

External Labor Market Punishment in Finance

Naser Hamdi, *Equifax Inc*

Ankit Kalda, *Indiana University*

Avantika Pal, *Washington University*

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Motivation

- Misconduct, bad faith dealings, and working in “gray area” are prevalent in Finance sector (e.g., Dimmock and Gerken 2012; Dyck, Morse, and Zingales 2014)
 - ▶ Egan, Seru, and Matvos 2019 show 15% of financial advisors in large firms have a misconduct record

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- We examine the extent of *external* labor market consequences of misconduct in finance and contrast these to those in non-finance sectors

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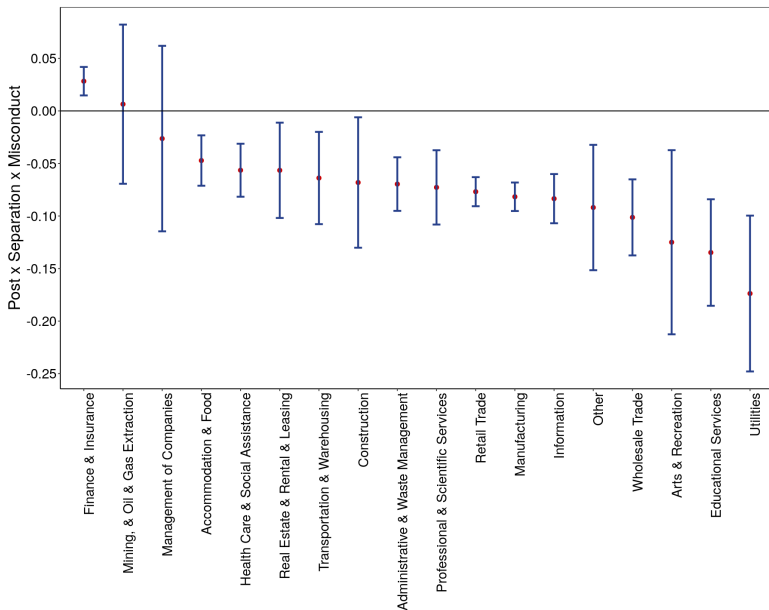
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 - ▶ Misconduct signals preferred characteristics \implies higher *relative* income

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- Results most consistent with assortative matching in labor markets
 - ▶ Certain firms prefer employees with characteristics correlated with “misconduct” background & pay a premium for them

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- Differences in **regulation** and **type of misconduct** across sectors less likely to drive the results
- Products & services based on **future cash flows & parameters** in finance
 - ▶ Results concentrated on finance-related-jobs in establishments located in areas with **low education** and **high elderly population**

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- document the prevalence of **misconduct wage premium** in finance &
- highlight that finance is **unique** in how it treats employees with misconduct background

Data

- Study relies on the intersection of two different data from Equifax
- Separations data
 - ▶ Reported by employers who subscribe to UI management services
 - ▶ All separations with detailed terms of separation (including reason for separation)
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- Employment and income data
 - ▶ Reported by employers who subscribe to Income verification services on a payroll-to-payroll basis
 - ▶ All employees with details including income, job type, title etc
 - ▶ Covers ~30 million employees from ~5,000 employers

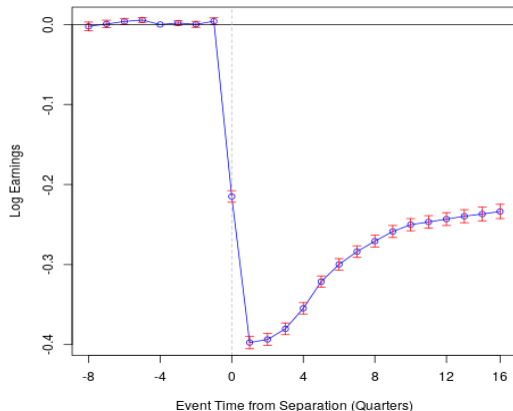
Validation – Earnings following Layoff: All Professions

