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

WALRAS–BOWLEY LECTURE: MARKET POWER AND WAGE INEQUALITY

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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.

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[1]See Acemoglu and Autor (2011).
[2]See Song, Price, Guvenen, Bloom, and von Wachter (2018).
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WALRAS–BOWLEY LECTURE: MARKET POWER AND WAGE INEQUALITY

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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]

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