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Foreign direct investment and employment rights in South-Eastern Europe

Geoffrey Wood, Shuxing Yin, Khelifa Mazouz and Jeremy Eng-Tuck Cheah*

The dominant neoliberal policy community holds that a reduction in employment rights and social protection is likely to promote economic recovery and growth. It has been suggested that investors are likely to shun countries where such rights are strong; in contrast, radical labour market deregulation is seen as encouraging both local business and multinationals to invest. This study explores whether labour market deregulation in South-Eastern Europe has really encouraged multinationals to invest in the region. We find that the weakening of important aspects of employment rights under the law appears to detract from, rather than encourage, foreign direct investment (FDI). We also show that stronger employment rights are more likely to attract FDI when the host country is located within the European Union. This finding suggests that the complementarities associated with stronger employment rights and more committed labour may offset the overall deterrent effects of the greater regulation associated with EU membership.

Key words: South-Eastern Europe, Foreign direct investment, Employment rights, Deregulation
JEL classifications: F16, F21

1. Introduction

This study investigates the impact of employment regulation on foreign direct investment (FDI) inflows to the South-Eastern European (SEE) region. An influential body of work suggests that stronger property owner rights is likely to optimise growth and, conversely, that countervailing employee rights under the law will make economies less attractive to investors, leading to poor macroeconomic performance (Botero *et al.*, 2004; La Porta *et al.*, 2008; Lehmann and Muravyev, 2009). Some studies, including Lehmann and Muravyev (2009), argue that there has been a trend towards labour market liberalisation across the region, most notably in the aftermath of the 2008 financial crisis, even if, in some areas, aspects of Europeanisation may have counter-strengthened worker rights.

The SEE region has been particularly severely affected by the 2008 economic crisis, even when compared with the rest of Central and Eastern Europe (Gardo and Martin,

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Address for correspondence: Shuxing Yin, Sheffield University Management School, University of Sheffield, Sheffield S10 1FL, UK; email: shuxing.yin@sheffield.ac.uk

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2010). Greece, which had borrowed the most from the advanced economies, was particularly badly affected (Berkmen *et al.*, 2009). Several post-state socialist countries in the region were, in the run-up to the 2008 crisis, also heavily over-reliant on foreign borrowing, with relatively high leverage and structural current account deficits (Berkmen *et al.*, 2009, p. 8), when compared with other former post-state socialist countries such as Slovakia, Poland and the Czech Republic (Bordo *et al.*, 2011). Hence a number of countries within the region were forced to turn to the International Monetary Fund (IMF), including Greece (initial IMF/EU loan of €110 billion in 2010, followed by subsequent loan tranches), Serbia (US$518 million in 2008) and Romania (US$17.1 billion in 2009), whilst others, such as Bulgaria and Macedonia, have come close to needing IMF bailouts (IMF, 2013). In turn, such countries have been forced to adopt a wide range of austerity measures and, to a lesser or greater extent, embarked on new rounds of labour market reform. For example, in Greece, *inter alia*, the power to set minimum wages was taken away from the social partners, the collective bargaining system decentralised and job security in the public sector weakened through a series of legal reforms, which were consolidated in legislation in 2012 and implemented as part of the bailout agreement (Karantinos, 2012, pp. 22–4). In 2011, Romania amended its labour code to weaken security of tenure and changed the laws governing social dialogue to make collective bargaining more flexible (European Commission, 2013, pp. 16–17). All these developments raise the question as to whether labour market deregulation in the SEE region has had any impact on the investment flows to the region. In other words, are less regulated labour markets more attractive to investors? And what has been the effect of labour market deregulation on FDI choices?

In this study we focus on the SEE countries, which include Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYRO Macedonia,[1] Greece, Montenegro, Romania, Serbia, and Serbia and Montenegro.[2] We recognise that there are problems in demarcating the countries in the region and that others could have been included. However, Kosovo has no recorded FDI data from the United Nations Conference on Trade and Development (UNCTAD) as it has only been independent since 2008 and has yet to attain United Nations membership. As part of the former Soviet Union, Moldova is in many respects more closely linked to the Commonwealth of Independent States (CIS) region and is geographically removed from the Balkans. Again, although part of the former Yugoslavia, it can be argued that Slovenia has converted into a fully fledged coordinated market economy with much more in common with the Rhineland region than the Balkans (Lane, 2007).

The remainder of the paper is structured as follows. Section 2 revisits the existing theoretical and applied debates on the relationship between labour market deregulation and competitiveness. Section 3 provides a brief review of the related literature and states the hypotheses. Section 4 discusses the data, variable definitions and empirical methods. Section 5 presents the empirical results and Section 6 contains concluding remarks.

2. Labour market deregulation and competitiveness: theoretical and applied issues

The role of labour market flexibility in explaining diverging patterns of FDI across different countries has been widely debated in the literature. Several studies, including Javorcik and Spatareanu (2005) and Lehmann and Muravyev (2009), argue that

[1] Former Yugoslav Republic of Macedonia, the term employed by many international bodies. The use of this term does not denote any views by the authors on the Macedonian Question.

[2] Serbia and Montenegro ceased to exist in 2006.

reductions in employment rights and social protection are likely to promote economic recovery and growth. It has also been suggested that strong employment rights—both in terms of social and employment protection—are inimical to job creation and, through diluting investor rights, to overall growth (Botero *et al.*, 2004, p. 1379, La Porta *et al.*, 2008, p. 324). Hence investors may choose to avoid countries where employment rights are strong.

However, it could be argued that stronger employment protection means that labour is less of a readily disposable commodity, forcing firms to take recruitment and selection more seriously and to use existing labour more effectively. This in turn may result in increased employee commitment, making for higher productivity and greater organisational effectiveness in the long run (Harcourt and Wood, 2007; An *et al.*, 2008). Hence stronger employment protection may discourage firms from excessive short-termism and encourage the engendering of deeper and denser ties not only with employees, but also with customers and suppliers. It has also been suggested that stronger employment protection may engender local production networks in denser and thicker interorganisational ties (Hall and Soskice, 2001; Deeg and Jackson, 2007). Therefore firms may attract investors on account of the advantages conferred by such production networks (Whitley, 1999).

