

Regional income disparities: localization, monopoly, and finance

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Four familiar topics

- Rise in income inequality
 - Localization economies (or lack of them) & regional income disparities
 - Urbanization economies (ditto)
 - Monopoly, the return of: big tech, big pharma, big banks ...
 - Financialization: enlarged financial sector role in governance of firms
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- The world since Thatcher and Reagan
 - We consider the US case

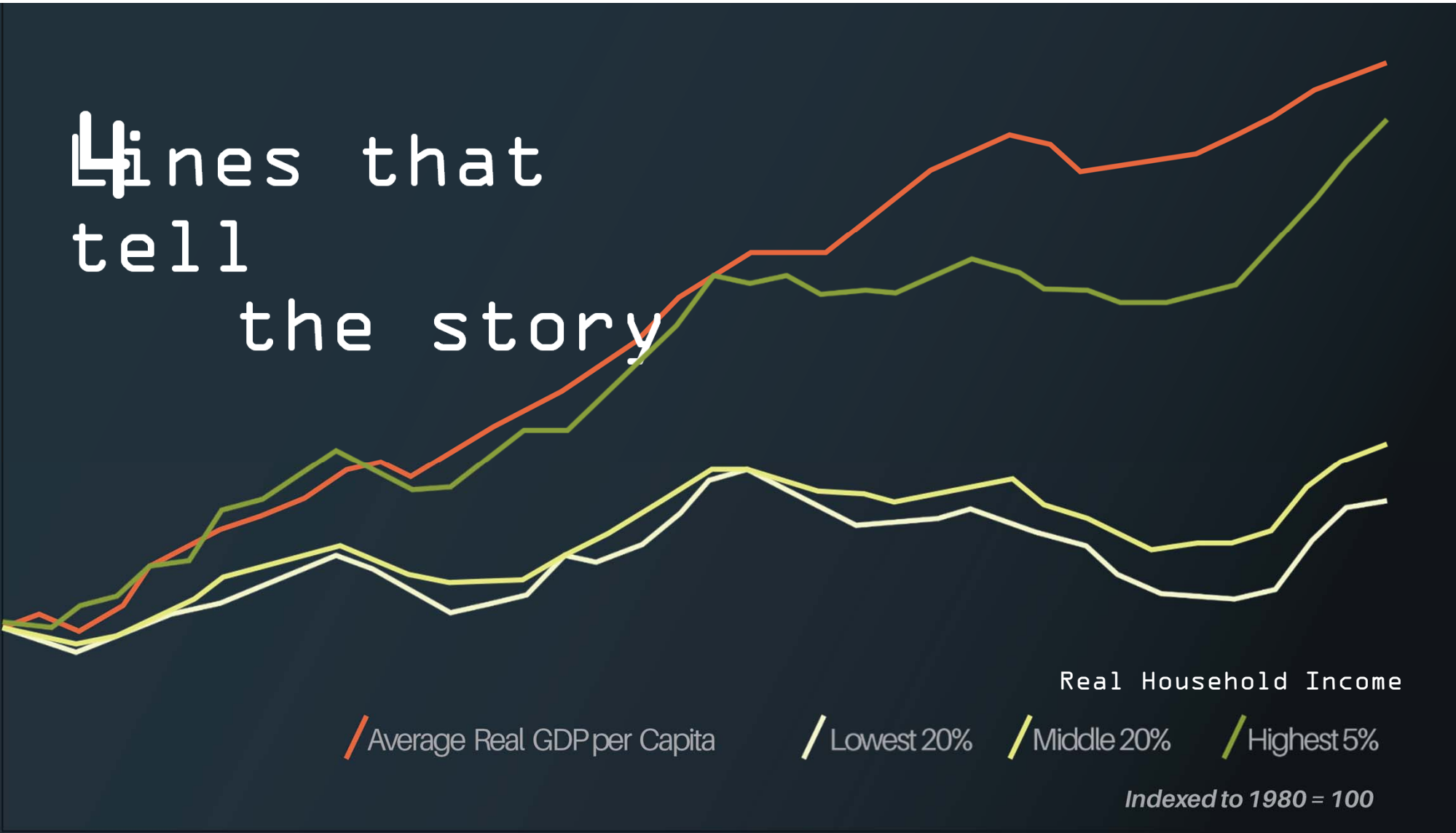
Lines that
tell
the story

175
150
125
100
75

1980 1985 1990 1995 2000 2005 2010 2015

Average Real GDP per Capita / Lowest 20% / Middle 20% / Highest 5%

Indexed to 1980 = 100



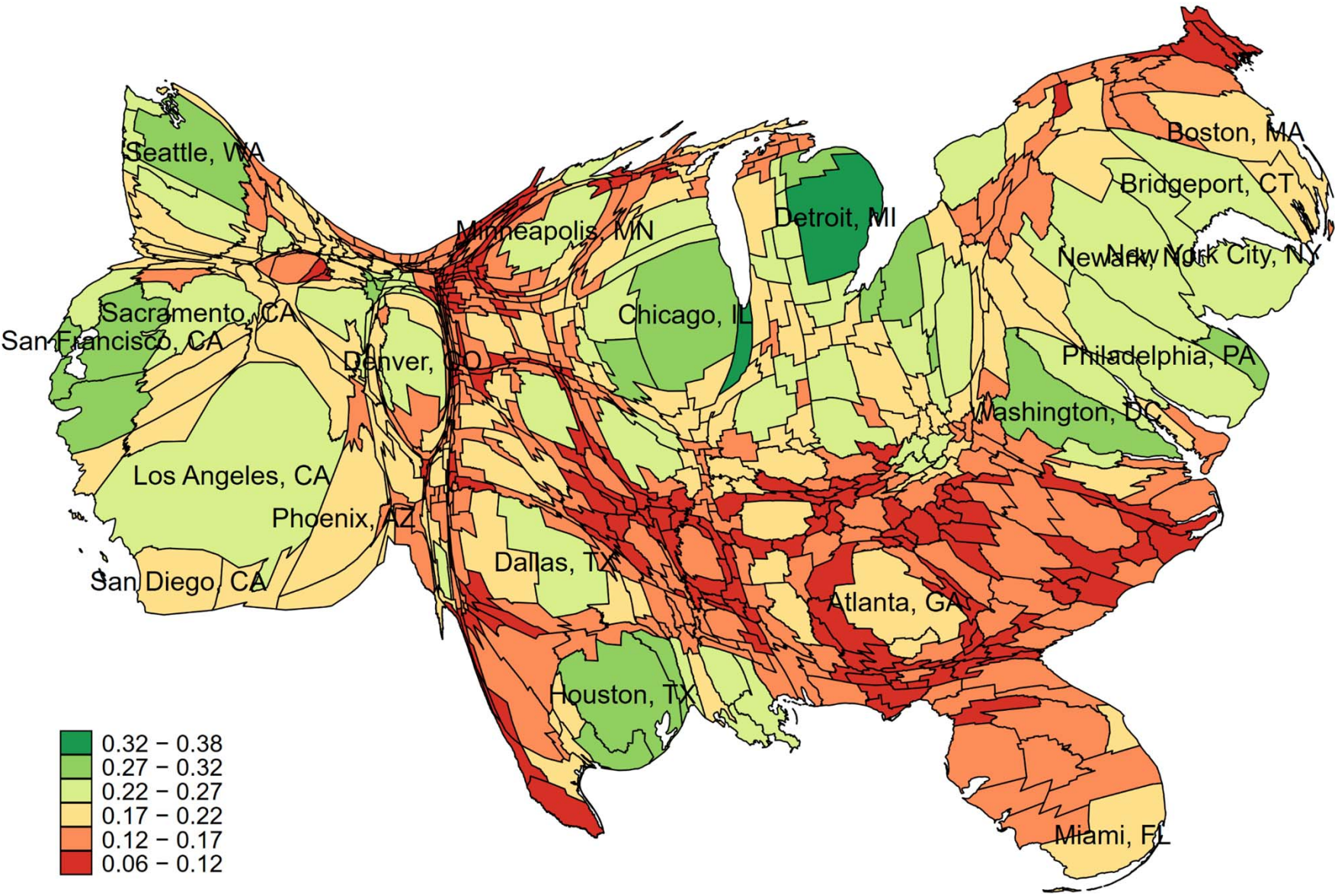
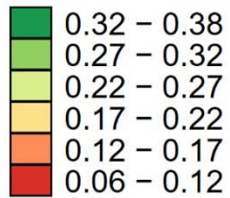
“I won the places that own two thirds of America’s gross domestic product. I won the places that are optimistic, diverse, dynamic, moving forward. And his whole campaign, Make America Great Again, was looking backwards.”

