
Constant	-0.032	-0.063	-0.176*
	(0.074)	(0.143)	(0.092)
Control Variables	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes
N	35,825	26,369	31,450
R ²	0.150	0.706	0.637

5. Research Conclusions and Policy Implications

Based on an empirical analysis of Chinese A-share listed firms from 2012 to 2024, the results suggest that stronger tax administration, largely driven by local fiscal pressure, is associated with a clear reduction in firms' tendency toward "shifting from real to virtual." The causal relationship remains stable after addressing endogeneity concerns, where fiscal pressure—proxied by the ratio of local government budget expenditure to budget revenue—is used as an instrumental variable. Taken together, the evidence implies that intensified tax enforcement helps compress the space for informal tax avoidance, raises the relative cost of holding financial assets, and in turn encourages a reallocation of resources back toward productive activities in the real economy.

The heterogeneity patterns provide additional nuance. The restraining effect of tax administration is more evident in firms with higher agency costs and weaker internal governance, suggesting that external tax enforcement can, to some extent, substitute for internal monitoring deficiencies. A similarly stronger effect is observed among firms with a higher proportion of executives with financial backgrounds, which may reflect greater sensitivity to policy signals and a more flexible capacity for asset reallocation under regulatory pressure. In contrast, state-owned enterprises, supported by implicit government guarantees, appear less responsive to changes in tax administration intensity compared with non-state-owned firms, whose financing constraints make them more sensitive to fiscal and enforcement conditions.

From a policy perspective, several implications follow from these findings. At the macro level, fiscal budgeting and economic growth targets need to remain reasonably aligned. Excessive pressure on local revenue performance may induce short-term fluctuations in tax enforcement intensity, which in turn could weaken the predictability of the institutional environment faced by firms. At the regulatory level, digital tax administration can be further leveraged as a governance tool beyond revenue collection. In particular, differentiated supervision may be considered for firms exhibiting weak internal governance or unusually high levels of financial asset allocation. The development of dynamic indicators tracking corporate financialization could also help improve early identification of abnormal asset structures and strengthen the precision of regulatory responses. At the firm level, greater attention could be given to the composition of executive teams and the role of managerial expertise in shaping asset allocation behavior. Enhancing policy awareness and risk management capabilities among executives may help firms better integrate financial decision-making into internal governance systems, thereby improving compliance and reducing excessive exposure to financial assets under tightening external regulation.

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Conflicts of Interest

The authors declare no conflict of interest.

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