Internationalization, business performance and employment

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Summary

Public opinion often associates the internationalization of companies with relocations, factory closures, more intense foreign competition, and more generally, the destruction of the French industrial fabric. An analysis of the most recent studies reveals that the reality is more mixed. On the one hand, companies' first internationalization has a positive impact on their turnover, innovation and employment levels in France, and thus contributes to the development of industrial activity in the country. On the other hand, it mainly benefits high-skilled workers (design, support functions) and brings about the destruction of low-skilled jobs.

Globalization cannot take all the blame for deindustrialization

The decreasing share of the manufacturing sector in France's GDP is not just due to globalization: it also comes from several natural evolutions in developed economies. When manufacturers outsource some service activities (e.g. cleaning, catering, support functions for production plants), the corresponding jobs statistically move to the service sector while there is no effective change on site. In addition, productivity gains in the manufacturing sector have the effect of reducing its need for labour. Although these efficiency gains also lower relative prices of manufactured products, and thus increase the demand for these goods, the latter effect does not compensate the initial effect of reduction in labour requirements. Lastly, as income rises, there is a shift in consumption from goods to services. All of these phenomena, which occur in all developed economies, owe nothing to globalization.

The main motivation for locating abroad is to win new markets

For multinational companies, accessing a growth market is the main deciding factor when choosing a location, over and above optimizing production costs or tax levels. 87% of French multinational business leaders say that the main motivation of their foreign location is to access high-growth markets. Only 10% of them are considerably motivated by manufacturing goods abroad to import back to France.

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[3] Most of this memorandum was written as part of my doctoral thesis at Paris-Dauphine University, which centres on French companies setting up abroad and the impact this has on production, employment and innovation in France. My research was carried out under a CIFRE contract (government-issued grant for student-university-company joint research) at the firm Pramex International (BPCE group). Contact: alexandre.gazaniol1@gmail.com

Investing abroad creates value in France

Empirical studies reveal that internationalized companies are bigger, more productive and pay higher wages than other companies, regardless of the country, sector or economic climate. The question is whether this good performance is the consequence of, or the reason behind, their decision to go multinational. In reality, the causality is two-fold. Setting up abroad requires a critical size, innovative products, skilled workers and a solid financial structure, which creates a natural selection of the most productive firms on foreign markets. However, firms investing abroad for the first time consolidate their initial advantage ex-post: during the three years following their investment, their parent company in France enjoys faster growth of sales, value added, employment and exports than companies that decided to remain domestic. There is also a positive effect on their innovation activities.

Table: Impact of the first investment abroad on the performance of the parent company in France after three years

Turnover	Value added	Employment
+8.03%	+9.30%	+6.57%

Scope: Manufacturers with more than 20 employees, 1996 - 2007
Source: EAE Industrie, LiFi – computed by Gazaniol & Peltrault (2010)

We can explain this positive impact, mainly concentrated on the subsidiaries of French groups, by an income effect: investing abroad accelerates the penetration of foreign markets and induces spillovers to the parent company in France (access to new markets, supply of the subsidiary abroad, creation of support functions).

The global-scale fragmentation of the production process generates productivity gains and boosts company exports

In order to appreciate the impact that the fragmentation of the production process has on productivity and exports, we need to look at the consequences of trading intermediate goods. The rise in imports of intermediate goods can increase companies' productivity thanks to three mechanisms: i) increased competition between producers brings down the price of these goods, ii) access to more varieties of intermediate goods increases the probability of finding one input that perfectly matches the firm's needs for its production process, and iii) the possibility of relocating some segments of the value chain enables the company to increase its efficiency.

For example, in France, all things being equal, manufacturers that double the number of varieties of imported intermediate goods increase their productivity by 4%. This effect goes up by 60% when imports come from developed countries, which suggests that the efficiency gains resulting from imports are mainly linked to technology transfers. As a result of its effect on productivity, the rise in imports thus allows French companies to increase their exports.

However, globalization hits some labour pools, trades and industries hard

Although relocations represent a small fraction of lost industrial jobs (i.e. 1 out of 300), they can severely affect low-skilled workers and some very specialized labour pools. On a microeconomic level, the impacts of relocation are thus more visible and significant. Unsurprisingly, labour-intensive industries, such as clothing, household equipment and electronic components, are more likely to relocate their activities towards low-wage countries. Large business groups are the main drivers of relocations: companies with more than 500 employees together represent two-thirds of offshored jobs.

Low-skilled workers are more vulnerable to the internationalization of their company

As offshoring increases, labour demand in the home country shifts from low-skilled to high-skilled workers within each industry. Multinational groups tend to gradually redirect the activities of the parent company towards support functions and R&D. Thus, the share of managers and engineers in their domestic workforce increases with their degree of internationalization. The most recent empirical studies, which use linked employer-employee data, tend to show that low-skilled workers are more keenly hit by relocations, both in terms of jobs and wages. This observation represents a challenge for public policies on employment, training and, more generally, territorial management of jobs and skills.

In conclusion

Dissuading companies from turning to foreign production would be counterproductive for their competitiveness and for industrial employment. However, relocations contribute to widening inequalities between high-skilled and low-skilled workers within each industry, both in terms of job security and remuneration. The keys to reducing these negative effects lie in training measures and seeking to improve the way the job market works.