

# Corporate Employee-Engagement and Merger Outcomes\*

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## Abstract

Extending the theories of employee incentives and inalienability of human capital, we investigate the link between a firm's engagement in employee relations and the returns to shareholders around mergers and acquisitions (M&As). Using firm-level data on employee-engagement in an international sample of 4,565 M&A deals from 48 countries, we find that an acquirer's employee-engagement – especially in terms of monetary incentives – is positively related to shareholder returns in domestic deals, but this relationship turns negative in cross-border deals. Workforce diversity, training and development, and health and safety do not affect shareholder returns around M&As. Consistent with the notion of the inalienability of human capital and employment policies, we find that the attenuating effect in cross-border deals is stronger when uncertainty about post-merger labor integration and transferability of employment policies across firms and countries is higher. These results hold after controlling for country-level differences in labor regulations and that most effects of employee-engagement on shareholder returns are driven by the acquirer rather than the target. Moreover, they persist in terms of long-run post-merger profitability.

Keywords: employee-engagement, labor protection, monetary incentives, mergers and acquisitions (M&As)

JEL Classifications: G34, M14, J24

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\* We are grateful to Renee Admans, Gennaro Bernile, Ekkehart Boehmer, Fabio Braggion, Simba Chang, Frank de Jong, François Derrien, Joost Driessen, Allen Ferrell, Thierry Foucault, Fangjian Fu, Nicolae Garleanu, Denis Gromb, E. Kim Han, Jarrad Harford, Jianfeng Hu, Sheng Huang, Paul Hsu, Thomas Lambert, Augustin Landier, Roger Loh, Xiaoji Lin, Paul Malatesta, Alberto Manconi, Pedro Matos, Lilian Ng, Paige Ouimet, Paolo Pasquariello, Shyaam Prasad, Thomas Schmid, Oliver Spalt, Matthew Spiegel, Sheridan Titman, Jeroen Vinders, and seminar and conference participants at Singapore Management University, University of Hong Kong, SMU Finance Summer Camp, Tilburg University, the 14<sup>th</sup> Corporate Finance Day (University of Antwerp), HEC Paris PhD Workshop, 2017 Global Corporate Governance Colloquia (Tokyo), and the 4th Indonesian Financial Management Association Conference for insightful discussions and comments.

# Corporate Employee-Engagement and Merger Outcomes

## I. Introduction

Corporations represent a nexus of implicit and explicit contracts between shareholders and stakeholders (Coase, 1937; Fama and Jensen, 1983; Shleifer and Summers, 1988). An important stakeholder group that is crucial to firms' operations and performance consists of employees, representing a firm's human capital. Employees are involved in the firm's daily operations and have a contractual claim on the company in the form of salaries and bonuses. Moreover, they can directly and indirectly influence corporate decision making and governance through workers' and unions' rights to appoint members to the board of directors (Gorton and Schmid, 2004), work councils, employees' ownership of company shares via participation in employee stock ownership plans, retirement accounts and personal accounts (Kim, 2009), or through collective actions such as strikes and political lobbying. That labor's bargaining power affects corporate decision making, corporate governance, and hence firm value has been established both theoretically and empirically in recent studies (e.g., Pagano and Volpin, 2005; Cronqvist, Heyman, Nilsson, Svaleryd, and Vlachos, 2009; Atanassov and Kim, 2009; Bae, Kang, and Wang, 2011).

However, the extant literature offers mixed evidence on the direction and mechanisms through which firms' employee-engagement—policies and practices that aim to provide better welfare (e.g., higher compensation and job security, more training and career advancement, the improvement of workforce health and safety, enhancement of workforce diversity) for employees—affects firm value. Some find a negative relation between shareholder value and labor orientation, explaining this relation by (too strong a) legal protection of workers (e.g., Gorton and Schmid, 2004; Dessaint, Golubov, and Volpin, 2016; Levine, Lin, and Shen, 2015) and manager-employee alliances (Pagano and Volpin, 2005; Cronqvist et al., 2009;

Masulis, Wang, and Xie, 2016). This line of research argues that labor’s interests do not always align with those of shareholders and that strong labor protection regulations constitute a cost to the firm. Others find a positive relation, especially with regard to employee satisfaction (Edmans, 2011, 2012; Edmans, Li, and Zhang, 2015). Here, the common argument is that a satisfied workforce increases labor productivity and thus firm value.

In this paper we revisit this important issue, aiming to reconcile the conflicting findings in the extant literature and offer a more comprehensive evaluation on the role of labor orientation in corporate governance by focusing on a key issue in corporate finance, namely the inalienability of human capital (Fama and Jensen, 1983; Hart and Moore, 1994; Almazan, De Motta, and Titman, 2007; Bolton, Wang, and Yang, 2015). “Inalienability” stands for the fact that, in important contracting and transactional situations such as an acquisition, a buyer of a firm cannot change the human capital employed at a target company without frictions nor can it change the contracts that a target firm has voluntarily—in the sense of going beyond incumbent regulation—adopted.<sup>1</sup> In addition, the target’s employees may also be less receptive to the labor policies implemented by the acquiring firm. Furthermore, whereas both human capital and explicit contracts are inalienable, it may also be difficult and even counter-productive if the acquirer were to break implicit contracts between the target’s employees and their management. Implicit contracts may depend on culture and norms, the social climate (driven by major social partners such as unions and employers), labor regulation, the importance of corporate social responsibility, etc. Consequently, a transfer of the acquirer’s employment policy to the target may not be straightforward nor, even if this were possible, would it be expected to have the same impact as in the acquirer (Tate and Yang, 2016). We refer to this friction in

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<sup>1</sup> For example, a sale of a firm triggers the “transfer of undertakings protection of employment” (TUPE) regulations of 1981, which stems from the European Acquired Rights directive. This regulation states that “all the [seller’s] rights, powers, duties and liabilities under or in connection with [an employee’s contract of employment], shall be transferred to the [buyer].” Furthermore, the buyer assumes the liability for “anything done before the transfer is completed by or in relation to the [seller] in respect of that contract or a person employed in that undertaking or part” (Calcagno and Renneboog, 2007). TUPE states that such an act “shall be deemed to have been done by or in relation to the [buyer].”

transferring employee-related policies as “the inalienability of employment policies”, stemming from the inalienability of employees’ human capital. In addition, we argue that frictions due to such inalienability may be less severe in a domestic takeover transaction because employees within a country may share similar values, cultures, and expectations which reduce the uncertainty about whether the labor policy of the acquirer will be successful after the merger.

We first contrast several major theories on labor in corporate finance. Human relations theories (e.g., Maslow, 1943; Herzberg, Mausner, and Snyderman, 1959; McGregor, 1960) take a positive view on labor, arguing that labor is a key organizational asset and that stronger employee incentives increase productivity. The incentive effect of a firm’s orientation towards labor can thus create substantial value for shareholders (Edmans, 2011; Edmans et al., 2015). Agency-based theories take a negative view, and argue that the employees’ objective function does not necessarily align with shareholder’s interests. Protecting employees’ interests increases the costs of their removal and can result in labor entrenchment, reducing operating efficiencies. Moreover, managers can protect themselves from being removed by hostile raiders through allying with labor and providing stronger employment protection, usually at the cost of shareholders (Pagano and Volpin, 2005; Cronqvist et al., 2009). In this context, a firm’s focus on its relations with employees is thus a deviation from value maximization. We take a third (and probably a more equilibrated and mixed) view, which hinges on the inalienability of human capital and employment policies. We argue that the benefits and costs of corporate employee-engagement depend on the extent to which human capital and employment policies are transferable across firms, which implies that the ultimate effect depends on their relative strength and the contracting environment. A firm’s engagement in, for example, employment and wage insurance may function as an incentive tool to increase labor productivity and firm value when there are few uncertainties concerning the firm’s contracting environment. However, such engagement could also turn into a burden for the firm by exposing it to greater uncertainties with regard to the implementation of its employment policies, thus reducing firm value.

We organize our analysis around a particular type of corporate event in a firm's lifecycle, namely mergers and acquisitions (M&As), which provide an ideal setting to study the inalienability of human capital and the transferability of a firm's employment policies to another firm, as they force firms to restructure their workforce and reallocate assets across firms. In a neoclassical framework, M&As are regarded as a means to enhance firms' capabilities and resources (good M&As) or reflect managerial empire building behavior and other agency problems resulting in value-destruction (bad M&As) (Ahern and Weston, 2007). During this process, a firm's commitment to explicit and implicit contracts with key stakeholders such as employees plays an important role in the wealth gains and losses of an acquirer's shareholders (Shleifer and Summers, 1988; Rhodes-Kropf and Robinson, 2008; Masulis et al., 2016). In addition, labor reallocation both within and across industries and countries is a crucial factor in post-merger corporate restructuring (Dessaint et al., 2016). The global scope of the M&A market enables us to compare the role of a firm's employee-engagement in driving shareholder value in a domestic setting and in a contractually and operationally more complex cross-border setting. This way, we can shed some light on how the contracting and operating environment interacts with the inalienability of human capital and employment policies in affecting employee-shareholder relations and ultimately firm value.

Analyzing a sample of 2,009 acquiring firms from 48 countries engaging in 4,565 M&A deals, we find that there is considerable cross-firm and cross-country variation in *firm-level* employee-engagement that is priced by the market around corporate takeover events. The effects of employee-engagement—especially in terms of monetary compensation and job security, but not in terms of training, diversity, and health and safety—on acquirers' announcement returns are significantly positive for firms conducting domestic deals, but they are significantly attenuated in cross-border deals. This finding holds even after controlling for differences in country-level labor regulations and other macroeconomic factors. The attenuating effect of acquiring a foreign target does not stem from the fact that cross-border deals on average destroy value as these deals have higher announcement returns than domestic acquisitions, but rather appears to be specific

to a firm's relation with its employees (the inalienability of human capital and employment policies, as we argue). These results reconcile the conflicting findings in the literature on the association between labor relations and announcement returns (Deng et al., 2013; Dessaint et al., 2016; Levine et al., 2015). We further investigate several mechanisms related to employee incentives and inalienability of employment policies that may account for the difference in the effect of employee-engagement on shareholder returns around domestic and cross-border M&A deals. In particular, we find that stronger "motivational factors" such as more pecuniary incentives and better monetary compensation are associated with higher acquirer announcement returns in domestic deals and lower returns in cross-border deals, but that this is not the case for "job security factors" such as employment retention and trade union relations. In addition, the negative employee-return relation in cross-border deals is stronger when uncertainty with regard to post-merger labor integration is higher and when economic nationalism in the target country is stronger. We also find that most effects of employee-engagement come from acquirers rather than targets, and we address potential endogeneity concerns using an Instrumental Variable (IV) approach. We rule out several alternative explanations based on country-level labor regulations, cultures, common language, degree of economic development, and the potential backfiring effect of over-engaging in employees. Overall, our results suggest that part of the value composition in M&As comes from increasing productivity that is not purely operational but partially stems from a firm's human capital, although the increase can be offset by the inherent inalienability of human capital and employment policies in cross-border acquisitions.

While some recent studies look at labor relations in the context of corporate restructuring and takeovers (Atanassov and Kim, 2009; Masulis et al., 2016; John, Knyazeva, and Knyazava, 2015; Dessaint et al., 2016; Levine et al., 2015; Kim et al., 2015; Lin, Schmid, and Xuan, 2017; Ahmad and Lambert, 2016), most research exclusively focuses on employment protection and labor regulations at the country level, investigating, for example, the level and rigidity of unionization and regulated labor representations, rather than the firm's voluntary initiatives. Our study focuses on the firm's voluntary engagement in its relations

with employees and dissects corporate employee orientation into its different dimensions, capturing both employee incentives and employment protection. We also compare the differential roles of labor in domestic and cross-border takeover deals, and investigate how employee-engagement interacts with the institutional environment. To our knowledge, we are among the first to provide global firm-level evidence on the role of employees in shaping corporate governance and firm value. In this regard, our study is also related to the emerging literature on the role of human capital in determining the boundaries of the firm and corporate policies (e.g., Bae et al., 2011; Hart and Moore, 1994; Bolton et al., 2015; Tate and Yang, 2016).

The remainder of the paper proceeds as follows. Section II reviews the literature on labor in corporate governance and M&As. Section III describes our data and methods, while Section IV presents the empirical results. Section V concludes.

## **II. Corporate Employee-Engagement, Inalienability of Human Capital, and Takeovers**

Employees are arguably the most important stakeholders in modern corporations. They provide skills and human capital that contribute to the company's core businesses and strengthen its competitiveness (Zingales, 2000; Schnepfer and Guillén, 2004; Pfeffer, 1998; Kang and Kim, 2015), but they also have claims on a significant share of the company's profits. Traditional studies have identified two major mechanisms through which employees matter for firm value. On the one hand, the employee incentive view suggests that properly incentivizing employees can lead to increased productivity which translates into higher profitability (March and Simon, 1958; Edmans, 2011). In addition, employee representation on the corporate board can also transfer valuable operational knowledge to the decision-making process, improving the efficiency of board decisions (Fauver and Fuerst, 2006). This view is closely related to the notion of implicit contracting with employees. That is, a firm's engagement in establishing close labor relations can reflect its commitment to strong implicit contracts with employees (Shleifer and Summers, 1988). In the context of acquisitions, this decreases the likelihood of encountering difficulties when renegotiating employee contracts (Ahmad and

Lambert, 2016), restructuring the workforce, and attracting talented and motivated employees, lowering the transaction costs related to these contracts, and increasing labor productivity, all of which can lead to increased firm value. In addition, a (perceived) breach of trust by renegeing on an implicit or explicit contract or commitment may negatively affect employees' performance (Robinson, 1996). From this employee incentives perspective, shareholders' and employees' interests are aligned: satisfied employees are more loyal and productive and hence create more shareholder value, an effect that should be especially strong during a firm's restructuring and expansion.

On the other hand, the labor entrenchment view argues that employees and shareholders usually have conflicting interests, and a firm's over-engagement in its employees may result in their entrenchment, constituting a cost for shareholders (Atanassov & Kim, 2009). In addition, management may ally with employees by providing generous employment benefits (for example in the form of employee stock ownership plans) in order to extract private benefits and fend off disciplinary takeover threats (Pagano and Volpin, 2005; Cronqvist et al., 2009). Under this more negative view, a firm's engagement in employee relations may come as a significant cost for shareholders and lead to management-labor collusion, reducing returns to shareholders and increasing the likelihood of value-destroying M&As (Masulis et al., 2016).

Some recent work also explores the risk and insurance aspects of employee relations, suggesting that labor incentives such as minimum wage and employment insurance provide a risk-sharing mechanism for employees within firms (Guiso, Pistaferri, and Schivardi, 2005; Belo, Lin, and Bazdresch, 2014; Ellul, Pagano, and Schivardi, 2014; Kim, Maug, and Schneider, 2015; Favilukis and Lin, 2016). This mechanism however depends on the extent to which the firm commits to honor its promises to insure employees against adverse shocks and on employees' valuation of such insurance (Ellul et al., 2014).

