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The labor market effect of foreign acquisitions: Evidence from Chinese manufacturing firms☆

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ABSTRACT

The potential impacts of foreign acquisitions have long been debatable in both academic and policy circles in China, which have more or less shaped China's regulation policy regarding foreign acquisitions. This paper examines the causal effect of foreign acquisitions on the labor market in China with self-constructed firm level panel data. We combine the propensity score matching and the difference-in-differences techniques in our estimation to deal with the potential selection biases in acquisitions. Our results show that the impacts of foreign acquisitions in China are different from but also comparable to those in developed countries found in the literature. Specifically, foreign acquisitions have significant positive effects on the levels of wage and employment of target firms, but mildly negative impact on employment growth and insignificant impact on wage growth. The impacts show heterogeneities. We also check the potential channels of the impacts.

1. Introduction

Foreign direct investment (FDI) has been one of the most important phenomena in the globalization era and has important implications for the economic development of the host country as well as the home country. Generally there are two forms of FDI, one is Greenfield FDI, and the other is cross-border mergers & acquisitions (M&As), with M&As taking an unnegligible share of about 38.9% for the whole world since 1990s.[1]

Different from Greenfield FDI which obviously creates jobs in the host country (at least in the short run) and are welcomed by host country governments, cross-border M&As usually arouse hot debates in the host country. One of the most important concerns is the possible negative shock to the workers of the target firms. These concerns are repeatedly raised in China in recent years in both academic and policy circles because of the emergence of foreign acquisitions in China in recent years, which more or less shaped China's regulation policy regarding foreign acquisitions. What's more, these concerns have also affected the economic activities in real life. For example, in China, almost all big foreign acquisition proposals in the recent years, e.g. Coca Cola's bidding for Huiyuan

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[1] The ratio is much higher in developed countries, e.g. nearly 70% during the same period in U.K. (Griffith, Redding, & Simpson, 2004).

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Juice Co., Carlyle Group for Xugong Heavy Machine, Nestle for Xu Fuji Food, Schneider for NVC lighting etc., drew strong attention in political, media and academic circles, and some deals finally failed due to obviously non-economic reasons.

However, what are the impacts of foreign acquisitions on the labor market of the host country, especially in a developing country like China? Though the answer to this question has important policy implications as far as cross-border M&As are concerned, neither the theory nor the empirical analyses in the current literature reach clear-cut conclusions, and the empirical findings show that the impacts are country-specific (Bandick, 2011; Huttunen, 2007, just to name a few). Furthermore, almost all existent empirical research on the impacts of foreign acquisitions focuses on developed host countries, leaving a gap for the research on developing host countries.

In this paper we investigate the impacts of foreign acquisitions on the labor market (in particular, wage and employment) in China, the second largest FDI recipient of the world and the largest developing country where foreign acquisitions are emerging. To the best of our knowledge, this paper may be the first effort to investigate the labor market effect of foreign acquisitions in a developing country.

To do this, we self-construct unique firm level data by manually linking cross-border M&A transactions from the Thomson Financial SDC database to China's Annual Surveys of Industrial Enterprises (ASIEs) for the period 1998–2007 firm by firm. In this way we assemble a panel dataset with both foreign acquisition transaction and firm performance information. This is likely the first comprehensive firm level panel dataset for studying foreign acquisitions in China. To deal with the potential bias in the estimation due to the selection of targets in acquisitions, following the literature (for example, Arnold & Javorcik, 2009; Bandick & Gorg, 2010; Girma & Gorg, 2007), we first employ the propensity score matching (PSM) technique to construct a control group consisting of comparable firms to the acquired firms (treatment group). Based on the sample of the treatment group and the control group, we then use the difference-in-differences (DID) technique to estimate the treatment effect of foreign acquisitions.

