

# **Entry of Foreign Multinational Firms and Productivity Growth of Domestic Firms: The Case of Japanese Firms**

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## **ABSTRACT**

This paper examines the effects of foreign entry on productivity growth of domestically-owned firms, using Japanese firm-level data for the period 2000-2007. The data are taken from the comprehensive annual survey by the Japanese government, which covers firms in the manufacturing industries, wholesale and retail trade, information services, business services, and other service industries. Although productivity analyses on foreign multinationals and domestic firms in the manufacturing sector have been conducted in many previous studies, such analyses for the service sector are still scarce. This paper focuses on the service sector, taking account of the importance of foreign entry in this sector, where cross-border trade is sometimes difficult and so that firms are less likely to be exposed to the international competition.

The analysis of this paper reveals that foreign multinationals perform better than domestically-owned firms in many sectors. Although the productivity levels of the former tend to be higher than the latter, a significant difference in productivity growth rates is not confirmed. Moreover, the foreign presence in an industry tends to be negatively associated with the productivity growth rate of domestically-owned firms in the same industry, when firm fixed effects are controlled for. However, firms which are catching up towards the frontier productivity can receive positive FDI spillovers, implying that foreign entry accelerates catch-up phenomenon.

Key words: foreign direct investment, non-manufacturing sector, productivity, spillover

JEL classification: F23, L25, D24

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