

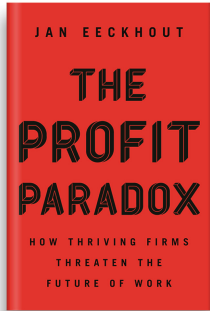
# DOMINANT FIRMS IN THE DIGITAL AGE

JAN EECKHOUT

UPF Barcelona

Bojos per l'Economia

18 January, 2025



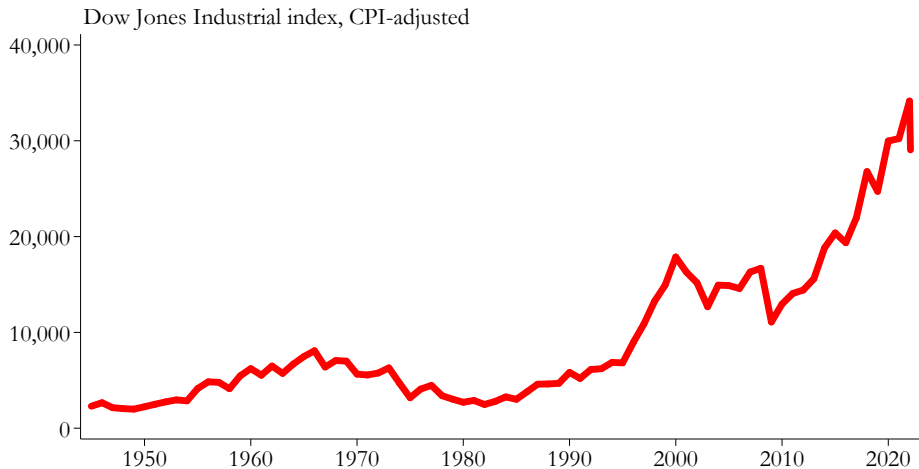
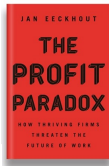
# THE PROFIT PARADOX

How Thriving Firms  
Threaten the Future  
of Work

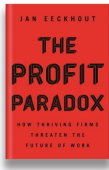
BY JAN EECKHOUT

[TheProfitParadox.com](http://TheProfitParadox.com)

# DOW JONES



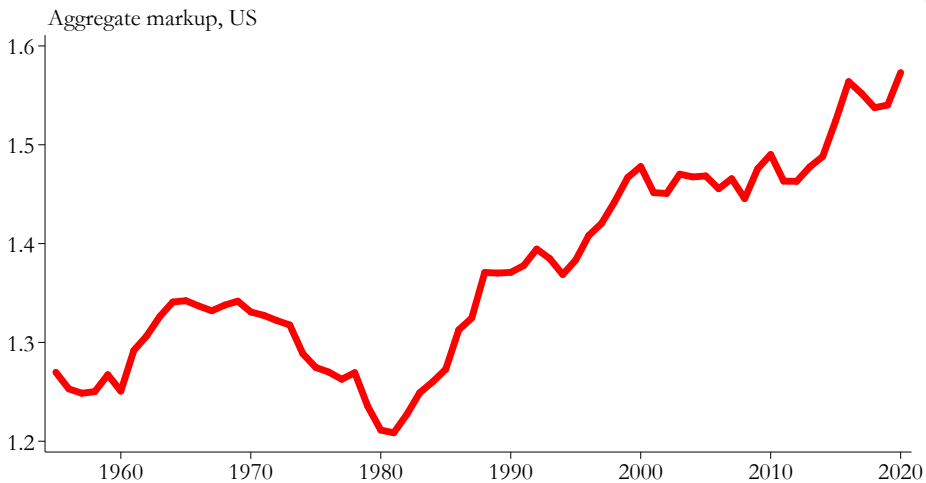
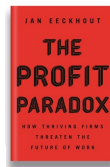
# RISE IN ECONOMY-WIDE MARKET POWER



