Large Firms and M&A

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UPF Barcelona

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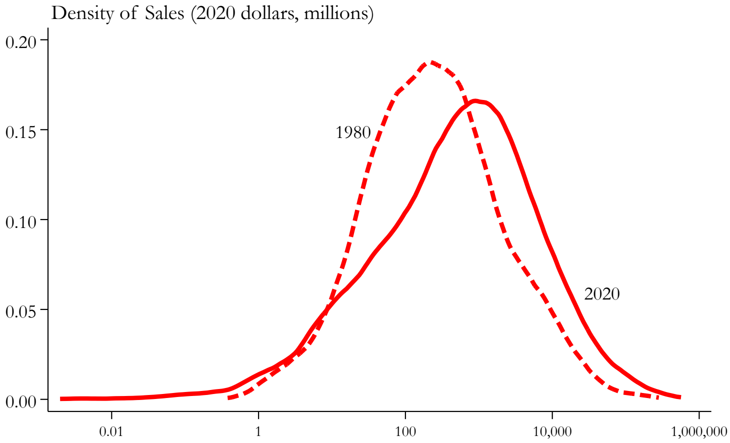
Large Firms: Size Distribution



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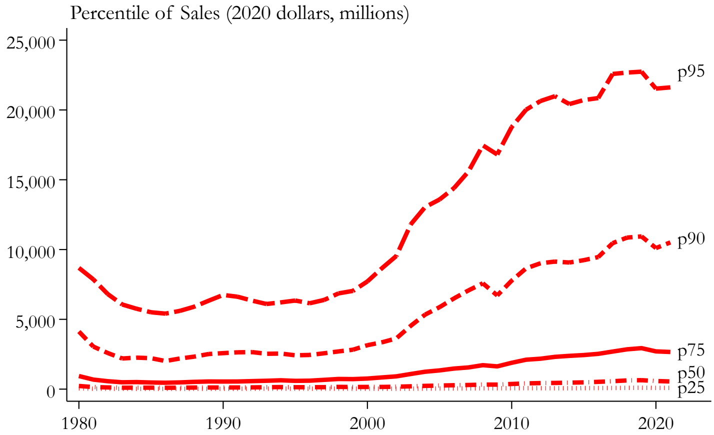
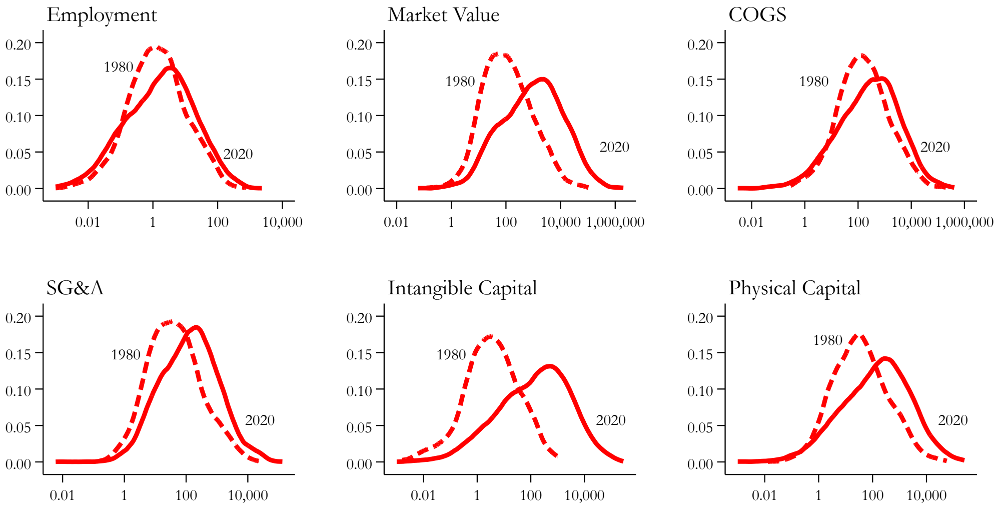
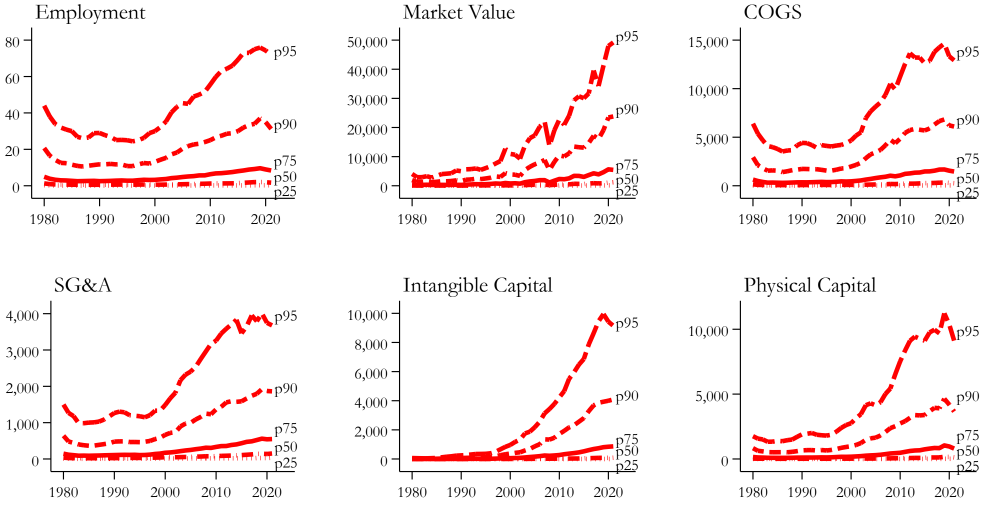