In this paper, we provide an alternative view on the role of employees based on the inalienability of human capital and employment policies for rank-and-file workers, which could reconcile the conflicting

findings in the extant literature. In general, strong employee-engagement serves as a signal to shareholders about the firm's reputation for committing and honoring implicit contracts with its labor force: it signals that the firm is unlikely to break such contracts in case of an event that pressurizes relations with employees, of which an M&A deal is a prime example. This increases labor's productivity and commitment to the firm, leads to higher firm value, and is consistent with the employee incentive view. However, the inalienability of human capital and employment policies can also reduce the productivity gains from incentivizing employees, and the net effect depends on uncertainties in the contracting and operational environment. For example, renegotiating contracts with employees becomes more complicated and costly when a firm conducts acquisitions which entail a reallocation of its workforce in more uncertain environments. Managers also tend to "over-engage" in employees during an aggressive expansion period so as to achieve greater economies of scale, usually resulting in clashes between organizational cultures between merging firms (Aguilera, Dencker, and Yalabik, 2008). Moreover, a corporate policy of strong employee-engagement under the uncertainty induced by an acquisition can lead to concerns by the acquiring firm's employees about partial transfers of their benefits to target employees, which could thus temper the morale of the employees of the acquirer. Consequently, conflicts of interest between shareholders and employees could also arise due to inability to adapt employment contracts and policies to changing market conditions, which then ultimately reduces the value accruing to shareholders. Recent empirical evidence indeed suggests that more rigid labor contracts resulting from stricter labor protection laws limit the extent to which firms can eliminate redundancies in the workforce and achieve the targeted economies of scale (John et al., 2015; Levine et al., 2015; Dessaint et al., 2016).

A natural classification of takeover transactions in terms of the degree of uncertainty about how easily human capital and employment policies of the two firms can be integrated is whether the deal is conducted domestically or across national borders. In particular, cross-border M&A deals are often associated with greater complexity in dealing with employee issues put up by frictions related to national boundaries. These

frictions comprise difficulties in (re)negotiating employee contracts and compensation with the target's employees, in navigating through the culturally and regulatory diverse employment environments, and in transplanting a specific employment policy to other parts of the combined organization. For instance, employees and shareholders in the acquiring firm, while enjoying the benefits of greater economies of scale achieved through a cross-border acquisition, may also be concerned that the same (or a greater) level of employee-engagement in the target constitutes higher costs due to difficulties of integrating their workforce and employment policies. We argue that frictions stemming from the inalienability of human capital of rank-and-file workers can potentially attenuate the positive effect of incentivizing employees on firm value, and this can turn strong employee-engagement into a burden for the firm. Which specific employee-related factors are more dominant in the above described relations is subject to our empirical investigation.

In the next section, we empirically test these predictions and mechanisms on a large international sample of M&A deals.

### **III. Data and Methodology**

#### *III.1. Data*

We measure a firm's employee-engagement using data from Thomson Reuters' ASSET4 database. This firm-level database provides information and ratings on firms' practice on social, corporate governance, economic, and environmental issues ("pillars") and covers more than 4,000 companies worldwide since 2002. Our main focus is on the variables related to the firm's workforce under the "social" pillar, which describe the firms' commitment and effectiveness with regard to the provision of (i) employment quality in terms of high-quality employment benefits and job security (*Employment Quality*), (ii) a healthy and safe workplace (*Health & Safety*), (iii) on-the-job training and development for employees (*Training & Development*), and (iv) equal opportunities within its workforce (*Workforce Diversity*). Each of these employee-related dimensions is an equally-weighted average of a set of underlying elements (sub-dimensional factors). For

example, *Employment Quality* consists of measures of the firm's salary level, wage distribution, trade union relations, bonus plans, fringe benefits, employment awards, employment creation, personnel turnover, layoffs, management departures, strikes, job security policies, and employment controversies in the media. This way we can test the importance of the above four employee-related dimensions but also go one level deeper within each sub-dimension and test the monetary incentive effects as well as employee insurance effects (such as job security) on shareholder returns around M&A announcements.

The four employee-engagement measures as well as their respective sub-dimensional scores are normalized by ASSET4 such that each firm is given a z-score relative to the performance of all firms in the same industry. The normalization to a scale of 100 implies that, by construction, firms with scores higher than 50 perform above the median in terms of employee-engagement. These measures enable us to assess a firm's orientation towards employee issues relative to the industry benchmark, and provide us with a natural yardstick to gauge whether the firm excessively engages in employee relations. This way, we can compare corporate employee-engagement across firms with similar demand for labor skills and operating in similar labor markets, and also disentangle explanations based on over-engagement versus inalienability of employment policies.

We obtain data on M&A deals from the SDC Mergers and Acquisitions database. In order to be included in our sample, the transactions should meet the following criteria: (1) the deal was announced between January 1<sup>st</sup>, 2002 and December 31<sup>st</sup>, 2014 and the SDC database contains detailed information on this transaction;<sup>2</sup> (2) the acquiring firm is publicly listed and its accounting and stock return data are available in Datastream; (3) the acquiring firm owns less than 50% of the target's shares before the offer and makes an offer with the intention to own more than 50% of the target's shares subsequent to a successful acquisition; (4) the acquiring firm has data available in ASSET4 for the fiscal year before the deal

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<sup>2</sup> It is not meaningful to include the deals announced before 2002 as the ASSET4 coverage starts in 2002.

announcement; and (5) labor protection data for both the acquirer's and target's countries are available in the Botero et al. (2004) labor regulation indices.

Merging the information from ASSET4 with our sample of M&A deals from SDC results in a final sample of 4,565 deals by 2,009 acquiring firms from 48 countries. Of these deals, 2,550 (56%) are domestic and 2,015 (44%) are cross-border. The descriptions of our key variables are given in Appendix A. Appendix B shows the sample distribution by acquirer industry and year. The acquiring firms in our sample are mostly active in Business Services (10%), Trading (8%), and Banking (7%) industries<sup>3</sup>. Appendix C shows the sample distribution by acquirer country. Acquiring firms originate mainly from the US (27%), Japan (15%), and the UK (13%). In addition, Appendices D1 and D2 respectively offer an overview of our employee-engagement scores by country and industry.

### *III.2. Empirical Strategy*

To assess shareholders' reactions to M&A announcements and thus draw inferences on shareholder value, we calculate cumulative abnormal stock returns (CARs) for the acquiring firm in the three days surrounding the deal announcement [-1,+1], where abnormal returns are defined as the difference between the firm's actual and expected returns. These expected returns are obtained from the market model estimated over a period starting 100 days before the announcement date until 30 days before this date:  $R_{it} = \alpha_i + \beta_i * R_{mt} + \varepsilon_{it}$ , where  $R_{it}$  is the actual return for firm  $i$  on day  $t$ , and  $R_{mt}$  is the return on the primary stock market of the country in which the firm's headquarter is located. The estimated coefficients enable us to calculate the returns expected for the case without a takeover offer. We then calculate the CARs by summing the abnormal returns in the three days around the announcement date. We necessarily focus on the acquiring firms' CARs because studying the combined CARs of both acquirers and targets makes us lose more than 80% of our sample (as the number of public target firms in our sample is limited).

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<sup>3</sup> To keep a sufficiently large number of observations, we do not exclude the financials and utilities industries. However, our conclusions remain unaffected after excluding these from the sample (results are available on request).

Similarly, we confine our analysis to the acquiring firms' employee relations, as the availability of data for firm-level employee-engagement and stock information for target firms is also very limited (less than 10% of the sample). Our core specification is:

$$\begin{aligned} \text{Acquirer CAR } [-1, +1]_i \\ = \alpha_i + \beta_1 \text{Employee Engagement}_{j,t-1} + \beta_2' X_{ij} + \beta_3' \text{Lab. Reg. Index}_c + \beta_4' \gamma + \varepsilon_i \end{aligned}$$

where  $\text{Employee Engagement}_{j,t-1}$  measures the acquiring firm's engagement in employee-related issues (including *Employment Quality*, *Health & Safety*, *Workforce Diversity*, and *Training & Development*) for the fiscal year prior to the deal announcement, and  $X_{ij}$  indicates a set of standard deal- and firm-level control variables including acquirer ROA, acquirer leverage, acquirer size, a serial acquirer dummy, relative deal size, and dummies for toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets.  $\text{Lab. Reg. Index}_c$  is a set of four (target and/or acquirer) country-level labor regulation indices from Botero et al. (2004), which have been widely used in studies on the role of labor protection in corporate investment (e.g. Atanassov and Kim, 2009; Levine et al., 2015). These indices consist of (1) an employment laws index, which measures the protection of labor and employment contracts; (2) a collective relations laws index, which measures the statutory protection and power of labor unions as well as protection of workers during collective disputes; (3) a social security laws index, which measures social security benefits related to old age, disability, death, sickness, and unemployment; and (4) a civil rights index, which captures the degree of statutory protection of vulnerable groups against employment discrimination. As our goal is to examine the role of firm-level employee-engagement, it is important to control for these country-level labor regulation variables so as to disentangle the firm-level effects of (voluntary) labor-orientation from the effects resulting from country-level (mandatory) labor protection regulations. Finally,  $\gamma$  is a set of year, acquirer- and target-industry fixed effects that we include to further reduce concerns related to a potential omitted variable bias in the relationship between corporate employee-engagement and stock returns around M&A announcements.

In addition, we explore the potential mechanisms that account for the differential relations between employee-engagement and shareholder returns in domestic and cross-border deals by considering a set of sub-dimensional factors of our main employee-engagement scores (e.g. monetary incentives such as bonus plans, fringe benefits, the wage ratio of employees/CEO, trade union relations policies, employment growth/loss, job security policies, etc.). We also interact these employee-engagement measures with country- and firm-level variables that capture uncertainty in the integration of human capital and the consistency of employment policies across firms. Definitions of all variables are available in Appendix A.

## **IV. Results**

### **IV.1. Descriptive Statistics**

Panel A in Table 1 reports descriptive statistics for our main measures of firm-level employee-engagement for the acquiring firms in domestic and cross-border deals, respectively. Our main explanatory variables on firm-level employee-engagement are *Workforce Diversity*, *Employment Quality*, *Health and Safety*, and *Training and Development*, which are measured in terms of industry-adjusted normalized scores (ranging from 0 to 100) and indicate a firm's engagement relative to its industry peers. In domestic deals, these employment policy variables are close to the sample mean (of 50), whereas in cross-border deals, they are significantly higher than the sample mean and median. Each of these employee policy scores are statistically significantly higher (8 to 13 points on a scale of 100) for firms engaging in cross-border deals relative to those involved in domestic transactions (Table 1, Panel A). The other variables shown in Panel A represent a set of sub-dimensional factors used to construct the *Employment Quality* score (see Appendix A for variable descriptions); in domestic deals, an average of 39% of the acquiring firms offer a bonus plan to their employees, 43% provide fringe benefits such as pension funds or health insurance, the average acquirer increased its workforce by 3.5% in the year prior to the acquisition, 18% of the acquiring firms has a policy in place for maintaining good relations with trade unions, and 6% of firms have policy to enhance job

security. In contrast, acquirers engaging in cross-border deals are more likely to offer a bonus plan to their employees (48%), are more likely to have a policy for maintaining good relations with trade unions (32%), and are more likely to have a job security policy in place (11%). Overall, these results suggest that firms conducting cross-border acquisitions are different from those conducting domestic acquisitions in terms of their relations with employees, and also appear to have above-average employee-engagement.

Panel B reports descriptive statistics for deal-level characteristics, starting with the acquirer's CARs over the window [-1, 1]. Consistent with findings in the literature, acquirer shareholders in domestic deals do not gain from M&A deals: the mean and median CARs are -25 and -22 basis points, respectively. About 41% of our sample consists of cross-border deals, and in these deals acquirer shareholders earn positive mean and median returns of 16 and 3 basis points, respectively. Although shareholders of acquirers conducting cross-border deals earn more positive returns on average, the median return is close to zero. Cross-border acquirers are less likely to acquire public targets, make all-cash offers, and acquire toehold stakes. Cross-border deal values are comparable to domestic deal values (16% of the acquirer's market capitalization in cross-border deals and 17% in domestic deals). The firm-level variables in Panel C show that firms acquiring domestically are comparable to firms acquiring cross-border targets in terms of leverage and profitability (as, although the difference in means is statistically significant, it is economically small), but are smaller in size and are less likely to be serial acquirers<sup>4</sup>. Panels D and E compare the acquirer's and target's country-level labor protection indices: acquiring firms in domestic deals tend to be located in countries with slightly lower protection in terms of employment, collective relations, and social security, but with stronger civil rights than acquiring firms in cross-border deals. Also, targets in cross-border deals have a higher employment laws index than acquirers in domestic deals.

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<sup>4</sup> A serial acquiring firm is defined as a firm engaging in more than 10 takeover deals across our sample period. Alternatively, when we define serial acquirers as firms engaging in more than two takeover deals per year, our conclusions are not affected. A relatively large number of deals— they make up 25% of our sample – involve serial acquiring firms.

[ Insert Table 1 about here ]

We can derive some interesting insights from our descriptive statistics: compared to acquirers in domestic deals, those engaging in cross-border deals have on average more generous employment policies at the firm-level, and their deals also earn higher announcement returns compared to domestic acquirers. However, they also differ on a number of deal-, firm-, and country-level characteristics. It is thus not clear whether the higher announcement returns in cross-border deals are causally related to stronger employee-engagement, which as we will show below, is in fact not likely the case.

We also show similar descriptive statistics for target firms, but only for the small subsample for which employee-engagement data are available, as ASSET4 mostly covers large firms included in the major global equity indices. Again, target firms' employee-engagement scores are higher for cross-border deals than for domestic deals. Consistent with the M&A literature, target firms also enjoy positive announcement CARs, which are higher for cross-border deals. Targets are smaller in size compared to acquirers, but they are more profitable. The relative deal size is much larger in this small subsample compared to the full sample in Table 1, which is of course due to ASSET4 only covering large publicly-listed firms. Overall, the descriptive statistics in Tables 1 and 2 indicate that there are substantial differences in employee-engagement and firm characteristics between acquirers and targets, and between domestic deals and cross-border deals.

[ Insert Table 2 about here ]

#### **IV.2. Employee-Engagement and Shareholder Returns in Domestic and Cross-Border Takeovers**

We now formally test the relations between firm-level employee-engagement and acquirer returns. As we argue above, a firm's engagement towards its employees' welfare can increase employee productivity and support, leading to higher shareholder value, partially reflected in higher stock returns at the firm's acquisition announcement. However, such a positive incentive effect can be attenuated if the acquisition takes place across national borders, due to the inalienability of human capital and the resulting uncertainties

regarding the transfer of employment policies. We test this hypothesis in Table 3, where we interact a cross-border deal dummy with the firm's employee-engagement scores, while including the firm- and deal-level controls specified in Section II (acquirer ROA, leverage, size, a serial acquirer indicator, relative deal size, and dummies for toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets), acquirer and target country-level labor protection indices, and year, acquirer- and target-industry fixed effects. In Models (1)-(4) we regress acquirer announcement CARs on four different employee-engagement scores—*Employment Quality*, *Health & Safety*, *Workforce Diversity*, and *Training & Development*—separately and combine them in one model (Model (5)) to cross-validate our results.

