SEVENTH FRAMEWORK PROGRAMME

"Ideas" Specific programme

European Research Council

Grant agreement for Advanced Grant

<u>Annex I - "Description of Work"</u>

Project acronym: **FINLAB**
Project full title: **Finance and Labour**
Grant agreement no.: **295709 - FINLAB**
Duration: **60 months**

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Principal Investigator: **Prof. Marco Pagano**
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Centro interuniversitario di Studi in Economia e Finanza (CSEF)

European Research Council

ERC Advanced Grant 2011
Research proposal (Part B1)

Finance and Labor

FINLAB

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Duration: 60 months

Proposal summary

How do financial market development affect employment, wages and unemployment risk? And how do labor market institutions and workers' behavior in turn affect corporate policies?

These issues are much under-researched, in spite of their prominence in public debate, often ideologically polarized between those who consider finance as socially harmful and those who view it as an efficient allocation machine. Most economic research indicates that financial development raises output growth, but is silent about its effects on the labor market: does it also raise employment and wages? If so, is it at the expense of greater employment risk and inequality? And how does the potential for systemic financial instability affect the answers to these questions?

The study of these issues naturally opens also another – equally under-researched – line of inquiry: that concerning the effects of labor relations on financial arrangements. Do corporate investment policies and leverage decisions take into account their own effects on firms' bargaining position in wage negotiations? And if so, how are these corporate decisions affected by job protection regulation, union density or workers' protection in bankruptcy? To what extent do companies insure workers against employment risk, and do family and non-family firms differ in this respect? Finally, can labor market competition damage the performance of employees with decision-making responsibilities? For instance, can it induce managers or traders to take excessively risky decisions, by providing them with an escape route once they make mistakes, especially when outcomes are observed long after decisions?

This research project purports to break new ground on both sets of issues, using a combination of analytical modelling and empirical analysis, which in some cases will require the collection of entirely new data.