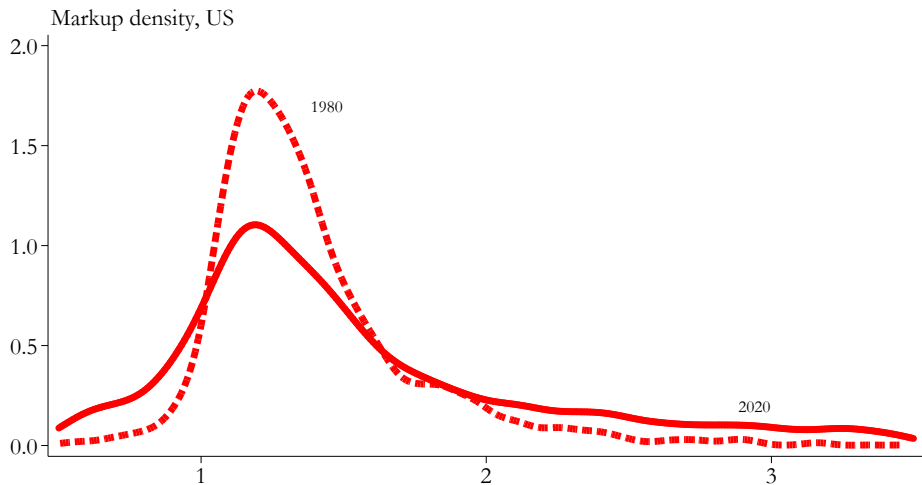
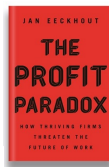
Economy-wide market power...

- Stock market valuations: p.a. growth  $< 1\% \rightarrow 7\%$
  - Markups:  $1.2 \rightarrow 1.6$
  - Profit rates:  $1\% \rightarrow 8\%$
- For a few dominant firms: distribution and reallocation

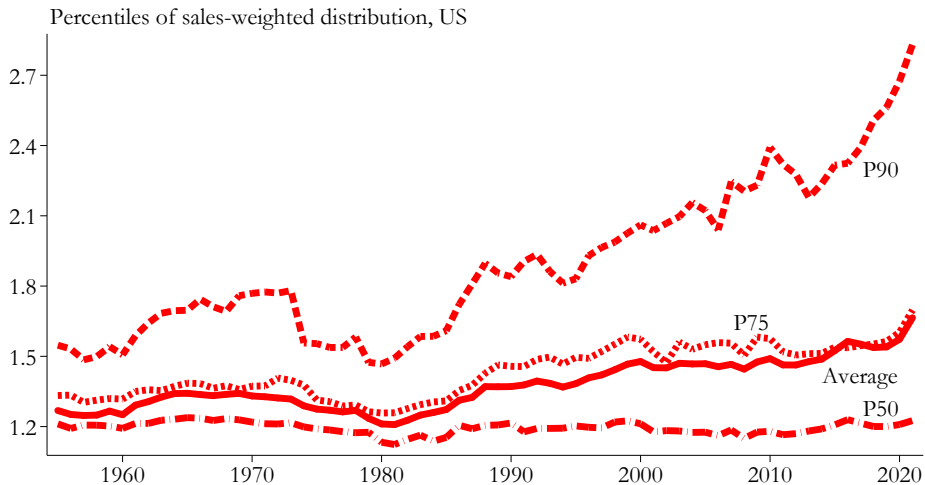
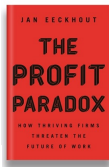
# AGGREGATE MARKUP



