The Effect of External Innovation on Firm Employment

by Alberto Marzucchi | Guillermo Arenas Díaz | Andrés Barge-Gil | Joost Heijs | GSSI Social Sciences | Department of Economic Policy, Università Cattolica del Sacro Cuore, Milano | Department of Economic Analysis, Complutense, Madrid, Spain, University of Madrid ICAE and GRIPICO | Department of Applied Economics, Structure and History, Complutense University of Madrid, Madrid, Spain

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This paper analyses the effects of product innovations introduced by firms in upstream and downstream sectors and firms in the same sector on firm employment. To this aim, we extend the Harrison et al. (2014) model to analyse the relationship between firm innovation and employment to account for innovation in the same and related sectors. We employ panel data for the innovation activities of Spanish firms together with input–output data. The results show that product innovation by firms in the same sector harms the firm's employment, which is consistent with a business-stealing mechanism. A negative effect on employment is found for the introduction of new products in upstream sectors, which results in the reduction of labour in the focal firm. The type of labour that is displaced by innovations introduced by both same-sector and upstream firms is predominantly low-skilled. No significant effects are found for innovations introduced in downstream industries.