Meeting 9-5-2017

September 5, 2017

- What is the role of my paper? It seems too stylized to be quantitative, too quantitative to be conceptual...caught in the middle..and I don't see it as explaining secular changes in worker flows (at least, not the kind of thing I'm talking about - maybe the rampant use of non-competes at places like Jimmy John's, I don't know, but that's not really what my paper is about).
- Effects of **USING non-competes**
  1. **Positive for growth:** Firms can train workers, tell them secrets, etc. without worrying about immediate defection. Workers can commit not to tell. I.e. they get over the commitment problem, which improves welfare...
     - Present whenever the argument in Franco & Filson fails - i.e. whenever flow benefit to workers of knowledge gained is less than flow loss to incumbent of reduction in monopoly position.
     - Many potential aspects of firm training that are missing here.
  2. **Positive for growth:** Firms can develop IP in the first place, knowing that they will be able to train workers in using that IP to produce goods and services without worry of destroying their monopoly position (the reason they developed the IP in the first place).
  3. **Positive for growth:** Increases the incentive for entry, since the value of having a monopoly position increases.
  4. **Negative for growth:** Less knowledge spillover, effectively shifting inwards the production possibility frontier of the economy. If the model exhibits too much innovation due to business stealing externality, this can be good: "two wrongs make a right."
     - Present in my model
  5. **Negative:** Harder for employees to figure out their ideal worker-employee match. Employees do not know for sure
     - Not present in my model at all.
  6. **Negative:** workers have less incentive to invest in their own human capital (because their employer does not have to pay a competitive wage)
     - Not present in my model at all.
     - However, is this a real thing? Why can't the employer just offer to pay the employee for developing their human capital? need to think more.
  7. **Negative:** to the extent that an individual firm is an "experiment" whose quality the worker can learn, using non-competes makes reallocation from "bad" trials to "good" trials slower. This is a headwind to growth. Related to #3, but different in that there it's the worker / firm match that is a trial, and here it is the firm on its own.
- Not all of these forces are present in my model so it is not clear how reliable of an answer it will give to the question of what are the effects on growth / innovation / etc. from binding employees with non-competes vs. not doing so.
- Moreover, we aren't interested in the effect on GROWTH of USING NON-COMPETES. We are interested in the effect on WELFARE of ENFORCING NON-COMPETES.

- So, my paper is an incomplete answer to a question which is not even really the question of interest.
- Would it be a more compelling contribution to isolate a specific way in which the option to enforce non-competes leads to agents signing a bilateral contract which then somehow hurts the rest of the economy? Not sure this would even be easier...

Other notes

- Adverse selection in the market for knowledge - firms don't know which workers are the ones who will run off and steal their ideas. Any wage carries with it an implicit price for the knowledge that will be spilled over. If they charge a given wage, calibrated to offset the cost of future spinoffs, then only agents of a higher type - more likely to spin off - will take the job. This means they have to pay an even lower wage, i.e. charge more for the knowledge. And so on. The market for knowledge of this form collapses, and non-competes are signed.
  - What happens if we don't allow non-competes in this scenario? Whatever wage ends up being the equilibrium wage $w(q, m)$
- Why is my model inefficient *without* noncompetes? The benefit to a worker of a successful spinoff is slightly larger than the cost to the incumbent of being replaced, since there is a quality improvement. However, the net benefit to the worker of acquiring the knowledge from the incumbent is lower than the loss to the incumbent. For, roughly speaking, the loss to the incumbent is simply the previously cited quantity (loss in the event of a successful spinoff) multiplied by the probability, but the gain to the worker is this same probability multiplied by: slightly more than this amount (bc of quality improvement) minus the discounted present value of the R&D costs the worker will pay. Thus, the employee will not be willing to take a pay cut that compensates the employer for the lost knowledge, and R&D will be distorted downwards.