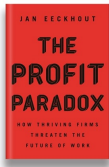
# MARKUP DISTRIBUTION



# MARKUP DISTRIBUTION: WEIGHTED PERCENTILES



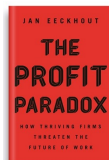
# MARKUP DISTRIBUTION



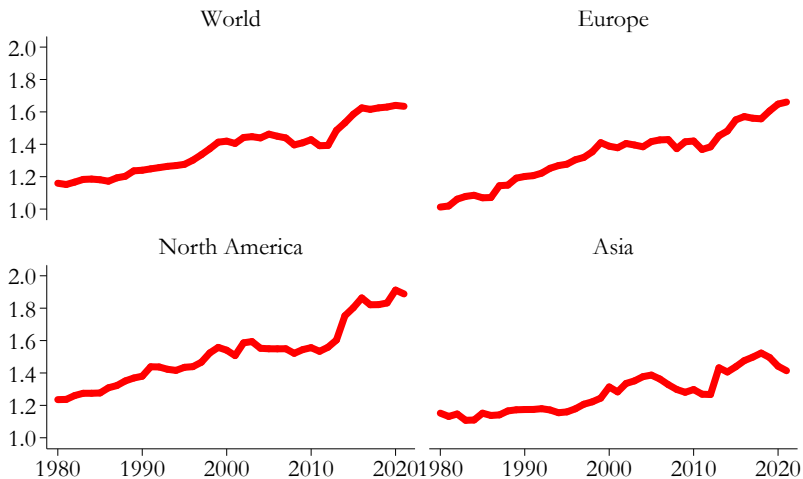
- Decomposition: within-sector, not between sectors
- Large reallocation to productive firms: Autor-Dorn-Katz-Patterson-Van Reenen (2020)
- In all sectors, from Tech to Textiles
- But, tech plays a role, Teulings-Van 't Klooster (2021)



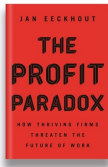
# A GLOBAL PHENOMENON



## Aggregate markups

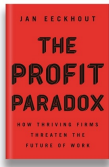


# HISTORY



- Market Power has always been part of economics:
  - Ancient Greece: Monopoly power granted by sovereign
  - British East India Company: built on monopoly power (origin of US independence)
  - First formal models economics: Cournot oligopoly in 1838
  - Any business person knows: gain and exploit market power to make money
  - Schumpeter: (temporary) market power is necessary for growth (creative destruction)
- Has its own discipline, Industrial Organization (IO)
- Macro: Monetary policy; Input-output connections and aggregate fluctuations
- Antitrust Policy: Herfindahl-Hirschman Index (HHI)

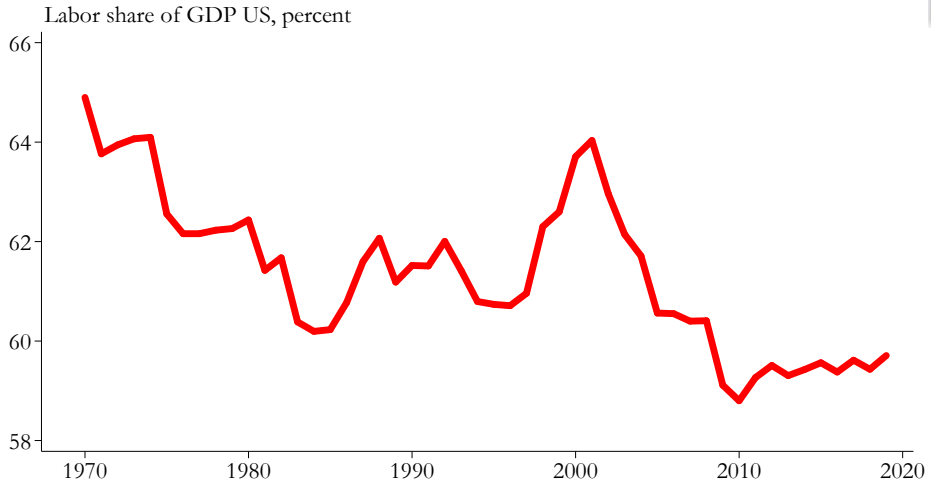
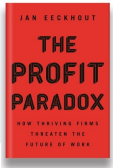
# MACROECONOMIC IMPLICATIONS