Several interesting observations emerge. First, an acquiring firm's employee-engagement is positively related to shareholder returns, but only in terms of employment quality—which captures compensation and job security (Model (1))—and not in terms of issues related to health and safety (Model (2)), workforce diversity (Model (3)), and training and development (Model (4)). When all employee-engagement scores enter into Model (5), we obtain similar results. The fact that only *Employment Quality* is significantly related to shareholder returns is consistent with the notion that employees are more likely to be incentivized by benefits in terms of monetary compensation and job security, rather than by improvement of their working environment (Herzberg et al., 1959). Second, cross-border deals generally earn higher returns for acquirer shareholders, consistent with findings in the extant literature that usually attributes this effect to the benefits of international diversification and the value of control (e.g., Doukas and Travlos, 1988; Chari, Ouimet and Tesar, 2010). Third, the interaction between employee-engagement and the cross-border dummy is negative in all models, but it is only statistically significant when employee-engagement is measured by our *Employment Quality* score. That is, the positive effect of employment quality is attenuated when the deal is conducted across national borders. In other words, stronger employee-engagement in cross-border deals may reduce the returns to acquiring firms' shareholders, a result further supported by our subsample analysis in which we conduct the same analysis for domestic and cross-border deals, separately (see Appendix E).

This contrast is economically remarkable: a one standard deviation increase (+ 30) in the acquirer's score on *Employment Quality* is associated with an increase of 0.20% (20 bps) in returns in domestic deals, but the increase in returns around cross-border deals drops from 1.18% to 0.78% (a 40 bps decrease) in Model (1) and even from 1.01% to 0.52% (a 50 bps decrease) in Model (5). Combining these results, we can conclude that, despite the summary statistics in Table 1 indicating that cross-border acquirers have higher levels of employee-engagement and experience on average higher announcement returns, these higher returns are not likely to result from the acquirer's stronger employee-engagement. Instead, they are consistent with the notion that acquiring across national borders reduces the potential gains for shareholders from their firm's engagement in employee interests and may turn it into a burden for the firm, possibly due to difficulties in transferring employment policies. Among the (intangible) assets the bidding firm will acquire is the human capital of the target firm, which includes the (explicit) contracts between the target firm and its employees, the implicit contracts between the target and unions/employees, the target's corporate culture etc. While the acquiring company 'inherits' the explicit employee contracts, it is ex ante unclear to what extent its own employment policies are congruent with the implicit contracts in the target firm, how responsive the target's employees are to incentive mechanisms that work well in the acquiring firm, to what extent job flexibility can be requested from target's employees, etc. Overall, the results in Table 3 suggest that firm-level employment policies with regard to monetary incentives and job security are priced by the market around M&As. Firms with higher scores on *Employment Quality* earn higher abnormal returns when taking over domestic targets, but lower abnormal returns when taking over targets abroad.<sup>5</sup>

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<sup>5</sup> Our results thus emerge from the fact that transferring and integrating employee policies is more easily done in domestic deals, which results in higher returns to acquirer shareholders. This however also raises the question as to why, if such employee policies raise shareholder value, the target did not introduce them before. One potential explanation is that the target may not have had the resources to do so. For a subsample of deals in which we have data on the target's leverage, we do indeed find that targets in domestic deals with high-employment quality acquirers are more financially constrained, and that the positive effects of acquirer employee engagement in domestic deals are largely driven by deals in which the targets are more financially constrained (higher levered).

It is important to note that we control in all specifications for labor regulations in the acquirer's and—in cross-border deals—also the target's country. In line with Dessaint et al. (2016), we find that in domestic deals a country's labor laws regarding employment regulation (which to a large extent measures the labor rigidity faced by a firm) are negatively related to announcement returns. However, the inclusion of country-level labor regulation indices does not erode the significance of our firm-specific employment quality score. This suggests that government-imposed labor protection regulations are not perfect substitutes for voluntary employee incentives at the firm level. In addition, the signs and significance for our other control variables are comparable to those found in the literature (e.g. Lin, Officer, and Zou, 2011): acquiring a public target negatively affects the returns to shareholders, whereas most firm-level characteristics and the financial performance of acquirers do not seem to play a significant role in driving the acquirer's own returns. In our robustness tests, we additionally control for, and interact our employee-engagement variables with, acquirer and target country-level measures of culture (proxied by indicators from the World Value Survey), the acquirer's and target's country GDP and GDP per capita, as well as the differences between the acquirer's and target's country cultural and economic attributes. None of these controls is consistently statistically significant and adding them does not affect the significance of our measures of employee-engagement.

[ Insert Table 3 about Here ]

### **IV.3. Employee-Engagement and Takeover Propensity**

Our above interpretations are largely based on the assumption that M&A decisions are exogenous to an acquiring firm's own degree of employee-engagement, and thus to the desire to acquire human capital or restructure its workforce (Gao and Ma, 2016; Ouimet and Zarutskie, 2016). However, we still need to verify whether this is really the case for our sample: does a firm's level of employee-engagement drive the returns around domestic and cross-border M&A deals through its effect on increasing/reducing the likelihood of

engaging in a domestic versus a cross-border M&A? In Table 4, we use a Heckman selection model to estimate the relation between the firm’s four measures of employee-engagement and the likelihood of the firm embarking on a domestic versus a cross-border takeover transaction, conditional on the firm having decided on performing an M&A deal. Our results show that, although a firm’s employment policies are positively related to engaging in M&A deals in the first stage (consistent with Gao and Ma, 2016; Ouimet and Zarutskie, 2016), these results are economically trifling (ranging between 1 and 0.5 basis points) and the firm’s employee policies are not significantly related to the choice between domestic versus cross-border deals (2<sup>nd</sup> stage regressions). This implies that a firm’s engagement towards its employees is not likely to be a significant driver of management’s decision to engage in domestic versus cross-border M&A deals, but—as we will show in the previous section—it does affect shareholders’ perceived value creation around these deals.

[ Insert Table 4 about here ]

#### **IV.4. Unbundling Employee Incentives**

Next, we further investigate the mechanisms underlying the above-documented employee-engagement effects. If the main effect of employee-engagement (particularly employment quality) does indeed capture an incentive effect as we hypothesized, we expect the positive employment quality effect in domestic takeovers and the attenuating effect in cross-border takeovers to mainly run through channels that are specific to enhancing employee incentives and increasing productivity. To test such channels, we dig deeper into the ASSET4 measures of employee welfare by decomposing the *Employment Quality* score into two broad categories capturing employees’ monetary incentives (including fair salaries, bonus plans, and other fringe benefits) and job security incentives (including growth in the workforce, trade union relations, and the presence of a job security policy), respectively. This classification also conceptually matches the dichotomy by Herzberg et al. (1959) who distinguish between “motivational” factors (such as monetary incentives) and

“maintenance” factors (such as job retention policies and improving working conditions). The former set of incentives, the monetary incentives, represent how much the firm values the specificity of human assets (Williamson, 1981), and thus can increase employee productivity and commitment by linking compensation to firm performance, providing a fair wage, attracting talented employees, and encouraging diligence. The latter set of incentives, which we refer to as “job security” factors, are directly related to employee loyalty and commitment and are thus more direct measures of the employment insurance dimension of employee relations. They represent the collective governance of human assets which are not necessarily employee-specific, and may not directly translate into superior labor productivity (Williamson, 1981). As argued by Herzberg (1959; 1964; 1966), while monetary incentives are important determinants for productivity and firm performance, job security factors do not lead to superior performance, and may even constitute a significant cost for shareholders. Based on these arguments, we expect that stronger monetary incentives increase employee productivity and reduce resistance against takeovers, which is reflected in higher announcement returns. In addition, value-increasing monetary incentives in the acquiring firm may not have the desired effects in a cross-border deal, due to the inalienability of employment policies in the target firm. In contrast, stronger job security incentives do not directly incentivize employees to increase productivity and can result in employment rigidity, redundancies, and inability to benefit from economies of scale.

In Panel A of Table 5, we consider three forms of monetary incentives: (i) the provision of a bonus plan (*Acquirer Bonus Plan Dummy*), (ii) the provision of fringe benefits such as pension funds and health insurance (*Acquirer Fringe Benefits Dummy*), and (iii) the wage ratio of the average worker’s salary and the CEO’s income (*Acquirer Wage Ratio Employees/CEO*).<sup>6</sup> We include the latter based on the argument that a smaller wage gap is likely to increase employees’ perception of being paid a fair wage, which may further increase their productivity and reduce the likelihood of resisting takeovers. We also interact all these monetary incentive variables with the cross-border indicator. From the results in Panel A, we note that each

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<sup>6</sup> The effect of the firm’s industry is controlled for by including industry fixed effects in all models.

of our monetary incentive indicators is positively related to acquirer announcement returns, supporting our incentive effect hypothesis. In addition, the positive effects are again attenuated by the cross-border dummy in the interaction term, in line with the results from Table 3. This can still be explained by the inalienability of employment policies with regard to monetary compensation, as employee compensation schemes differ significantly across countries (e.g., Card, Heining, and Kline, 2013; Mueller, Ouimet, and Simintzi, 2017) and an overly generous compensation policy for all employees with different backgrounds and productivities could easily distort workforce incentives in general (Mueller et al., 2017), which is more likely to happen for cross-border deals. However, the afore-documented effect of employee-engagement on acquirer CARs mostly come from monetary incentives, and not from the job security factors, presented in Panel B and measured by (i) whether or not the firm has a trade union relations policy (*Acquirer Trade Union Relations Policy*), (ii) employment growth (*Acquirer Net Employment Creation*), and (iii) whether the firm has a job security policy (*Acquirer Job Security Policy*). Overall, we find no significant association between the factors related to job security and the abnormal announcement returns. We also test a set of alternative variables related to job security (not reported): the percentage of trade unionization in the acquirer firm, the rate of turnover in the workforce, and the number of controversies regarding lay-offs or wages reported in the media. In general, these results are consistent with Herzberg's conjecture, namely that job security does not lead to superior performance, and with our above arguments that motivational factors (in terms of monetary incentives) enhance firm performance through the channel of incentivizing employees to increase productivity, efficiency, and support around takeovers. Our results also echo those of Table 3: monetary incentives enhance firm value in domestic deals, but this effect is reduced in cross-border deals. The inalienability of human capital and employment policies creates uncertainties regarding the transfer of implicit contracts and the extent to which monetary incentives can increase employees' productivity and efficiency in the foreign target firm. In addition, they are in line with our results in Table 3 showing that higher levels of workforce diversity, training, and health and safety are not significantly related to shareholder returns; these dimensions

of employee relations are more closely related to the job security factors than to the monetary incentives and are less important drivers behind the employee-engagement effect. Overall, the results in Table 5 further support the employee incentive channel that we hypothesized.

[ Insert Table 5 about here ]

#### **IV.5. Inalienability of Human Capital and Employment Policies in Cross-Border Takeovers**

While we have shown the role of incentive effects above, we now turn to investigating whether the attenuating effect in cross-border transactions is really driven by the inalienability of human capital and employment policies. In other words, since cross-border deals on average generate higher announcement returns, which implies that going cross-border in itself is not likely to explain the attenuating effect, what other (especially employee-specific) factors then account for the negative interaction effects shown in Table 3? Frictions such as geographical distance and cross-country differences in rules and regulations make the transaction environment in cross-border deals more complex than that in domestic ones. As we argued above, these frictions induce uncertainties about employee integration and consistency of employment policies of the merging firms, which exemplify the inalienability of employment policies. We therefore consider several mechanisms that potentially reduce these uncertainties about the transfer and integration of employment policies, and therefore diminish the negative effect of employee-engagement in cross-border deals that we established in Table 3. In particular, we focus on seven variables at both the firm-level, industry-level, and the country-level, and interact them with our *Employment Quality* score for the subsample of cross-border deals, as reported in Table 6. As before, we find for each of our proxies that the main effect of employee-engagement is significantly negative.<sup>7</sup> The first variable captures whether or not the transaction is a repeat acquisition in the target country, as repeatedly acquiring firms in the same country familiarizes the acquirer with the target country's employment cultures and labor market, which reduces the uncertainty

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<sup>7</sup> This echoes our results in Table 3 and Appendix E on the effect of employee-engagement and a deal's geographical focus on acquirer CARs.

about how to transfer and integrate its human capital policies. As shown in Model (1), while the coefficient on *Employment Quality* is negative, the interaction term “*Acquirer Employment Quality*<sub>*t-1*</sub> × *Repeat Acquisition*” is positive and statistically significant at the 10% level, supporting the above argument. In economic terms, a 30 point increase in *Employment Quality* (one standard deviation) increases CARs by 0.09% if the acquirer has acquisition experience in the target’s country, relative to a -0.33% decrease if this were not the case.

The second variable is a target country’s remuneration culture regarding the importance of ‘good pay’, because when there is a similar attitude towards monetarily incentivizing employees in both the target and acquirer countries, it will be easier for the acquirer to implement in the target firm the same incentivizing policies that can effectively enhance employee productivity (which we have documented in Table 5). We obtain the data on the country-level “Importance of Good Pay” from the World Value Survey, and consider the case in which people in the target’s country have a higher predilection for good pay in their job relative to those in the acquirer’s country. This predilection could signal the potential effectiveness of introducing or maintaining monetary incentives for employees in the target firm to acquiring firms’ shareholders. The positive interaction of “*Acquirer Employment Quality* × (*Target Country* > *Acq. Country ‘Good Pay is Important’*)” in Model (2) supports this argument. In deals where the target’s country has a higher predilection for good pay, the negative effect of employment quality is weaker.

The third variable captures the attitude towards saving in the target’s country. It indicates whether people in the target’s country attach more importance to saving money relative to people in the acquirer’s country. An acquiring firm may more easily transfer monetary incentive policies to countries where people think saving money is relatively important (or value the possession of money more). This is supported by the positive interaction of “*Acquirer Employment Quality* × (*Target Country* > *Acq. Country ‘Saving is Important’*)” in Model (3). A one standard deviation increase in *Employment Quality* increases CARs from -0.96% to -0.21% when acquiring a target firm in such a country.

