

Monopsony and Outside Options

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Strategic Complements

*“...an improved outside option for workers places upward pressure on wages, even if employment in the sector is unaffected. This implication of a search and bargaining model is very basic and implies that **wages in different sectors act as strategic complements.**”*

– Beaudry et al. 2012

Outside Options

Typically a simple search and matching model yields a Nash bargained wage:

$$w = \beta \cdot \text{Match Surplus} + (1 - \beta) \cdot \text{Outside Option}$$

This work suggests that wages are influenced by two *outside options*.

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This work suggests that wages are influenced by two *outside options*. Consider an Oxford economist:

- Within academia - depends on labour market concentration in Oxford (very high!)
- Outside academia - where is the best job offer and what do they pay?

Brief Summary

- Regress average wage in each occupation-city-year cell on the two outside options
- $\log \bar{w}_{o,k,t} = \alpha + \alpha_{o,t} + \alpha_{k,t} + \gamma_1 \log oo_{o,k,t}^{occs} + \gamma_2 \log HHI_{o,k,t} + \xi_{o,k,t}$
- Construct **outside-occupation option** with empirical occupation transition data:

$$\sum_{i \neq \text{prof}} P(\text{move to occ. } i | \text{leave academia}) \times (\text{mean wage in occ. } i)$$

- Significant % of local wage variation attributed to both outside options

Comments

1. Outside-occupation option
2. Role of MPL
3. Gabaix and Koijen (2020) GIV

Outside-occupation Option

- Model:

$$\begin{aligned} & \sum_{p \neq o} P(\text{best job offer in occ. } p) \\ & \quad \times \sum_{m=1} P(\text{job at firm } m \text{ is best offer in occ. } p) \\ & \quad \times W_{m,p} \end{aligned}$$

- Empirical:

$$\begin{aligned} & \sum_{p \neq o} P(\text{move from occ. } o \text{ to } p \mid \text{leave job in occ. } o) \\ & \quad \times \text{rel. employment share of occ. } p \text{ in city } k \\ & \quad \times \text{mean wage in occ. } p \text{ in city } k \end{aligned}$$

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Role of MPL

- In main specification, the residual contains $MPL_{o,k,t}$ - dealt with by occ-year and city-year FEs
- Model: is assumption of constant within city:occupation MPL consistent with significant variation in market power? Does this matter much?

- Novel instrument for labour market concentration
- Can we reconcile exogeneity and relevance?
- Will local idiosyncratic shocks be uncorrelated with firm size?