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Takeovers Cut Central-Office Costs

Between 1980 and 1986, the value of U.S. companies that changed owners through mergers, acquisitions, and leveraged buyouts increased almost sixfold. Corporate "raiders" claimed that takeovers (actual or threatened) were necessary to encourage changes in management practices, while others worried about corporate efficiency and thus competitiveness.

In **The Effect of Takeovers on the Employment and Wages of Central-Office and Other Personnel** (*NBER Working Paper No. 2895*), NBER researchers **Frank Lichtenberg** and **Donald Siegel** find that takeovers *do* reduce corporate overhead. In companies changing owners, the ratio of central-office employees to plant employees declined about 11 percent. Over 51 percent of central-office workers are engaged in administrative, managerial, or clerical activities. Therefore, change in ownership meant 7.2 fewer administrators per 1000 plant employees.

Moreover, in the central-office operations of those firms, payroll costs per employee were 9 percent lower than in similar establishments that did not change owners. When fringe benefits were taken into account, the relative decline in total compensation was about 12 percent.

Overall employment in central offices of acquired firms grew about 16 percent less than in central offices that did not change owners. Even after taking account of growth in the administrative offices of the acquiring firms, Lichtenberg and Siegel estimate that employment growth in the central offices of firms with new owners was 11 percent less than in firms without an ownership change. However, the growth of the research and development staff in both types of firms was similar.

In the production plants of newly owned firms, employment growth was only 5 percent lower than in establishments that had not changed owners. Lichtenberg and Siegel find that the employment of production workers declined in two or three years *before* the takeover. After the takeover, employment recovered a bit, but not enough to offset the previous decline. Still, in U.S. manufacturing, the ratio of central-office to plant employees rose from 4.5 in 1963 to 7.2 in 1982.

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Lichtenberg and Siegel note that "restructuring" of a company can occur even without a takeover or bankruptcy. For instance, General Electric slashed its headquarters staff from 1700 to 1000, and Monsanto eliminated most of its foremen, supervisors, and quality inspectors in its factories. However, such staff reductions are more likely as a result of takeovers, the authors suggest.

"Some people express concern about the number of lawyers, investment bankers, and other highly

paid professionals devoted to facilitating or implementing takeovers, and think that this may constitute a waste of valuable human resources," Lichtenberg and Siegel note. "But the quantity and quality of labor engaged in this activity may not be high relative to the quantity and quality of central-office labor 'saved' as a consequence of ownership change."

The authors' conclusions are based on Census Bureau establishment-level data for 1977 and 1982.

DRF

There Is No Market for Reverse Annuity Mortgages

Much of the wealth of older Americans is locked away in the family home. Converting home equity into cash typically has required the elderly to move. Often it is claimed that the high cost—psychic as well as monetary—of moving prevents the elderly from using their equity to boost current consumption as much as they would like. The proposed solution is a market for reverse annuity mortgages, in which homeowners agree to convey their house, at the time of their death, to a bank in exchange for a life annuity equal to the equity in their home.

However, NBER Research Associates **Steven Venti** and **David Wise** find that the demand for reverse annuity mortgages is extremely limited. Contrary to economic theory, "the typical elderly family has no desire to reduce housing equity," they conclude in **But They Don't Want to Reduce Housing Equity** (*NBER Working Paper No. 2859*).

Drawing on a survey of several thousand households in the 1970s, Venti and Wise find that most of the elderly prefer to remain in their homes. Just 8 percent of the families surveyed moved in any two-year period. For families who did move, the major motive usually was a change in personal circumstances: retirement, death of a spouse, or ill health. Families that experienced such changes were twice as likely to move as others, Venti and Wise report.

Reshuffling assets was not an important reason for pulling up stakes, since the potential benefit was negligible for most families. Venti and Wise estimate that the difference between actual and desired home equity for households surveyed averaged just $1000.

Typically, the high cost of moving does not prevent the elderly from making choices that would improve their standard of living. Indeed, families in the survey who moved *increased* their average housing equity. Elderly households with little income and a lot of housing wealth would choose to shrink their housing stake if they moved, but only slightly. Those with high incomes and low equity would choose more equity, often substantially more. Indeed, if all the elderly moved and chose the levels of housing equity that they considered ideal, their total housing equity would increase, not decrease.

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Venti and Wise use data from the Retirement History Survey that tracked 3423 homeowner families headed by persons aged 58 to 63 in 1969 for a decade. The families, about a quarter of whom had moved by 1979, were interviewed every two years, a total of six times. In 1979 their average annual income was $10,892 and their average home equity was $41,735.

SN

Government Impact on Black Progress Uncertain

Federal antidiscrimination policy contributed significantly to the improvement in black economic status in the South in the mid-1960s, according to NBER Research Associate **James Heckman** and **Brook Payner.** In **Determining the Impact of Federal Antidiscrimination Policy on the Economic Status of Blacks: A Study of South Carolina** (*NBER Working Paper No. 2854*), they note that black-to-white male wage rates (for those aged 25 to 54) converged almost twice as fast in the South as in the rest of this country from 1960–80. Since roughly half of American blacks live in the South, two-thirds of the growth in their relative status over the period was attributable to developments there.

In South Carolina, the focus of this study, the black share of total manufacturing employment remained constant at about 15 percent from 1940–65, when it began to rise significantly. Wages for blacks also rose after 1965, but less dramatically than employment.

