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Does Stock Price Informativeness Affect Labor Investment Efficiency?*

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Abstract

In this paper, we examine whether managers use information included in stock prices when making labor investment decisions. Specifically, we examine whether stock price informativeness affects labor investment efficiency. We find that a higher probability of informed trading (*PIN*) is associated with lower deviations of labor investment from the level justified by economic fundamentals i.e., higher labor investment efficiency. This finding is robust to using alternative proxies for stock price informativeness and labor investment efficiency, when we control for earnings quality and mispricing, and when we address endogeneity issues. Furthermore, we report evidence suggesting that the positive impact of stock price on labor investment efficiency is more (less) pronounced in firms from highly unionized industries and firms facing higher financial constraints (firms from industries that rely more on skilled labor).

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Keywords: Stock Price Informativeness, Private Information; Managerial learning, Investment Efficiency; Labor Investment; Corporate Governance

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