HARVARD Kennedy School
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Comment on "The Fall of the Labor Share and the Rise of Superstar Firms"

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Outline

1. Do changes in the labor share reflect *more* competition or *less* competition?
   a. Could reduced competition also lead to greater shifts in the labor share between firms than within firms?
   b. Is this theory compatible with other facts: higher markups, slowing investment, a larger/more skewed return to capital, and slowing productivity growth?
   c. What is the direct evidence for "good" and "bad" sources of increased concentration?

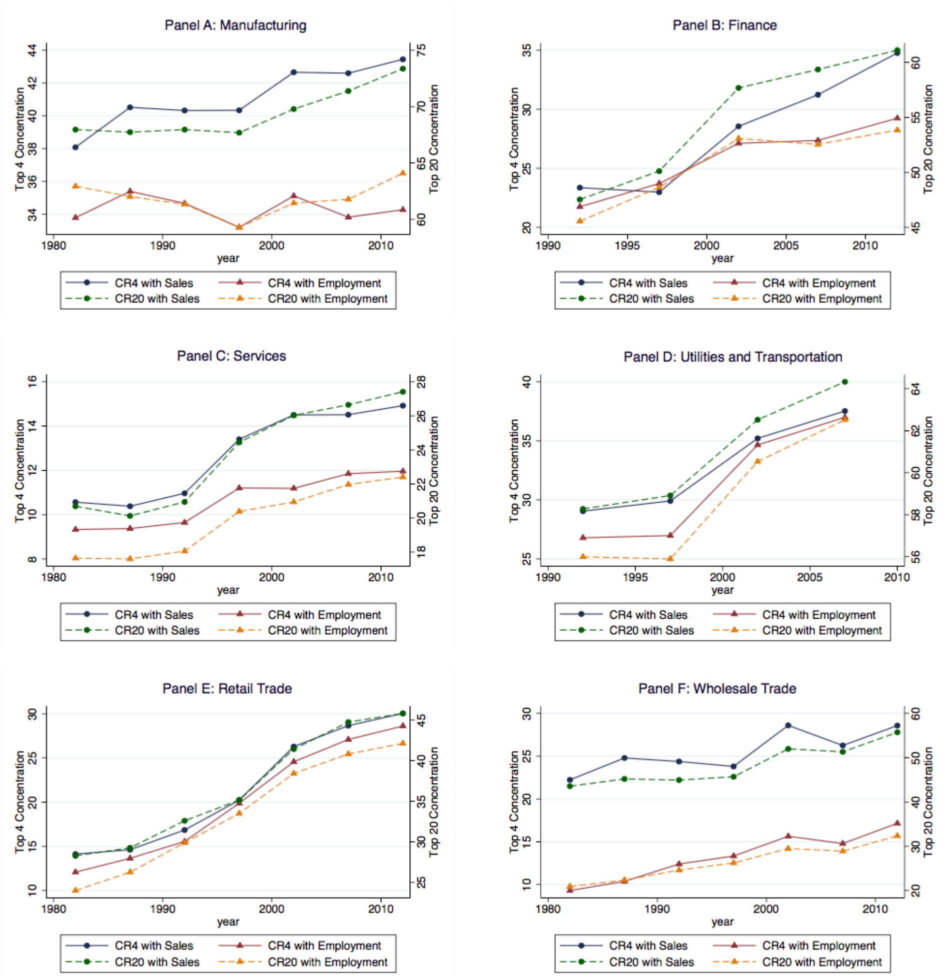
2. How much does the reduction of the labor share matter?

3. Do firm-level channels play a role in inequality *within* labor income?

4. What are the policy implications of this research?

ADKPV Shows Overwhelming Evidence of Increased Concentration—But Is This *More* or *Less* Competition?

Figure 4: Average Concentration Across Four Digit Industries by Major Sector



(A) Key "Proof" in Paper is Rise in Labor Share is Largely Between Firms, Not Within Reasonable But Not Overwhelming Evidence For This

- Paper does not distinguish between reallocation to firms with lower labor shares and firms with declining labor shares.