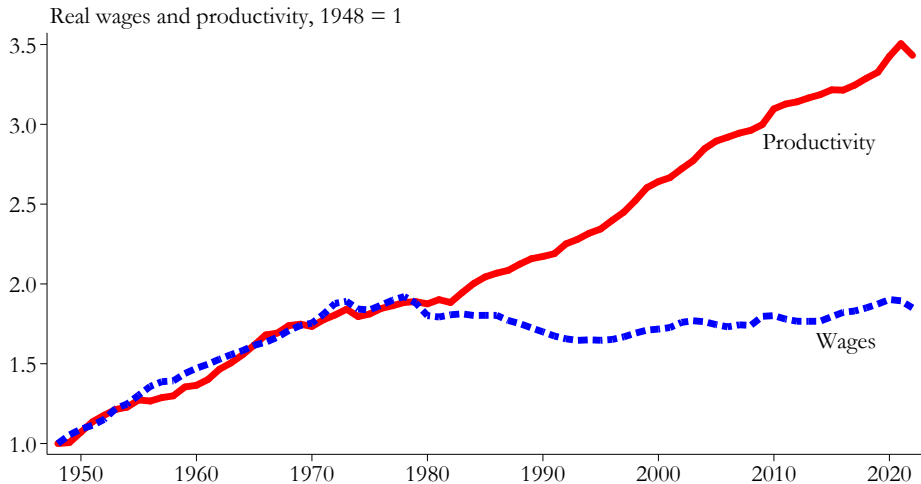
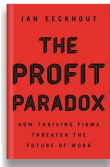
Economy-wide market power ... has an **economy-wide** impact

- Declining labor share
  - Wage stagnation (wedge productivity–wages)
  - Falling labor force participation
- Declining business dynamism
  - Labor reallocation
  - Startup rate
- Rising Wage Inequality

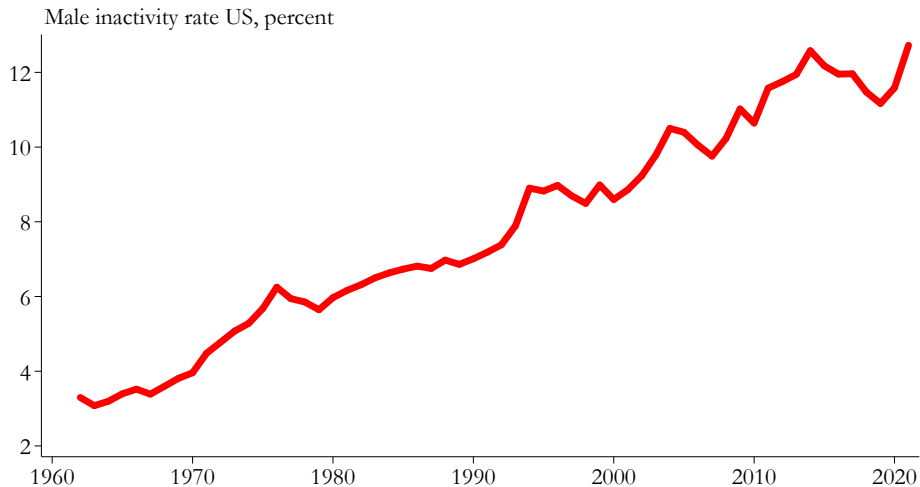
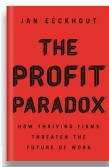
# LABOR SHARE



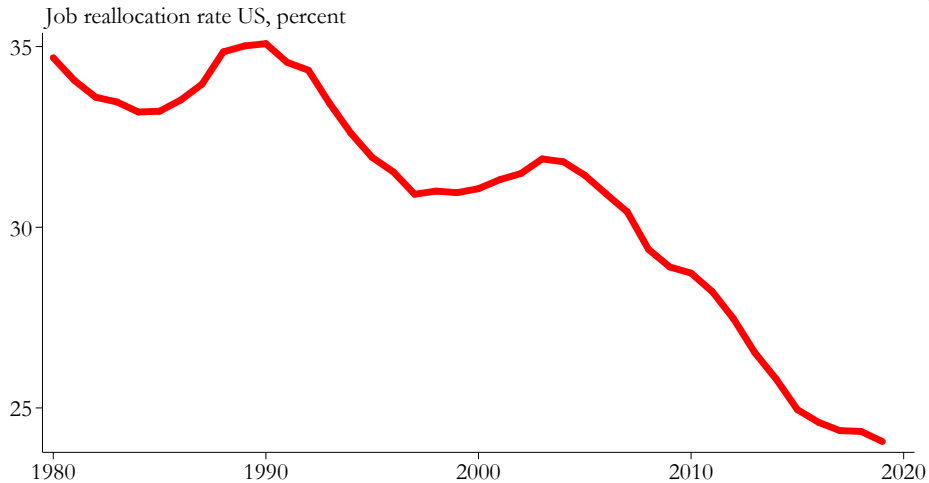
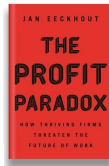
# LABOR SHARE: WAGE STAGNATION



