

Discussion of “International Diversification, Reallocation, and the Labor Share”

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One-page summary

- 1 Aggregate labor share has declined in the US and other developed countries. But firm-level labor share is increasing.
- 2 Model with risk-adjusted production decisions: quantity and price of firm-specific risk drives labor share.
 - Predicts within-firm increases and reallocation towards low-share firms.
- 3 Additional predictions confirmed in Compustat data:
 - Risky firms have lower labor share.
 - Firms with foreign equity are more responsive to risk.

Outline

- 1 Intuition for the main mechanism
- 2 Are public firms representative of the economy?
- 3 Can we replicate the results in Hungary?

Risk-adjusted profit maximization

$$\max_L \mathbb{E}[AF(K, L) - wL]$$

VS

$$\max_L \mathbb{E}[\Lambda[AF(K, L) - wL]]$$

Intuition

Firm is a *leveraged* portfolio with a risky asset Q and a safe liability L .

Optimal leverage depends on risk-return tradeoff: higher risk means lower leverage.

Leverage ratio is the “labor share.”

Key assumption: labor is less risky than capital.

Are public firms representative of the economy?

Publicly traded firms have a very different risk trajectories from private firms (Comin and Philippon 2006 vs Davis et al 2007).

Volatility trends for public and private firms

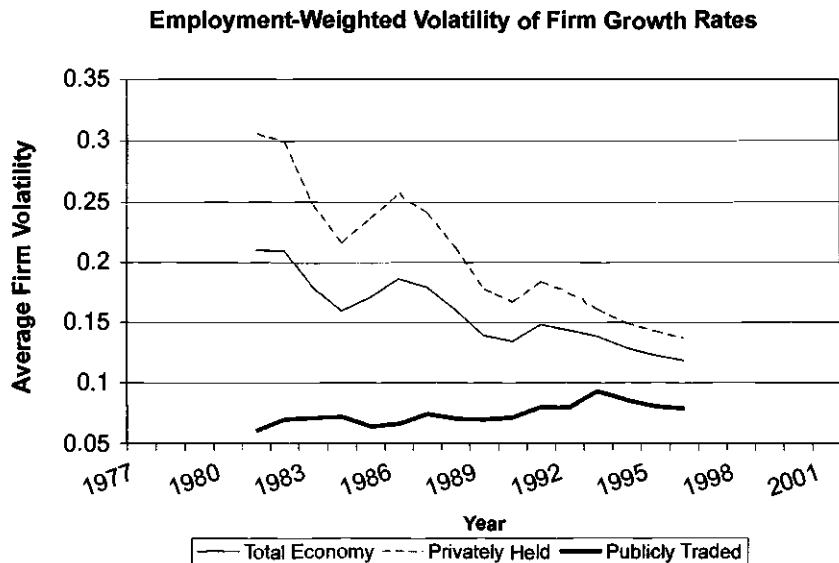


Figure 1: Davis et al 2007 (Figure 2.5)

Data from Hungary

Universe of corporations, 1989-2019: 870k businesses, of which 99% are private.

Labor share: personnel costs / value added (as in paper)

Firm beta: 2-year growth rate of log sales on log aggregate growth (unlike in paper)

Higher beta firms have lower labor share

Beta portfolio	Mean labor share
0	0.619
1	0.589
2	0.523
3	0.457
4	0.456

Foreign-owned firms have lower labor share

		Mean labor share
Majority owner		
Domestic		0.589
Foreign		0.440

Bigger firms have lower labor share

Size portfolio	Mean labor share
0	0.785
1	0.725
2	0.665
3	0.582
4	0.508

Except for largest firms, labor share is driven by size, not beta

Beta	Size 0	Size 1	Size 2	Size 3	Size 4
0	0.772	0.702	0.640	0.527	0.621
1	0.786	0.732	0.664	0.596	0.587
2	0.788	0.741	0.680	0.594	0.519
3	0.775	0.723	0.663	0.574	0.449
4	0.787	0.720	0.661	0.580	0.441

Smaller points

- What if markets are incomplete? Λ_{it} rather than Λ_t
- Cattaneo et al (2023) “On Binscatter”: cannot do covariate adjustment before binscatter