Hillary Clinton, speaking in Mumbai, 2018

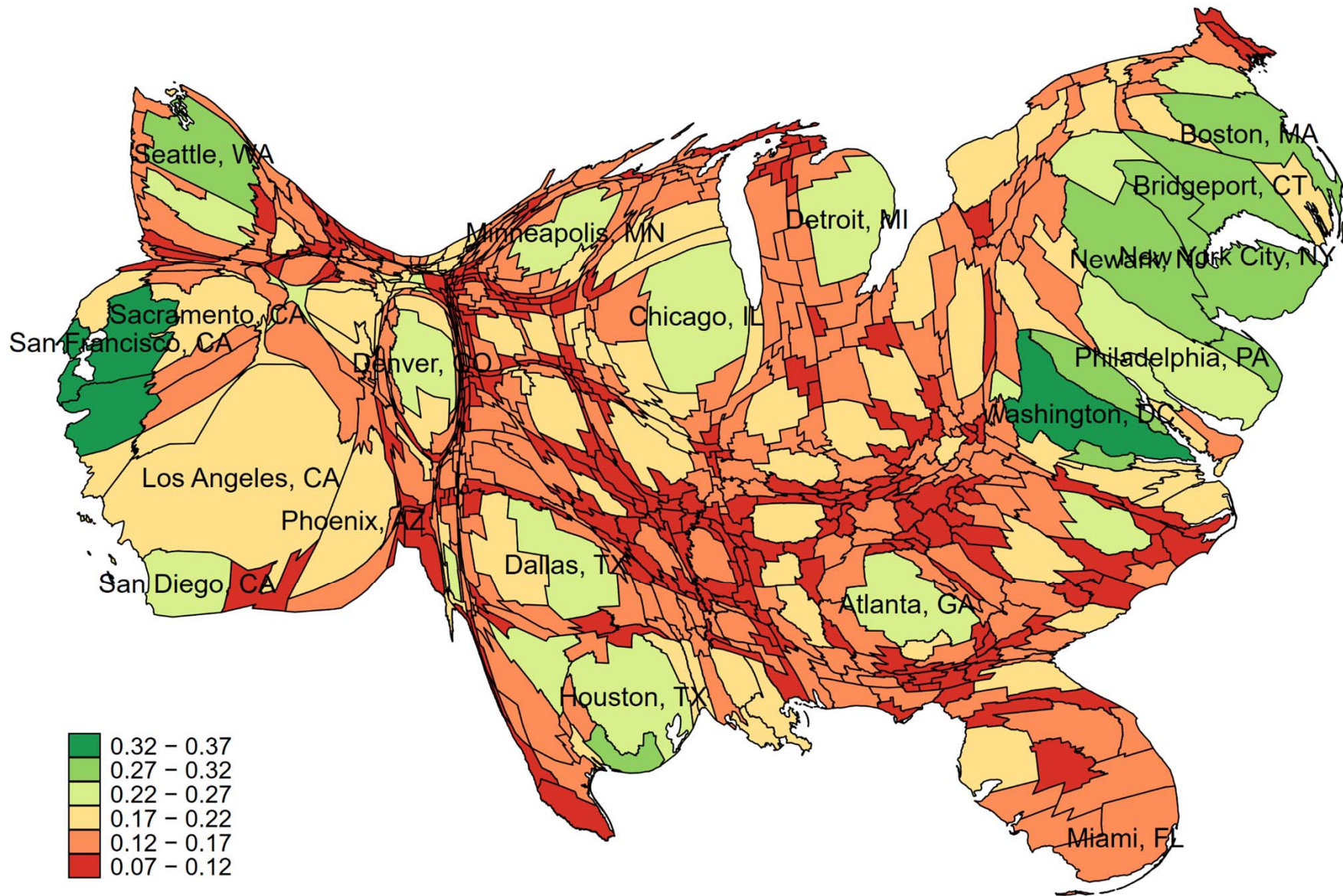
1980

Looking backward (1980):
proportion of employed people earning more than national 80th percentile in 1980

