Foreign Ownership and Firm Response to Foreign Demand Shocks (Job Market Paper)

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Abstract

This paper studies firm response and welfare implication of foreign demand shocks in a developing country when foreign-owned firms repatriate their gains. Using an enterprise survey in Vietnam, I first show that trade activities in Vietnam are predominantly conducted by foreign-owned manufacturers rather than domestic ones, even conditional on firm size. Exploiting the US-China trade war episode in 2018-2019 as a positive foreign demand shock to all Vietnam-based manufacturers, I provide evidence that the positive responses in input sourcing, product export, and employment are mainly driven by foreign-owned manufacturers, especially Chinese manufacturers. Motivated by the findings, I develop and estimate a quantitative model of trade participation with foreign ownership, where domestic and foreign-owned firms differ in their productivity, fixed costs of sourcing and exporting, as well as whether they retain net profits in Vietnam. The welfare contribution of a simulated demand shock to Vietnam similar in magnitude to the trade war would be 10 percent higher if foreign-owned manufacturers were to retain all their profits locally.

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