The fourth variable captures the absence of economic nationalism in the target country's government as, in the inverse case, foreign acquirers can face more resistance from target countries' governments who may fear that foreign acquirers will infringe national interests and that corporate restructuring will induce massive lay-offs in the target firm, and who thus prefer that the target remains domestically owned. If such "economic nationalism" is low, foreign acquirers with better employee relations may face less political opposition such that transposing their employment policies to the target is likely to be more effective than in the case with stronger protectionist attitudes. We follow Dinc and Erel (2013) and use the ruling of a liberal government (a dummy variable indicating whether the ruling government is right-wing; data obtained from the Database of Political Institutions) in the target's country to proxy for the absence of economic nationalism, as (rightwing-)liberal parties usually and traditionally favor more free trade (Dinc and Erel, 2013). This argument is supported by the positive coefficient on the interaction term "*Acquirer Employment Quality t-1 × (Absence of Economic Nationalism in Target Country)*" in Model (4), which indicates that the absence of strong economic nationalism reduces the uncertainty with regard to employee policy integration.

The fifth variable is the perceived strength of labor unions in the acquirer and target's country. The rationale is that strong labor unions increase contract rigidity and difficulty in negotiating with employees. Therefore, low union strength in the target's country (as perceived by the acquirer) indicates the relative ease with which acquirers can restructure the workforce and implement post-merger employment policies in line with those in the acquiring firm. Of course, if in the acquirer country there are strong labor unions, the employees of the acquiring firm may attempt to resist such implementation of favorable employment policies in the target firm as this may shift resources from the acquirer's to the target's employees. We therefore specifically consider the case in which both the acquirer and target countries' have low perceived union strength ("low" is defined as being in the bottom tercile of the distribution), where perceived union strength is measured by "Confidence in Unions", also from the World Value Survey. As shown in Model (5), the interaction term "*Acquirer Employment Quality × (Acquirer and Target Country Low Union Strength)*" has a

positive loading, suggesting that the negative effect of employee-engagement in cross-border deal becomes less negative when both acquirer and target country have low perceived union strength.

In Model (6), we test whether employee policies are more easily transferred and integrated in the case of low-tech deals (in which target and acquirer are both in low-tech industries), relative to deals in which at least one of the parties is in a high-tech industry. High-tech industries are fast-changing and more complex than traditional low-tech industries, especially in terms of incentivizing and motivating employees (Eyob, 1994). We thus expect that transferring and integrating employee policies in a high-tech target is more difficult, as in such industries corporate culture or the reputation of the employer may be more important than purely monetary incentives (see e.g. Focke, Maug and Niessen-Runzi, 2016) reducing the returns to acquirer shareholders. In low-tech deals on the other hand, integration is done more easily, alleviating the negative effects of employee-engagement in cross-border deals that we have identified above. As shown in Model (6), “*Acquirer Employment Quality × Low-Tech deal*” is significantly positive, indicating that acquirer shareholders react more positively to cross-border deals by high-employment quality acquirers that engage in low-tech deals versus high-tech deals.

Overall, the results in Table 6 suggest that when there are fewer uncertainties about the transfer and integration of human capital and employment policies, the relatively negative effect of employee-engagement (especially employment quality) in cross-border acquisitions becomes weaker and can be even completely off-set. Combining this with the fact that cross-border deals usually achieve higher abnormal returns, our results point to the explanation that the negative interaction between employment quality and cross-border deals as found in Table 3 is not due to a deal being cross-border per se, but to a unique aspect of cross-border deals that is related to the inalienability of human capital and employment policies and the resulting uncertainties regarding the transfer and integration of such policies in a foreign target firm.

[ Insert Table 6 about here ]

#### IV.6. The Role of Target Firm's Employee-Engagement

One could wonder whether our above results are driven by the target's employee-engagement, which may coincide with the acquirer's employee-engagement. Empirically this is a difficult question because we do not have sufficient data on the targets' employee-engagement in the ASSET4 database, as the database mainly covers large firms included in the major global equity indices and most (small) targets do not receive a rating from ASSET4. Nevertheless, we conduct tests on a subsample of deals with employee-engagement data available for both the target and the acquiring firm (362 deals in total). We classify both the acquirer's and the target's *Employee Quality* scores into high- and low-groups ("high" or "low" refers to the employee-engagement score being above or below the sample median). We then interact the cross-border dummy with different combinations of the acquirer's and target's employee-engagement scores such that we concentrate on four subsamples based on a two-by-two matrix capturing high/low scores by acquirers/targets, as shown in Table 7 (the "Acquirer Low, Target Low" combination is omitted as it is the benchmark case). Likewise, we do this for all the four measures scores of employee-engagement: *Employment Quality* (Model (1)), *Health & Safety* (Model (2)), *Workforce Diversity* (Model (3)), *Training & Development* (Model (4)), and for all of these scores in the same regression (Model (5)). Again, some interesting observations can be made. First, most of the significant results arise from *Employment Quality* (Models (1) and (5)), consistent with our results in Table 3. Second, the significance is mainly present in combinations when acquirer's *Employment Quality* score is high (above the sample median), regardless of the target's *Employment Quality* score. In other words, the target's employee-engagement does not seem to matter much for the incentive effect and the attenuating effect of cross-border deals. Of course, these results should be interpreted with caution as they come from a relatively small subsample.

[ Insert Table 7 about here ]

#### **IV.7. Robustness and Alternative Explanations**

Our above analyses have established that a firm's orientation towards employee interests has both positive and negative effects on the returns to shareholders and firm value around M&A deals. These results are in line with our hypothesis that acquirer shareholders value their firm's employee-engagement (in particular in terms of monetary incentives) to improve employees' productivity and reduce resistance around takeovers, as is illustrated by the increase in CARs for firms with higher levels of employment quality, especially for domestic deals. However, in cross-border deals, higher levels of employee-engagement reduce the CARs, as acquirer shareholders face uncertainties regarding the transfer and integration of such employee policies in a foreign target firm. To further check the robustness of our results and rule out alternative explanations, we conduct a battery of additional tests, which we discuss below.

##### *Instrumental Variable Approach*

Our analysis is based on a sample of M&A announcements, which are largely exogenous events relative to the degree of employee-engagement acquiring firms adopt (as shown in Table 4) and thus alleviate the concern regarding a reverse causality problem in the relationship between employee-engagement and announcement CARs. In addition, it seems unlikely that bidding firms adjust their level of employee-engagement because they may do a takeover bid in the next year. To reduce a potential omitted variable bias, we have already used industry and year fixed effects and a large number of control variables in our specifications. However, to further account for any remaining endogeneity bias from unobservable omitted variables, we perform a two-stage instrumental variable (IV) regression as a robustness test. Specifically, we use the acquirer's industry peers' average employee wages and benefits as an IV for *Employment Quality*. Whereas a firm's expenses in terms of wages and benefits are influenced by the wage expenses by its industry peers (satisfying the relevance requirement of instrumental variables), it is unlikely that these

expenses by industry peers affect the firm's announcement returns directly or through channels other than the focal firm's employment policies, thus satisfying the exclusion condition. Similar arguments on peer effects are made for other corporate policies such as capital structure (Leary and Roberts, 2014), corporate financial policies (Ferrell, Liang, and Renneboog, 2016), corporate social responsibility (Cao, Liang, and Zhan, 2016; Liang and Renneboog, 2016), and corporate culture (Fiordelisi, Li, Stentella-Lopes, and Ricci, 2016). We take the within-sample mean of the lagged employee salaries and benefits expenses (as obtained from Worldscope) for the focal company's peer firms by industry and by year (industry-year average) as the IV. The results for the first- and second-stage regressions are presented in Models (1) and (2) of Table 8. Model (1) indicates that the industry peers' average wage expenses are strongly positively related to *Employment Quality*, our measure of employee-engagement. We find in Model (2) that using an IV approach does not affect our conclusions from Table 3: strong employee-engagement (as predicted from the first stage) is still positively related to shareholder returns in domestic deals, and the effect again turns negative in cross-border deals. This increases our confidence that the effects on shareholder value we have identified are indeed driven by the acquirer's level of employee-engagement.

[ Insert Table 8 about here ]

### *The Role of Labor Regulations*

The majority of the literature on the role of employees in corporate governance focuses on country-level labor regulations, which is why we have controlled in all of the above analyses for both acquirer and target country labor regulations. We revisit this issue here in detail. In particular, one could argue that the negative coefficient on employment quality in cross-border deals simply reflects the rigidity of labor regulations in the target country or "regulatory arbitrage" whereby firms acquire targets in countries with lower levels of labor regulation so as to avoid stricter regulations at home or, alternatively, bond themselves to stronger regulations abroad to signal their commitment to employee welfare. We therefore explore how

an acquiring firm's choices in terms of employee-engagement, captured by our *Employment Quality* variable, interact with differences in state-imposed labor regulations between its home country and the target's country. If the strength of labor regulation at the country-level does shape firm-level employee-engagement, we expect the interaction terms to be significant. To do so, we regress the acquirer's 3-day CARs on the interaction between *Employment Quality* and the difference between the acquirer country's and the target country's labor regulation indices developed by Botero et al. (2004). In Table 9, we find that none of the interaction terms is significant, suggesting that the cross-country differences in labor regulation do not explain the negative returns to shareholders of firms with strong employee-engagement in cross-border deals. Overall, acquirer and target countries' labor regulations do not seem to either strengthen or attenuate the effects of firm-level employee-engagement.

[ Insert Table 9 about here ]

Another alternative explanation for our main findings is that our cross-border results are driven by the fact that firms acquiring targets in countries with stronger labor regulations face higher restructuring and integration costs due to the rigidity of laws (Levine et al., 2015). That is, the negative coefficient of firm-level *Employment Quality* could possibly capture the direct effect of (target) country-level labor regulations. However, this is not likely the case because we already control for acquirer and target country labor regulation indices in all regressions. To better understand the relative importance of imposed regulations and the firm's choice of employment policies, we regress the acquirer's three-day CARs on the separate acquirer's and target's country-level labor regulation indices (not taking differences as in Table 9). In unreported results, we find that only the target and acquirer country's employment law indices are significant determinants of acquirer CARs. After adding our firm-level *Employment Quality* variable, we find that the country-level labor regulations coefficients remain significant, and that firm-level *Employment Quality* also remains highly significant. This indicates that our previous results on firm-level *Employment Quality* are not

explained by country-level labor regulations. Although others have documented that labor market regulations and ownership structure are substitutive governance mechanisms (e.g., Bennedsen, Huang, Wagner, and Zeume, 2015), we show that this may not be the case for corporate labor-orientation; firm- and country-level measures of employee policies capture different aspects and cannot be used as substitutes.

#### *Other Alternative Explanations*

In Table 10, we further conduct several more tests to rule out other alternative explanations for our results, especially with regard to the attenuating effect of cross-border deals. First, the attenuating effect may be driven by a greater geographical distance between the acquirer's and target's countries and thus the unfamiliarity of the different parties with regard to e.g. the quality of the human capital and the ease with which employment policies can be harmonized. We therefore interact the *Employment Quality* score with an indicator of whether the geographical distance between the acquirer's and target's countries is above the sample median (Model (1)). Second, many have documented that the acquirer and target countries sharing a common language or a common border may explain the propensity and returns of cross-border deals. We therefore interact the *Employment Quality* score with indicator variables capturing whether the acquirer's and target's countries have a language in common (Model (2)), or a share a common border (Model (3)). Third, our results may also be driven by a difference in GDP per capita between the acquirer's and the target's countries. That is, if acquirers with high employee-engagement are firms from high GDP per capita countries that acquire targets in low GDP per capita countries, it could be that it is such difference in economic development that drives the negative announcement returns around cross-border deals. We therefore interact the *Employment Quality* score with the difference between two countries' GDP per capita (in logarithm) (Model (4)). Fourth, the level of employee-engagement may be driven by the difference between the cultures of the target's and the acquirer's countries (Ahern, Daminelli, and Fracassi, 2015). Hence, in Models (5) and (6), we interact *Employment Quality* score with two World Value Survey variables

capturing the difference between the acquirer and target countries in terms of people's attitudes towards work and are measured by the percentage of people considering “*Responsibility Is Important*” and “*Job Security Is Important*.” None of the above interactions have significant coefficients. For the cultural explanation, interacting with the widely-used Hofstede cultural variables gives similar insignificant results (results not reported).

#### *Inalienability or Over-engagement?*

The above analyses rule out several alternative explanations of our results with regard to the negative effect of employment quality in cross-border takeovers. What remains unclear is whether this negative effect is due to the fact that the inalienability of human capital and employment policies reduces shareholder gains from employee-engagement in cross-border deals, as we have hypothesized, or results from over-engaging in employee issues, which could then reduce firm value. The descriptive statistics in Panel A of Table 2 indicate that these two effects may coincide, and we need to disentangle them to further pin down the exact mechanism. Therefore, we regress announcement CARs on a dummy indicating whether the acquirer's *Employment Quality* score is above the score of 50 (which we consider as “over-engagement” in employees) along with other controls as in the previous specifications, but on the subsample of *domestic deals only*. If the over-engagement story holds, we expect a significant and negative coefficient of the “*High Employment Quality*” dummy in this subsample of domestic deals. The positive coefficient in Model (7) refutes this, and suggests that the negative effect of employee-engagement in cross-border deals arises from the inalienability nature of human capital, rather than from the acquirer over-engaging in employee issues in general.

[ Insert Table 10 about here ]

#### **IV.8. Employee-Engagement and Post-Merger Performance**

Finally, we investigate the effects of employee-engagement on the acquirer's long-run performance after an M&A deal, that is, whether the announcement returns may contain information about the deal's

future performance. Therefore, following our results on announcement CARs, we focus on the acquirer's *Employment Quality* scores and measure long-run performance using the acquirer's returns on assets (ROA) two years after the completion of the takeover. We follow the approach in Harford, Humphery-Jenner, and Powell (2012), and include the acquirer's industry-adjusted pre-merger ROA in the model as a control. Table 11 indicates that having a higher *Employment Quality* score increases the average post-merger industry-adjusted ROA in domestic deals, whereas it decreases the post-merger profitability in cross-border deals. These effects translate into an increase in post-merger ROA of 0.41% for a one standard-deviation increase in *Employment Quality* in domestic deals. Although cross-border deals on average show an increase in post-merger ROA, having a one standard-deviation higher level of *Employment Quality* in such deals decreases the post-merger profitability by 0.30%. We find similar but weaker results for the post-merger industry-adjusted return on sales (ROS) in Model (2), and Model (3) shows that an increase in *Employment Quality* results in a decrease in post-merger labor productivity (measured as Sales-to-Employees ratio, similar to Tate and Yang (2016)) in cross-border deals but not in domestic deals. This again confirms the hypothesis that uncertainties regarding the transfer and integration of employee policies in foreign targets can have a material impact on firm profitability and shareholder value, and that they are priced in by forward-looking stock markets at the takeover announcement. Moreover, consistent with investors' reactions at the merger announcement, we find that higher employee-engagement negatively affects post-merger labor productivity in cross-border takeovers.

