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THE EFFECT OF EMPLOYMENT PROTECTION LEGISLATION ON THE INTERNATIONALIZATION OF SMALL FIRMS

Abstract:

A broad economic literature has evaluated the impact of employment protection legislation (EPL) on various firm-level outcomes. We complement this literature by studying the effect of a reduction in employment protection on the internationalization of small firms. Exploiting a comprehensive survey on Italian firms, we assess how small firms' engagement in complex international activities (e.g., FDI and offshoring) has been affected by the 2012 Labor Market Reform, the so-called "Fornero Law", that reduced firing costs for firms above the 15-employee threshold. Using a difference-in-differences identification strategy, we find a positive effect of EPL retrenchment on small firms' complex international activities. We document minor heterogeneous effects by geographic areas but no heterogeneity across different sectors of economic activity. Finally, the positive effect on internationalization is greater in firms with a higher level of volatility.

Keywords:

EPL, internationalization, FDI, small firms, labor market reform, difference-in-differences

JEL Classification: J08, F16, J63