

Corporate M&As and labor market concentration: Efficiency gains or power grabs?

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Overview of the Paper

- Part 1: Mergers with a larger increase in labor market concentration have higher abnormal returns
- Part 2: Differentiate between monopsony power story vs labor efficiency story
 - Returns of product market rivals, suppliers, and customers
 - Heterogeneity by labor market mobility and initial level of labor market concentration
 - More IT investments in overlapping labor markets
- Interpretation: merging firms benefit from labor efficiencies rather than monopsony power when there is a greater overlap in labor markets

Labor Market Concentration

- Concentration can be good or bad (Covarrubias, Gutiérrez, and Philippon, 2020)
- Good concentration: more productive firms expand yet competition remains stable or increases. E.g.
 - Technological change leading to increasing returns to scale
 - Increase in the elasticity of substitution
- Bad concentration: increases economic rents, reduces competition and productivity. E.g.
 - Rising barriers to entry
- This paper sheds new light on this question in the context of M&As

Discussion

- Measurement of labor market concentration
- Recent labor economics literature on monopsony and labor market power

Measuring Labor Market Concentration

- The paper defines labor markets at the county-industry (3-digit SIC) level
- Issue 1: there is considerable mobility across industries (and occupations)
 - Arnold (2021): conditional on switching jobs, the probability the job transition is within the same 4-digit industry is 37 percent; the probability the job transition is within the same 3-digit occupation is about 34.9 percent
- Issue 2: increase in labor market concentration is correlated with monopoly power
 - Consistent with many findings: larger increase in monopoly power $\Rightarrow$ higher probability of merger, higher returns, and negative spillovers to product market rivals
 - Find a positive and sig relationship between Δ Labor Market Concentration and deal challenge by FTC/DOJ, but “in practice, no merger has ever been challenged due to reducing competition in the labor market” (Arnold, 2021)
- Suggestion:
 - Control for product market competition
 - Tradable vs. non-tradable industries

Recent Literature on Labor Market Power

- Several recent papers measure labor market concentration accounting for mobility across industries and occupations. For example:
 - Arnold (2021): construct HHI adjusting for flows across industries
 - Schubert et al. (2022): correct for bias in the HHI (arising from failure to consider mobility across occupations) by controlling for the outside-occupation option index
- Most of these papers find a negative effect of labor market concentration on wages
 - Arnold (2021): mergers with a positive Δ Labor Market Concentration on average reduce wages by 2.1%, while mergers with zero Δ Labor Market Concentration do not reduce wages
- The wage effect seems to be big enough to explain a non-negligible part of the abnormal returns
 - 1.3-1.7% difference in abnormal returns between mergers with positive Δ Labor Market Concentration and mergers with zero Δ Labor Market Concentration

Recent Literature on Labor Market Power

- Several other papers take a different approach and estimate the wedge (markdown) between marginal revenue product of labor and wage
 - Hershbein et al. (forthcoming): a worker employed at the average manufacturing plant earns 65 cents on each dollar generated on the margin
 - Berger et al. (2022) and Jarosch et al. (2021) show that labor market concentration increases the wedge
 - Kirov and Traina (2021): the wedge is strongly correlated with ICT investments, and not so much labor market concentration
 - Seegmiller (2021): the wedge is strongly correlated with labor productivity
 - Firms in the top (bottom) quartile of labor productivity pay 62% (94%) of marginal product
- Mergers could lead to more ICT investments and higher productivity and at the same time increase labor market power, which may not be reflected in labor market concentration

Some Further Thoughts

- Wages of (staying) workers usually decline following mergers (Arnold, 2021; Prager and Schmitt, 2021; He and le Maire, 2021), which is hard to explain using labor efficiency story alone
- Both stories (labor market power and efficiency) may be present, and some channels (ICT investments) may drive both
- Why not look at the labor productivity (and output) of the combined firm?
- Would be useful to quantify the merger gains from labor market power (markdown of wages below the marginal product of labor) and labor efficiency (increase in marginal product of labor)

Conclusion

- Very ambitious paper looking at an important question
- Comments:
 - Refine the measure of labor market concentration and rule out product market power
 - Look at productivity and provide more evidence on labor market power (or lack thereof)

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