[ Insert Table 11 about here ]

#### **IV. Conclusion**

The importance of human capital in modern corporations has been widely discussed, and scholars and practitioners largely agree that corporate engagement in employee-related issues has considerable consequences for both management and shareholders. In spite of the voluminous literature on this topic,

how corporate employee-engagement really matters remains inconclusive. Mergers and acquisitions (M&As) often put substantial pressure on a firm's relation with its employees, providing a setting in which the firm-labor dynamics are particularly prominent. In this paper, we investigate the effect of an acquiring firm's engagement in employee welfare on the returns to shareholders around M&A announcements for a sample of large public corporations around the world. We find that acquirers engaging in cross-border deals have on average more generous employment policies at the firm level, and their deals also earn higher announcement returns compared to domestic acquirers. Acquirers with higher levels of employment quality (especially in terms of monetary compensation) earn substantially higher returns around domestic M&A announcements, but this effect is attenuated in cross-border acquisitions. This appears to reflect the greater uncertainties with regard to employee integration and consistency of employment policies, which we call the inalienability of human capital and employment policies. The underlying idea is that since employees and their human capital cannot easily be separated, the acquiring firm cannot easily change the explicit and implicit contracts (such as compensation contracts and policies) in the foreign target firm, so as to align acquirer's and target's employment policies and to properly incentivize employees in both firms and unleash their combined human capital. In addition, among the various aspects of corporate employee-engagement policies, employment quality in terms of monetary benefits (but not job security) affects shareholder returns around takeover transaction announcements, but this is not the case for employment policies related to training and development, health and safety, or workforce diversity. All these results are conditional on controlling for acquirer and target country labor regulations in terms of employment laws, collective relations laws, social security, and civil rights. However, the inclusion of country-level labor regulation indices does not erode the significance of our firm-specific employment quality score. This suggests that government-imposed labor protection regulations are not perfect substitutes for policies on employee incentives that firms voluntarily adopt. Furthermore, our main findings stem from the employee-engagement of the acquirer rather than of the target, and we address potential endogeneity concerns using

an Instrumental Variable (IV) approach. We also explore several alternative explanations for the positive relation of employee-engagement in domestic takeovers and the negative one in cross-border deals, but do not find consistent evidence that (differences in) country-level labor regulations, economic development, culture, geographical distance between target and acquirer, or their main languages drive our results. Finally, we find that our main conclusions on abnormal announcement returns also persist in the firm's long-run operating performance after the merger.

Taken together, our findings may provide an explanation for the conflicting findings in the existing literature on the role of labor orientation in driving firm and shareholder value and shed light on how various stakeholder groups exert an intertwined influence on corporate governance and firm behavior. Perhaps the most intuitive implication of our results is that firms and shareholders should not consider generous employee benefits as being absolutely good or bad for firm value. A trade-off exists between value-enhancing incentive effects and value-destroying "inalienability" effects of a firm's focus on employee interests. Which effect dominates depends on the extent of employee-engagement, as well as uncertainties in the contracting and transaction environment. Overall, our findings reinforce the notion that employees play a fundamental yet nuanced role in a corporation, and highlight the importance of taking into account such nuances when studying the interplay between finance and labor, a topic that remains a fruitful area for future research.

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**Table 1. Descriptive Statistics - Acquirer**

This table shows summary statistics for the variables used in our study for domestic and cross-border deals. Panel A shows descriptive statistics for the acquiring firms' labor orientation measures. Panel B shows a set of deal-level variables, including the acquirer's announcement returns. Panel C shows firm-level variables and Panels D and E show country-level labor regulation indices for the acquirer's and target's country, respectively. Continuous variables are winsorized at the 1<sup>st</sup> and 99<sup>th</sup> percentiles.

Variables	N	Mean	Median	St. Dev.	Min.	Max.	N	Mean	Median	St. Dev.	Min.	Max.	Difference
	Domestic Deals						Cross-Border Deals						
<i>Panel A: Labor Orientation Variables (Acquirer)</i>													
Workforce Diversity Score	2,550	49.81	45.61	31.40	4.830	98.67	2,015	56.66	57.80	30.94	6.11	98.79	-6.84***
Employment Quality Score	2,550	49.31	47.92	29.91	2.950	98.45	2,015	58.64	64.75	30.40	2.88	98.57	-9.34***
Health and Safety Score	2,550	45.50	38.62	29.60	2.800	99.44	2,015	58.09	58.22	30.27	3	99.49	-12.59***
Training and Development Score	2,550	47.97	45.29	31.25	5.160	97.40	2,015	61.66	72.34	29.49	5.16	97.39	-13.69***
Bonus Plan (Dummy)	2,550	0.386	0	0.486	0	1	2,015	0.478	0	0.499	0	1	-0.09***
Fringe Benefits (Dummy)	2,550	0.436	0	0.495	0	1	2,015	0.442	0	0.496	0	1	-0.006
Wage Ratio Empl./CEO	2,550	0.337	0.315	1.552	0.001	11.25	2,015	0.369	0.001	1.631	0.001	10.96	-0.03
Net Employment Creation	2,550	0.035	0	0.339	-0.79	8.06	2,015	0.023	0	0.599	-0.65	25.61	0.01
Trade Union Relations Policy	2,550	0.176	0	0.381	0	1	2,015	0.316	0	0.465	0	1	-0.14***
Job Security Policy	2,550	0.060	0	0.238	0	1	2,015	0.110	0	0.313	0	1	-0.05***
<i>Panel B: Deal-level Variables</i>													
Acquirer CARs	2,550	-0.246	-0.219	4.275	-12.13	13.42	2,015	0.159	0.028	4.027	-12.13	13.42	-0.41***
Public Target	2,550	0.193	0	0.395	0	1	2,015	0.147	0	0.354	0	1	0.07***
Diversifying Deal	2,550	0.485	0	0.500	0	1	2,015	0.398	0	0.490	0	1	0.09
Hostile Deal	2,550	0.009	0	0.0946	0	1	2,015	0.012	0	0.111	0	1	-0.003
All-Cash Financing Deal	2,550	0.411	0	0.492	0	1	2,015	0.369	0	0.483	0	1	0.04***
Multiple Bidders	2,550	0.033	0	0.177	0	1	2,015	0.041	0	0.199	0	1	-0.01
Toehold Stake	2,550	0.154	0	0.361	0	1	2,015	0.106	0	0.308	0	1	0.05***
Relative Deal Size	2,550	0.169	0.032	0.007	0	3.28	2,015	0.159	0.021	0.604	0	20.07	0.01
<i>Panel C: Firm-level Variables</i>													
Acquirer Leverage	2,550	0.443	0.406	0.257	-0.005	1.000	2,015	0.429	0.388	0.253	0.001	1.000	0.01*
Acquirer ROA	2,550	0.110	0.0986	0.105	-0.972	2.209	2,015	0.127	0.118	0.093	-0.60	0.645	-0.02***
Serial Acquirer	2,550	0.217	0	0.412	0	1	2,015	0.300	0	0.458	0	1	-0.08***
Acquirer Size (USD Mil)	2,550	38,906	6,925	123,507	249.9	1,107,776	2,015	65,855	8,733	186,560	249.9	1,107,776	-35,010***
<i>Panel D: Country-level Variables (Acquirer)</i>													
Employment Laws Index	2,550	0.318	0.218	0.180	0.161	0.828	2,015	0.411	0.282	0.216	0.161	0.828	-0.09***
Collective Relations Laws Index	2,550	0.382	0.259	0.174	0.188	0.711	2,015	0.410	0.384	0.178	0.188	0.711	-0.03***
Social Security Laws Index	2,550	0.678	0.646	0.0868	0.177	0.873	2,015	0.702	0.692	0.092	0.177	0.873	-0.02***
Civil Rights Index	2,550	0.685	0.733	0.0997	0.233	0.850	2,015	0.660	0.733	0.119	0.233	0.850	0.02***
<i>Panel E: Country-level Variables (Target) – Cross-Border Only</i>													
Employment Laws Index							2,015	0.437	0.403	0.201	0.148	0.828	
Collective Relations Laws Index							2,015	0.400	0.378	0.155	0.188	0.711	
Social Security Laws Index							2,015	0.679	0.692	0.135	0.105	0.873	
Civil Rights Index							2,015	0.667	0.733	0.125	0.233	0.933	

**Table 2. Descriptive Statistics - Target**

This table shows summary statistics for the variables used in our study for domestic and cross-border deals. Panel A shows descriptive statistics for the target firms' labor orientation measures. Panel B shows a set of deal-level variables, including the target's announcement returns. Panel C shows firm-level variables and Panel D shows country-level labor regulation indices target's country. Continuous variables are winsorized at the 1<sup>st</sup> and 99<sup>th</sup> percentiles.

Variables	N	Mean	Median	St. Dev.	Min.	Max.	N	Mean	Median	St. Dev.	Min.	Max.	<i>Difference</i>
	<b>Domestic Deals</b>						<b>Cross-Border Deals</b>						
<i>Panel A: Labor Orientation Variables (Acquirer)</i>													
Workforce Diversity Score	202	52.98	50.00	30.17	8.260	97.35	160	58.63	58.43	28.12	10.21	97.94	-5.65*
Employment Quality Score	202	54.42	59.34	29.83	3.520	97.78	160	62.36	70.76	28.79	3.330	97.81	-7.94**
Health and Safety Score	202	48.89	44.13	28.87	10.23	98.99	160	59.65	59.77	28.60	10.57	98.84	-10.75***
Training and Development Score	202	55.01	63.28	30.98	5.200	96.58	160	60.28	73.57	30.45	5.190	96.45	-5.27
<i>Panel B: Deal-level Variables</i>													
Target CARs	202	6.307	3.185	12.02	-41.00	53.12	160	7.386	2.491	12.54	-12.48	55.21	-1.08
Weighted CARs	202	1.321	0.524	4.014	-5.140	12.15	160	1.166	0.541	3.729	-5.140	12.15	0.15
<i>Panel C: Firm-level Variables</i>													
Target ROA	202	0.301	0.0998	1.533	-6.680	10.63	160	0.299	0.110	1.426	-2.540	12.23	0.002
Relative Deal Size	202	0.699	0.553	0.604	0.00237	3.278	160	0.461	0.301	0.604	0.001	4.930	0.24***
Target Size (USD Mil)	202	29,567	6,985	60,273	48.10	289,603	160	25,006	5,661	57,277	89.30	289,603	4,561
<i>Panel D: Country-level Variables (Target)</i>													
Employment Laws Index	202	0.324	0.218	0.182	0.164	0.809	160	0.394	0.282	0.200	0.164	0.828	-0.07***
Collective Relations Laws Index	202	0.343	0.259	0.161	0.188	0.667	160	0.349	0.259	0.159	0.188	0.667	-0.006
Social Security Laws Index	202	0.678	0.646	0.0677	0.400	0.873	160	0.704	0.692	0.0741	0.400	0.873	-0.03***
Civil Rights Index	202	0.685	0.733	0.0918	0.461	0.807	160	0.654	0.692	0.109	0.500	0.850	0.03***

**Table 3. Employee Orientation and Announcement CARs: Full Sample**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around an M&A announcement. The independent variables are the acquirer's pre-merger employee relations scores in terms of (a combination of (Model (5)) employment quality (Model (1)), health and safety (Model (2)), workforce diversity (Model (3)), and training and development (Model (4)). All specifications include a set of deal- (dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets, and the relative deal size), firm- (acquirer ROA, size, and leverage), and acquirer and target country-level (labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	(1)	(2)	(3)	(4)	(5)
Cross-Border	1.178*** (0.294)	0.537* (0.279)	0.771*** (0.272)	0.522* (0.299)	1.013*** (0.352)
Acquirer Employment Quality <sub>t-1</sub>	0.007** (0.003)				0.008** (0.003)
Acquirer Employment Quality <sub>t-1</sub> × Cross-Border	-0.013*** (0.004)				-0.016*** (0.005)
Acquirer Health & Safety <sub>t-1</sub>		0.002 (0.003)			-0.0002 (0.004)
Acquirer Health & Safety <sub>t-1</sub> × Cross-Border		-0.002 (0.004)			0.002 (0.0051)
Acquirer Workforce Diversity <sub>t-1</sub>			0.004 (0.003)		0.004 (0.004)
Acquirer Workforce Diversity <sub>t-1</sub> × Cross-Border			-0.006 (0.004)		-0.005 (0.005)
Acquirer Training & Development <sub>t-1</sub>				0.0002 (0.003)	-0.006 (0.004)
Acquirer Training & Development <sub>t-1</sub> × Cross-Border				-0.001 (0.004)	0.009 (0.006)
Serial Acquirer Dummy	-0.055 (0.143)	-0.063 (0.143)	-0.062 (0.143)	-0.061 (0.143)	-0.048 (0.144)
Acquirer ROA t-1	0.787 (0.812)	0.793 (0.818)	0.778 (0.819)	0.827 (0.819)	0.818 (0.814)
Acquirer Leverage t-1	-0.124 (0.421)	-0.102 (0.422)	-0.118 (0.421)	-0.104 (0.422)	-0.103 (0.421)
Toehold Dummy	-0.022 (0.177)	-0.013 (0.178)	-0.020 (0.177)	-0.014 (0.178)	-0.004 (0.178)
Acquirer Size	-0.011 (0.060)	-0.014 (0.060)	-0.016 (0.062)	-0.003 (0.062)	-0.015 (0.064)
Multiple Bidders Dummy	-0.592 (0.392)	-0.593 (0.392)	-0.596 (0.393)	-0.599 (0.393)	-0.592 (0.391)
All Cash Financing Dummy	0.127 (0.136)	0.129 (0.136)	0.126 (0.136)	0.128 (0.136)	0.134 (0.137)
Hostile Deal Dummy	0.597 (0.678)	0.586 (0.680)	0.600 (0.681)	0.587 (0.680)	0.586 (0.679)
Diversifying Deal Dummy	0.005 (0.146)	0.008 (0.146)	0.011 (0.146)	0.008 (0.146)	0.015 (0.146)
Public Target Dummy	-0.260* (0.142)	-0.265* (0.142)	-0.272* (0.142)	-0.265* (0.142)	-0.262* (0.142)
Relative Deal Size	-0.191 (0.162)	-0.197 (0.160)	-0.195 (0.159)	-0.197 (0.161)	-0.184 (0.161)
Constant	-1.764 (1.315)	-1.392 (1.304)	-1.550 (1.317)	-1.396 (1.305)	-1.797 (1.322)
Observations	4,565	4,565	4,565	4,565	4,565
R-squared	0.037	0.035	0.036	0.035	0.038
Year FE	Yes	Yes	Yes	Yes	No
Acquirer Industry FE	Yes	Yes	Yes	Yes	Yes
Target Industry FE	Yes	Yes	Yes	Yes	Yes
Acquirer Country Level Controls	Yes	Yes	Yes	Yes	Yes
Target Country Level Controls	Yes	Yes	Yes	Yes	Yes