Empirical evidence on the issue is mixed (Kucera, 2001; Javorcik and Spatareanu, 2005; Dibben *et al.*, 2011). It should be recognised that there are a number of emerging markets with weak or ineffective employment regulation that have been highly successful in attracting FDI, including India, China and Vietnam. However amongst low-wage economies, FDI has been concentrated towards those with large domestic markets or rich natural resources. Many African economies with weak or ineffective employment regulation have been very much less successful in attracting FDI than their Asian counterparts, especially in non-primary sectors (see Wood *et al.*, 2014). We argue that an important limitation of the existing empirical work is that most studies have tended to focus on the impact of relative employment rights at a particular time, rather than exploring the impact of their changes on FDI flows. This is a particularly serious limitation given that a study of the impact of employment rights at different times is likely to yield very different results.

Although La Porta *et al.* (2008) argue that different legal traditions exert long-term effects that are difficult to depart from, critics have argued that legal origin or legislative tradition are not always an accurate guide to employment regulation and the time period covered by their studies is deliberately selective to show less regulated systems in a more positive light (Dam, 2007; Deakin, 2009). Moreover many countries have mixed or hybrid legal systems with variations on regional lines (e.g. Scotland versus the rest of the UK) or in terms of different aspects of law (e.g. South Africa) (Deakin, 2009). Even in common law countries such as the UK, key aspects of English corporate law owe more to the direct effects of specific items of legislation than past court decisions (Dam, 2007; Deakin, 2009). Therefore, the law should be seen as more diverse and dynamic than suggested by the legal origin literature, and, which would suggest that assumptions of investor behaviour cannot be predicted by legal family (Dam, 2007; Deakin, 2009). This study uses panel regressions to examine the relationship between employment rights and FDI flows dynamically. More specifically it explores the impact of employment rights and changes across the SEE region on FDI. In contrast to the previous studies that use a single index to measure employment rights, our study investigates the dynamic

relationship between FDI flows and key dimensions of labour market regulation, including rigidity of hours and hiring and firing regulation.[3] Such analysis allows us to identify, with greater precision, the aspects of labour market regulation that do affect FDI inflows.

3. Brief review of related literature and hypotheses

Variations in property owner and employee rights might not only impact on organisational performance and strategies, but also on decisions to invest in different settings. However the latter will potentially be moulded not only by regulatory but also physical resources, relative development, the nature of labour and consumer markets and government fiscal and industrial policies. At the same time, regulatory and government policy choices have dominated applied debates, as countries cannot readily change their natural endowments or developmental history.

3.1 The determinants of FDI: existing evidence

A large body of the FDI literature has focused on the determinants of investment locations. Country-level studies tend to divide the determinants of FDI inflows into non-policy-related factors, such as market size, natural resources, foreign exchange risk and economic growth, and policy-related ones, which include tax structure, investment incentives and labour market and industrial relations regulation.[4] This study focuses mainly on the role of the host country's labour market flexibility in determining FDI inflows. Previous empirical studies on the impact of labour market flexibility on FDI inflows have tended to use the average wage rate as a measure of labour costs (see, e.g., Flamm, 1984; Cheng and Kwan, 2000; Fung *et al.*, 2002) with little attention given to the non-wage aspects of labour costs, which include hiring and firing costs.[5] This study contributes to filling this gap in the literature, through investigating the role of changes in the regulation governing the non-wage aspects of labour markets in determining FDI inflows. Specifically we study the impact of labour market flexibility and its components, including hiring, firing and hours at work, on foreign investors' decisions.

The extant literature suggests that the relationship between labour market flexibility and FDI inflows is hard to predict. Several studies, including Botero *et al.* (2004) and La Porta *et al.* (2008), argue that strong employment rights—both in terms of social and employment protection—are inimical to job creation and, through diluting owner rights, to growth. It has further been argued that investors are likely to be sensitive to anything that might dilute their property rights and are likely to avoid settings where employment rights are stronger (Javorcik and Spatareanu, 2005; Campos and Kinoshita, 2008). However other work suggests a positive interaction effect between FDI and the quality of human capital (Dunning and Lundan, 2008, p. 317). In turn

[3] Parcon (2008) also disaggregates the labour market flexibility index into components, but his cross-sectional analysis does not take into consideration the time variations in the FDI flows and employment rights.

[4] See Cooke (1997, 2001), Cooke and Noble (1998), Yeyati *et al.* (2002), Nicoletti *et al.* (2003), Onyeiwu and Shrestha (2004), Blonigen (2005), Addison *et al.* (2006) and Whyman and Baimbridge (2006) for a detailed review of these factors.

[5] Existing evidence in this area is mixed, with some studies showing that higher wages discourage FDI inflows (Culem, 1988; Cheng and Kwan, 2000; Bellak *et al.*, 2007) and others, including Gupta (1983) and Wheeler and Mody (1992), finding that wages are not related, and even positively related, to FDI inflows.

this would suggest that there is more to FDI than the relative disposability of labour: FDI may be driven by the need for further efficiency gains or to access strategic assets, which in turn may include human capabilities (Dunning and Lundan, 2008, p. 470).

In looking across Eastern Europe, Bandelj (2008) argues that FDI flows are determined not so much by economic realities (gross domestic product per capita, foreign debt and budgetary shortfalls), but by the extent of privatisation and the general pro-market nature of the regime and the relative legitimation of FDI (King, 2009, p. 364). However many FDI decisions also reflect cultural dynamics and the operation of extended interpersonal networks (King, 2009, p. 365). The fact that the SEE region has been rather less successful in attracting FDI than the post-state socialist Central European countries may reflect variations in politics and society (King, 2009, p. 366). Spillman (2009) also argues that in the post-state socialist world, informal relations play a more important role in determining FDI flows to the post-state socialist world than formal regulatory institutions.

3.2 Hypothesis development

The work of La Porta and colleagues (Botero *et al.*, 2004; La Porta *et al.*, 1997, 1999) has informed the World Bank's *Doing Business* reports, with countries that have more extensive employment regulation being condemned as having worse climates for doing business (Cooney *et al.*, 2011, p. 84); in turn this may guide investment choices. The EU's Labour Market Effects of European Foreign Direct Investments (LABFDI) report of 2002 similarly suggests that an environment with weaker levels of employment rights and protection will lower labour costs, which also may attract Multinational Corporation (MNC) investments (see also Floyd, 2003).