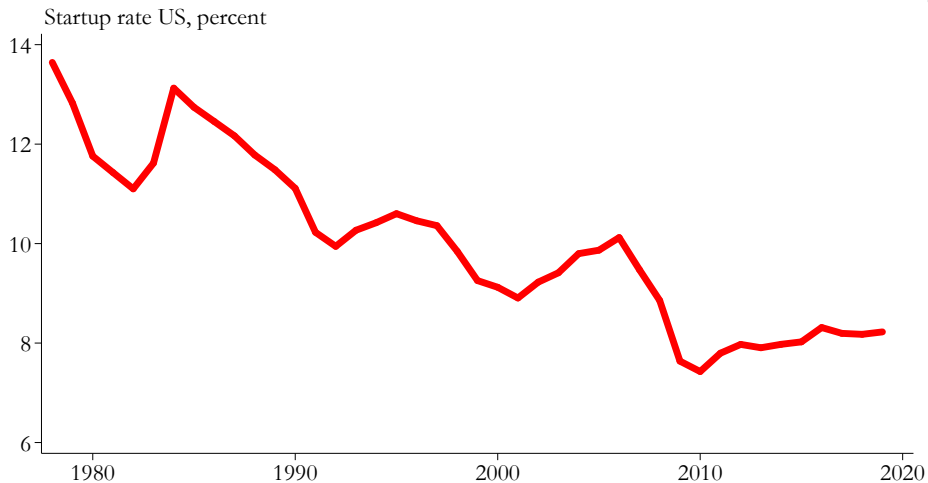
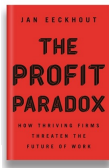
# LABOR SHARE: LABOR FORCE PARTICIPATION



# BUSINESS DYNAMISM: JOB REALLOCATION

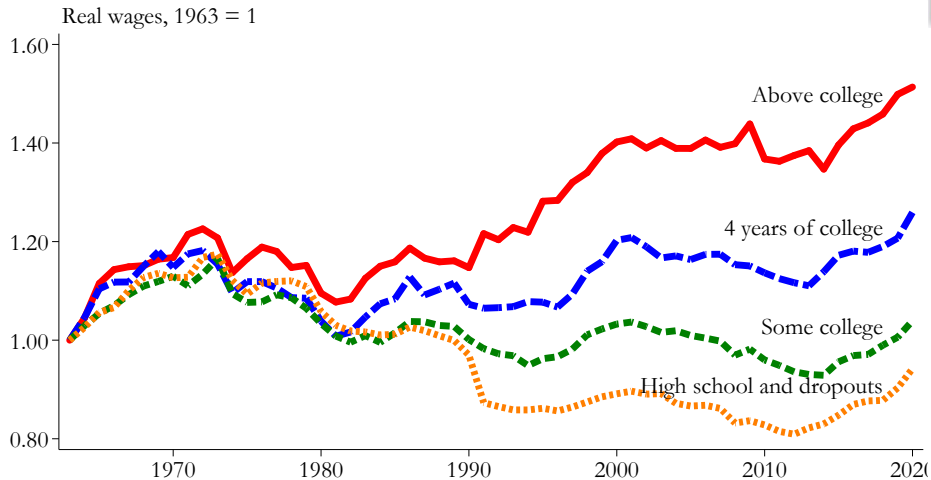
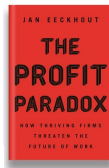