**Table 4. Employee-Engagement and M&A Likelihood**

This table shows marginal effects for Heckman regressions showing the effect of a firm's employee-engagement in terms of Employment Quality (Models 1 and 2), Health and Safety (Models 3 and 4), Workforce Diversity (Models 5 and 6), and Training and Development (Models 7 and 8) on the likelihood of engaging in a domestic M&A deal versus a cross-border M&A deal (uneven models), conditional on engaging in an M&A deal in the first stage (even models). The second stage control variables include the firm's lagged market-to-book ratio, country-level labor regulations, and year dummies, the first stage additionally controls for lagged firm size. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	<i>2<sup>nd</sup> Stage: Prob</i>	<i>1<sup>st</sup> Stage:</i>						
	<i>(C-B M&amp;A)</i>	<i>Prob(M&amp;A)</i>						
Employment Quality <sub>t-1</sub>	0.002 (2.730)	0.00005** (0.00002)						
Health & Safety <sub>t-1</sub>			0.003 (2.041)	0.00005** (0.00002)				
Workforce Diversity <sub>t-1</sub>					0.001 (101.7)	0.0001*** (0.00002)		
Training & Development <sub>t-1</sub>							0.002 (50.10)	0.00008*** (0.00002)
Market-to-book ratio	0.386 (583.8)	0.013 (0.016)	0.671 (529.1)	0.013 (0.012)	0.371 (14,635)	0.011 (0.017)	0.401 (11,633)	0.012 (0.016)
Acq. Country Employment Laws Index	0.756 (1,136)	0.025*** (0.004)	0.671 (436.8)	0.0256*** (0.004)	0.806 (33,021)	0.026*** (0.004)	0.724 (20,962)	0.023*** (0.004)
Acq. Country Collective Relations Laws Index	-0.781 (1,334)	-0.0180*** (0.005)	-0.723 (536.1)	-0.019*** (0.005)	-0.815 (28,050)	-0.019*** (0.005)	-0.777 (22,979)	-0.019*** (0.005)
Acq. Country Social Security Laws Index	0.395 (786.6)	0.004 (0.007)	0.411 (356.1)	0.004 (0.007)	0.378 (7,955)	0.002 (0.007)	0.410 (12,550)	0.005 (0.007)
Acq. Country Civil Rights Index	-0.278 (429.1)	-0.009 (0.005)	-0.191 (113.7)	-0.009 (0.005)	-0.302 (11,590)	-0.009 (0.005)	-0.277 (8,184)	-0.007 (0.005)
EBITDA/Total assets		-0.028*** (0.008)		-0.028*** (0.008)		-0.0290*** (0.008)		-0.029*** (0.008)
Ln(firm size)		0.0003 (0.0005)		0.0004 (0.0005)		-0.0003 (0.0005)		0.0002 (0.0005)
Observations	31,618	31,618	31,618	31,618	31,618	31,618	31,618	31,618
Control variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

**Table 5. Unbundling Employee Incentives (Full Sample)**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around domestic and cross-border deal announcements. The main independent variables are the acquirer's pre-merger employee quality dimensions in terms of monetary incentives (Panel A), and job security factors (Panel B), interacted with a cross-border deal dummy. Monetary incentives consist of a bonus plan (Model 1a), fringe benefits (Model 2a), and the wage ratio of an average worker and the CEO (Model 3a). Job security factors consist of an indicator for having a trade union relations policy in place (Model 1b), net employment creation, measured as employment growth in the previous year (Model 2b), and a dummy for whether the firm has a job security policy (Model 3b). Each specification includes a set of deal- (relative deal size, and dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets), firm- (acquirer ROA, size, and leverage), and country-level (acquirer country labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	<b>Panel A: Monetary Incentives</b>		
	(1a)	(2a)	(3a)
Cross-Border	0.701*** (0.190)	0.745*** (0.185)	0.496*** (0.139)
Acquirer Bonus Plan Dummy t-1	0.360* (0.196)		
Acquirer Bonus Plan Dummy t-1 × Cross-Border	-0.566** (0.261)		
Acquirer Fringe Benefits Dummy t-1		0.452** (0.211)	
Acquirer Fringe Benefits Dummy t-1 × Cross-Border		-0.649** (0.254)	
Acquirer Wage Ratio Employees/CEO t-1			0.106** (0.048)
Acquirer Wage Ratio Employees/CEO t-1 × Cross-Border			-0.118* (0.072)
Observations	4,565	4,565	4,565
R-squared	0.036	0.037	0.024
Deal, Firm, and Country Controls	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Acquirer and Target Industry FE	Yes	Yes	Yes
<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	<b>Panel B: Job Security Factors</b>		
	(1b)	(2b)	(3b)
Cross-Border	0.417** (0.169)	0.433*** (0.144)	0.464*** (0.145)
Acquirer Trade Union Relations Policy t-1	-0.158 (0.215)		
Acquirer Trade Union Relations Policy t-1 × Cross-Border	0.106 (0.282)		
Acquirer Net Employment Creation t-1		-0.098 (0.254)	
Acquirer Net Employment Creation t-1 × Cross-Border		0.186 (0.288)	
Acquirer Job Security Policy t-1			-0.114 (0.320)
Acquirer Job Security Policy t-1 × Cross-Border			-0.258 (0.418)
Observations	4,565	4,565	4,565
R-squared	0.033	0.035	0.035
Deal, Firm, and Country Controls	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Acquirer and Target Industry FE	Yes	Yes	Yes

**Table 6. Acquirer Employment Quality: Mechanisms (Cross-Border Deals)**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around cross-border deal announcements. The main independent variables are a dummy for whether the acquirer does a repeat acquisition in a particular country (Model 1), a dummy indicating whether the target country's population considers "good pay" more important in a job than the acquirer's country (Model 2), a dummy indicating whether the target country's population considers "saving money" a more important child quality than the acquirer's country (Model 3), a dummy indicating whether the target country has a main executive party that is not considered "nationalist" (Model 4), a dummy indicating whether the target's and the acquirer's country's population have low confidence in unions (union strength) (Model 5), or a dummy indicating low-tech deals (both the acquirer and target are in low-tech industries) (Model 6), all interacted with employment quality. Each specification includes a set of deal- (dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, and public targets), firm- (acquirer ROA, size, and leverage), and country-level (acquirer and target country labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	Repeat Acquirer	Importance of Good Pay	Importance of Savings	Economic Nationalism	Confidence in Unions	Low-Tech Deal
Acquirer Employment Quality t-1	-0.011*** (0.004)	-0.008*** (0.003)	-0.032*** (0.012)	-0.043** (0.017)	-0.009*** (0.003)	-0.016*** (0.006)
Acquirer Employment Quality t-1 × Repeat Acquisition	0.014* (0.008)					
Acquirer Employment Quality t-1 × (Target Country > Acq. Country "Good Pay is Important")		0.027** (0.013)				
Acquirer Employment Quality t-1 × (Target Country > Acq. Country "Saving Money is Important")			0.025** (0.012)			
Acquirer Employment Quality t-1 × (Absence of Economic Nationalism in Target Country)				0.037** (0.018)		
Acquirer Employment Quality t-1 × (Acquirer and Target Country Low Union Strength)					0.018** (0.009)	
Acquirer Employment Quality t-1 × Low-Tech Deal						0.015** (0.006)
Repeat Acquisition	-0.544 (0.549)					
Target Country > Acq. Country "Good Pay is Important"		-2.722*** (1.005)				
Target Country > Acq. Country "Saving Money is Important"			0.172 (0.784)			
Absence of Economic Nationalism in Target Country				-1.713 (1.064)		
Acquirer and Target Country Low Union Strength					-1.184 (0.730)	
Low-Tech Deal						-0.794** (0.366)
Observations	2,015	2,015	2,015	2,015	2,015	2,015
R-squared	0.061	0.036	0.066	0.034	0.034	0.033
Acquirer Country-Level Controls	Yes	Yes	Yes	Yes	Yes	Yes
Target Country-Level Controls	Yes	Yes	Yes	Yes	Yes	Yes
Deal and Firm Controls	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Acquirer Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Target Industry FE	Yes	Yes	Yes	Yes	Yes	Yes

**Table 7. Aligning the Target's Employee-Engagement with Acquirer's Employee-Engagement**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around an M&A announcement. The independent variables dummies for combinations of above- and below-median target and acquirer employee relations in terms of employment quality (model 1), health and safety (model 2), workforce diversity (model 3), and training and development (model 4), and all combined (model 5). All specifications include a set of deal- (dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and relative deal size), firm- (acquirer ROA, size, and leverage, and target ROA), and acquirer and target country-level (labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects.

<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	(1)	(2)	(3)	(4)	(5)
Cross-Border	0.879 (1.273)	-1.688 (1.231)	0.598 (1.205)	0.117 (1.195)	1.111 (1.580)
Low Acq. Employment Quality, High Target Employment Quality	-0.541 (1.041)				-0.623 (1.080)
Low Acq. Employment Quality, High Target Employment Quality × Cross-Border	0.270 (1.590)				0.840 (1.596)
High Acq. Employment Quality, Low Target Employment Quality	0.997 (1.067)				1.366 (1.223)
High Acq. Employment Quality, Low Target Employment Quality × Cross-Border	-2.924* (1.567)				-3.789** (1.653)
High Acq. Employment Quality, High Target Employment Quality	2.288** (1.145)				2.357* (1.307)
High Acq. Employment Quality, High Target Employment Quality × Cross-Border	-3.376** (1.626)				-3.266* (1.808)
Low Acq. Health and Safety, High Target Health and Safety		-0.384 (1.098)			-0.455 (1.296)
Low Acq. Health and Safety, High Target Health and Safety × Cross-Border		1.536 (1.600)			2.802 (1.883)
High Acq. Health and Safety, Low Target Health and Safety		-0.992 (0.954)			-1.215 (1.109)
High Acq. Health and Safety, Low Target Health and Safety × Cross-Border		1.643 (1.595)			3.837* (1.981)
High Acq. Health and Safety, High Target Health and Safety		0.00713 (1.216)			-0.668 (1.449)
High Acq. Health and Safety, High Target Health and Safety × Cross-Border		0.703 (1.628)			2.890 (2.029)
Low Acq. WF Diversity, High Target WF Diversity			-0.547 (1.157)		-0.410 (1.337)
Low Acq. WF Diversity, High Target WF Diversity × Cross-Border			-0.981 (1.725)		-1.406 (1.849)
High Acq. WF Diversity, Low Target WF Diversity			-0.254 (1.260)		-0.232 (1.433)
High Acq. WF Diversity, Low Target WF Diversity × Cross-Border			-0.990 (1.754)		-1.260 (1.941)
High Acq. WF Diversity, High Target WF Diversity			0.386 (0.943)		0.267 (1.170)
High Acq. WF Diversity, High Target WF Diversity × Cross-Border			-3.226** (1.428)		-3.767** (1.538)
Low Acq. Training and Dev., High Target Training and Dev.				0.260 (1.193)	0.401 (1.355)
Low Acq. Training and Dev., High Target Training and Dev. × Cross-Border				-1.416 (1.861)	-2.756 (2.122)
High Acq. Training and Dev., Low Target Training and Dev.				-0.449 (1.087)	-0.698 (1.403)
High Acq. Training and Dev., Low Target Training and Dev. × Cross-Border				-0.998 (1.716)	-1.109 (2.114)
High Acq. Training and Dev., High Target Training and Dev.				0.223 (1.069)	-0.365 (1.330)
High Acq. Training and Dev., High Target Training and Dev. × Cross-Border				-1.360 (1.392)	-0.447 (1.741)
Observations	362	362	362	362	362
R-squared	0.164	0.139	0.154	0.139	0.206
Deal, Firm, and Country Controls	Yes	Yes	Yes	Yes	Yes
Acquirer Industry, Target Industry, and Year FE	Yes	Yes	Yes	Yes	Yes

**Table 8. Robustness and Alternative Explanations: Instrumental Variable Approach**

This table shows results for a two-stage instrumental variable regression (IV-2SLS) where the dependent variable in the first stage (Model (1)) is the acquirer's employment quality score and the independent variables are the industry-year average of the salaries and benefits expenses in the focal firm's industry peers (IV), along with a cross-border deal dummy, their interaction, and a set of firm-, deal-, and country-level control variables. The dependent variable in the second stage (Model (2)) is the acquirer's three-day CAR and the main independent variable is the acquirer's instrumented pre-merger employment quality score, a cross-border deal dummy, and their interaction, along with the same set of deal- (relative deal size, dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets, and relative deal size), firm- (acquirer ROA and leverage), and country-level (labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. The underidentification test refers to the Anderson canonical correlation statistics. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

	(1)	(2)
<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	<i>1<sup>st</sup> stage: DV = Employment Quality</i>	<i>2<sup>nd</sup> stage: DV = CAR [-1, 1]</i>
Acquirer Employment Quality $t-1$		0.095** (0.046)
Acquirer Employment Quality $t-1 \times$ Cross-Border		-0.081** (0.041)
Ind-Yr Average Salaries & Benefits Expenses $t-1$	1.942*** (0.516)	
Ind-Yr Average Salaries & Benefits Expenses $t-1 \times$ Cross-Border	-1.039 (0.717)	
Cross-Border	15.39 (9.398)	4.866** (2.363)
Observations	4,511	4,511
F-test	27.10	1.954
Underidentification test (p-value)	0.004	
Deal-, Firm-, and Country-level Controls	Yes	Yes
Year FE	Yes	Yes
Acquirer Industry FE	Yes	Yes
Target Industry FE	Yes	Yes

**Table 9. Difference of Labor Regulations between Acquirer and Target Countries in Cross-Border Deals**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around cross-border deal announcements. The independent variables in are the acquirer's pre-merger employee relations in terms of employment quality, and the difference between the acquirer and target country's employment laws index (model 1), collective relations laws index (model 2), social security laws index (model 3), civil rights index (model 4), and their interactions with employment quality. Each specification includes a set of deal- (relative deal size, dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets), firm- (acquirer ROA and leverage), and country-level (acquirer country labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

<i>Dependent Variable: Acquirer CAR [-1,+1]</i>	(1)	(2)	(3)	(4)	(5)
Acquirer Employment Quality	-0.007** (0.003)	-0.006** (0.003)	-0.007** (0.003)	-0.007** (0.003)	-0.005* (0.003)
Difference Acquirer-Target Employment Laws Indices	-0.387 (0.829)				-0.061 (0.695)
Acquirer Employment Quality × Difference Acquirer-Target Employment Laws Indices	0.006 (0.012)				-0.002 (0.010)
Target Country Collective Relations Laws Index		0.098 (0.864)			-0.449 (0.792)
Acquirer Employment Quality × Difference Acquirer-Target Collective Relations Laws Indices		0.003 (0.013)			0.012 (0.012)
Target Country Social Security Laws Index			1.004 (1.260)		0.694 (1.037)
Acquirer Employment Quality × Difference Acquirer-Target Social Security Laws Indices			-0.019 (0.019)		-0.020 (0.015)
Target Country Civil Rights Index				0.030 (1.225)	0.454 (1.001)
Acquirer Employment Quality × Difference Acquirer-Target Civil Rights Indices				0.006 (0.018)	-0.001 (0.015)
Observations	1,819	1,819	1,819	1,819	1,819
R-squared	0.028	0.029	0.029	0.029	0.030
Deal and Firm Controls	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes
Acquirer Industry FE	Yes	Yes	Yes	Yes	Yes
Target Industry FE	Yes	Yes	Yes	Yes	Yes