3.2.1 Hypothesis 1A: Host country's labour market rigidity deters FDI inflows. However it could also be argued that knowledge of institutional complementarities allows firms to optimise benefits in a particular setting (Crouch, 2005), with different types of complementarity emerging in different locales. Hence no specific institutional context is necessarily superior (Hall and Soskice, 2001). As Whitley (2010) argues, firms may be attracted to a range of very different settings according to the specific advantages they each offer. Hence, as An *et al.* (2008) suggest, MNCs may be guided in their decisions by rent extraction times: while some will seek fast profits and a flexible workforce, others may be willing to wait, anticipating that increased employee commitment will yield higher returns in the long run. Thus investing in an environment with strong employment rights may be more attractive than the one with weak rights, as stronger employment protection within a more cooperative business system can add higher value in production paradigms. In other words, higher levels of commitment and optimised human capital development can be achieved by stronger employment protection (Harcourt and Wood, 2007). The *Doing Business* report has been widely criticised for its weak evidence base and an unwillingness to take on board any evidence that does not support its conclusions (Cooney *et al.*, 2011, p. 84). Although the IMF staff claim that it has no particular brief or knowledge on labour market issues, in its 2006 Consultation Staff Report on Romania it condemned the country for having an 'overly rigid' labour market, based on the *Doing Business* recommendation about ease of hiring and firing indicators, and pressed the country to further deregulate its labour market despite the fact

that reforms have already been introduced after the indicators' publication (Bakvis, 2006; see also IMF, 2006, p. 29).[6]

3.2.2 Hypothesis 1B: Host country's labour market rigidity attracts, or at least does not deter, FDI inflows. To identify those aspects of labour market regulation that are particularly significant to foreign investors, labour market flexibility is disaggregated into three components: hiring, hours at work and firing regulation. Again the relationship between these components and the FDI inflows is difficult to predict. It has been argued that if it is more difficult to dismiss inappropriately hired personnel, firms would prefer offering a short- or medium-term contract or being given the freedom to offer fixed-term contracts for any task which in turn increase employees' job security (see Botero *et al.*, 2004). Those seeking temporary work may do so owing to the absence of more secured alternatives; hence they may be willing to accept a lower rate of pay relative to regular workers, effectively lowering labour costs. Therefore, relaxing the restrictions on hiring attracts may attract MNC investments.

3.2.3 Hypothesis 2A: Host country's difficulty of hiring employees deters FDI inflows. However it can also be argued that rigidity in hiring may contribute to more collaborative employment relations in the long run, enhancing improve productivity. Greater difficulty in firing staff means that firms cannot rely on the type of numerical flexibility engendered through frequent bouts of upsizing and downsizing. If employees are likely to be with the firm for a longer time, more rigorous (and expensive) selection methods are more likely to be deployed. Taking more care in recruitment processes would in turn result in a better match between individual employees and organisations (Jenkins and Wolf, 2002). As turnover rates are lower, employers can spread the cost of training and development over many years, whilst employees have strong incentives to develop their firm-specific human capital (Brewster *et al.*, 2012). Thus rigidity in hiring may be conducive to high-value-added incrementally innovative production paradigms and may also be associated with longer-term relations between firms, suppliers and customers. Such networks may in turn be attractive to the types of investor who would benefit from such developed local government regimes (Whitley, 2010; Dunning and Lundan, 2008, p. 679).

3.2.4 Hypothesis 2B: Host country's difficulty of hiring employees attracts, or at least does not deter, FDI inflows. The potential impact of changes in labour market regulation, such as redundancy restrictions, on the costs of doing business in a foreign country can be ambiguous. MNCs must consider the flexibility and financial implications of firing workers. Restrictions on firing constrain the ability of firms to respond to market force changes. MNCs may shift production activities to countries where it is easier to

[6] There is much controversy even within the World Bank as to the relevance of the *Doing Business* index. In 2013 the Manuel Commission, commissioned by the World Bank's President Jim Kim, argued that the *Doing Business* index was a 'poor guide for policy makers' as it focuses mainly on *de Jure* (according to law) aspects of the business environment and pays limited attention to implementations and customary practices (Eurodad, 2013). It also suggested that the task of compiling the index should be moved to the World Bank's research department, so that its recommendations will be more closely founded on evidence. However the recommendations of the Manuel Commission were not implemented at the time of writing; critics have charged that the unwillingness to reform the highly influential index despite its weak factual basis reflected political rather than practical concerns (Eurodad, 2014).

make workers redundant in order to enhance numerical flexibility. Thus a reduction in redundancy restrictions could increase FDI. Görg (2005) examines the impact of hiring and firing costs on the location of US outward FDI in 33 host countries. He finds host countries with higher firing costs attract less FDI from the USA. Similarly, Javorcik and Spatareanu (2005) suggest that labour market flexibility in the host country is positively associated with FDI in some Western and Eastern European countries.

3.2.5 Hypothesis 3A: Host country's difficulty of firing employees deters FDI inflows. In contrast, Dewit *et al.*'s (2003) analysis shows that stronger employment protection may not necessarily hinder a country's ability to attract and retain FDI as greater job security may result in stronger mutual commitment. In other words, as Whitley (1999) notes, higher job security means that employers and employees will be more interdependent. Employers would have to rely on their existing employees (as they cannot be easily substituted) and therefore have strong incentives not only in pre-hiring screening, but also in maximising their capabilities. And as employees do not have to constantly monitor the external labour market, they will, as noted above, have more incentives to develop their firm-specific capabilities rather than externally marketable skills. This would be conducive to certain types of incrementally innovative production. In other words, rather than deterring FDI, difficulty in firing may make the country in question more attractive to specific types of investors (see Whitley, 2010).

3.2.6 Hypothesis 3B: Host country's difficulty of firing employees attracts, or at least does not deter, the FDI inflows. There are also two conflicting views on the impact of working hours' flexibility on the FDI inflows. On the one hand, it can be argued that less rigid restrictions on working hours give MNCs more flexibility to increase profit potential. For example, if there are no restrictions on work hours and overtime pay, firms can persuade employees to work for longer hours to respond to a seasonal increase in demand and pay just the same regular hourly wage for the additional hours of work.

3.2.7 Hypothesis 4A: Host country's rigidity in working hours deters FDI inflows. On the other hand, the World Bank's 'World Business Environment Survey' and 'Investment Climate Survey'[7] concede that if labour rules do not exist at all—or are too flexible and fail to offer sufficient protection—which results in workers being at risk of abusive work conditions, this can harm the development of businesses. Such practice may discourage workers' loyalty and enthusiasm of work and may be associated with low productivity. Thus it can be argued that more restrictions on working hours may improve the productivity of workers. Consistent with this view, Locke and Romis (2007) find that productivity is higher, and ultimate unit labour cost lower, in firms that provide better employment conditions (wages, overtime, job satisfaction and employee voice).

