

Macro Roundup Article

Headline: **Profit Puzzles**

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Tweet: Public firms' returns on the book value of assets are down ~ 50% from 1980 and private firms' returns have doubled. @EconTraina @ASollaci @CarterDavisFin

Summary: Why have US aggregate profit rates increased while financial market rates decreased since 1980? We propose a mismatch hypothesis: Profit rates in the national accounts track the return on capital for all firms, while financial market rates track the cost of capital for public firms only. We show public-firm profit rates halved since 1980, matching trends in financial markets and suggesting low market power. Mechanically, this residual private capital return series shows private capital returns had to have increased substantially to account for this secular break between aggregate and public firm profitability. The degree of this shift is significant: Private firms' profit rates are on average 10% higher than public firms' in the post-2000 period. Nonfinancial domestic private-firm profit rates doubled, suggesting high market power or risk. Size and sector differences cannot explain the divergence, though intangible-intensity might. Our results indicate substantial biases in extrapolating public-firm trends to the aggregate economy.

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