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Variables	Log Earnings		
	(1)	(2)	(3)
Layoff \times <i>Post</i>	-0.294*** (0.002)	-0.287*** (0.002)	-0.285*** (0.002)
Individual FE	Y	Y	Y
Month FE	Y	N	N
Industry \times <i>Month FE</i>	N	Y	Y
Wage Bin \times <i>Month FE</i>	N	N	Y
N	62,618,513	62,618,513	62,618,513
<i>Adj.R</i> ²	0.842	0.844	0.845

- Based on Jacobsen et al 1993 specification (i.e., column 3), income declines by $\sim 28.5\%$
- Estimates within 20% to 30% range found in literature (e.g., Couch 2001, Jacobson et al 2005, Moore and Scott-Clayton 2019)

Validation – Earnings following Layoff: All Professions



- No considerable pre-trends but large decline on separation
- Initial decline comparable to the literature (e.g., Coucher et al 2011 (AER) find a 35% initial decline)

Earnings following Misconduct Separation

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	Log Earnings	
	Finance	Non-Finance
	(1)	(2)
Misconduct \times <i>Separated</i> \times <i>Post</i>	0.075*** (0.007)	0.028*** (0.007)
<i>Separated</i> \times <i>Post</i>	-0.303*** (0.004)	-0.320*** (0.004)
Individual FE	Y	Y
Wage Bin \times <i>Month FE</i>	Y	Y
Industry \times <i>Month FE</i>	Y	N
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year FE</i>	N	Y
Separation Cohort \times <i>Year FE</i>	N	Y
N	21,152,903	21,152,903
<i>Adj.R</i> ²	0.880	0.896
Baseline estimates	0.077	0.039

- Finance misconduct separations \implies 2.8% to 7.5% higher relative income

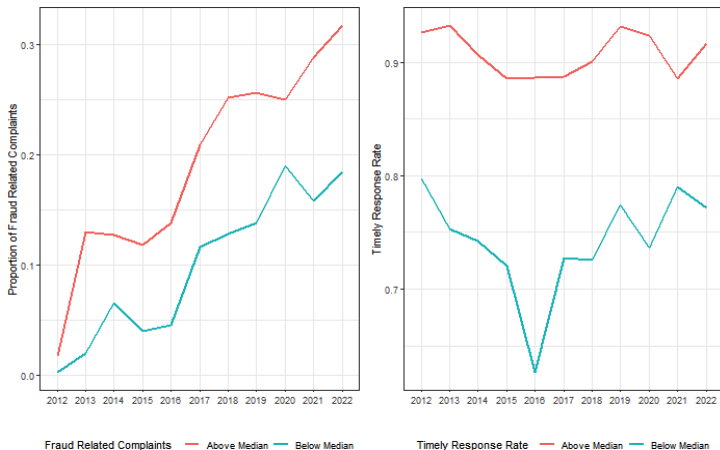
Earnings following Misconduct Separation

	Log Earnings			
	Finance		Non-Finance	
	(1)	(2)	(3)	(4)
Misconduct \times <i>Separated</i> \times <i>Post</i>	0.075*** (0.007)	0.028*** (0.007)	-0.044*** (0.003)	-0.069*** (0.003)
<i>Separated</i> \times <i>Post</i>	-0.303*** (0.004)	-0.320*** (0.004)	-0.290*** (0.002)	-0.310*** (0.002)
Individual FE	Y	Y	Y	Y
Wage Bin \times <i>Month FE</i>	Y	Y	Y	Y
Industry \times <i>Month FE</i>	Y	N	Y	N
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year FE</i>	N	Y	N	Y
Separation Cohort \times <i>Year FE</i>	N	Y	N	Y
N	21,152,903	21,152,903	52,471,961	52,471,961
<i>Adj.R</i> ²	0.880	0.896	0.817	0.849
Baseline estimates	0.077	0.039	-0.048	-0.081

- Finance misconduct separations \implies 2.8% to 7.5% higher relative income
- Non-Finance misconduct separations \implies 4.4% to 6.9% higher relative income

Assortative matching in labor markets

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- Persistent differences across the two groups

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 - ▶ 33% to low complaint firms

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- Among misconduct separations from low complaint firms
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- Conditional on moving from low- to high- complaints/untimely responses, what happens to income?