3.2.8 Hypothesis 4B: Host country's rigidity in working hours attracts, or at least does not deter, FDI inflows. Following the demise of state socialism, all economies in the SEE region have moved to a lesser or greater extent towards more flexible labour markets

[7] See 'World Business World Business Environment Survey' and 'Investment Climate Survey', conducted in more than 80 countries by the World Bank in 1999–2000. https://www.wbginvestmentclimate.org/research-and-diagnostics/ (date last accessed 6 June 2014).

(Cazes and Nesporova, 2007, p. 19; Lehmann and Muravyev, 2009). The deregulation process in some of these countries has, as we have seen, accelerated since the onset of the 2008 global economic crisis. However, EU accession and Europeanisation is an ambiguous process that brings with it both aspects of regulation and liberalisation (O'Hagan, 2002; Scharpf 2002; Thatcher, 2007). Van Vliet (2010) argues that, in particular, Europeanisation has been associated with a tendency towards more active labour market policies. However it has been argued that this process has only partially tempered a broader trend towards lighter regulation of the firm. In particular the decisions of the European Court of Justice, in prioritising individual rights, have served to weaken collective employment rights by constraining the range of actions open to unions and their ability to negotiate living wage agreements (Dølvik and Visser, 2009; Ewing, 2009, pp. 2–4). Afonso and Papadopoulos (2013) contend that although it has been argued that Europeanisation promotes greater corporatist concertation, it appears that moves in this direction tend to more closely reflect domestic party political dynamics in individual countries. Once more, despite regulatory or institutional shortcomings, low wages associated with some European Union countries and market access may compensate for any regulatory costs associated with doing business within economic free-trade zones (see Dunning and Lundan, 2008, p. 33).

3.2.9 Hypothesis 5A: Host countries with stronger employment rights attract more FDI when they are located within the European Union. Nonetheless, it could be argued that MNCs may be deterred from investing within the European Union on account of greater—and more complex—employment regulation.

3.2.10 Hypothesis 5B: Host countries with stronger employment rights attract more FDI when they are located outside the European Union.

4. Methodology and data

4.1 Methodology

Our empirical strategy involves estimating a panel regression of the following form:

$$FDI_{i,n} = \alpha + \theta Flexibility_{i,n} + \sum_{k=1}^{k} \varphi_k X_{i,k,n} + \varepsilon_{i,n} \tag{1}$$

where $FDI_{i,n}$ is the FDI inflows to country i in year n. $Flexibility_{i,n}$ captures the level of labour market flexibility associated with country i in year n. To test our hypotheses, we use four different employment rights measures, which are the overall rigidity of employment index, difficulty of hiring index, rigidity of hours index and difficulty of redundancy index. $X_{i,k,n}$ is the kth control variable associated with country i in year n. The control variables included in equation (1) are as follows: the EU membership dummy (EU); the interaction variable between the EU membership dummy and labour market flexibility (EU*Flexibility); an exchange rate regime dummy variable, which is equal to one for the floating exchange mechanism and zero otherwise; the exchange rate, which is defined as the local currency per US$; perceived level of corruption; gross national income (GNI) per capita; wage level; tax rate; manufacturing value

added; and an education level proxy, which is measured as the number of researchers in R&D per million people. The EU membership dummy is used to test whether EU membership was conducive to attracting FDI. The variable EU*Flexibility tests whether the importance of labour market rigidity as a determinant of FDI depends on whether or not the host country is located within the European Union. The selection of the remaining variables is guided by existing studies, which suggest that exchange rates (Blonigen, 2005; Taylor, 2008), taxation (Hartman, 1984, 1985), corruption level (Habib and Zurawicki, 2002), wages (Farrell *et al.*, 2006; Parrinello, 2008), the level of host market development (Kinda, 2010) and the quality of human capital (Addison *et al.*, 2006; Kinda, 2010) are amongst the key determinants of FDI inflows.[8] To avoid multicollinearity-related issues, we ensure that highly correlated explanatory variables are not included in the same regression. Finally, $\varepsilon_{i,n}$ is the error term, which can be heteroscedastic.

4.2 Data and descriptive statistics

Given the significant amount of transition and integration happening in the region and the potential effects on economic growth and FDI, the theoretical hypotheses are tested for the SEE countries over the period from 2003 to 2011.[9] Our sample of the SEE countries consists of Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYRO Macedonia, Greece, Montenegro, Romania, Serbia and Serbia and Montenegro.[10]

We collect FDI data from the UNCTAD *World Investment Report*. The yearly FDI inflows are measured in US$ at current prices and current exchange rates. The measures for employment rights, specifically as they affect the hiring of workers, the rigidity of working hours and the redundancy of workers are presented by the overall rigidity of employment index, difficulty of hiring index, rigidity of hours index and difficulty of redundancy index, respectively. The index values for 2003–09 are collected from the World Bank's *Doing Business* reports. The index values for 2010–11 are constructed using the same methodology described in the reports. Specifically, the overall rigidity of employment index is the average of three subindices: a difficulty of hiring index, a rigidity of hours index and a difficulty of redundancy index. All three subindices have several components and take values between 0 and 100, with higher values indicating more rigid regulation (see the Appendix).

The EU membership and year of entry data are collected from the European Union web site (EUROPA). The classification of exchange rate arrangements is collected from the IMF web site. The Corruption Perceptions Index (CPI) is published by Transparency International and ranks countries 'by their perceived levels of corruption as the misuse of public power for private benefit'. The ranks are on a scale from 10 (very clean) to 0 (highly corrupt). Here it is worth noting that the 2003 Europe Criminal Law Convention on Corruption and its additional protocols, as well as national legislation such as the UK's 2010 Bribery Act, may have made operating in corrupt contexts more risky for MNCs and may, therefore, have discouraged FDI. The GNI per capita (US$) data are collected from the World Bank's *Doing Business* reports. The data on monthly wages (in US$) are obtained from Datastream. Finally, the data on exchange rates per US$, the manufacturing value added and the number

[8] Similar sets of variables are also used by Wood *et al.* (2014).

[9] The starting of the sample period is chosen to coincide with the release of the *Doing Business* report.

[10] Serbia and Montenegro ceased to exist in 2006.

of researchers in R&D per million people are downloaded from the World Bank's *World Development Indicators*.