**Table 10. Testing Alternative Explanations for the Attenuating Effect of the Cross-Border Dummy**

This table shows regression results where the dependent variable is the acquirer's three-day CAR around cross-border (Models 1-6) or cross-border and domestic (Model 7) deal announcements. The main independent variables are a dummy for whether the distance between the target's and acquirer's country is higher than the sample median (Model 1), whether the target's and acquirer's countries have a common language (Model 2) or a border (Model 3), the difference in log(GDP/Capita) between the target's and acquirer's country (Model 4), the difference in the percentage of the target's and acquirer's country's population that considers "responsibility" important (Model 5), a dummy indicating whether the target's country's population considers "job security" more important in a job than the acquirer's country's population (Model 6), all interacted with employment quality. Model 7 reports the result of regressing acquirer CAR on a dummy variable indicating that the acquirer has high employment quality (defined as the Employment Quality score above 50) and without any interaction on the subsample of domestic deals only. Each specification includes a set of deal- (dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, relative deal size, and public targets), firm- (acquirer ROA, size, and leverage), and country-level (acquirer and target country labor protection indices as in Botero et al. (2004)) control variables. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

<i>Dependent Variable: Acquirer CAR [-1,+1] Sample</i>	(1) <i>Cross- Border</i>	(2) <i>Cross- Border</i>	(3) <i>Cross- Border</i>	(4) <i>Cross- Border</i>	(5) <i>Cross- Border</i>	(6) <i>Cross- Border</i>	(7) <i>Domestic</i>
Acquirer Employment Quality t-1	-0.009** (0.005)	-0.009*** (0.003)	-0.007** (0.003)	-0.008** (0.004)	-0.007* (0.004)	-0.007** (0.003)	
Distance > Median	-0.265 (0.422)						
Acquirer Employment Quality t-1 × (Distance > Median)	0.004 (0.006)						
Target and Acquirer Country Share Common Language		-0.299 (0.542)					
Acquirer Employment Quality t-1 × (Target and Acquirer Country Share Common Language)		0.008 (0.008)					
Target and Acquirer Country Share Border			-0.148 (0.510)				
Acquirer Employment Quality t-1 × (Target and Acquirer Country Share Border)			0.003 (0.007)				
Difference in log(GDP/Capita)				0.079 (0.198)			
Acquirer Employment Quality t-1 × (Difference in log(GDP/Capita))				-0.002 (0.003)			
Target > Acquirer Country "Responsibility is Important"					-0.017 (0.016)		
Acquirer Employment Quality t-1 × (Target > Acquirer Country "Responsibility is Important")					0.0003 (0.0002)		
Target > Acquirer Country "Job Security is Important"						-0.090 (0.913)	
Acquirer Employment Quality t-1 × (Target > Acquirer Country "Job Security is Important")						-0.001 (0.011)	
Acquirer High Employment Quality (Dummy)							0.401** (0.182)
Observations	2,015	2,015	2,015	1,735	1,432	2,015	2,550
R-squared	0.031	0.033	0.032	0.036	0.044	0.032	0.036
Deal, Firm, and Country-Level Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Acquirer and Target Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes

**Table 11. Long-Run Operating Performance**

This table shows regression results where the dependent variables are the acquirer's average 2-year post-merger industry-adjusted ROA (defined as net income/assets) (Model 1), the acquirer's 2-year post-merger industry-adjusted ROS (return on sales) (Model 2), or the acquirer's Sales-to-Employees ratio (Model 3) following domestic and cross-border deal announcements. The independent variables are the acquirer's pre-merger employment quality score and the acquirer's pre-merger industry-adjusted ROA (Model 1), ROS (Model 2), or the combined industry-adjusted Sales-to-Employees ratio (Model 3). Each specification includes a set of deal- (relative deal size, dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets), firm- (acquirer ROA and leverage), and country-level (index for acquirer and target country labor regulations as in Botero et al. (2004)) control variables. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

<i>Dependent variable:</i>	(1) <i>2-Year Post-Merger Acquirer ROA</i>	(2) <i>2-Year Post-Merger Acquirer ROS</i>	(3) <i>2-Year Post-Merger Acquirer Sales/Employee</i>
Acquirer Employment Quality	0.014* (0.008)	0.002 (0.001)	0.012 (0.010)
Cross-Border	1.736** (0.796)	0.385 (0.270)	1.150* (0.666)
Acquirer Employment Quality x Cross-Border	-0.024** (0.012)	-0.004* (0.002)	-0.020** (0.009)
Pre-Merger Acquirer ROA (industry-adjusted)	0.069*** (0.025)		
Pre-Merger Acquirer ROS (industry-adjusted)		0.526** (0.259)	
Pre-Merger Combined Sales/Employees Ratio (industry-adjusted)			1.224*** (0.200)
Deal, Firm, and Country Controls	Yes	Yes	Yes
Observations	1,113	2,478	85
R-squared	0.094	0.010	0.809

## Appendix A. Variable Descriptions

<i>Deal Characteristics</i>	
Cross-Border	A dummy equal to one if the deal is labelled as “Cross-Border” in SDC, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
Public Target	A dummy equal to one if the target’s public status is “Listed”, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
Diversifying Deal	A dummy equal to one if the acquirer’s 2-digit SIC code is different from the target’s 2-digit SIC code, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
Hostile Deal	A dummy equal to one if the deal’s attitude is labelled as “Hostile” in SDC, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
All-Cash Financing	A dummy equal to one if the deal is fully financed in cash, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
Multiple Bidders	A dummy equal to one if more than one bidding firm was involved in the deal, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
<i>Firm Characteristics</i>	
Toehold	A dummy equal to one if the acquiring firm had a toehold before the acquisition, and zero otherwise. <i>Source: SDC Mergers and Acquisitions Database.</i>
Relative Deal Size	Value of the deal, divided by the market value of equity of the acquiring firm. <i>Source: SDC Mergers and Acquisitions Database.</i>
Acquirer Size	Log of the acquirer’s total assets. <i>Source: Datastream.</i>
Acquirer Leverage	Book value of the acquirer’s total liabilities, divided by the market value of assets. <i>Source: Datastream.</i>
Acquirer ROA	Acquirer’s EBITDA, divided by the book value of assets. <i>Source: Datastream.</i>
Serial Acquirer	A dummy equal to one if the acquiring firm made more than 10 takeover announcements over the sample period, and zero otherwise.
<i>Country Labor Regulations</i>	
Employment Laws Index	Measures the protection of labor and employment laws, calculated as the average of (i) alternative employment contracts; (ii) cost of increasing hours worked; (iii) cost of firing workers; and (iv) dismissal procedures. <i>Source: Botero et al. (2004).</i>
Collective Relations Laws Index	Measures the protection of collective relations laws, calculated as the average of (i) labor union power and (ii) collective disputes. <i>Source: Botero et al. (2004).</i>
Social Security Laws Index	Measures social security benefits, based on measures of (i) old age, disability and death benefits; (ii) sickness and health benefits; and (iii) unemployment benefits. <i>Source: Botero et al. (2004).</i>
Civil Rights Index	Measures the degree of protection of vulnerable groups against employment discrimination, based on measures of (i) labor discrimination on grounds of race is expressly prohibited by law, (ii) labor discrimination on grounds of gender is expressly prohibited by law, (iii) statutory duration of maternity leave with retention of 100% of earnings, (iv) minimum working age, and (v) mandatory minimum wage. <i>Source: Botero et al. (2004).</i>
<i>Employee-Engagement</i>	

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Employment Quality	A score measuring the firm’s commitment and effectiveness towards providing high-quality employment benefits and job conditions, such as distributing fair employment benefits, focusing on long-term employment growth and stability, avoiding lay-offs, and maintaining relations with trade unions. The score ranges from 0 to 100, with larger value indicating better employment relations. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Health and Safety	A score measuring the firm’s commitment and effectiveness towards providing a healthy and safe workplace, concern for physical and mental health, well-being, and stress levels of all employees. The score ranges from 0 to 100, with larger value indicating better employment relations. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Workforce Diversity	A score measuring the firm’s commitment and effectiveness towards maintaining diversity and equal opportunities in its workforce, such as promoting an effective work-life balance, a family-friendly environment, and equal opportunities regardless of age, gender, ethnicity, religion, or sexual orientation. The score ranges from 0 to 100, with larger values indicating better employment relations. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Training and Development	A score measuring the firm’s commitment and effectiveness towards providing training and development (education) for its workforce. The score ranges from 0 to 100, with larger values indicating better employee relations. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Bonus Plan Dummy	A dummy indicator for whether the firm provides a bonus plan to at least the middle management level whether employees' compensation based on personal or company-wide targets. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Fringe Benefits Dummy	A dummy indicator for whether the firm provides its employees with a pension fund, health care, or other insurances. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Wage Ratio Employees/CEO	Ratio between an average worker’s salary and the CEO’s salary, measured as Average Salaries and Benefits/Highest Salary. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Net Employment Creation	Growth in the firms’ employee base, measured as Number of Employees, scaled by last year’s Number of Employees, -1. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Trade Union Relations Policy	A dummy indicator for whether the firm has a policy in place to ensure good relations with trade unions. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>
Job Security Policy	A dummy indicator whether the firm has a policy in place to maintain job security. <i>Source: Thomson Reuters ASSET4 ESG Database.</i>

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*Mechanisms*

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Repeat Acquisition	A dummy equal to one if the firm has acquired a firm in the target’s country in the past. It is equal to zero if the firm has not previously acquired any firms in the target’s country.
Target Country > Acq. Country “Good Pay is Important”	A dummy equal to one if the target’s country is in the top tercile and the acquirer’s country is in the bottom tercile for the variable “importance of good pay in a job”, aggregated at the country level. <i>Source: World Value Survey.</i>
Target Country > Acq. Country “Saving Money is Important”	A dummy equal to one if the target’s country is in the top tercile and the acquirer’s country is in the bottom tercile for the variable “saving money is an important child quality”, aggregated at the country level. <i>Source: World Value Survey.</i>
Absence of Economic Nationalism in Target Country	A dummy equal to one if the target country’s government has a rightwing/liberal main executive party. It is equal to zero if it has a leftwing/nationalist main executive party. <i>Source: Database of Political Institutions.</i>

Acquirer and Target Country Low Union Strength	A dummy equal to one if the target's and acquirer's country are in the bottom tercile for the variable "confidence in unions", aggregated at the country level. <i>Source: World Value Survey.</i>
Ind-Yr Average Salaries & Benefits Expenses	Firms' annual expenses in terms of employee salaries and benefits, averaged annually by industry. <i>Source: Worldscope.</i>
Distance > Median	A dummy equal to one if the log distance between the acquirer's and target's capitals is above the sample median, and zero otherwise. <i>Source: CEPII.</i>
Target and Acquirer Countries Share Common Language	A dummy equal to one if the acquirer's and target's country have an official language in common, and zero otherwise. <i>Source: CEPII.</i>
Target and Acquirer Countries Share Common Border	A dummy equal to one if the acquirer's and target's countries share a common border, and zero otherwise. <i>Source: CEPII.</i>
Low-Tech Deal	A dummy equal to one if the target and acquirer are in low-tech industries, as defined by SDC. <i>Source: SDC.</i>
Difference in log(GDP/Capita)	The difference in log(GDP/Capita) between the acquirer's and target's countries. <i>Source: CEPII.</i>
Target Country > Acq. Country "Responsibility is Important"	A dummy equal to one if the target's country is in the top tercile and the acquirer's country is in the bottom tercile for the variable "a feeling of responsibility is important", aggregated at the country level. <i>Source: World Value Survey.</i>
Target Country > Acq. Country "Job Security is Important"	A dummy equal to one if the target's country is in the top tercile and the acquirer's country is in the bottom tercile for the variable "job security is important in a job", aggregated at the country level. <i>Source: World Value Survey.</i>

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## Appendix B. Industry Distribution

This table shows the sample distribution by acquirer industry and year for the domestic and cross-border deals in our sample.

Acquirer Industry (Fama-French 48)	Year												Total
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	
Agriculture	0	0	2	1	3	0	3	4	6	7	2	0	28
Food Products	2	0	3	7	6	7	5	16	16	16	11	6	95
Candy & Soda	0	1	0	5	4	0	1	2	5	3	4	0	25
Beer & Liquor	6	5	6	3	3	4	2	1	5	11	1	2	49
Tobacco Products	1	1	0	0	3	1	4	0	1	1	0	1	13
Recreation	2	1	2	3	7	7	6	0	2	2	4	0	36
Entertainment	1	0	0	3	1	2	1	1	1	3	1	0	14
Printing and Publishing	3	4	4	11	6	3	2	9	8	5	6	2	63
Consumer Goods	0	1	4	3	4	5	2	16	9	13	6	4	67
Apparel	0	2	3	1	2	1	1	1	1	2	0	0	14
Healthcare	1	0	3	2	5	1	0	4	1	3	3	2	25
Medical Equipment	9	4	11	13	8	12	8	10	11	13	12	5	116
Pharmaceutical Products	6	4	8	19	18	15	21	20	22	14	16	8	171
Chemicals	3	6	7	13	9	12	6	17	16	21	17	6	133
Rubber and Plastic Products	0	0	0	0	1	0	2	2	3	2	1	2	13
Textiles	0	0	2	0	1	1	1	2	2	1	2	0	12
Construction Material	5	3	6	9	8	8	6	8	7	10	5	3	78
Construction	3	2	7	9	19	5	12	9	8	5	11	4	94
Steel Works Etc	4	2	9	8	9	10	11	15	14	8	4	8	102
Fabricated Products	0	0	0	0	0	0	4	2	0	0	0	0	6
Machinery	4	1	8	15	15	9	15	13	23	21	9	8	141
Electrical Equipment	2	2	3	1	2	3	2	2	7	3	7	1	35
Automobiles and Truck	1	3	2	4	8	7	3	3	7	3	5	3	49
Aircraft	3	4	0	2	4	4	3	4	5	2	5	1	37
Shipbuilding, Railroad Equipment	0	0	0	1	0	0	4	1	0	1	1	1	9
Defense	2	0	1	1	2	5	1	2	0	0	1	2	17
Precious Metals	0	0	3	3	2	6	25	18	22	16	10	2	107
Non-Metallic and Industrial Metal Mining	0	0	4	5	8	11	15	17	19	15	7	4	105
Coal	0	0	1	2	5	3	2	6	1	4	1	0	25
Petroleum and Natural Gas	5	2	15	20	25	23	36	30	31	32	17	10	246
Utilities	13	7	9	20	11	21	19	20	14	14	4	3	155
Communication	8	6	28	24	18	18	30	19	24	18	23	13	229
Personal Services	0	0	3	4	2	0	4	2	3	2	4	1	25
Business Services	24	21	41	42	38	49	29	35	47	53	43	37	459
Computers	1	5	6	6	11	5	11	11	11	14	12	2	95
Electronic Equipment	11	10	13	23	22	13	19	17	13	23	11	11	186
Measuring and Control Equipment	1	2	7	8	9	3	2	3	3	6	1	3	48
Business Supplies	2	1	2	2	1	2	3	3	3	5	2	3	29
Shipping Containers	3	2	1	3	3	0	1	0	2	3	1	1	20
Transportation	4	4	12	12	8	13	10	15	5	8	9	4	104
Wholesale	8	3	9	17	14	10	13	11	17	12	13	6	133
Retail	1	1	4	19	15	22	14	15	27	22	18	14	172
Restaurants, Hotels, Motels	2	5	6	6	3	4	2	0	7	2	3	3	43
Banking	12	19	36	44	49	29	24	31	38	30	21	18	351
Insurance	5	5	5	11	20	15	9	12	9	12	12	11	126
Real Estate	1	4	4	3	5	4	4	4	8	3	4	5	49
Trading	7	10	42	43	51	28	28	41	35	42	32	18	377
Other	2	1	2	5	2	12	2	2	1	8	2	0	39
<b>Total</b>	<b>168</b>	<b>154</b>	<b>344</b>	<b>456</b>	<b>470</b>	<b>413</b>	<b>428</b>	<b>476</b>	<b>520</b>	<b>514</b>	<b>384</b>	<b>238</b>	<b>4,565</b>

### Appendix C: Sample Distribution by Acquirer Country

This table shows the sample distribution by acquirer country for the domestic and cross-border deals in our sample.

