Discussion of:

Capital Share Dynamics When Firms Insure Managers

by Hartman-Glaser, Lustig, Zhang

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EFG Spring Meeting 2017
Agenda

- Recap of Their Fact and Story
- The Only Mechanism?
- Measurement
- Organizing the Literature
• Emergence of strong link between $s_K (= 1 - s_L)$ and size
• Implies divergence between average and aggregate labor share
Their Story

- Stationary productivity distribution
- Owners match with manager to run firm
Their Story

- Owners have reservation value to start firm ($P$)
- Managers get fixed wage as they are risk averse
- Manager/Owner split is equal ex-ante, but not ex-post
Their Story

Increase in firm-level volatility widens support of distribution
Implies fat-tail on the right, with greater $s_K$ dispersion
Their Story

Productivity Cutoff Shifts
due to Option Value

Fixed wage for manager implies capital share rises as

- Additional effect is increases incentive to "wait and see"
- Implies larger mass of tiny firms with negative $s_K$
Their Story

- Summary: More mass on large firms with low $s_L$, gap between aggregate and (unweighted) average firm’s experience

- Very creative and interesting idea, also nicely capture seemingly larger mass of tiny firms with losses

- Connects well with empirics on rise of idiosyncratic risk

- “As far as we know, [KN hypothesis about factor substitution] does not predict a divergence between the average and aggregate labor share that we document...”
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The Only Mechanism?

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$$Y_A = K_A^\alpha L_A^{1-\alpha} \text{ and } Y_B = K_B^\beta L_B^{1-\beta}$$
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- Average $s_K$ is constant but aggregate $s_K$ changes
Preceding story was simplified version of Oberfield and Raval (2014, and Houthakker and Sato before them).

With CES production and heterogeneous $A_K$ and $A_N$, average and aggregate factor shares can easily diverge:

- Plausible that Charles Schwab or Walmart grew as they leaned more heavily on technology, which got a lot cheaper.

- Not proof of course, but KN story is about aggregates, so increasing shares of low $s_L$ firms isn’t obviously inconsistent.
The Only Mechanism?

- Nice points about behavior of small/exiting firms, but might do more on testable implications of their story for aggregate
- Should it hold for private firms or sole proprietorships?
- Sectors/firms where options/bonuses/\(\pi\)-sharing prevalent?
- CEO compensation?
- Other countries?
- True for any concentration shock plus fixed-cost or market-share dependent markup (such as nested CES)?
The Only Mechanism?

- Why did volatility increase? Orthogonal to other stores?
- Timing?
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Micro and Macro

• Supportive of integrating micro and macro data, but mismatch of basic levels gives some pause

• For instance, do we really think the labor share is in the high 30s? At least worth addressing...

• And why measure size with Assets as in Figure 2? In above example with firms A and B, if $p_A Y_A = p_B Y_B$ we’d have:

$$K_A > K_B \text{ and } \alpha > \beta$$

• The difference appears to matter empirically...
Micro and Macro

• “The Global Rise in Corporate Saving” by Chen, Karabarbounis, and Neiman (2017)

• Similar dataset, but filter out firms with $|GS/GVA| > 1$, which greatly impacts negative among small firms.

• Replicate (for 2000) positive relationship between $s_K$ and assets, but do not between $s_K$ and sales (GVA is in between):
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- $\Pi$: Increasing markups in KN (2014), Rognlie (2014), Gutierrez and Philippon (2016), Barkai (2017), and this paper.


- $R$: Wedge between $r$ and $R$ from risk premium or financial frictions in Caballero et al. (2017) and this paper.
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- $R$ : Wedge between $r$ and $R$ from risk premium or financial frictions in Caballero et al. (2017) and this paper. Do we measure either correctly? Non U.S. public Co’s?
Conclusion

• Nice Paper!

• Very interesting and creative. Focused on issues quite different from vast literature I’ve been seeing.

• Lots of evidence their story is possible, but still unclear if it’s first-order driver. Paper would be strengthened by:
  • More evidence consistent with their mechanism and not others
  • Link discussion of why idiosyncratic shocks increased
  • Defend empirical choices from micro data that don’t accord well with macro data