Econometrica, Vol. 92, No. 3 (May, 2024), 603–636

WALRAS–BOWLEY LECTURE: MARKET POWER AND WAGE INEQUALITY

SHUBHDEEP DEB
Department of Economics, UPF Barcelona

JAN EECKHOUT
UPF Barcelona and ICREA-BSE-CREI

ASEEM PATEL
Department of Economics, University of Essex

LAWRENCE WARREN
US Census Bureau

We propose a theory of how market power affects wage inequality. We ask how goods and labor market power jointly determine the level of wages, the skill premium, and wage inequality. We then use detailed microdata from the U.S. Census Bureau between 1997 and 2016 to estimate the parameters of labor supply, technology, and the market structure. We find that a less competitive market structure lowers the average wage of high-skilled workers by 11.3%, and of low-skilled workers by 12.2%, contributes 8.1% to the rise in the skill premium, and accounts for 54.8% of the increase in between-establishment wage variance.

KEYWORDS: Market power, wage inequality, skill premium, technological change, market structure, endogenous markups, endogenous markdowns.

1. INTRODUCTION

WAGE INEQUALITY IN THE UNITED STATES has risen sharply since the 1980s. The skill premium, the ratio of the average wage of workers with college education or more over the average wage of workers with up to a high school education, has risen from 50% in 1980 to nearly 100% in recent years.[1] Furthermore, recent work has highlighted the significant role played by heterogeneous firms in shaping the evolution of wage inequality. Most of the rise in wage inequality is due to the increase in between-firm inequality.[2] Over the same period, there has been a corresponding rise in market power.[3]

Shubhdeep Deb: shubhdeep.deb@upf.edu
Jan Eeckhout: jan.eeckhout@upf.edu
Aseem Patel: aseem.patel@essex.ac.uk
Lawrence Warren: lawrence.fujio.warren@census.gov
The present paper formed the basis of the Walras–Bowley Lecture given by Jan Eeckhout at the North American Meeting in June 2021, scheduled to be held at the Université du Québec à Montréal and delivered online due the pandemic. We thank colleagues and seminar audiences for many useful comments and insightful discussions. Eeckhout gratefully acknowledges support from the ERC, Advanced Grant 882499 and Deb from "la Caixa" Foundation (ID 100010434) fellowship (code LCF/BQ/DR19/11740003). We have benefited from superb research assistance by Renjie Bao and Wei Hua. Any opinions and conclusions expressed herein are those of the authors and do not represent the views of the U.S. Census Bureau. All results have been reviewed to ensure that no confidential information is disclosed. Data Management System (DMS) number: P-7083300, Subproject number 7508369. Disclosure Review Board number: CBDRB-FY20-CED006-0001, CBDRB-FY20-CED006-0032, CBDRB-FY21-202, CBDRB-FY22-360, CBDRB-FY23-0372.

[1]See Acemoglu and Autor (2011).
[2]See Song, Price, Guvenen, Bloom, and von Wachter (2018).
[3]See Hall (2018), De Loecker, Eeckhout, and Unger (2020), and Hershbein, Macaluso, and Yeh (2022).

Econometrica, Vol. 92, No. 3 (May, 2024), 603–636

WALRAS–BOWLEY LECTURE: MARKET POWER AND WAGE INEQUALITY

SHUBHDEEP DEB
Department of Economics, UPF Barcelona

JAN EECKHOUT
UPF Barcelona and ICREA-BSE-CREI

ASEEM PATEL
Department of Economics, University of Essex

LAWRENCE WARREN
US Census Bureau

We propose a theory of how market power affects wage inequality. We ask how goods and labor market power jointly determine the level of wages, the skill premium, and wage inequality. We then use detailed microdata from the U.S. Census Bureau between 1997 and 2016 to estimate the parameters of labor supply, technology, and the market structure. We find that a less competitive market structure lowers the average wage of high-skilled workers by 11.3%, and of low-skilled workers by 12.2%, contributes 8.1% to the rise in the skill premium, and accounts for 54.8% of the increase in between-establishment wage variance.

KEYWORDS: Market power, wage inequality, skill premium, technological change, market structure, endogenous markups, endogenous markdowns.

1. INTRODUCTION

WAGE INEQUALITY IN THE UNITED STATES has risen sharply since the 1980s. The skill premium, the ratio of the average wage of workers with college education or more over the average wage of workers with up to a high school education, has risen from 50% in 1980 to nearly 100% in recent years.[1] Furthermore, recent work has highlighted the significant role played by heterogeneous firms in shaping the evolution of wage inequality. Most of the rise in wage inequality is due to the increase in between-firm inequality.[2] Over the same period, there has been a corresponding rise in market power.[3]

Shubhdeep Deb: shubhdeep.deb@upf.edu
Jan Eeckhout: jan.eeckhout@upf.edu
Aseem Patel: aseem.patel@essex.ac.uk
Lawrence Warren: lawrence.fujio.warren@census.gov

The present paper formed the basis of the Walras–Bowley Lecture given by Jan Eeckhout at the North American Meeting in June 2021, scheduled to be held at the Université du Québec à Montréal and delivered online due the pandemic. We thank colleagues and seminar audiences for many useful comments and insightful discussions. Eeckhout gratefully acknowledges support from the ERC, Advanced Grant 882499 and from "la Caixa" Foundation (ID 100010434) fellowship (code LCF/BQ/DR19/11740003). We have benefited from superb research assistance by Renjie Bao and Wei Hua. Any opinions and conclusions expressed herein are those of the authors and do not represent the views of the U.S. Census Bureau. All results have been reviewed to ensure that no confidential information is disclosed. Data Management System (DMS) number: P-7083300, Subproject number 7508369. Disclosure Review Board number: CBDRB-FY20-CED006-0001, CBDRB-FY20-CED006-0032, CBDRB-FY21-202, CBDRB-FY22-360, CBDRB-FY23-0372.

[1]See Acemoglu and Autor (2011).
[2]See Song, Price, Guvenen, Bloom, and von Wachter (2018).
[3]See Hall (2018), De Loecker, Eeckhout, and Unger (2020), and Hershbein, Macaluso, and Yeh (2022).