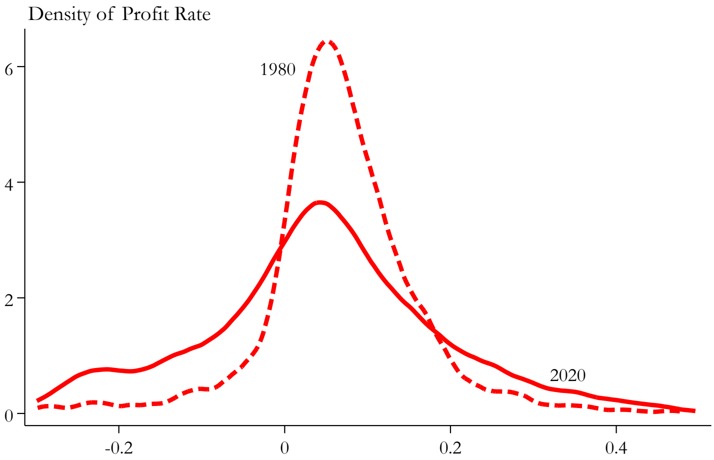
Which Size?


Employment
Market Value
COGS
SG&A
Intangible Capital
Physical Capital
1980
2020
0.00
0.05
0.10
0.15
0.20
0.01
1
100
10,000
1,000,000