- In manufacturing, the best measured sector, the within firm labor share falls for all but one five year period (although in the regression estimate this is not linked to declining competition)

- ADKPV report the shift-share: (a) larger role for within firm and (b) concentration loads on within firm. "[W]ithin-firm declines in the labor share make some contribution to the aggregate decline in the labor share, but this within-firm contribution primarily comes from larger firms".

- The CR4 estimates are generally smaller/less significant than the CR20, which is inconsistent with the "superstar" interpretation.

(A) Also, Less Competition Does Not Necessarily Imply a Falling Labor Share Within Firms

- Model assumes a perfectly competitive labor market.
- With imperfect competition labor may share in the rents, for example trucking and airlines before deregulation.
- *Would be useful to see a few case studies of the impact that exogenous changes in <u>competition</u> have on the labor share within firms.*

(B) Some Other Stylized Facts in the Aggregate Data that Are Not Readily Compatible With the "More Competition" Interpretation

1. <u>Markups have risen</u>. Model implies markups have fallen.

2. <u>Investment growth has slowed</u>. Evidence links this to increased markups and reduced competition (Gutierrez and Philippon 2017)

3. <u>Returns to capital higher and more skewed</u>. Rate of return on capital relative to Treasuries has risen from ~4 pp to ~8 pp and become increasingly skewed (Furman and Orszag 2015)

4. <u>Productivity growth has slowed</u>. Model implies reallocation to more productive firms.

(C) Increased Concentration Likely Has Both Good/Natural Causes and Bad/Unnatural Causes