Table 1 reports the descriptive statistics of dependent and explanatory variables used in our analysis. It shows that Romania receives the highest amount of FDI (US$6,752 million) while FYRO Macedonia receives the least (US$342 million). It also shows that Serbia experiences the highest level of difficulty in hiring (71) while Montenegro has the least difficulty (17). Greece has the highest level of rigidity in hours (72) and Serbia has the lowest (18). The difficulty level in redundancy ranges from the highest value of 48 for companies in Croatia to the lowest value of 8 for companies in Bulgaria. When the respective individual employment rights (difficulty of hiring, rigidity in hours and difficulty in redundancy) are averaged to form the level of rigidity in employment variable, Greece is found to be the most rigid country in the SEE region in terms of employment rights (55) and Montenegro is the least rigid country, with an employment rights index of 23. Greece, Bulgaria and Romania are the only countries in our sample that belong to the European Union. The SEE countries are quite similar in terms of their corruption levels. With an average CPI score of 3, the SEE region is perceived as relatively highly corrupted.

Table 1 also reports the descriptive statistics of other potential determinants of the FDI inflows. It shows that four (six) out the 10 SEE countries use fixed (floating) exchange rate regimes. The SEE countries differ considerably in terms of the value of their currencies, with the exchange rate ranging from 0.77 euro per US$ in the cases of Greece and Montenegro[11] to 99.64 Albanian lek per US$. Greece has the highest GNI per capita (US$21,944), while Serbia and Montenegro (for the period 2003–06) has the lowest GNI per capita (US$1,977). The average monthly wage in the SEE countries is approximately US$671, with the highest (lowest) average monthly wage of US$1,474.35 (US$314.05) observed in the case of Greece (Bulgaria). Finally, the average tax rate in the SEE region is approximately 40%, ranging from the highest of 47.19% in Albania to the lowest of 29.73% in Greece.

The (percentage) changes in indices for employment rights and FDI inflows from 2003 to 2011 are report in Table 2. The figures indicate considerable increases in FDI inflows to the region. The negative signs associated with the average changes in different measures of employment rights reflect the increase in the level of labour market flexibility in the region.

Previous studies show that labour market flexibility measures tend to be highly correlated with other determinants of FDI inflows, particularly those related to human capital and innovation (Michie and Sheehan, 2003). Consequently we estimate the bilateral correlations between the different determinants of FDI inflows to avoid the multicollinearity issues that may rise from including highly correlated variables in the same models. The correlation matrix is reported in Table 3. The 90% correlation between wage and GNI reflects the positive association between wages and national wealth. We also report a 60% correlation between EU membership dummy and GNI. This figure suggests that EU members tend to be wealthier than non-EU countries. Correlations in excess of 70% are also found between overall rigidity of employment index and its various components. The correlation between the difficulty of hiring

[11] Montenegro does not have its own currency. The Deutsche Mark was the *de facto* currency prior to the introduction of the euro in 2002. After that, Montenegro began using the euro without any objection from the European Central Bank.

Table 1. *Descriptive statistics of workers' rights, FDI and other control variables*

	Difficulty in hiring index	Rigidity in hours index	Difficulty in redundancy index	Rigidity in employment index	FDI (US$ million)	EU membership	Exchange rate regime	Corruption perception index	GNI per capita (US$)	Monthly wages (US$)	Tax (% revenue)	Exchange rate (per US$)
Albania	40	44	17	34	647	No	Floating	3	2,868.44	343.84	47.19	99.64
Bosnia and Herzegovina	61	31	30	41	615	No	Fixed	3	3,094.00	734.87	40.56	1.50
Bulgaria	31	52	8	31	5,145	Yes (2007 onwards)	Fixed	4	4,020.78	314.05	43.86	1.50
Croatia	64	45	48	52	2,765	No	Floating to Fixed (in 2007)	4	9,508.22	860.97	46.24	5.66
FYRO Macedonia	39	44	27	37	342	No	Fixed	3	3,159.78	564.03	40.54	47.03
Montenegro[a]	17	23	28	23	952	No	Floating	4	5,386.67	717.52	–	0.77
Serbia[a]	71	18	28	39	2,238	No	Floating	3	4,905.83	551.74	43.76	64.74
Serbia and Montenegro[b]	41	29	36	36	2,774	No	Floating	3	1,976.67	–	–	–
Average	49	44	30	41	2,548	–	–	3	6,603.26	670.96	39.81	24.95

[a]From 2008 onwards.[b]For the period 2003–06.

Table 2. *(Percentage) changes in FDI and employment rights during the period 2003–11*

	Change in FDI (US$ million)	Change in difficulty of hiring index	Change in difficulty of redundancy index	Change in rigidity of hours index	Change in difficulty of employment index
Albania	853.34	17	−56	−5	−14
	(4.79)	(0.52)	(−0.74)	(−0.33)	(−0.35)
Bosnia and Herzegovina	54.00	−3	−63	−1	−22
	(0.14)	(−0.06)	(−1.00)	(−0.03)	(−0.46)
Bulgaria	−224.36	−18	−70	−26	−38
	(−0.11)	(−0.42)	(−0.78)	(−1.00)	(−0.72)
Croatia	−494.98	−1	−69	19	−17
	(−0.25)	(−0.01)	(−0.78)	(0.61)	(−0.26)
FYRO Macedonia	308.58	−65	−33	−22	−40
	(2.72)	(−1.00)	(−0.62)	(−0.69)	(−0.80)
Greece	547.68	−28	−31	−13	−24
Montenegro[a]	−402.37	−33	−40	−10	−27
	(−0.42)	(−1.00)	(−1.00)	(−0.33)	(−0.80)
Romania	474.14	27	−65	1	−12
Serbia[a]	−246.02	67	−40	−20	2
	(−0.08)	(2.03)	(−1.00)	(−0.50)	(0.05)
Serbia and Montenegro[b]	2856.94	−7	−88	11	−28
	(1.88)	(−0.14)	(−1.00)	(0.38)	(−0.50)
Average	372.69	−4	−56	−7	−22
	(0.93)	(0.01)	(−0.81)	(−0.22)	(−0.44)

[a]From 2008 onwards.[b]For the period 2003–06.

index and the difficulty of redundancy index is almost 50%, reflecting the fact that employee rights are affected by both hiring and firing regulations. Table 3 also shows that the perceived level of corruption is highly correlated with GNI (70%), wage (50%) and exchange rate (−51%). These figures suggest that corruption levels tend to be lower in wealthy nations with stronger currencies and higher wages. The remaining bilateral correlations in Table 3 are relatively low in magnitude, ranging from +47% between EU membership dummy and perceived level of corruption to −1.1% between difficulty of hiring index and foreign exchange rate.

5. Findings

In our study, the fixed-effects panel regression is applied to analyse the data. A statistically significant Hausman test suggests that the use of fixed effects is more appropriate than a random-effects specification for our data. In addition, the use of a fixed-effects application not only reduces econometric problems arising from autocorrelation and heteroscedasticity (Hitt *et al.*, 1998; Bowen and Wiersema, 1999), but also provides control for unobserved country- and year-specific heterogeneity (Greene, 2002; Tuggle *et al.*, 2010). The F-test suggests that the various sets of independent variables included in equation (1) are jointly statistically significant.

