LABOR MARKET POWER & THE DISTORTING EFFECTS OF INTERNATIONAL TRADE

MATTHIAS MERTENS

WHAT DOES THE STUDY DO?

- Question: How do trade shocks shape and interact with labor market distortions that create market power in labor markets and prevent an efficient allocation of labor?
- Builds a simple partial equilibrium framework to answer this question

WHY IS THIS INTERESTING?

- Gains/losses from trade in terms of allocative efficiency → welfare gains change with imperfect labor markets → over/underestimation of trade gains
- Rent sharing between firms and employees → who loses and gains from trade?
- Framework readily extendable to other data sources

HOW TO CALCULATE LABOR MARKET DISTORTIONS

Production: $Q_{it}(.) = Q_{it}(L_{it}, M_{it}, K_{it}, \omega_{it})$

Observed wages are: $V_{it}^{L} = (V_{it}^{L^*} + \delta_{it}^{L})$

$V_{it}^{L^*} = MRPL_{it}$

Intermediate input markets: $V_{it}^{M} = MRPM_{it}$

Distortion: $\boldsymbol{f_{it}(S_{it}) = \delta_{it}^{L} = \frac{V_{it}^{L} L_{it}}{L_{it}} - \frac{\alpha_{it}^{L}}{\alpha_{it}^{M}} * \frac{V_{it}^{M} M_{it}}{L_{it}}}$

δ_{it}^{L} → Distributional aspects

δ_{it}^{L} < 0 Labor market power for firms

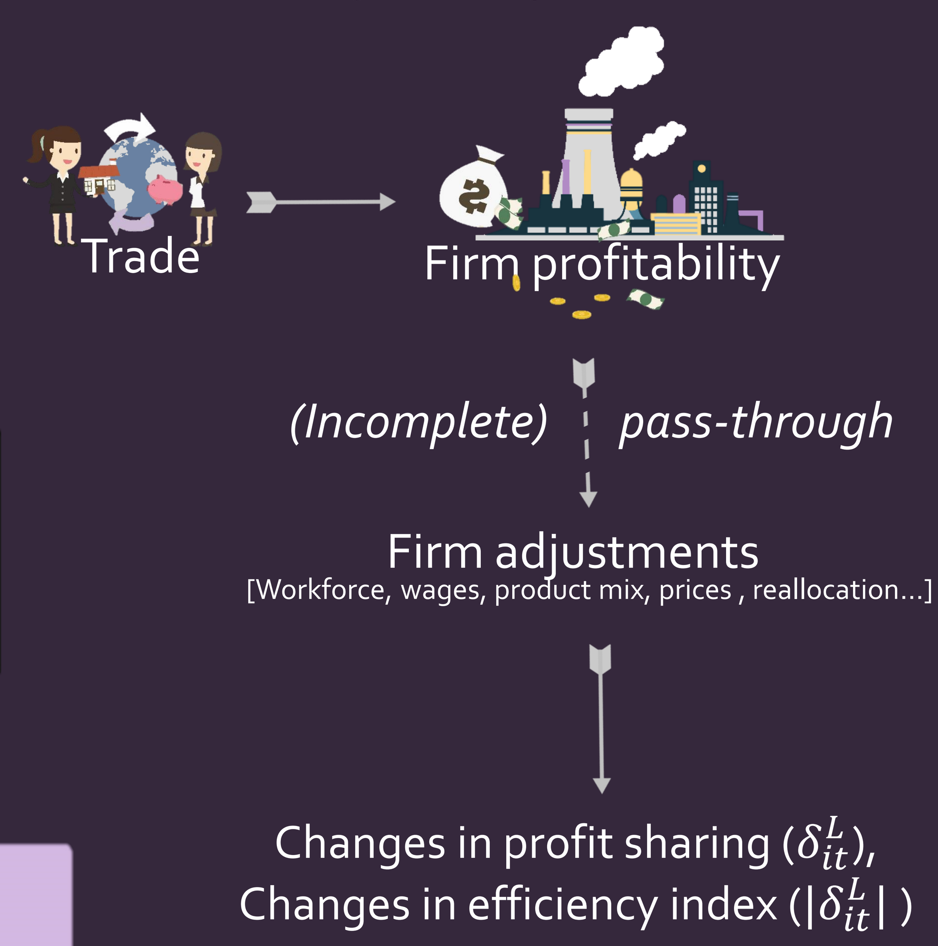
δ_{it}^{L} > 0 Labor market power for workforce

$|\delta_{it}^{L}|$ → Firm contribution to inefficiency

$i = firm; t = period; j = sector;$
$Q_{it} = output; L = labor; K = capital;$
$M = intermediates;\ \omega_{it} = TFP;$
$V_{it}^{X} = observed\ unit\ costs\ for\ X;$
$V_{it}^{X^*} = optimal\ unit\ costs\ for\ X;$
$\alpha_{it}^{X} = output\ elasticity\ for\ X;$
$MPX_{it} = marginal\ product\ of\ X;$
$\delta_{it}^{X} = input\ market\ distortion\ for\ X;$
$X = \{L, K, M\}$
$\boldsymbol{S}_{it} = sources\ of\ distortions$

SOURCES OF LABOR MARKET POWER

MECHANISM



LABOR MARKET DISTORTIONS AND TRADE SHOCKS

$$\underbrace{y_{it}}_{y_{it} = \{\delta_{it}^{L},\ |\delta_{it}^{L}|\}} = \underbrace{\overbrace{\gamma_{IMP} IMP_{it-1}^{CHN}}^{\text{Import from China}} + \overbrace{\gamma_{EXP} EXP_{it-1}^{CHN}}^{\text{Exports to China}}}_{\text{Instrumented}} + \underbrace{\boldsymbol{C}'_{it-1}\boldsymbol{\gamma}}_{\text{Controls}} + \overbrace{\upsilon_{i*j} + \upsilon_{t}}^{\text{Fixed effects}}$$

FINDINGS

- Most of the time, export demand and import competition shocks fortify existing distortions.
- Firms with labor market power do not raise labor expenditures after export profit gains (profit relative to labor share inefficiently increases).
- Firms in which workers have labor market power do not decrease labor expenditures sufficiently (profit relative to labor share inefficiently falls).
- Export effects four times more important than import effects.
- Implies losses in terms of allocative efficiency from trade.
- Diminishes trade gains compared to a standard model with competitive labor markets.

MORE RESEARCH? GO HERE:

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