# BUSINESS DYNAMISM: STARTUPS

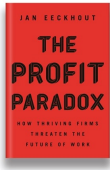




# WAGE INEQUALITY



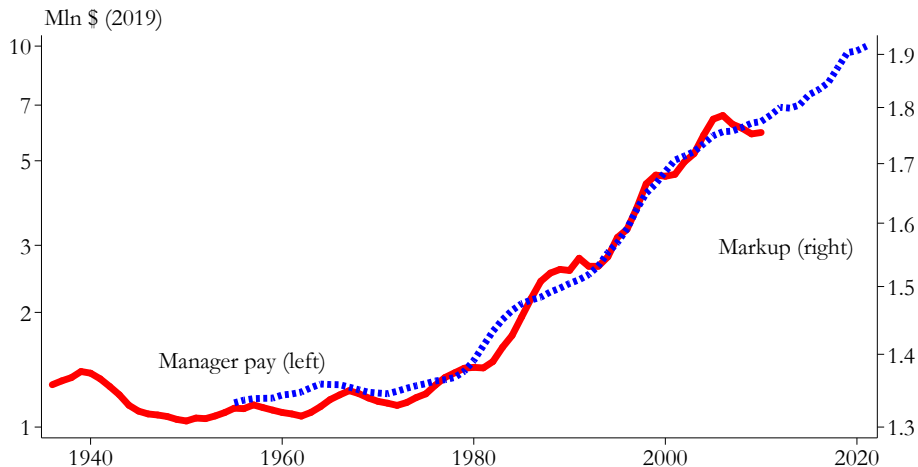
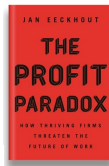
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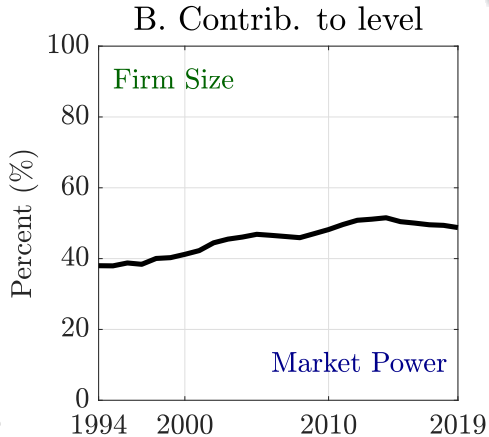
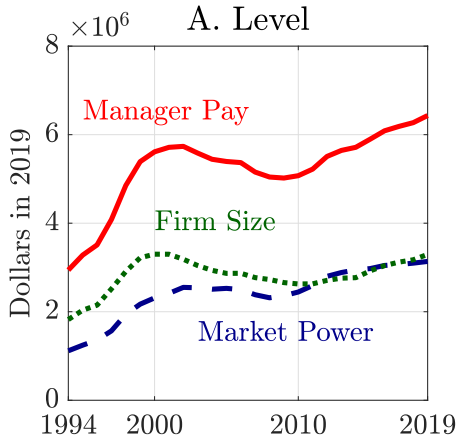
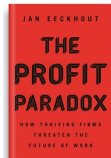
## The role of Market Power

- Between-firm inequality: increases due to market power ( $> 50\%$ )
- Wage stagnation: wage decline even without **technological regress**

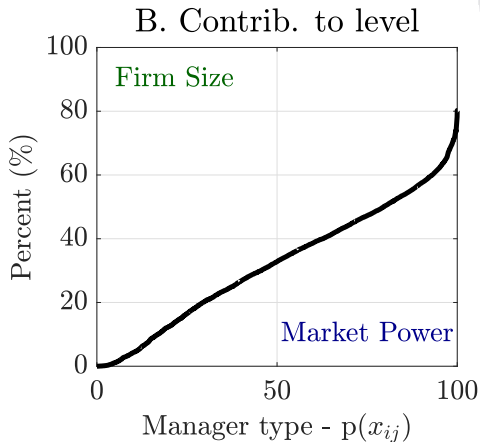
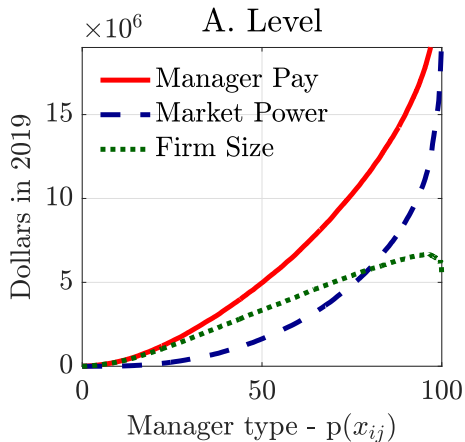
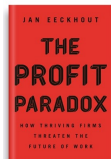
# WAGE INEQUALITY: SUPERSTAR PAY