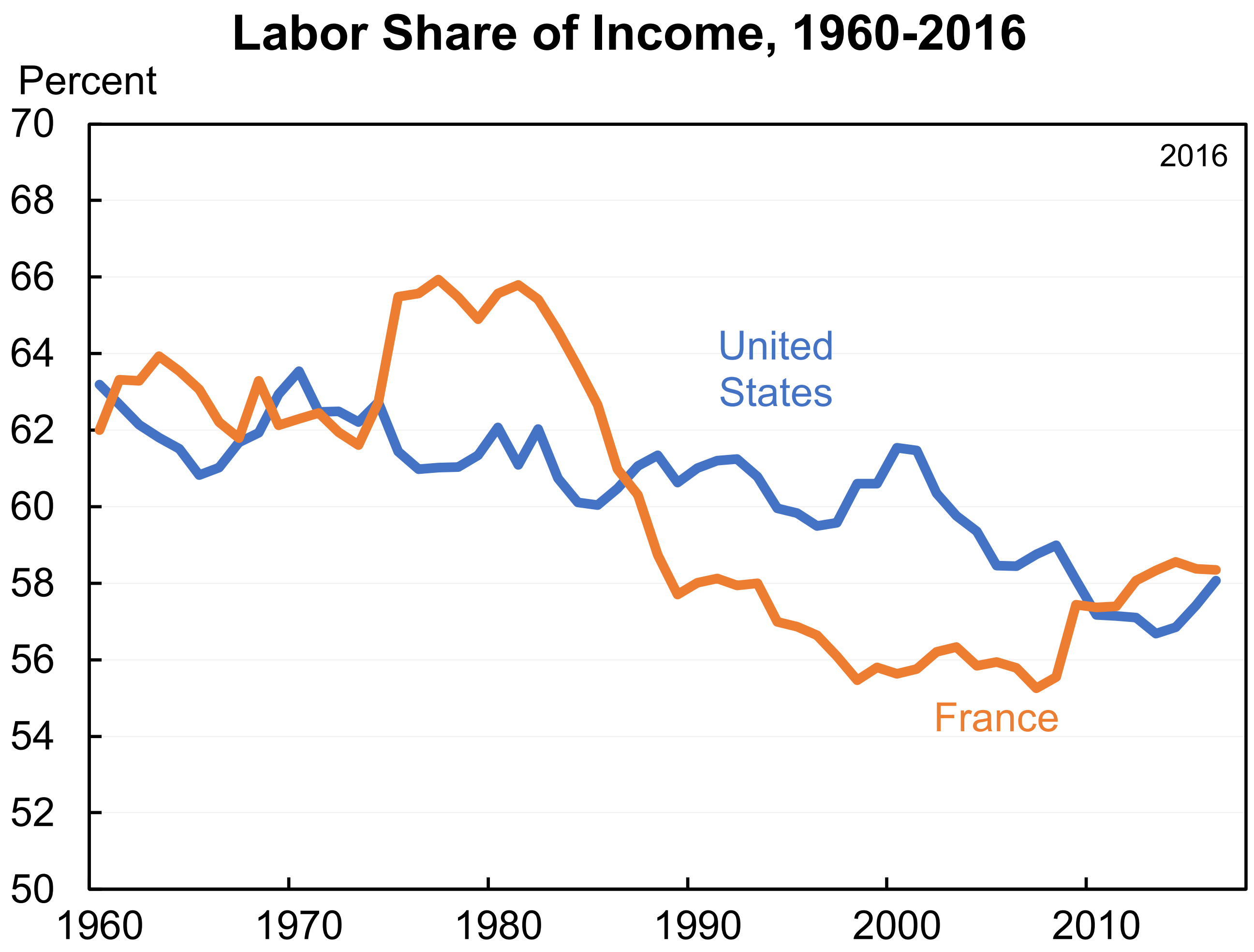
<u>Good/Natural Causes</u>

- Increasing returns to scale generally
- Network externalities specifically
- Increased price sensitivity
- Global competition leads to increased national concentration

<u>Bad/Unnatural Causes</u>

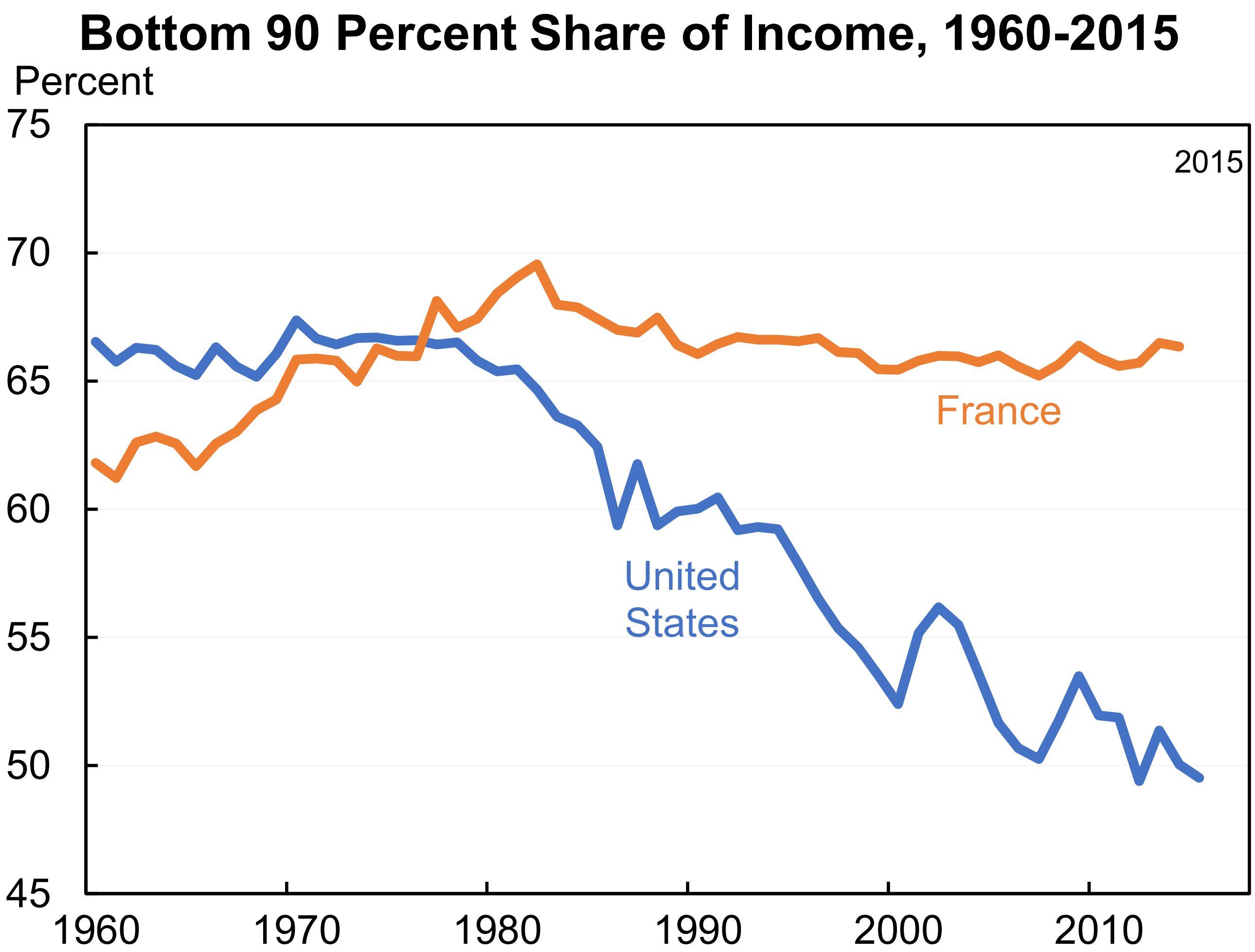
- Changes in antitrust enforcement (e.g., between 1996 and 2008 the FTC stopped enforcing mergers down to 5, 6 or 7 competitors according to Kwoka 2014)
- Increased common ownership through asset managers
- Increased regulatory barriers to entry
- Land use and occupational licensing restrictions