We find that the impacts of foreign acquisitions in China are different from but also comparable to those in developed countries found in the literature. Specifically, foreign acquisitions have significantly positive effects on the level of wage and the level of employment of target firms, but mildly negative impact on the employment growth rate and insignificant impact on the wage growth rate. For example, in our preferred full specification regressions, foreign acquisitions increase worker wage and employment by 11.87% and 8.44%, respectively, while decrease employment growth rate by 0.92%. These results imply that foreign acquirers tend to adjust wage and employment levels quickly in the first few years after the deal, and then keep in a steady state.

We also find that the impacts of foreign acquisitions show substantial heterogeneity. Acquirers from Europe and North America generally raise wages after the acquisitions while acquirers from East Asia enlarge employment scale; both wage and employment are increased in high-tech sectors, but not in low-tech sectors; toehold (step-by-step) acquisitions have positive effects on the wage and employment levels but non-toehold acquisitions have a negative effect on the employment growth rate. Employee training, fixed-asset investment and market expansion are possible channels of these labor market effects.

The labor market effects of foreign acquisitions are worth (and are under) intensive empirical investigation for two reasons in academics, besides the important policy implications for the host country.[2] First, the theoretical analyses do not reach a consensus. On one hand, it is well established that multinational enterprises (MNEs) possess firm-specific assets and have productivity advantage (Caves, 1974; Helpman, Melitz, & Yeaple, 2004; Markusen, 1995)[3] and thus foreign acquisitions may be accompanied with higher wage (due to, for example, efficiency wage consideration) and employment expansion. On the other hand, however, MNEs are more likely to have monopolistic position in the wage bargaining due to its ability of allocating resources worldwide, and MNEs are "footloose" and also may re-locate the production to other countries after the acquisition, which may be detrimental to the wage and employment of the targets.

Second, the empirical findings about the wage and employment effect of foreign acquisitions are mixed and country-specific. For example, Conyon, Girma, Thompson, and Wright (2002), Huttunen (2007) and Oberholfer, Stockl, and Winner (2012) find a positive effect of foreign acquisitions on target firms' wages in U.K., Finland and EU, while Martins (2004), Heyman, Sjoholm, and Tingvall (2007) and Bandick (2011) reach the opposite conclusion in Portugal and Sweden. Almeida (2007) finds an insignificant effect of foreign acquisitions in Portugal on average wage but a positive effect on employment. In addition, Girma and Gorg (2007) find heterogeneity of the wage effect depending on the country origins of acquirers and the skill level of workers. Girma and Gorg (2004) show that foreign acquisitions reduce unskilled labors in electronic sector of U.K.; Huttunen (2007) finds skilled labors has been reduced by foreign acquisitions in Finland.

Our paper extends upon and improves the empirical literature in several aspects. Firstly, this paper may be the first to investigate the labor market effects of foreign acquisitions in a developing country. The large empirical literature is overwhelmingly on developed countries till now (as shown above). However, the welfare implication of foreign acquisitions for developing host countries is no less important than that for developed host countries. What's more, the literature has shown clearly that the impacts are country-specific; therefore the findings in developed countries are not necessarily true for developing countries.

[2] There is a large body of empirical literature looking at the impacts of foreign acquisitions from different perspectives, besides the aforementioned labor market perspective. For example, Conyon et al. (2002), Harris and Robinson (2002), Benfratello and Sembenelli (2006), Karpaty (2007), Bertrand and Zitouna (2008), Salis (2008), Arnold and Javorcik (2009), Bandick (2011), Chen (2011), Liu, Lu, and Qiu (2014), etc, investigate the productivity (and some for profits and sales) effect of foreign acquisition. Bertrand and Zuniga (2006), Bandick, Gorg, and Karpaty (2009), Bertrand (2009), Stiebale and Reize (2011), etc, look at the effect on R&D of the targets. Girma and Gorg (2004), Bandick and Gorg (2010), etc, look at the effect on the survival rate as well as employment growth of the targets. However, almost all these papers employ developed country data and investigate aspects other than the labor market. In this paper we look at a developing country and investigate the labor market effect, which differentiates our paper from these papers.

[3] Liu and Qiu (2013) confirm empirically that foreign acquirers do perform better than targets in many ways.