The textile industry employed 80 percent of all manufacturing workers in 1940 and 40 percent in 1980. Blacks made up about 5 percent of textile production workers in 1950 and 1960 and over 30 percent by the end of the 1970s. Similar increases occurred in other southern states with large textile industries. Heckman and Payner write, "Through two world

wars, the Great Depression, and the booms of the '50s and '20s, the share of blacks in textile employment remained constant at a low level. . . ." This was true despite the growth in the quantity and quality of black schooling and periods of tight labor markets. Suddenly in 1965 the black share in employment began to improve "when Title VII legislation becomes effective, the Equal Employment Opportunity Commission begins to press textile firms to employ blacks, and Executive Order 11246 forbids discrimination by government contractors at the risk of forfeit of government business." The authors point out that in 1965, the South Carolina textile industry sold 5 percent of its output to the U.S. government.

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The South Carolina economy was booming in the mid-1960s. New industries entered the state, but there was no longer a pool of white farm labor from which they could hire. Real wages in the textile industry rose because of this labor scarcity, and competition with foreign firms became more difficult. Thus, textile manufacturers had incentives to draw on a new source of low-wage labor: blacks. Heckman and Payner conclude that the confluence of tight labor markets and new laws caused integration in the textile industry to occur so rapidly.

As evidence for the importance of government activity, they note that black textile employment was virtually unaffected by any events from 1910–65. Then suddenly, black employment began to increase in textiles at about the same time that white employment began to decrease. The real wages of white males, which had been increasing from 1959–65, were practically unchanged from 1966–71 despite growth in the industry's output and employment. Yet, in other manufacturing industries, wages of white males continued to grow. As real wages of blacks in textiles grew through the 1960s, white males left the industry. Defense contracts had a similar impact, Heckman and Payner discover: these contracts affected black employment positively and white employment negatively.

Heckman and Payner also find that while education raised employment in other sectors, especially government and the emerging new industrial sector of South Carolina, it did not help in textiles. Blacks were significantly underrepresented in the textile industry prior to 1960 when compared to whites with the same level of education. Even in 1970, younger blacks remained underrepresented in textiles.

Japan's Tax on Corporate Investment to Rise

Recent changes in Japan's tax law, along with declines in the rate of inflation, have sharply increased the effective tax rate on corporate investment in Japan, according to NBER Research Associate **John Shoven.** He estimates that the effective tax rate on Japanese corporations rose from about 5 percent in 1980 to about 32 percent in 1988. By comparison, the effective U.S. tax rate in 1988 was about 41 percent, up from 29 percent before the Tax Reform Act of 1986, he estimates.

In **The Japanese Tax Reform and the Effective Rate on Japanese Corporate Investments** (*NBER Working Paper No. 2791*), Shoven notes that the effective tax rate depends on a country's expected rate of inflation as well as on its tax rules. Japan's inflation rate fell from 9 percent during the 1970s to under 1 percent during 1986–8. Shoven estimates that the decline in inflation since the 1970s by itself would have raised effective tax rates by 23 percentage points. Tax reforms in Japan raised the rate an additional nine percentage points.

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Shoven also notes that individual savings were taxed very lightly in Japan prior to the 1987 changes in tax law. For example, a family of four could have held more than $455,000 legally in tax-free saving vehicles. On the other hand, interest payments by corporations were totally deductible, just as in the United States. But in 1987 Japan's government abolished the tax-exempt saving system for all except the "truly needy" (the elderly, single-parent families, and the handicapped), and replaced it with a flat 20 percent withholding tax on all interest income.

Finally, Shoven reports that revenues from individual income taxes were 7 percent of Japan's gross domestic product in 1985, compared with 10 percent for the United States. Revenues from corporate income taxes were 6 percent for Japan and 2 percent for the United States, while total tax revenues in 1985 were 28 percent of gross domestic product (GDP) in Japan and 29 percent in the United States. By comparison, tax revenues were 35 percent of GDP in Italy in 1985, 38 percent in Germany and the United Kingdom, 46 percent in France, and 51 percent in Sweden.

DRH

Recent NBER Books

Money, History, and International Finance

Money, History, and International Finance: Essays in Honor of Anna J. Schwartz, edited by Michael D. Bordo, is now available from the University of Chicago Press for $35. This NBER conference report presents five papers and the discussions from a 1987 conference in honor of the publication of Schwartz's *Money in Historical Perspective.* The volume also includes special remarks by Milton Friedman and Karl Brunner, an introduction written by Bordo, and a brief foreword by Martin Feldstein. It should be a helpful reference work in monetary economics for students, policymakers, and academic economists.

Bordo is an NBER research associate and a professor of economics at the University of South Carolina.

This volume may be ordered directly from the University of Chicago Press, Order Department, 11030 South Langley Avenue, Chicago, IL 60628. Academic discounts of 10 percent for individual volumes and 20 percent for standing orders for *all* NBER books published by the University of Chicago Press are available to university faculty; orders must be sent on university stationery.

Tax Policy and the Economy

Tax Policy and the Economy, edited by Lawrence H. Summers, is now available from The MIT Press for $13.95. This is the third in an annual series of NBER paperback volumes based on a conference on tax policy held each November. The papers in this volume cover: venture capital and capital gains taxation; sources of IRA savings; the effect on the 1983-4 recovery of budget deficits, tax incentives, and the dollar; the incentive effects of the corporate alternative minimum tax; and Japanese tax reform and corporate investment.

This volume is nontechnical and should appeal not only to academic, government, and corporate economists, but also to tax attorneys, individuals in business, and anyone with an interest in the policy debate over taxes.

Summers is the Nathaniel Ropes Professor of Political Economy at Harvard University and an NBER research associate.

This volume may be ordered directly from The MIT Press, 55 Hayward Street, Cambridge, MA 02142; the telephone number is (617) 253-2884.

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