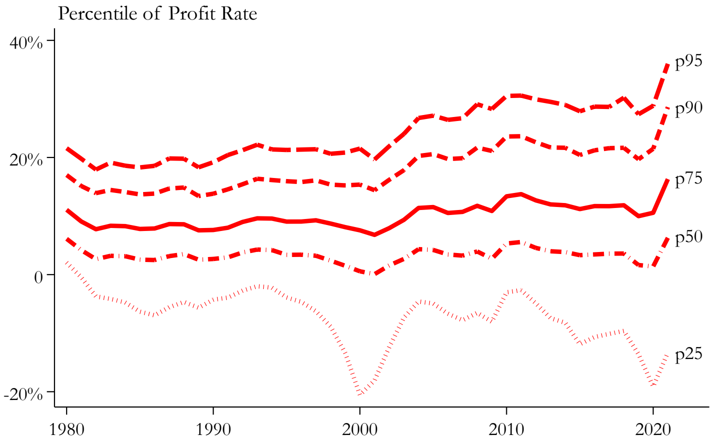
Which Size? Percentiles



Economic Profits



Economic Profits: Percentiles

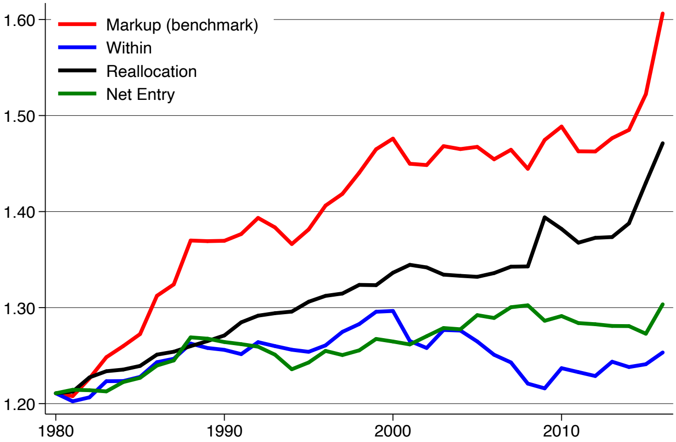


Why Superstar Firms?

1. Mergers and Acquisitions
2. Technological Change
3. Firm Strategies

M&A and the decomposition of markups

$$\Delta\mu_t = \underbrace{\sum_i m_{i,t-1}\Delta\mu_{it}}_{\Delta\text{ within}} + \underbrace{\sum_i \mu_{i,t-1}\Delta m_{i,t}}_{\Delta\text{ market share}} + \underbrace{\sum_i \Delta\mu_{i,t}\Delta m_{i,t}}_{\Delta\text{ cross-term}} + \underbrace{\sum_{i\in\text{Entry}} \mu_{i,t} m_{i,t} - \sum_{i\in\text{Exit}} \mu_{i,t-1} m_{i,t-1}}_{\text{net entry}}$$



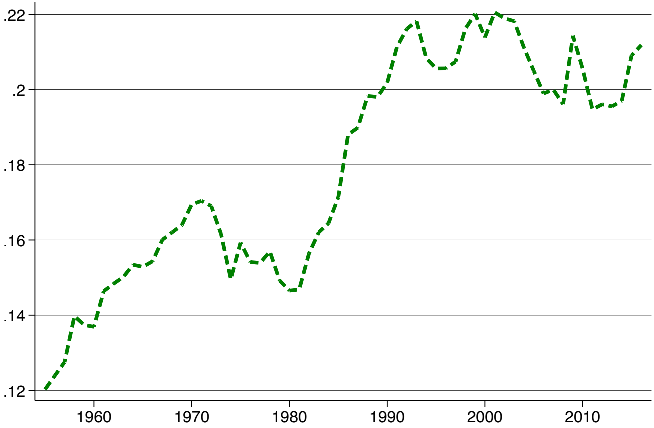
Trading off the Good and the Bad

Firm dispersion:

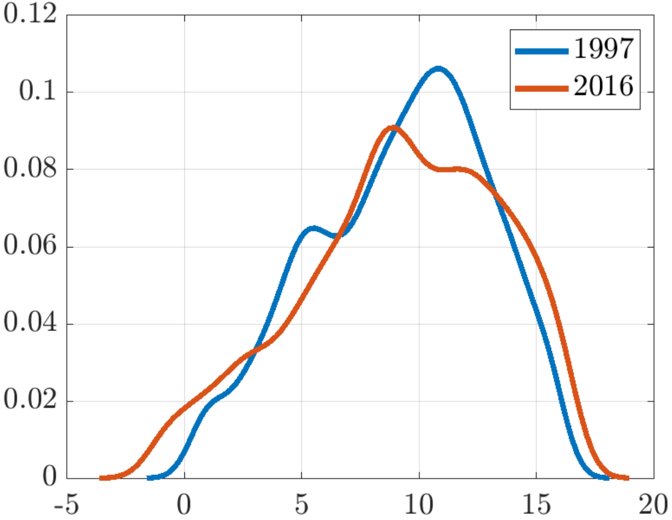
+ Reallocation towards more productive firms
  - Cost $\searrow\searrow$
  - Price $\searrow$
− Incomplete Passthrough: firms do not pass on all the efficiency gains to customers
  - Markup = Price/Cost $\nearrow$
  - Fewer competitors
  - Higher dispersion in technology
  - Deadweight loss