Acquirer Nation	Freq.	Percent	Cumulative Percent
Argentina	3	0.07	0.07
Australia	172	3.77	3.83
Austria	27	0.59	4.42
Belgium	35	0.77	5.19
Brazil	84	1.84	7.03
Canada	289	6.33	13.36
Chile	9	0.2	13.56
China	61	1.34	14.9
Colombia	10	0.22	15.12
Czech Republic	1	0.02	15.14
Denmark	26	0.57	15.71
Finland	44	0.96	16.67
France	237	5.19	21.86
Germany	54	1.18	23.04
Greece	26	0.57	23.61
Hong Kong	16	0.35	23.96
Hungary	4	0.09	24.05
India	31	0.68	24.73
Indonesia	10	0.22	24.95
Ireland-Rep	28	0.61	25.56
Israel	3	0.07	25.63
Italy	116	2.54	28.17
Japan	672	14.72	42.89
Malaysia	21	0.46	43.35
Mexico	17	0.37	43.72
Morocco	1	0.02	43.75
Netherlands	58	1.27	45.02
New Zealand	3	0.07	45.08
Nigeria	1	0.02	45.1
Norway	54	1.18	46.29
Peru	2	0.04	46.33
Philippines	11	0.24	46.57
Poland	26	0.57	47.14
Portugal	16	0.35	47.49
Russian Fed	51	1.12	48.61
Singapore	37	0.81	49.42
South Africa	49	1.07	50.49
South Korea	86	1.88	52.38
Spain	114	2.5	54.87
Sweden	81	1.77	56.65
Switzerland	112	2.45	59.1
Taiwan	35	0.77	59.87
Thailand	13	0.28	60.15
Turkey	7	0.15	60.31
Ukraine	6	0.13	60.44
United Kingdom	593	12.99	73.43
United States	1,213	26.57	100
<b>Total</b>	<b>4,565</b>	<b>100</b>	

### Appendix D1: Employment Engagement by Acquirer Country

<i>Acquirer Country</i>	<i>Employment Quality</i>	<i>Training &amp; Development</i>	<i>Workforce Diversity</i>	<i>Health &amp; Safety</i>
Argentina	32.40	65.44	29.92	92.64
Australia	41.04	38.83	53.87	54.18
Austria	54.14	67.91	48.09	39.36
Belgium	64.09	64.45	45.45	53.00
Brazil	68.48	68.05	55.06	64.94
Canada	39.25	34.02	37.64	47.46
Chile	31.49	75.57	26.66	24.19
China	51.34	44.01	25.96	32.45
Colombia	46.97	70.07	37.78	60.28
Czech Republic	69.88	77.75	57.75	28.70
Denmark	57.55	51.28	47.34	55.14
Finland	67.41	80.49	48.99	60.50
France	75.68	80.27	75.15	70.69
Germany	76.78	83.03	72.10	64.23
Greece	68.97	71.89	47.03	49.24
Hong Kong	59.87	52.90	29.53	32.32
Hungary	89.23	78.68	90.59	91.11
India	44.17	63.48	40.72	56.01
Indonesia	77.85	82.32	20.98	48.08
Ireland-Rep	48.92	54.77	36.26	60.90
Israel	40.17	53.52	27.13	22.58
Italy	65.19	67.30	55.06	54.92
Japan	35.38	49.26	56.11	43.16
Malaysia	43.12	60.08	32.29	40.76
Mexico	48.90	39.07	43.33	41.41
Morocco	61.42	91.92	15.37	13.76
Netherlands	67.16	74.46	59.01	66.74
New Zealand	69.24	45.92	46.72	51.77
Nigeria	10.76	24.15	22.39	36.98
Norway	71.62	68.91	78.47	68.48
Peru	34.57	38.57	16.40	65.72
Philippines	39.43	40.25	19.90	26.20
Poland	37.32	40.67	15.15	25.93
Portugal	71.44	68.41	38.12	54.58
Russian Fed	65.62	66.16	26.20	52.46
Singapore	34.12	61.59	30.50	43.31
South Africa	60.13	69.84	63.02	80.66
South Korea	50.96	57.32	44.88	45.92
Spain	78.55	83.34	73.74	69.33
Sweden	70.54	61.76	57.43	45.61
Switzerland	68.12	74.26	61.16	68.41
Taiwan	63.94	58.27	40.55	40.83
Thailand	57.37	63.45	46.76	65.24
Turkey	61.26	83.49	54.28	35.21
Ukraine	6.80	21.58	10.50	26.18
United Kingdom	64.47	64.34	58.79	62.57
United States	48.68	39.29	49.64	41.38
<b>Total</b>	<b>53.43</b>	<b>54.01</b>	<b>52.84</b>	<b>51.06</b>

### Appendix D2: Employee-Engagement by Acquirer Industry

<i>Acquirer Country</i>	<i>Employment Quality</i>	<i>Training &amp; Development</i>	<i>Workforce Diversity</i>	<i>Health &amp; Safety</i>
Agriculture	39.11	63.68	33.83	62.72
Food Products	48.97	52.89	47.29	51.36
Candy & Soda	60.12	65.50	60.64	68.34
Beer & Liquor	53.09	57.60	52.77	50.77
Tobacco Products	56.56	72.32	67.90	75.18
Recreation	67.06	75.77	82.93	84.33
Entertainment	37.71	30.51	34.23	35.60
Printing and Publishing	51.93	53.60	57.89	41.32
Consumer Goods	67.16	63.90	65.03	67.29
Apparel	38.03	32.93	35.95	35.08
Healthcare	48.77	47.27	51.31	35.58
Medical Equipment	54.73	57.28	55.68	48.56
Pharmaceutical Products	54.55	50.76	58.70	58.86
Chemicals	56.58	60.98	62.46	74.67
Rubber and Plastic Products	46.17	52.71	52.82	47.38
Textiles	29.16	46.58	58.71	55.80
Construction Material	55.44	56.83	47.19	68.62
Construction	54.29	62.87	50.09	57.95
Steel Works Etc	56.20	60.69	47.43	64.61
Fabricated Products	26.36	41.31	26.45	27.67
Machinery	46.22	53.02	44.94	51.43
Electrical Equipment	59.70	62.68	63.86	61.10
Automobiles and Truck	55.20	71.49	61.77	69.38
Aircraft	57.26	64.19	56.70	72.50
Shipbuilding, Railroad Equipment	67.50	69.95	42.64	43.21
Defense	57.35	52.76	57.65	61.29
Precious Metals	37.69	38.26	34.76	52.93
Non-Metallic and Industrial Metal Mining	53.33	52.22	46.36	69.27
Coal	55.99	66.54	57.90	75.97
Petroleum and Natural Gas	52.52	49.26	48.67	64.20
Utilities	64.73	68.13	67.54	71.80
Communication	58.40	56.55	58.28	49.74
Personal Services	41.04	33.22	42.94	32.91
Business Services	51.76	48.71	49.20	43.61
Computers	46.65	50.94	49.90	43.67
Electronic Equipment	49.55	49.72	49.89	47.72
Measuring and Control Equipment	43.21	36.69	43.77	43.81
Business Supplies	65.95	60.88	63.32	68.39
Shipping Containers	50.28	65.73	57.95	60.30
Transportation	50.88	49.45	44.31	46.04
Wholesale	45.46	51.88	57.29	39.91
Retail	44.58	51.38	50.45	36.88
Restaurants, Hotels, Motels	67.89	59.72	59.75	43.18
Banking	64.45	62.17	56.84	42.35
Insurance	62.54	63.38	69.29	40.84
Real Estate	45.27	47.99	51.50	38.91
Trading	50.03	44.50	45.66	35.00
Other	53.21	51.19	61.16	55.31
<b>Total</b>	<b>53.43</b>	<b>54.01</b>	<b>52.84</b>	<b>51.06</b>

### Appendix E. Employee-Engagement and Announcement CARs: Domestic versus Cross-Border Takeovers

This table shows regression results where the dependent variable is the acquirer's three-day CAR around domestic (Models (1)-(5)) and cross-border (Models (6)-(10)) deal announcements. The independent variables are the acquirer's pre-merger employee relations scores in terms of employment quality, health and safety, workforce diversity, and employee training and development, and a set of deal- (relative deal size, dummies for serial acquirers, toeholds, multiple bidders, all-cash financed deals, hostile deals, diversifying deals, and public targets, and relative deal size), firm- (acquirer ROA and leverage), and country-level (acquirer country labor protection indices as in Botero et al. (2004)) control variables. Models (6) –(10) additionally include target country labor protection indices. Each specification includes year, acquirer industry, and target industry fixed effects. Robust standard errors are reported in parentheses. \*, \*\* and \*\*\* stand for statistical significance at the 10%, 5%, and 1%, respectively.

Dependent Variable: Acquirer CAR [-1,+1]	Domestic Deals					Cross-Border Deals				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Acquirer Employment Quality t-1	0.008** (0.003)				0.008** (0.004)	-0.009** (0.003)				-0.010*** (0.004)
Acquirer Health & Safety t-1		0.003 (0.003)			0.002 (0.004)		-0.002 (0.004)			-0.0003 (0.004)
Acquirer Workforce Diversity t-1			0.003 (0.003)		0.001 (0.004)			-0.0009 (0.003)		0.002 (0.004)
Acquirer Training and Development t-1				0.0009 (0.003)	-0.004 (0.004)				-0.002 (0.004)	0.002 (0.005)
Serial Acquirer Dummy	0.008 (0.203)	-0.004 (0.202)	-0.006 (0.203)	-0.008 (0.203)	0.021 (0.203)	-0.195 (0.211)	-0.191 (0.211)	-0.190 (0.211)	-0.184 (0.212)	-0.201 (0.212)
Acquirer ROA t-1	2.296** (0.960)	2.330** (0.964)	2.368** (0.961)	2.385** (0.965)	2.313** (0.964)	-1.857 (1.342)	-2.083 (1.347)	-2.091 (1.348)	-2.053 (1.352)	-1.926 (1.344)
Acquirer Leverage t-1	-0.575 (0.587)	-0.595 (0.588)	-0.599 (0.588)	-0.596 (0.588)	-0.569 (0.587)	0.498 (0.629)	0.512 (0.632)	0.519 (0.632)	0.517 (0.633)	0.505 (0.629)
Toehold Dummy	-0.064 (0.231)	-0.052 (0.232)	-0.056 (0.232)	-0.054 (0.232)	-0.053 (0.232)	-0.039 (0.281)	-0.042 (0.281)	-0.041 (0.281)	-0.047 (0.281)	-0.036 (0.282)
Acquirer Size	0.0006 (0.084)	0.036 (0.0834)	0.032 (0.086)	0.051 (0.087)	0.009 (0.088)	-0.025 (0.090)	-0.072 (0.092)	-0.075 (0.095)	-0.070 (0.093)	-0.050 (0.098)
Multiple Bidders Dummy	-0.611 (0.613)	-0.607 (0.615)	-0.617 (0.616)	-0.622 (0.615)	-0.604 (0.613)	-0.780 (0.481)	-0.786 (0.484)	-0.781 (0.484)	-0.781 (0.485)	-0.779 (0.481)
All-Cash Financing Dummy	0.159 (0.189)	0.151 (0.189)	0.151 (0.189)	0.152 (0.189)	0.161 (0.189)	0.160 (0.207)	0.162 (0.207)	0.163 (0.208)	0.161 (0.207)	0.157 (0.208)
Hostile Deal Dummy	1.676** (0.825)	1.641* (0.843)	1.661** (0.846)	1.656** (0.843)	1.654** (0.822)	-0.762 (0.993)	-0.747 (0.995)	-0.749 (0.994)	-0.746 (0.991)	-0.757 (0.998)
Diversifying Deal Dummy	0.0352 (0.200)	0.0164 (0.200)	0.0245 (0.200)	0.0209 (0.200)	0.0348 (0.200)	-0.187 (0.224)	-0.173 (0.225)	-0.174 (0.225)	-0.177 (0.225)	-0.185 (0.224)
Public Target Dummy	-0.609*** (0.189)	-0.619*** (0.189)	-0.624*** (0.190)	-0.616*** (0.189)	-0.607*** (0.189)	0.145 (0.228)	0.151 (0.228)	0.150 (0.228)	0.148 (0.228)	0.148 (0.228)
Relative Deal Size	-0.314 (0.343)	-0.320 (0.343)	-0.318 (0.343)	-0.325 (0.343)	-0.310 (0.343)	-0.158 (0.175)	-0.167 (0.171)	-0.166 (0.171)	-0.167 (0.172)	-0.157 (0.175)
Constant	0.345 (2.353)	0.179 (2.342)	0.217 (2.343)	0.198 (2.344)	0.269 (2.351)	-1.569 (1.705)	-1.384 (1.697)	-1.447 (1.717)	-1.393 (1.702)	-1.451 (1.716)
Observations	2,550	2,550	2,550	2,550	2,550	2,015	2,015	2,015	2,015	2,015
R-squared	0.075	0.073	0.073	0.073	0.075	0.058	0.055	0.055	0.055	0.059
Year, Acq. Ind. And Target Ind. FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Acquirer Country Level Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Target Country Level Controls	No	No	No	No	No	Yes	Yes	Yes	Yes	Yes