The Fall in the Labor Income Share Has Been Similar in Both the United States and France…



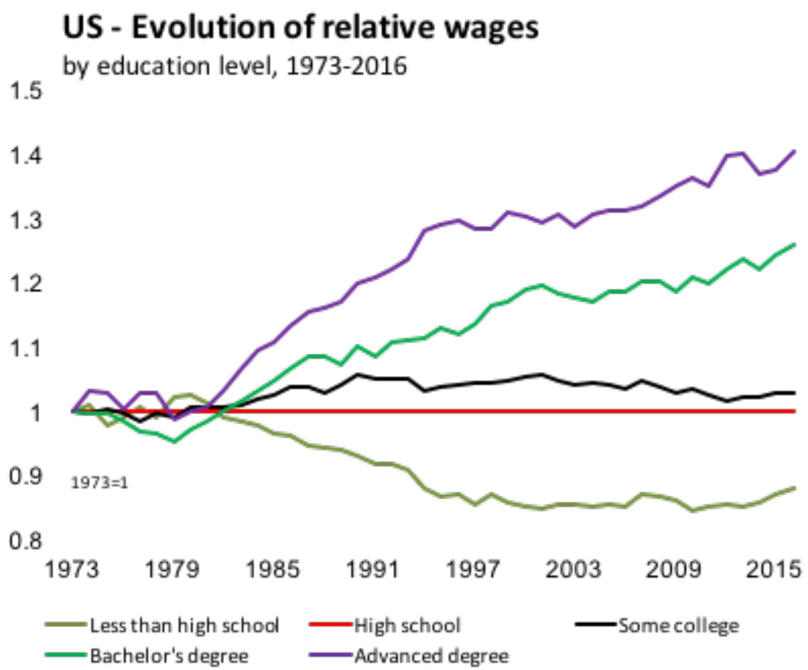
Source: AMECO; author's calculations.

