The Internal Labor Markets of Business Groups

Huneeus, Huneeus, Larrain, Larrain, and Prem

Discussion by Liu Yang

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Summary of the Paper

- Research Question
  - How do internal labor markets function in business groups?
- Empirical Strategy
  - Data: Employer-employee matched data from Chile
  - Economic Shocks: Firm level exposure to changes of export/import prices
  - Analysis: Examine how differential trade exposure affects labor mobility of firms within and outside of business groups
- Main Findings
  - There are active ILMs inside business groups
    - Workers flow from firms that receive negative shocks to firms that receive positive shocks
  - The internal reallocation mostly applies to top employees
    - Based on relative rank within the firm rather than the absolute wage distribution
  - Wages increase as employees move within the group

General Comments

- Very interesting paper!
  - Most of existing literature on business groups focus on internal capital markets
  - We know very little about ILMs inside business groups
- Cool data sets
  - Matched employer-employee data spanning the entire private sector of the economy
  - Business groups composed of both listed and private firms
- My discussion
  - The big picture
  - Empirical design and findings
  - Suggestions for future work

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Comment #1:
Business Groups vs. Conglomerates

How do business groups differ from conglomerates?

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One firm
Headquarter and divisions – clear hierarchy and full control
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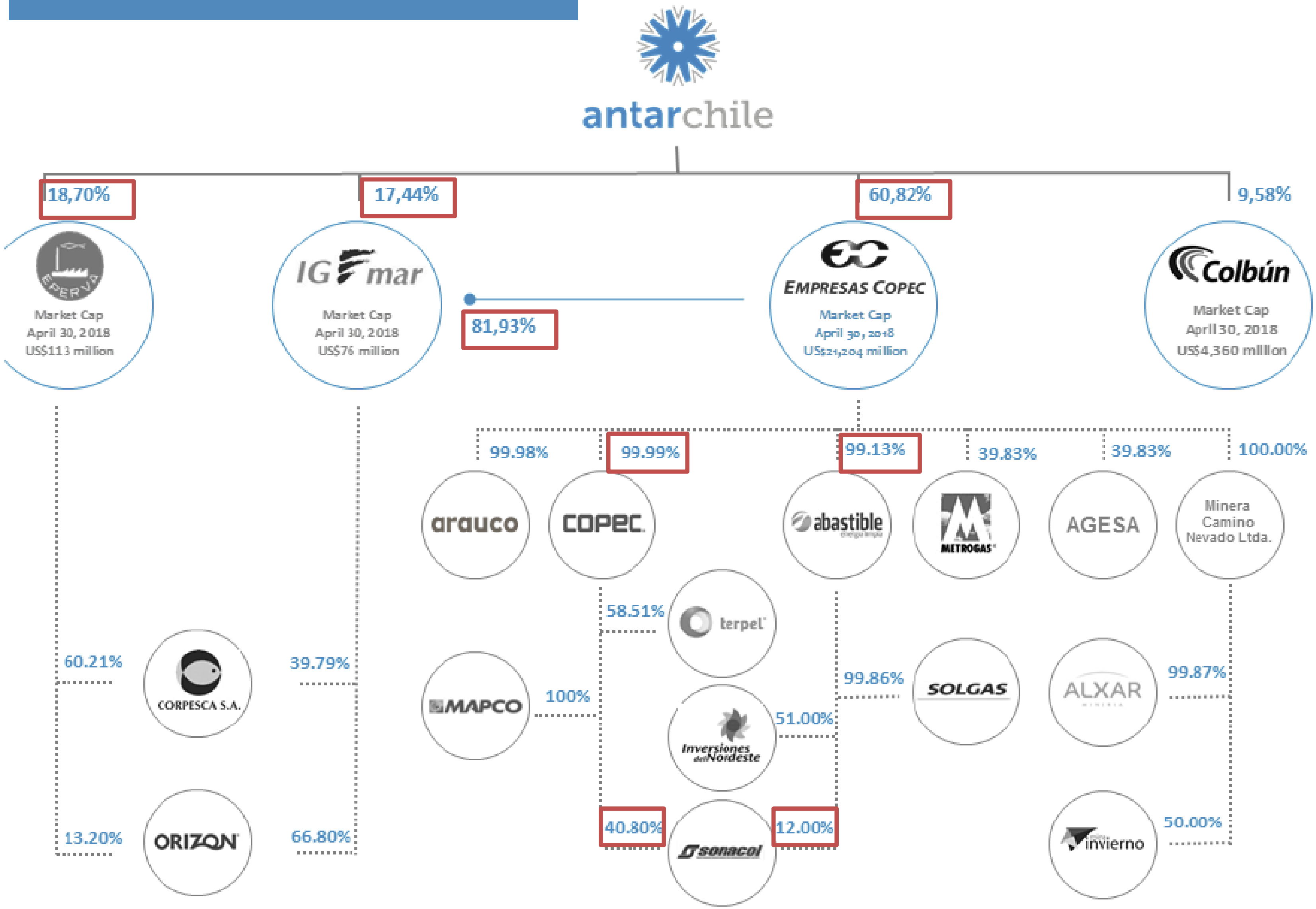
One stock price – common incentives	

PARENT LEVEL INFORMATION



Comment #1:
Business Groups vs. Conglomerates

How do business groups differ from conglomerates?