Technology and Intangible Capital

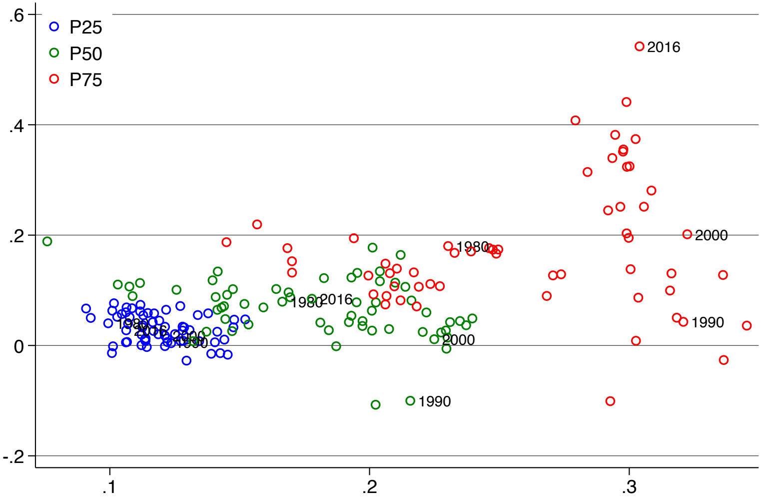
Rise in Overhead (SG&A): +40%



Widening Productivity Distribution – US Census Data



High investment, high profits (high productivity)



Firms manipulate market structure and size

What do firms do to affect market structure:

1. M&A: little evidence of synergies/complementarities
2. Killer Acquisitions $\rightarrow$ Florian

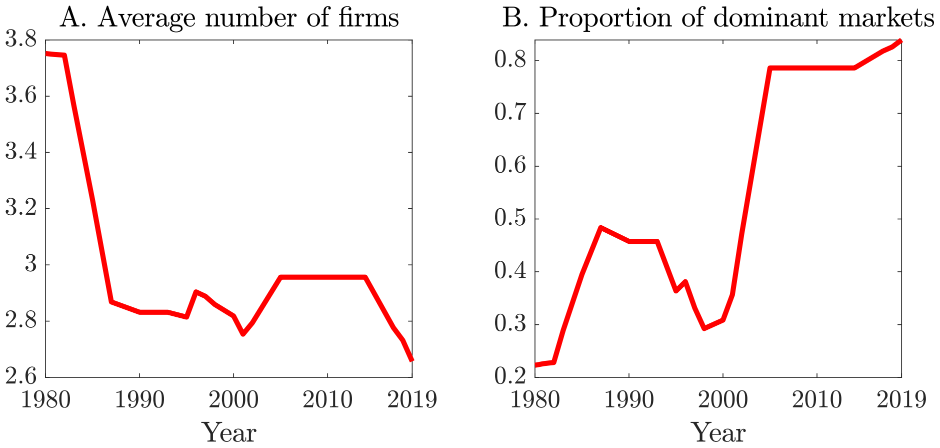
   Kill competition; dry up talent; deny access to technology (Kiva and Amazon)

3. 'Create' stronger network effects: self-preferencing,...
4. Predatory Innovation: make technology not interoperable
5. Over-invest in innovation to manipulate market structure (Sutton 1991, 2001)

Innovation and Large Firms

1. Leaders over-invest in innovation when oligopolistic competition
   - Deter entry
   - Reduce innovation by followers
2. Followers under-invest or don't invest at all
3. Falling # competitors; sharp rise in dominant firms in 2000s