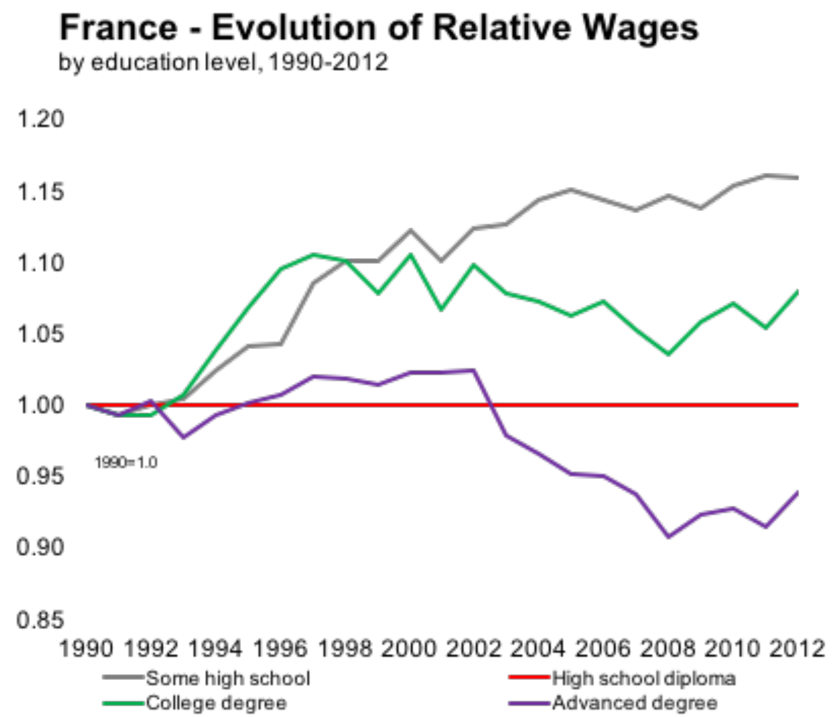
…But the Share of Income Going to the Bottom 90% Has Fallen Only in the United States



Source: World Wealth and Income Database; author's calculations.

Skill Premia Have Widened in the United States and Compressed in France





Source: Blanchard (2017)

However, Increased Labor Income Inequality Matters Less to Increased Total Income Inequality the Further Up the Distribution One Looks

Table: Decomposition of Increases in Shares of Total Income, 1979-2013

	Top 10%	Top 1%	Top 0.1%	Top 0.01%
Due to Increased Inequality in Labor Income	76%	47%	38%	28%
Due to Increased Inequality in Capital Income	8%	39%	50%	60%
Due to Change in Overall Labor/Capital Shares	16%	14%	12%	12%

Note: Changes in the share of total income accruing to each portion of the distribution are decomposed using a shift-share analysis, with equal weights for each time period (such that there are no interaction effects between changes in the labor/capital share of overall income and each group's share of overall labor/capital income).
Source: Piketty, Saez, and Zucman (2017); author's calculations.

How Much of the Rise of Inequality Does Concentration Explain?

From the paper: Concentration explains a reasonable fraction of the decline in the labor share from 1982 to 2012:

~33% in services
10% in manufacturing
25% in utilities and transportation
100%+ in retail

Using the 33% ⇒ concentration explains 5% of the increase in inequality through the labor shares channel. Or about ½ percentage point of the about 10 percentage point increase in the top 1% or top 10% income shares over this period.

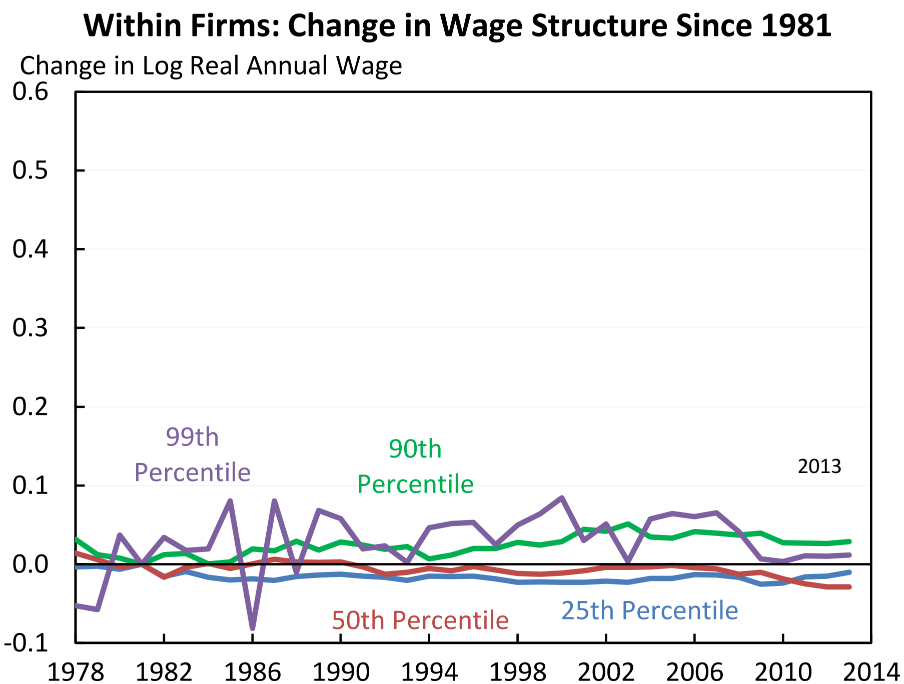
ADKPV Assume Away the Question of Inequality Within Labor Income by Assuming Perfect Competition