Assortative matching in labor markets

	Log Earnings			
	Fraud Complaints		No Timely Response	
	Above to Below (1)	Below to Above (2)	Above to Below	Below to Above
Misconduct \times <i>Separated</i> \times <i>Post</i>	0.048 (0.029)	0.091*** (0.031)		
<i>Separated</i> \times <i>Post</i>	-0.182*** (0.017)	-0.215*** (0.017)		
Individual FE	Y	Y		
Wage Bin \times <i>Month FE</i>	Y	Y		
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year FE</i>	Y	Y		
Separation Cohort \times <i>Year</i> \times <i>FE</i>	Y	Y		
Hiring Firm Size \times <i>Hiring Firm Industry</i>	Y	Y		
N	5,862,987	4,175,508		
Adj.R ²	0.904	0.901		

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Misconduct \times <i>Separated</i> \times <i>Post</i>	0.048 (0.029)	0.091*** (0.031)	0.020 (0.022)	0.099*** (0.022)
<i>Separated</i> \times <i>Post</i>	-0.182*** (0.017)	-0.215*** (0.017)	-0.162*** (0.015)	-0.210*** (0.012)
Individual FE	Y	Y	Y	Y
Wage Bin \times <i>Month</i> FE	Y	Y	Y	Y
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year</i> FE	Y	Y	Y	Y
Separation Cohort \times <i>Year</i> \times FE	Y	Y	Y	Y
Hiring Firm Size \times <i>Hiring Firm Industry</i>	Y	Y	Y	Y
N	5,862,987	4,175,508	5,578,247	4,575,474
Adj.R ²	0.904	0.901	0.897	0.909

- Results concentrated on moves from firms with lower to higher complaints/untimely responses

Assortative matching in labor markets

- Among misconduct separations from low complaint firms
 - ▶ 49% move to high complaint firms
 - ▶ 33% to low complaint firms
- Earnings differential between misconduct and no-fault concentrated on moves from firms with low- to high- complaints/untimely responses

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 - ▶ 49% move to high complaint firms
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- Earnings differential between misconduct and no-fault concentrated on moves from firms with low- to high- complaints/untimely responses
- For misconduct employees, tenure at new job 10-15% higher when moving from low- to high- complaint firms than opposite moves

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- Similar results using **collapsed** triple interaction vs **sub-sample** analysis

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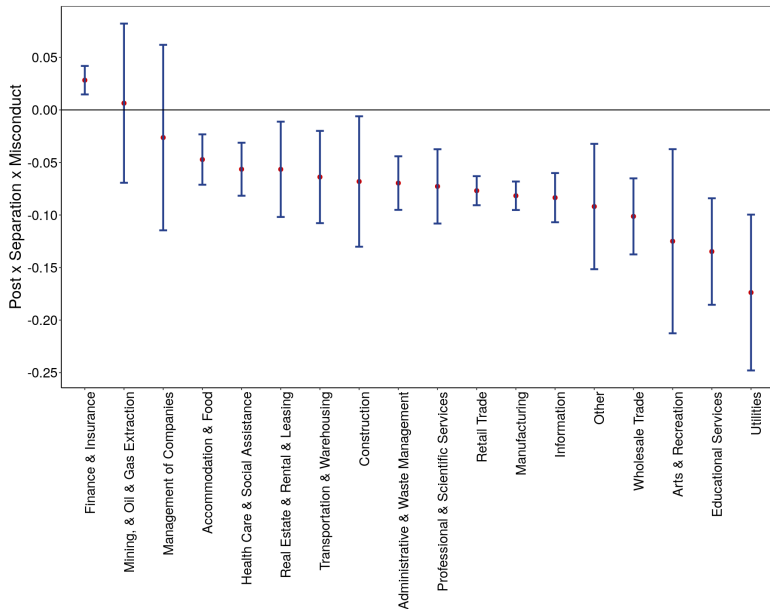
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- Similar results using collapsed triple interaction vs sub-sample analysis
- Compare misconduct separations to mass layoffs
- Condition on employees separated from finance and estimate heterogeneity based on where they move

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What makes Finance Special?

