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Are cross-border acquisitions enemy of labor? An examination of employment and productivity effects

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ABSTRACT

We examine the employment, efficiency and productivity effects of cross-border acquisitions using a large sample of firms. After accounting for industry-wide influences, we observe that targets of cross-border acquisitions were less productive than those of domestic acquisitions before the takeover, but after the acquisition, their productivity levels improve significantly and they increase wages (more than domestic targets), albeit they reduce employment levels. In addition, cross-border targets become more efficient than their counterparts acquired by domestic bidders. Interestingly, while in general acquisitions in the resource sector and related acquisitions do not generate any labor efficiency gains, if the acquisitions are undertaken by foreign bidders then the targets realize significant efficiency improvements. At the macro-level over the long run, cross-border acquisitions are associated with improvements in aggregate labor conditions (i.e., higher wages, lower levels of unemployment, and higher labor productivity). At the same time, firms targeted in cross-border acquisitions have greater impact on GDP than those targeted in domestic acquisitions. This suggests that cross-border takeovers spur a reallocation of labor which generates positive outcomes for the host country. This significant contribution is often overlooked in the discourse on the benefits of cross-border acquisitions to the host country.

1. Introduction

Over the past couple of decades Canada has experienced a significant increase in cross-border mergers and acquisitions (M&A) activities. Data from Thompson Financial Corporation show that annual cross-border takeover transactions in Canada increased from 463 in 2001 to 539 in 2006, an increase of 16.4% per annum. Fig. 1 highlights the remarkable increase in both domestic and cross-border acquisitions in Canada from 1985 to 2010. High-profile cases of foreign takeovers of Canadian firms have included Seagrams, MacMillan, Bloedel, Inco, Dofasco, and Stelco, and some of these firms were established over a century ago. The surge in cross-border mergers and acquisitions has generated fierce debate among politicians and policy makers on the merits of cross-border acquisition. At the center of the debate on the net benefits of cross-border acquisition in Canada is the effect of cross-border mergers and acquisition on the Canadian labor markets.

Opponents of foreign takeovers argue that foreign ownership results in a range of negative welfare outcomes, the most rousing being the relocation of headquarters to foreign countries and the loss of national identity. They contend that the rise in foreign ownership is a de facto “hollowing out of corporate Canada” (Reguly, 2002) and that cross-border takeovers raise important questions in terms of foreign ownership of national icons. More importantly, from the standpoint of this study, opponents argue that

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cross-border acquisitions lead to the elimination of jobs in Canada. Thus far, the debate on the effects of cross-border acquisitions on labor markets has been based on anecdotal evidence.

The literature is not clear on the real impact of cross-border takeovers on host nation's welfare and in particular, on its labor capital. Some empirical research, for example, Conyon et al. (2002) and Girma (2005), shows that cross-border transactions have adverse welfare effects since they generally lead to a decrease in the workforce numbers. Decreases in employment levels, however, tell only part of the story. Other studies, including Almeida (2003), find that there is a wage premium involved in cross-border acquisitions as foreign bidders typically increase wages after the acquisition. The increase in wages is typically accompanied by an increase in productivity levels (Bertrand and Zitouna, 2008). In light of these findings, it is not entirely clear that cross-border takeovers decrease host country welfare through decreases in employment levels. Moreover, it is not clear that cross-border takeovers impact negatively on the host nation's labor market or whether they impact on the host nations in ways that are different from those of domestic acquisitions.

Using data on cross-border acquisitions in Canada from 1980–2010, we perform a series of empirical analyses designed to capture the labor market effects of cross-border takeovers. Unlike previous studies, we provide a comprehensive view of labor effects by investigating four labor market variables, namely employment levels, wage levels, employee productivity, and employee efficiency. We evaluate these labor market effects by comparing changes in these variables for targets of cross-border acquisitions and their non-merging industry counterparts. For benchmarking purposes, we also estimate the labor market effects of domestic acquisitions as well. Our sample of cross-border and domestic targets and their rivals that were not involved in takeovers during our study period presents an interesting laboratory for examining the performance of two distinct groups of targets operating in the same (Canadian) host market, and this allows us to ascertain whether indeed cross-border acquisitions generate undesirable welfare effects that are different from those associated with domestic acquisitions. Also, comparisons of the performance of the targets and their rivals, to a greater extent, allows for the control of changes over time in the underlying structure of the industry.

We find that both targets of cross-border and domestic acquisitions shed jobs after the acquisition; however, targets of cross-border acquisitions reduce employment levels more than targets of domestic acquisitions. Although cross-border acquisitions lead to more attrition, targets of cross-border acquisitions increase wage levels more than domestic targets after acquisitions, which translates into higher post-acquisition productivity levels. In addition, the firms targeted in cross-border acquisitions become more efficient in the post-acquisition period than those acquired by domestic firms. Interestingly, we observe that in general acquisitions in related industries and in the resource sectors do not generate any efficiency gains after the acquisitions; however, those undertaken by foreign bidders in these industries generate significant efficiency improvements. Contrary to the popular view among some critics of cross-border acquisitions, we do not find any evidence that foreign acquirers target firms with good pension assets.

Having documented firm-level evidence relating to the effects of cross-border acquisitions on employees, we examine the effects of such acquisition on labor market conditions at the macro-level. We find that over the long run, cross-border acquisitions are associated with improvements in aggregate labor conditions (i.e., higher wages, lower levels of unemployment, and higher labor productivity). This suggests that cross-border takeovers spur a reallocation of labor that increases aggregate labor productivity, employment, and wage levels. This significant contribution is sometimes overlooked in the debate about the benefits of cross-border acquisitions to the host country. Our findings are inconsistent with the position of critics of cross-border acquisitions who argue that cross-border acquisitions negatively impact on the host country's labor market.

The remainder of the paper is organized as follows. In section two, we review the literature on cross-border acquisitions and their effects on labor productivity and efficiency. The data and methodology are presented in section three. Section four contains the results and analysis at the firm-level. The effect of aggregate cross-border mergers and acquisitions on the economy is presented in section five, and section six concludes the study.

2. Literature review

2.1. Cross-border acquisitions

Conceptually, cross-border acquisitions occur for the same reasons as domestic acquisitions. In general, two firms will merge when the bidding firm views the combination will increase firm value. However, national borders add an extra element to the cross-border acquisitions process because there are additional factors that can impede or enable cross-border transactions. For example, differences in national culture can increase the costs of combining two firms and can also influence the likelihood of successful combination. Differences in governance and legal protection can also motivate cross-border acquisitions if the combined firm has better protection for target-firm's shareholders because of higher governance standards in the acquirer's country. Imperfect integration of capital markets across countries can lead to a merger in which a higher-valued bidder purchases a relatively inexpensive target following changes in exchange rates or stock market valuations in the host country's currency.

Though national borders introduce different frictions into the outcomes of cross-border acquisitions transaction, such acquisitions are increasing in Canada (see Fig. 1). Theories of foreign direct investment (FDI) help explain this trend with an emphasis on the comparative advantages offered by multinational enterprises (Hymer, 1976; Dunning, 1977; Markusen and Venables, 1998). A firm needs to possess ownership advantages (e.g., a superior product, a strong brand, more efficient production or administrative processes) in order to compete in the international financial markets as a multinational. Research also shows that multinational enterprises typically enjoy higher productivity, pay higher wages, and usually exhibit higher profitability than their indigenous counterparts (Dunning, 1981; Doms and Jensen, 1998). Upon taking over domestic targets, the multinational bidder's unique characteristics could be exploited to the advantage of the subsidiaries (targets) abroad (Caves, 1974). According to this theory,

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