Innovation and Large Firms



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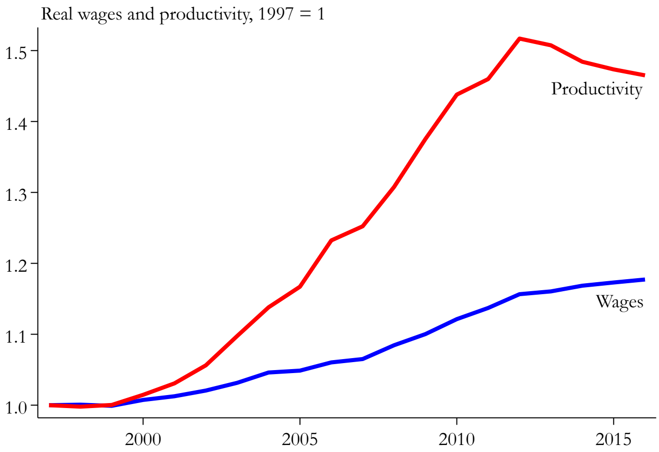
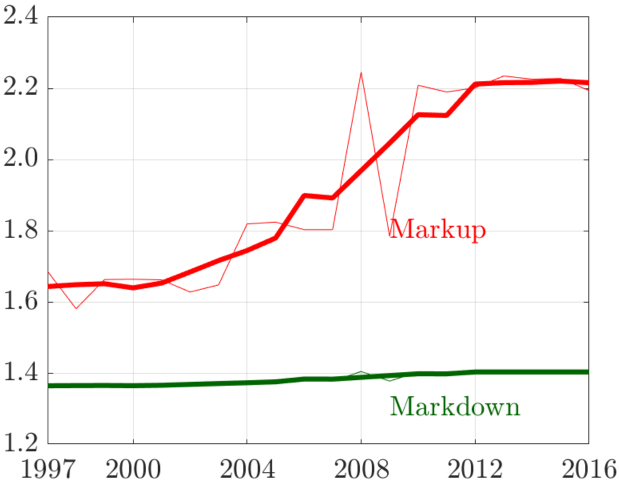
⇒ Net effect:

1. Superstar firms and increased firm dispersion
2. Net investment in innovation is down: large welfare cost of 15% of GDP

Monopsony


Real wages and productivity, 1997 = 1
1.5
1.4
1.3
1.2
1.1
1.0
2000
2005
2010
2015
Productivity
Wages

Monopsony



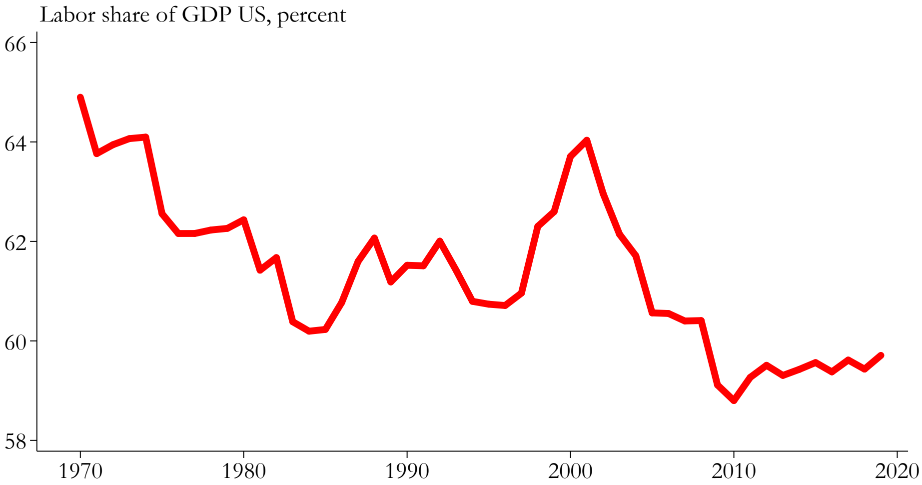
2.4
2.2
2.0
1.8
1.6
1.4
1.2
1997
2000
2004
2008
2012
2016
Markup
Markdown

Consequences of Market Power and Large Firms

The rise of dominant firms have an economy-wide impact (role of GE)

