# Article information:

Labor protection and dynamic leverage adjustments in the OECD countries - ScienceDirect  
<https://www.sciencedirect.com/science/article/pii/S1059056022002453>

# Article summary:

1. Labor protection laws impact firms' leverage adjustment speed.

2. Stringent labor regulations increase labor adjustment costs and reduce operating flexibility, leading to slower leverage adjustments.

3. The effectiveness of a country's legal enforcement also impacts the association between labor regulations and leverage SOA.

# Article rating:

May be slightly imbalanced: The article presents the information in a generally reliable way, but there are minor points of consideration that could be explored further or claims that are not fully backed by appropriate evidence. Some perspectives may also be omitted, and you are encouraged to use the research topics section to explore the topic further.

# Article analysis:

The article "Labor protection and dynamic leverage adjustments in the OECD countries" explores the impact of labor regulations on firms' leverage adjustment speed. The authors develop two competing hypotheses based on the literature that examines the essential roles of labor market mechanisms on firms' financing decisions. They use the EPL index developed by the Organization for Economic Cooperation and Development (OECD) for its 19 member countries over the 1985–2007 period to test their hypotheses.

The article provides a comprehensive review of prior studies that have examined factors affecting firms' leverage adjustments, including firm-level factors such as cash flows, corporate governance, crash risk, debt covenants, and news media coverage, as well as country-level determinants such as macroeconomic conditions, institutional arrangements, and political uncertainty. However, it notes that previous literature has largely ignored the importance of labor regulations related to employees in determining leverage adjustments.

The authors present two competing hypotheses regarding the impact of labor regulations on firms' leverage adjustment speed. On one hand, they argue that strict EPLs increase labor adjustment costs and reduce operating flexibility, negatively impacting corporate performance and growth. On the other hand, they suggest that stringent employment protections can lower firms’ financial risks and thus lower external financing costs.

The article's baseline results show that when labor protection becomes more stringent in a country, firms operating in that country adjust more slowly to their target leverage ratios. The authors find robust evidence supporting their first hypothesis that strong EPLs promote firms’ leverage adjustment costs and reduce leverage SOA.

However, there are potential biases in this study. For example, it is possible that other unobserved factors may be driving both changes in labor regulations and changes in firms' leverage adjustment speeds. The authors attempt to address endogeneity concerns by using an instrumental variable approach using legal origin as an instrument for labor protection. They also control for additional variables to capture potential confounding impacts.

Another limitation is that the study only examines the impact of labor regulations on leverage adjustment speed and does not consider other potential effects, such as the impact on firms' investment activities or governance. Additionally, the study only focuses on OECD countries and may not be generalizable to other regions.

Overall, the article provides valuable insights into the impact of labor regulations on firms' leverage adjustment speed. However, readers should be aware of potential biases and limitations in the study's methodology and scope.

# Topics for further research:

* Impact of labor regulations on firms' investment activities
* Corporate governance and leverage adjustments
* Macroeconomic conditions and firms' financing decisions
* Political uncertainty and corporate performance
* Labor market mechanisms and external financing costs
* Labor protection and firms' growth strategies

# Report location:

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