

Firm-size dynamics and the role of labour market institutions

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Literature review

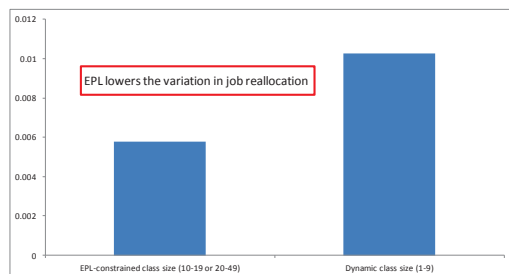
- Firm characteristics**
 - Smaller firms tend to produce more jobs (Birch 1979; Lotti et al 2003; Neumark et al 2011) but only after controlling for age (Haltiwanger et al 2013)
 - Younger firms tend to produce more jobs (Gomez-Salvador et al 2004; Haltiwanger et al. 2013)
 - Evidence that more productive firms produce more jobs (OECD 2009)
- Labour market institutions**
 - Stringent EPL inhibits the emergence of high-risk entrepreneurial firms (Henrekson and Johansson 2010)
 - Stringent EPL reduces dismissal probabilities for permanent workers that are concerned by restrictions (Boeri and Jimeno 2005)
 - size-contingent EPL makes allocation of labour sub-optimal (Schivardi and Torrini 2008; Garicano, Lelarge and Van Reenen 2013)

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Job reallocation rate: cross-country variation

Size-contingent EPL reduces reaction of jobs to market-driven shocks

Job reallocation rate (st. dev.): most constrained versus most dynamic size class; pre-crisis sample (2000-2008)



Source: own calculations based on CompNet Labour Module and OECD.

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EPL and the 20-employee threshold

Stricter EPL increases the difference in the growth performance between firms not covered by the EPL and those that would become covered (i.e. if exceeding the 20E threshold).

$$\Delta e_{cst}^{10E} - \Delta e_{cst}^{20E} = f(EPL_{ct})$$

c country
s sector
t year
 Δe^{XE} % of firms growing over X employees threshold.

OLS: ($\Delta e^{10E} - \Delta e^{20E}$)	
Real value added growth	-0.03 (0.029)
EPL ID: Individual dismissals	0.08* (0.042)
EPL CD: Collective dismissals	0.01 (0.022)
Constant	-0.29* (0.120)
Country, Sector, Year FES	Yes
Observations	537
R ²	0.499

Notes: Standard errors in parentheses; ** p<0.01, * p<0.05, + p<0.1

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Outline

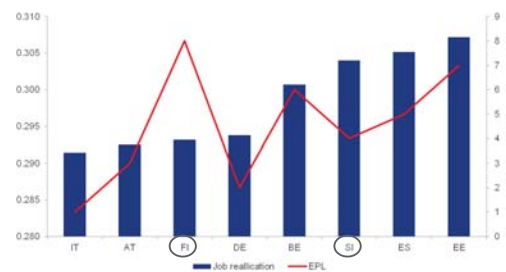
- Research questions**
 - Does EPL have an impact on job reallocation?
 - What is the role of size-contingent EPL? Does EPL bind more firms of a size close but below the threshold than others?
 - How does it behave over the cycle and what was the impact of the crisis? Is it more binding for growing or downsizing firms?
- Data**
 - CompNet size class dataset: firms changing size class or remaining in the same one during 3-year periods (per country, sector and year)
 - Size classes: 1-9 employees, 10-19 employees, 20-49 employees, 50-249 employees, 250 employees and above
 - Sample: 8 EU countries (AT, BE, DE, EE, ES, FI, IT, PT), 9 macro-sectors over the period 1998-2012 (about 2,000 observations)
 - Institutional variables: EPL distinguishing between rules for individual and collective dismissal (OECD). In most countries applies to firms with 20 and more employees.

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Job reallocation rate and EPL

Greater job reallocation in more flexible EPL regimes

Job reallocation rate: share of expanding and shrinking firms; pre-crisis sample (2000-2008)



Source: own calculations based on CompNet Labour Module and OECD.
Note: higher EPL numbers indicate more flexible labour markets.

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Stricter EPL reduces firm dynamics (threshold 20E)

Logit: growing firms			Logit: downsizing firms			
Labor productivity	-0.06 (0.037)	-0.06 (0.037)	0.05 (0.035)	-0.17** (0.035)	-0.16** (0.035)	-0.17** (0.035)
Real value added growth	0.74** (0.147)	0.74** (0.148)	0.74** (0.136)	-1.87** (0.099)	-1.83** (0.097)	-1.89** (0.099)
EPL ID: Individual dismissals	-1.80** (0.416)	-1.65** (0.452)	-1.39** (0.407)	-1.17** (0.218)	-1.20** (0.246)	-1.20** (0.217)
EPL CD: Collective dismissals	-0.12 (0.087)	-0.05 (0.096)	-0.03 (0.076)	-0.05 (0.057)	-0.20** (0.063)	-0.05 (0.058)
EPL ID * crisis			-0.38** (0.064)		0.68** (0.074)	
EPL CD * crisis			-0.02 (0.027)		0.31** (0.022)	
EPL ID * size class 2 (10-19 employees)						-1.18** (0.217)
EPL ID * size class 3 (20-49 employees)						-1.20** (0.218)
EPL ID * size class 4 (50-249 employees)						-0.82** (0.229)
EPL CD * size class 2 (10-19 employees)						-0.05 (0.059)
EPL CD * size class 3 (20-49 employees)						-0.01 (0.062)
EPL CD * size class 4 (50-249 employees)						0.01 (0.081)
Constant	3.91** (1.053)	3.38** (1.197)	1.991 (1.024)	0.88 (0.571)	3.80** (0.676)	0.96+ (0.572)
Country, Sector, Year FES	Yes	Yes	Yes	Yes	Yes	Yes
Observations	1769	1769	1769	1651	1651	1651
R ²	0.715	0.722	0.761	0.835	0.843	0.837

Notes: Base groups: growing firms: size class 1; downsizing firms: size class 2. Standard errors in parentheses; ** p<0.01, * p<0.05, + p<0.1.

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Conclusions

- Main results**
 - Stricter EPL (e.g. by imposing positive hiring and firing costs) reduces the likelihood that firms grow or shrink (in terms of employment), as predicted by the literature.
 - EPL has a stronger (negative) effect on the growth of firms above the 20 employee-threshold, which is in line with the institutional setup of most countries in the dataset (e.g. concerning restrictions on collective and individual dismissals).
 - During the financial crisis, the negative effect of EPL on growing firms was aggravated, while the effect on downsizing firms was muted.
 - Qualitative results are robust across sectors, country groups, and some additional controls available in the CompNet dataset.
- Policy implications**
 - EPL has a stronger negative impact on firm growth during the financial crisis, acting as a drag on recovery.
 - Softening of threshold effects would lead to improved allocation of jobs.

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