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Income for sales professionals following company policy violation separations

	Log Earnings	
	Finance	Non-Finance
	(1)	(2)
Misconduct \times <i>Separated</i> \times <i>Post</i>	0.070* (0.041)	-0.063*** (0.019)
<i>Separated</i> \times <i>Post</i>	-0.293*** (0.025)	-0.264*** (0.013)
Individual FE	Y	Y
Wage Bin \times <i>Month FE</i>	Y	Y
Firm \times <i>Location</i> \times <i>Year FE</i>	Y	Y
Separation Cohort \times <i>Year FE</i>	Y	Y
N	1,642,767	3,473,614
<i>Adj.R</i> ²	0.949	0.945

- Similar contrast for this sub-sample

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 - ▶ Results concentrated for finance-related jobs and absent for non-finance-related jobs within the finance sector
 - ▶ Concentrated on finance-related-jobs assigned to areas with low education and high 65+ population
 - ▶ No heterogeneity in non-finance related jobs or non-finance sector across education and age levels

Heterogeneity by geography of hiring establishment

	Log Earnings			
	%college		%65 or older	
	Above Median (1)	Below Median (2)	Above Median (3)	Below Median (4)
Panel A: Finance Job Profiles				
Misconduct \times <i>Separated</i> \times <i>Post</i>	-0.0003 (0.055)	0.123*** (0.046)	0.152*** (0.052)	0.119** (0.056)
<i>Separated</i> \times <i>Post</i>	-0.237*** (0.028)	-0.221*** (0.030)	-0.266*** (0.026)	-0.151*** (0.037)
N	8,195,671	8,194,824	8,197,564	8,196,441
Adj. R^2	0.910	0.909	0.910	0.909
Panel B: Non-Finance Job Profiles				
Misconduct \times <i>Separated</i> \times <i>Post</i>	0.0007 (0.087)	0.010 (0.070)	-0.035 (0.076)	0.001 (0.067)
<i>Separated</i> \times <i>Post</i>	-0.127** (0.061)	-0.120** (0.051)	-0.147*** (0.037)	-0.060 (0.041)
N	3,864,187	3,864,685	3,864,938	3,862,485
Adj. R^2	0.907	0.907	0.907	0.907
Individual FE	Y	Y	Y	Y
Wage Bin \times <i>Month FE</i>	Y	Y	Y	Y
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year FE</i>	Y	Y	Y	Y
Separation Cohort \times <i>Year FE</i>	Y	Y	Y	Y

- Results **concentrated** on finance job profiles within the finance sector

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	Above Median (1)	Below Median (2)	Above Median (3)	Below Median (4)
Misconduct \times <i>Separated</i> \times <i>Post</i>	-0.047*** (0.013)	-0.043*** (0.013)	-0.043*** (0.013)	-0.056*** (0.013)
<i>Separated</i> \times <i>Post</i>	-0.284*** (0.008)	-0.304*** (0.010)	-0.309*** (0.010)	-0.277*** (0.009)
N	34,751,633	34,577,836	34,874,183	34,528,699
Adj.R ²	0.862	0.862	0.862	0.862
Individual FE	Y	Y	Y	Y
Wage Bin \times <i>Month FE</i>	Y	Y	Y	Y
Firm \times <i>Location</i> \times <i>Tenure</i> \times <i>Year FE</i>	Y	Y	Y	Y
Separation Cohort \times <i>Year FE</i>	Y	Y	Y	Y

- No heterogeneity by education or age in **non-finance** sectors

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- **Non-finance** employees experience the **opposite**
- Most consistent with **assortative matching** in labor markets
- Finance sector is **unique** likely because products based on future cash flows