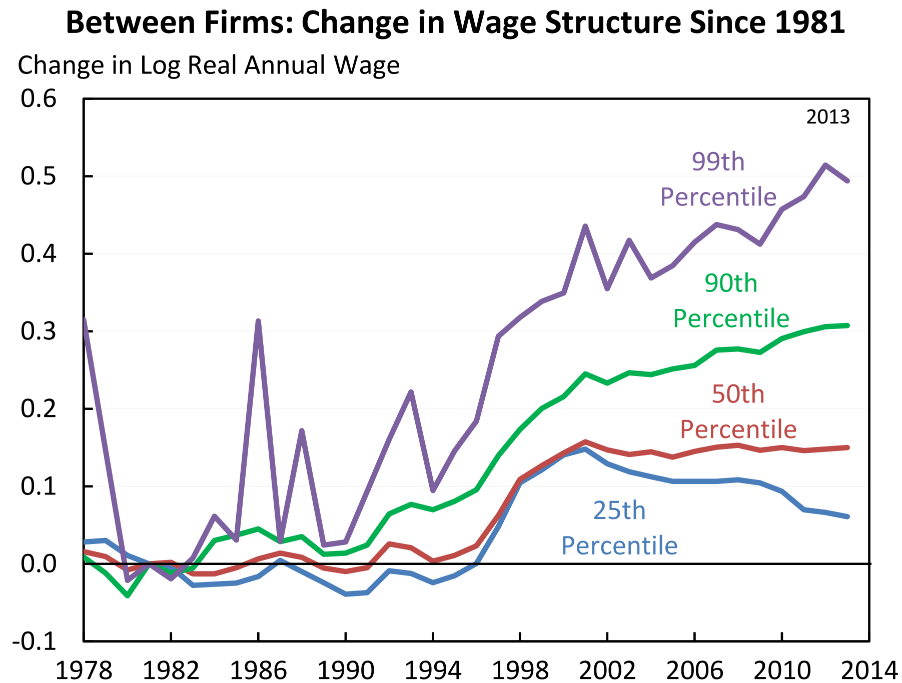
Factors that affect relative wages in the firm: marginal product of the worker

Factors that do not affect relative wages within the firm:

- Bargaining power / institutional factors
- Profitability
- Degree of competition/concentration
- Luck

Most of the Action is In Wages Between Firms—That May Reflect Some Combination of Sorting and Rent Sharing





Note: Only firms and individuals in firms with at least 20 employees are included. Only full-time individuals aged 20 to 60 are included in all statistics, where full-time is defined as earning the equivalent of minimum wage for 40 hours per week in 13 weeks. Individuals and firms in public administration or educational services are not included. Firm statistics are based on the average of mean log earnings at the firms for individuals in that percentile of earnings in each year. Data on individuals/their firms are based on individual log earnings minus firm mean log earnings for individuals in that percentile of earnings in each year. All values are adjusted for inflation using the PCE price index.
Source: Song et al. (2016).

What Are the Policy Implications of this Research?

- **ADKPV has few policy implications.** The mechanism they describe is benign—greater information leads to smaller markups and a shift to more productive firms.

- **The alternative interpretation has three implications for policies that could potentially address productivity and inequality.**
  1. Increases in product market competition
  2. Reducing barriers to labor and firm fluidity
  3. Tougher issue: network externalities and common ownership

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