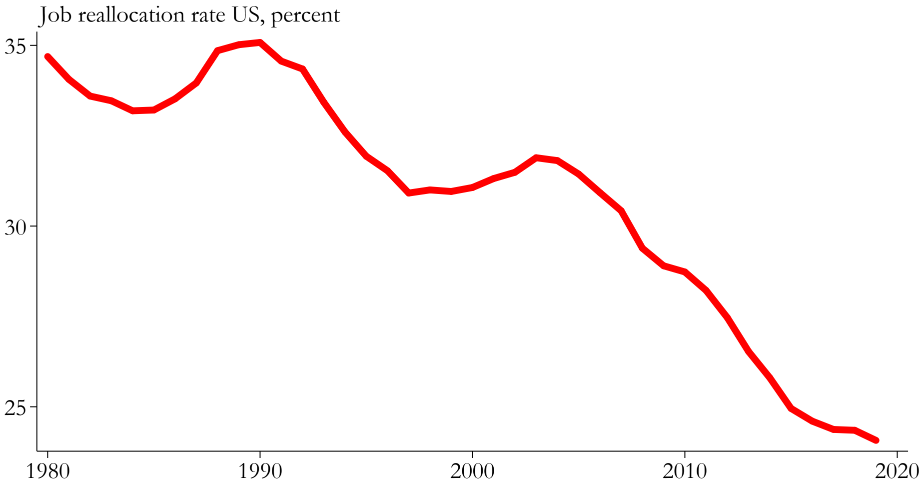
- Declining labor share
- Declining business dynamism
  - Labor reallocation
  - Startup rate
- Rising Wage Inequality