To test whether a relaxation of the overall rigidity of employment index attracts or deters FDI, we regress the rigidity in the employment index and other control variables on FDI. The results are shown in Table 4. The coefficient on the rigidity in

Table 3. *Correlation matrix*

	Diff_ hiring	Rigidity_ hours	Diff_ redundancy	Rigidity_ employ	Corruption perception	Exchange rate	EU	Exchange rate regime	Wage	Tax	GNI	Value added	Researchers	EU*Rigi_ employ	EU*Diff_ hiring	EU*Rigi_ hours	EU*Diff_ redundancy
Rigidity_hours	0.2	1.0															
Rigidity_ employ	0.7***	0.7***	0.7***	1.0													
Corruption perception	0.0	0.2	0.1	0.1	1.0												
Exchange rate	−0.1	−0.2	−0.3***	−0.2*	−0.5***	1.0											
EU	0.0	0.3**	0.0	0.1	0.5***	−0.4***	1.0										
Exchange rate regime	0.0	0.0	0.1	0.0	−0.3**	0.3***	−0.1	1.0									
Wage	0.2	−0.2	0.5***	0.1	0.5***	−0.4***	0.4***	0.0	1.0								
Tax	−0.1	−0.4***	−0.3**	−0.4***	−0.3*	0.3**	−0.4***	−0.2	−0.3**	1.0							
GNI	0.1	0.0	0.3***	0.1	0.7***	−0.4***	0.6***	0.1	0.9***	−0.3**	1.0						
Value added	0.4***	0.2	0.1	0.4***	0.2*	0.0	0.3**	−0.2	−0.1	0.3*	0.3**	1.0					
Researchers	−0.1	0.2	0.1	0.1	0.6***	−0.2	0.4**	0.2	0.1	0.3*	0.6***	0.7***	1.0				
EU*Rigi_ employ	0.2	0.4***	0.2	0.4***	0.5***	−0.4***	0.9**	0.0	0.5***	−0.6***	0.6***	0.3*	0.3**	1.0			
EU*Diff_hiring	0.2**	0.3***	0.2	0.3***	0.4***	−0.3***	0.9***	0.1	0.4***	−0.6***	0.6***	0.3**	0.3*	0.9***	1.0		
EU*Rigi_hours	0.1	0.4***	0.1	0.3***	0.5***	−0.3***	0.9***	0.0	0.4***	−0.6***	0.6***	0.2*	0.3**	0.9***	0.9***	1.0	
EU* Diff_redundancy	0.2*	0.3***	0.3**	0.4***	0.5***	−0.3***	0.8***	0.1	0.5***	−0.7***	0.7***	0.2	0.3*	0.9***	0.9***	0.9***	1.0

Note: Significant at -p<0.1, **p<0.05 and ***p<0.01.

Table 4. *Result of fixed-effect panel regressions on FDI*

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Rigidity in employment	0.097**	0.173**	0.186**	0.014	0.184***	0.154**	0.119**	0.021	0.178***	0.067
	(2.03)	(3.19)	(3.02)	(0.97)	(2.94)	(2.46)	(2.63)	(1.48)	(3.95)	(1.68)
EU*Rigidity in employment				0.123***				0.606***		0.083***
				(3.78)				(43.76)		(5.38)
Perceived corruption	1.620				3.515*					
	(1.28)				(1.91)					
LnWage		5.724				−10.100			6.628	
		(1.37)				(−1.06)			(1.25)	
LnGNI			3.557***				−1.071			
			(4.82)				(−0.42)			
European Union	2.060	−0.904		−3.337	5.729**	7.080		−11.450***	−0.771	−0.529
	(1.37)	(−0.21)		(−1.30)	(2.78)	(1.86)		(−16.02)	(−0.14)	(−0.24)
LnTax	−0.722	−2.480	−2.484		1.503	−0.234	−0.782		−2.838	
	(−0.21)	(−0.78)	(−0.88)		(0.45)	(−0.11)	(−0.51)		(−0.50)	
Exchange rate regime	0.424	0.230	0.163	0.277	−0.142	−2.871	−1.341*	−0.891***	−0.539	−1.199
	(0.31)	(0.32)	(0.42)	(0.24)	(−0.08)	(−1.94)	(−2.16)	(−3.85)	(−0.58)	(−1.27)
Exchange rate		−0.006	−0.097**	−0.041*		−0.031	0.037	0.013	0.029	−0.128*
		(−0.10)	(−3.48)	(−2.06)		(−0.65)	(0.42)	(0.39)	(0.16)	(−2.05)
LnValue added					1.598	10.138	5.179	1.531		
					(0.67)	(1.27)	(1.27)	(1.68)		
LnResearchers									1.808	1.473
									(0.39)	(1.53)
Constant	−5.420	−32.091	−25.658***	2.205*	−59.060	−163.377	−104.949	−31.936	−48.355	−8.213
	(−0.39)	(−1.89)	(−6.62)	(2.07)	(−1.26)	(−1.33)	(−1.45)	(−1.55)	(−1.62)	(−1.09)
N	53	52	54	71	37	36	38	52	36	42
Adj. R^2	0.084	0.156	0.131	0.088	0.107	0.222	0.027	0.598	0.138	0.074

Note: Significant at * $p<0.1$, ** $p<0.05$ and *** $p<0.01$. The t-statistics are shown in parentheses.

employment variables is positive and, in most cases, statistically significant, indicating that foreign investors are more likely to invest in countries where employment rights are strong. This could reflect the extent to which there are many low-wage lightly regulated economies in intense competition with each other, making it difficult to secure lasting competitive advantage. Thus investors who seek competitive advantages through very low labour costs may find themselves constantly being undercut by rivals located in even lower-cost locales. However it is also possible to argue that stronger employment rights may lead to unique, locally or nationally specific, competitive advantages in specific areas with higher value-added production, which may attract more patient longer-term investors (Hall and Soskice, 2001). The significantly positive coefficient on the interaction variable (EU*Rigidity) in Table 4 indicates that employment rights play a more important role in the location decision within the European Union. Specifically, foreign investors find EU members with stronger employment rights to be more attractive investment destinations. Thus, hypothesis 1A is rejected and 1B is supported.[12]