Conglomerates	Business Groups
One firm	A set of firms connected through a common controlling shareholder
Headquarter and divisions – clear hierarchy and full control	How much control does parent firm have? Across different layers of ownership?
One stock price – common incentives	Different firms with different stock prices

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ILMs in Conglomerates

- ILMs in conglomerate firms (Tate and Yang (2015))
  - Greater labor mobility within conglomerate firms as compared to that in external labor markets
  - Workers are reallocated from low- to high-growth sectors
  - Workers from diversified firms experience higher wage changes when they move to industries operated by previous firms
    - Stronger effect for workers in high-skill industries

ILMs in Business Groups

- Would the ILMs forces be ***weaker*** in business groups as compared to conglomerates?
  - Do firms in the business group share similar culture, corporate strategy, managerial practices etc. (i.e. firm-specific human capital) that creates a wedge between internal and external moves?
  - Can firms within a business group integrate labor forces as easily as divisions within conglomerate firms?
    - To what extent can parent company direct to reallocate employees across firms in the group?
    - Why would one firm be willing to lose its star top employee to other firms within the group?

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ILMs in Business Groups: Cross-Sectional Variation

- The effect would be stronger in business groups
  - with more similar firms (in industry, corporate strategy, culture, managerial practices etc.) that overlap in firm-specific investments
  - with firms that have more significant cross holdings so incentives are more aligned

Comment #2: Trade Shocks and Labor Mobility

- Pair-wise price shocks are defined as the differential exposure to export or import prices between destination and origin firms $(\Delta p^{k}_{dt} - \Delta p^{k}_{ot})$
- Sample: Firms that simultaneously export and import
- **How selective is this sample?**
  - Larger firms?
  - Better quality firms (esp. among exporters)?
  - A certain group of industries?

"Among firms that appear in both the UI and the trade dataset, 73% are only importers, 6% are only exporters and <u>21%</u> do both" (Appendix A.1)

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Comment #2: Trade Shocks and Labor Mobility

- **How to separate general human capital about trade from firm-specific investments?**

- Firms with growth potential in export markets may want to hire executives from other firms with knowledge about exports

- They are more likely to succeed if destination firms face declining demand

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Comment #3: Top Employees and Wage Effect

- **The effect is much stronger for top employees**
  - Top 25, but more significant for Top 10

Table 3: Internal Labor Mobility Test

	All Workers		Bot. 25	Mid. 50	Top 25	Top 20	Top 10
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Δ Exports x Same BG	0.004	0.004*	-0.000	0.008	0.032**	0.027*	0.091***
	(0.002)	(0.002)	(0.002)	(0.005)	(0.013)	(0.014)	(0.029)
Same BG	0.024***	0.022***	0.018***	0.024**	0.044***	0.052**	0.016
	(0.006)	(0.006)	(0.007)	(0.010)	(0.016)	(0.023)	(0.030)

- Who are these employees?
  - Engineers or managers?
  - What are the skills to be transferred? General managerial or firm-specific?

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Comment #3: Top Employees and Wage Effect

- **Wage increase is higher for moves in firms that belong to the same business group → support of transfer of intangible capital**

- Business group firms pay higher wages than non-business group firms on average (size effect?)
  - The proper benchmark should be other similar BG firms. Alternatively, control for size differences between O and D firms

- Are internal moves more likely to be voluntary moves compared to external moves? Promotions?
  - Use moves in conglomerates as benchmark to control for voluntary/involuntary moves?

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Comment #4: The Underlying Mechanism

- Benefits of ILMs in business groups
  - "*Business-groups have an advantage over stand-alone firms because, by virtue of the control rights over multiple firms, they reduce the specificity of the investment. … Simply put, intangibles can be used over many more assets*"

- This is a very similar argument as what we have already know about ILMs in conglomerate firms.

- Can there be other mechanisms?

An Alternative Story: Asymmetric Information

- Firms have more information about employees from other firms in the same business group.
- They are more likely to tap into top employees (managers) from the same group when opportunities rise.
- Simply more information about the employees can generate the same pattern without common firm-specific human capital.
- Business groups offer a way for capable employees to move up the corporate ladder
  - Origin firms pay higher wages then destination firm
  - Effect in mobility is stronger when O has control over D
  - Employees move up in relative rank

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Benefits of ILM in Business Groups

- We know that workers benefit from exposure to knowledge/skills in other sectors in conglomerate firms.
- It would be very cool to show that benefits of ILMs go beyond that in a much looser setting such as business groups – for example, through information asymmetry.
  - Do we see mobility between industry pairs that are often not common in the external labor markets?
  - Are effects robust in industry pairs that have little overlap in knowledge?

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Conclusion

- Very interesting paper!
  - Nice topic, cool datasets, lots interesting empirical patterns
  - Highly recommend it
- My main suggestions
  - Focus on the unique feature of business groups
  - Explore how ILMs function differently between conglomerates and business groups
  - Emphasize on new insights we can learn from examining business groups
- I am looking forward to the next version!

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