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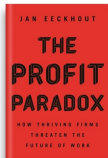
# WAGE INEQUALITY: SUPERSTAR PAY





*“I don’t want a business that’s easy for competitors. I want a business with a moat around it. [...] Our managers of the businesses we run, I’ve got one message for them, which is to widen the moat.” – Warren Buffett (2007)*

# ECONOMIC MECHANISMS

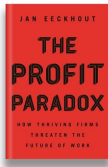


What are the economic mechanisms (including General Equilibrium effects)

Causes

1. Lax antitrust enforcement – ‘Bork doctrine’ starts in early 1980s
2. Fast technological change
  - Scale economies: Fixed cost + 40%; Returns to scale: from 1 to 1.05
  - Rising dispersion in productivities:  $\sigma = .03 \rightarrow .07$
3. Globalization

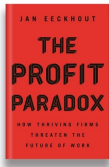
# WELFARE COST



- Output (and welfare) loss: 8% of GDP – De Loecker e.a. (2022), Edmonds e.a. (2022)
  - Large reallocation towards most productive firms
  - Even larger decline due to rent-extraction (deadweight loss)
- Efficiency gain + market power:
  - price  $p$  ↘
  - cost  $c$  ↘ ↘
  - markup  $\frac{p}{c}$  ↗

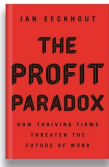


# POLICY



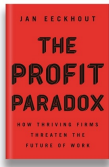
- Taxation: can redistribute, but cannot get rid of inefficiency
- Only reducing economy-wide market power will reduce inefficiency

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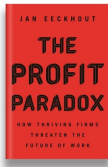
- Taxation: can redistribute, but cannot get rid of inefficiency
- Only reducing economy-wide market power will reduce inefficiency
- But, current antitrust/regulation
  - focuses on direct harm to consumers and workers
  - has limited tools to deal with (pecuniary) externalities from economy-wide market power

# POLICY



- More competition
  - Split up firms? Maybe
  - Regulation: **interoperability** – separate network from operators (pro-competitive)
  - Antitrust policy: merger review, Ex ante regulation, market investigations,...
  - Regulate dominant firms as utilities

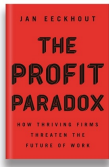
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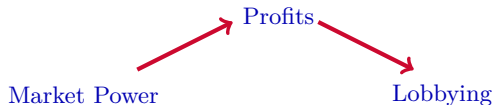
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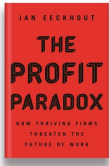
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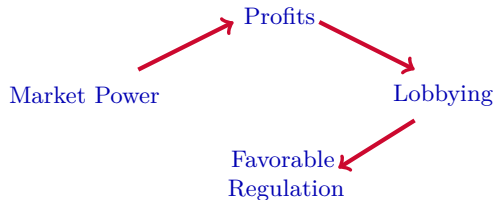
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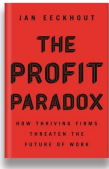
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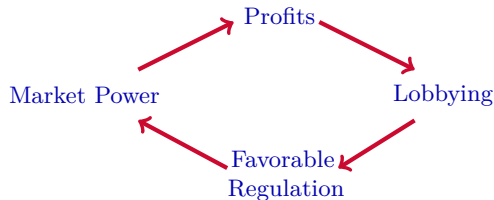
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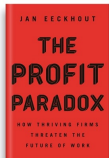
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# DOMINANT FIRMS IN THE DIGITAL AGE



- Fast technological change → market power → economy-wide implications
- Large welfare cost (8% of GDP); future?
- Not first time:
  - 1900, electricity, telegraph, railways → now all are regulated utilities
  - But... it took 2 wars and the great depression to undo market power



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