Table 5 reports the results from testing hypotheses 2, 3 and 4 whether reduced scores on the difficulty in hiring, rigidity of hours, difficulty in redundancy, respectively, attract or deter FDI after controlling for other variables.[13] The rigidity of hours and difficulty in redundancy are positive, showing support for hypotheses 3B and $8, respectively. In line with the World Bank's 'World Business Environment Survey' and 'Investment Climate Survey' and the explanation of Dewit *et al.* (2003), but contrary to the empirical findings of Görg (2005) and Javorcik and Spatareanu (2005), inflexibility in working hours and firing workers implies commitment power; greater mutual commitment incentivises the development of firm-specific skills and may improve the productivity of workers, attracting FDI. The only stringency of regulation that seems to deter FDI, as suggested by hypothesis 2A, is shown by the negative, and in some cases statistically significant, coefficient on the difficulty of hiring index. The results indicate that MNCs like the flexibility of offering a short- or medium-term contract, fixed-term contracts for any task and a lower rate of pay relative to regular workers in order to reduce labour costs. However restrictions on the use of temporary labour may have very different effects on restrictions on dismissals. Specifically, in environments where security of tenure for regular employees is stronger, firms may use temporary labour as a screening device to ensure greater rigour in the appointment of permanent employees. In other words, firms may attempt to compensate for difficulty in firing by the greater use of temporary probationary labour, allowing them to be sure about permanent hires (see, e.g., Crouch, 2005).

Again we use interaction variables (EU*Flexibility) to test whether the role of employment rights on FDI inflows depends on EU membership. The significantly positive coefficients associated with the interaction variables in Models 11 and 12 indicate that host countries with stronger employment rights (measured by difficulty of

[12] To control for the possible effect of endogeneity on our results, we re-estimate Models 1–10 using the generalised method of moments estimator suggested by Arellano and Bover (1995). Our results suggest the significance of the coefficient on the rigidity of employment index remains largely unchanged. Further details on these results are available upon request.

[13] Similar results are reported in other models, which contain manufacturing value added and number of researchers in R&D per million people as dependent variables. The details of these models are not reported for the sake of brevity and the results are available upon request.

Table 5. *Result of fixed-effect panel regressions on FDI*

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10	Model 11	Model 12
Diff_hiring	−0.047***			−0.038			−0.043*			−0.004		
	(−4.14)			(−1.65)			(−2.02)			(−0.43)		
Rigidity_hours		0.068*			0.106***			0.123***			0.034*	
		(2.26)			(4.64)			(4.88)			(1.97)	
Diff_redundancy			0.177**			0.183*			0.153			0.075
			(2.48)			(2.20)			(1.82)			(1.45)
EU*Diff_hiring										−0.047		
										(−1.77)		
EU*Rigidity_hours											0.129**	
											(3.08)	
EU*Diff_redundancy												0.119***
												(8.22)
Corruption perception	2.229**	1.498**	1.891**									
	(2.58)	(2.83)	(2.68)									
LnWage				1.234	7.350*	2.071				0.815	4.838*	2.583
				(0.31)	(2.26)	(0.68)				(0.34)	(1.98)	(1.13)
LnGNI							0.014	4.836***	1.083			
							(0.02)	(6.05)	(1.26)			
European Union	0.225	2.453*	1.996	−0.180	−1.875	0.857				2.333	−7.620***	−2.687
	(0.67)	(2.09)	(1.74)	(−0.07)	(−0.65)	(0.32)				(0.97)	(−4.89)	(−0.82)
LnTax	−0.736	0.456	−0.255	−1.717	−1.072	−1.319	−0.552	−0.964	−0.968			
	(−0.19)	(0.15)	(−0.07)	(−0.32)	(−0.56)	(−0.33)	(−0.13)	(−0.63)	(−0.32)			
Exchange rate regime	−0.127	−0.448	1.175***	−0.980	−1.018	0.452	−1.155**	−1.272***	0.248	−1.251*	0.321	0.198
	(−0.20)	(−0.34)	(3.74)	(−1.29)	(−1.55)	(0.77)	(−2.59)	(−6.59)	(0.48)	(−2.15)	(0.44)	(0.58)
Exchange rate				0.001	0.088	−0.008	−0.017	−0.018	−0.046	−0.017	0.058	0.025
				(0.03)	(1.21)	(−0.13)	(−0.43)	(−0.56)	(−1.10)	(−0.33)	(1.30)	(0.43)
Constant	0.370	−8.024	−9.580	4.050	−45.63**	−11.51	8.073	−40.45***	−7.047	−1.324	−31.31*	−16.98
	(0.02)	(−0.63)	(−0.72)	(0.36)	(−3.08)	(−1.30)	(0.93)	(−6.13)	(−0.75)	(−0.08)	(−1.91)	(−1.05)
N	53	53	53	52	52	52	54	54	54	68	68	68
Adj. R^2	0.039	0.213	0.122	0.052	0.359	0.070	0.042	0.369	0.034	0.020	0.527	0.087

Note: Significant at *p<0.1, **p<0.05 and ***p<0.01. The t-statistics are shown in parentheses.

redundancy and rigidity of hours) are more likely to attract FDI when they are located within the European Union. This finding is consistent with the predictions of hypothesis 5A. However the absence of statistical significance on the coefficient EU*Diff_hiring in Model 10 indicates that the effect of the difficulty of hiring on FDI inflows does not depend on EU membership.

In (unreported) tests, we also investigate the impact of employment rights on the FDI inflows to the EU members and non-EU countries separately.[14] Whilst the sign and statistical significance on the overall rigidity index is highly sensitive to model specifications, our results suggest that countries with higher rigidity of hours and difficulty of redundancy index are more likely to attract FDI when they are located within the European Union. However, our findings indicate that difficulty of hiring is more likely to deter FDI inflows when the host country is located within the European Union.

With the exception of GNI and perceived level of corruption, which suggests foreign investors are more likely to invest in rich countries (i.e. market-seeking MNCs) and less corrupt countries, the statistical significance of the remaining control variables in Tables 4 and 5 is sensitive to model specifications. Overall, our results suggest that stronger employment rights—measured by the rigidity of hours index, the difficulty of redundancy index and the overall rigidity of employment index—seem to attract, rather than deter, FDI inflows. This evidence is consistent with the view that greater job security increases employees' commitment and value-added production paradigms (Whitley, 1999; An *et al.*, 2008). We also report a negative association between the difficultly of hiring index and FDI inflows to the SEE region. We attribute this finding to the possibility that some firms make routine use of temporary work as a screening device for those earmarked for stable long-term employment (see Harcourt *et al.*, 2006) and others use temporary workers to reinforce the position of highly vulnerable categories of labour. Furthermore we show some evidence that host countries with strong employment rights are more likely to attract more FDI when they are located within the European Union. This suggests that the complementarities associated with stronger employment rights and more committed labour (see Hall and Soskice, 2001) may offset the overall deterrent effects of the greater regulation associated with EU membership. When employment regulation is weaker, complementarities are similarly less developed and hence the negative consequences of overall regulation are likely to be more pronounced.