Labor Share

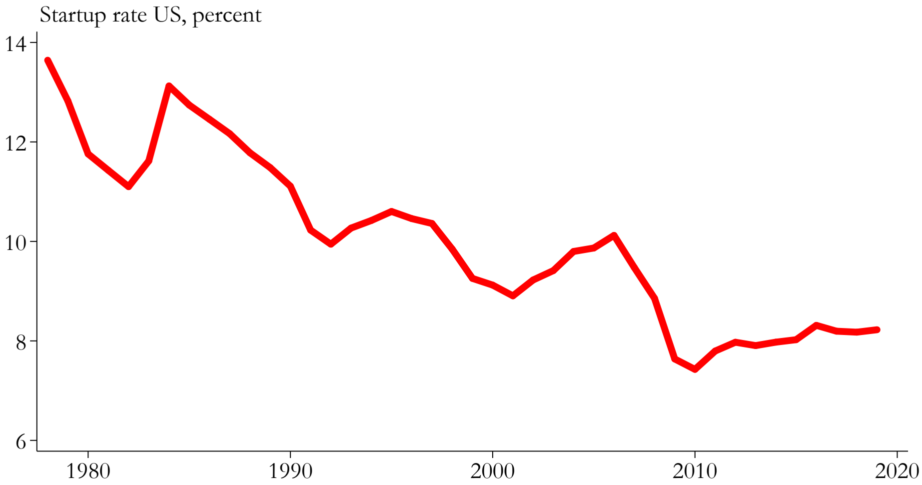


Labor share of GDP US, percent
66
64
62
60
58
1970
1980
1990
2000
2010
2020

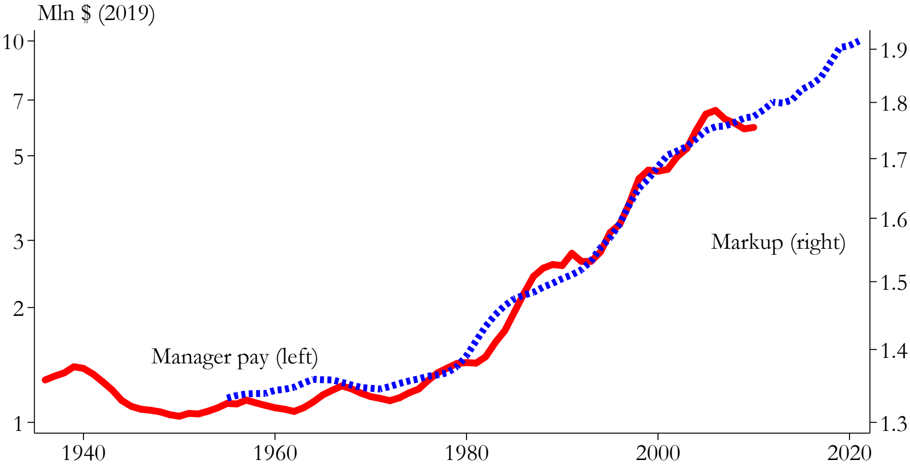
Business Dynamism: Job Reallocation



Business Dynamism: Startups



Wage Inequality: Superstar Pay



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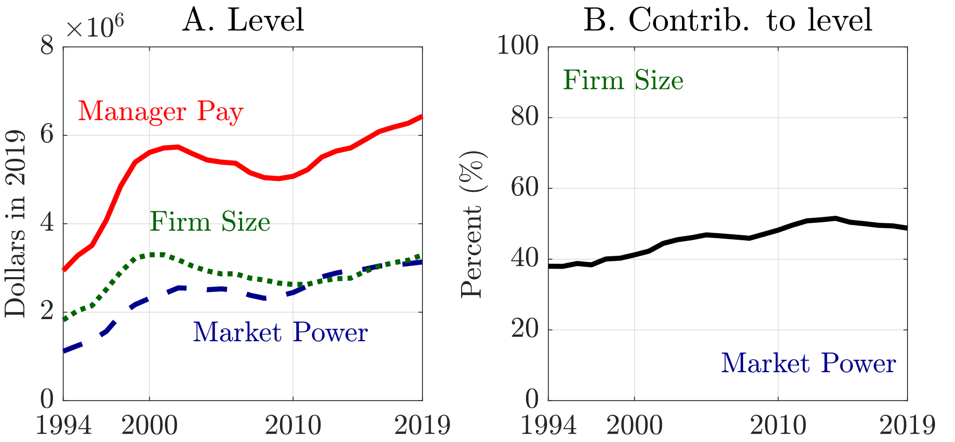

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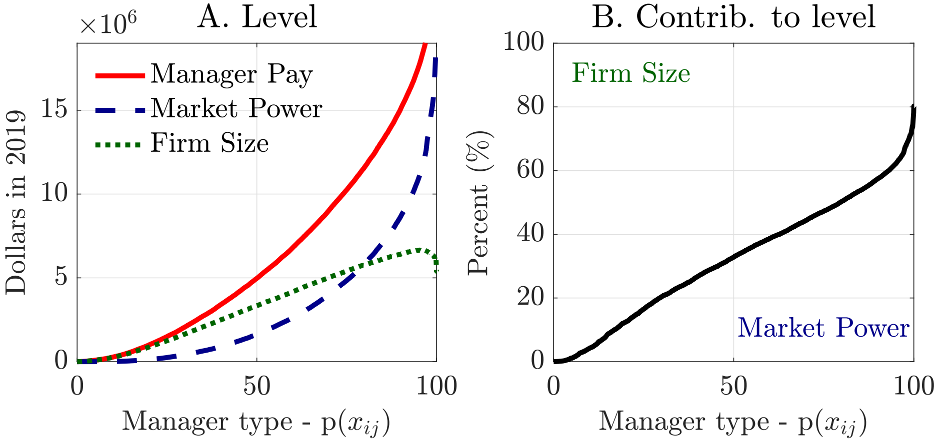

Policy: Large Welfare Effects (8% of GDP)

1. Split up firms?
2. Taxing profits: no effect on efficiency, except if strategic investm. affects mkt structure
   - Progressive profit taxation...
3. Only reducing economy-wide market power will reduce GE effects and inefficiencies:
   - M&A: panel discussion!
   - antitrust has limited tools to deal with externalities from economy-wide market power
4. Ex ante regulation (e.g. DMA): interoperability, regulate as utilities?

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→ Antitrust policy as redistribution

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