There are certain limitations to this research. Firstly, all the countries in the SEE region are characterised by very extensive Small and Medium Enterprises (SME) sectors and the inflow of foreign investment into these SMEs may be poorly documented and/or unconventional. For example, a large numbers of Italian SMEs from northern Italy have forged close relations with Romanian SMEs. Whilst it may seem that these SMEs have a purely supplier/customer relationship, in reality the ties may be much deeper and may include issues such as equity transfers through the transhipment of machinery (Majocchi, 2000, p. 6). Furthermore, investments by SMEs into the region can assume innovative forms, such as 'forfeiture', which seeks to separate out local transaction-orientated risks from broader contextual ones (McKibben and Pistrui, 1997). Secondly, the region is a fast-changing one, undergoing not only varying degrees of austerity but also Europeanisation. Thus, future FDI flows may follow very different patterns. Finally, any analysis of the consequences of formal regulation needs

[14] Whilst these results are not tabulated, further details are available upon request.

to recognise that enforcement mechanisms are variable in efficacy. In all the countries in the region, institutional and regulatory coverage is highly uneven. Fertile areas for future research might include a closer analysis as to the impact of weak regulatory enforcement capabilities on FDI and on the alternative mechanisms used by SMEs to invest in the region as well as the determinants of investment decisions in such circumstances.

6. Conclusions

Our findings suggest that employment rights do not serve to discourage FDI. Rather, countries where workers enjoy more job security and greater restraints on working hours under the law seem to be more attractive investment destinations. We also find that host countries with stronger employment rights are more likely to attract FDI when they are located within the European Union. Thus our findings imply that strong pressures to deregulate labour markets may have perverse effects, leaving countries embarking on labour market reform worse off. As Whitley (1999) notes, greater job security will lead to a higher degree of interdependence between employer and employee and encourage the development of firm-specific skills and capabilities (Brewster *et al.*, 2012), which would be conducive to higher value-added production paradigms. And, as Knox and Walsh (2005) suggest, restraints on working time may also make for a more productive workforce. In the absence of such restraints, employers may arbitrarily adjust employees' working day, impinging on leisure time and/or failing to pay a premium for working longer hours. This may increase the quantity of work performed per worker but reduce quality. The only area where weaker employment rights appear better in terms of attracting FDI is in terms of the difficulty of hiring index. This is probably owing to the fact that in certain countries, firms make routine use of temporary work as a screening device for those earmarked for stable long-term employment (see Harcourt *et al.*, 2006). In other countries, temporary working may be widely used as a mechanism to reinforce the position of highly vulnerable categories of labour. Firms originating in either context may be deterred from investing in countries where the difficulty of hiring ranking is high for opposite reasons. Hence ease in hiring may not be always associated with weaker employment rights in other areas.

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Appendix

Table A1. *Panel A: the difficulty of hiring index is constructed by averaging the scores from the following three components and scaling to 100, with higher values indicating more rigid regulation*

Component	Score
Whether fixed-term contracts are prohibited for permanent tasks	A score of 1 if fixed-term contracts are prohibited for permanent tasks and 0 if they can be used for any task
The maximum cumulative duration of fixed-term contracts	A score of 1 if the maximum cumulative duration of fixed-term contracts is less than 3 years; 0.5 if it is 3 years or more but less than 5 years; and 0 if it can last 5 years or more
The ratio of the minimum wage for a trainee or first-time employee to the average value added per worker	A score of 1 is assigned if the ratio is 0.75 or more; 0.67 for a ratio of 0.50 or more but less than 0.75; 0.33 for a ratio of 0.25 or more but less than 0.50; and 0 for a ratio of less than 0.25

Source: Employing Workers methodology in World Bank's *Doing Business* report.

Table A2. *Panel B: the rigidity of hours index is constructed by averaging the scores from the following five components and scaling to 100, with higher values indicating more rigid regulation*

Component	Score
Whether there are restrictions on night work	A score of 1 if restrictions other than premiums apply and 0 if there are no restrictions
Whether there are restrictions on weekly holiday work	A score of 1 if restrictions other than premiums apply and 0 if there are no restrictions
Whether the workweek can consist of 5.5 days or is more than 6 days	A score of 1 if the legally permitted workweek is less than 5.5 days or more than 6 days and 0 otherwise
Whether the workweek can extend to 50 hours or more (including overtime) for 2 months a year to respond to a seasonal increase in production	A score of 1 if the answer is 'no' and 0 otherwise
Whether the average paid annual leave for a worker with 1 year of tenure, a worker with 5 years and a worker with 10 years is more than 26 working days or fewer than 15 working days	A score of 0 is assigned if the average paid annual leave is between 15 and 21 working days; 0.5 if it is between 22 and 26 working days; and 1 if it is less than 15 or more than 26 working days

Source: Employing Workers methodology in World Bank's *Doing Business* report.

Table A3. *Panel C: the difficulty of redundancy index is constructed by adding the scores from the following eight components and scaling to 100, with higher values indicating more rigid regulation*

Component	Score
Whether redundancy is disallowed as a basis for terminating workers	A score of 10 if the answer is 'yes' for workers of any income level and 0 otherwise
Whether the employer needs to notify a third party (such as a government agency) to terminate 1 redundant worker	A score of 1 if the answer is 'yes' and 0 otherwise
Whether the employer needs to notify a third party to terminate a group of 9 redundant workers	A score of 1 if the answer is 'yes' and 0 otherwise
Whether the employer needs approval from a third party to terminate 1 redundant worker	A score of 2 if the answer is 'yes' and 0 otherwise
Whether the employer needs approval from a third party to terminate a group of 9 redundant workers	A score of 1 if the answer is 'yes' and 0 otherwise
Whether the law requires the employer to reassign or retrain a worker before making the worker redundant	A score of 1 if the answer is 'yes' and 0 otherwise
Whether priority rules apply for redundancies	A score of 1 if the answer is 'yes' and 0 otherwise
Whether priority rules apply for re-employment	A score of 1 if the answer is 'yes' and 0 otherwise

Source: Employing Workers methodology in World Bank's *Doing Business* report.