By commuting zone (CZ); areas scaled by population

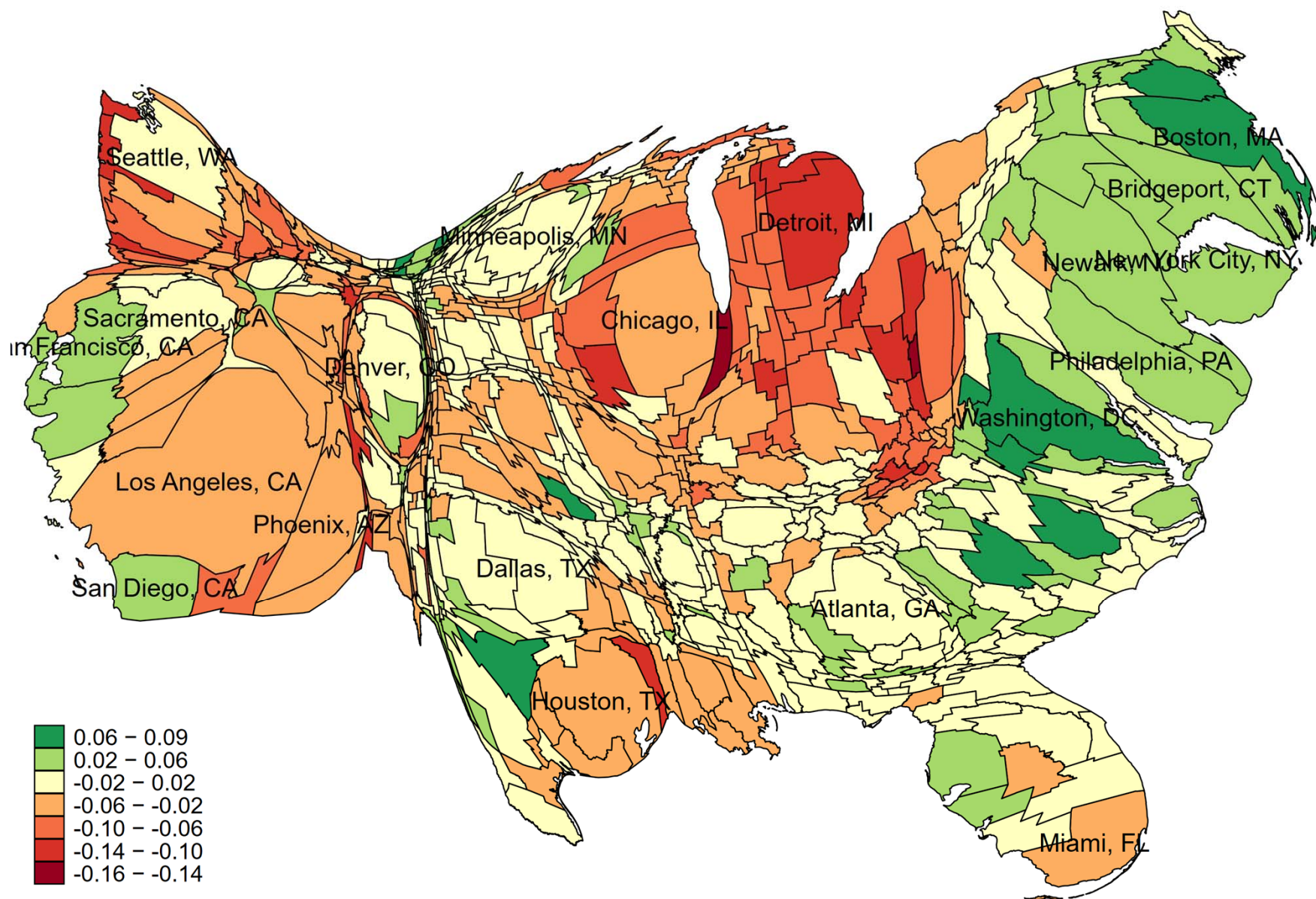


2016



At time of Clinton/Trump (2016): Proportion of employed people earning more than national 80th percentile

By commuting zone (CZ); areas scaled by population



Change from 1980 to 2016:
*some places are optimistic,
 diverse,
 dynamic,
 moving forward*

Increasing returns *to place* (external to firms)

- **Localization:** benign Marshallian forces
 - Specialized labor, knowledge spill-overs, value chain proximity
- Spatial unbundling → Increased local specialization within value chains
 - Technology: greater complexity, division of labor
 - Reduced communication & transport costs, higher speed
 - And, internationally, reduced tariff & regulatory barriers, regulatory arbitrage
 - Allows spatial concentration of high value added functions
- **Urbanization: bigger is better**

Fixing inequality when it's due to increasing returns to place

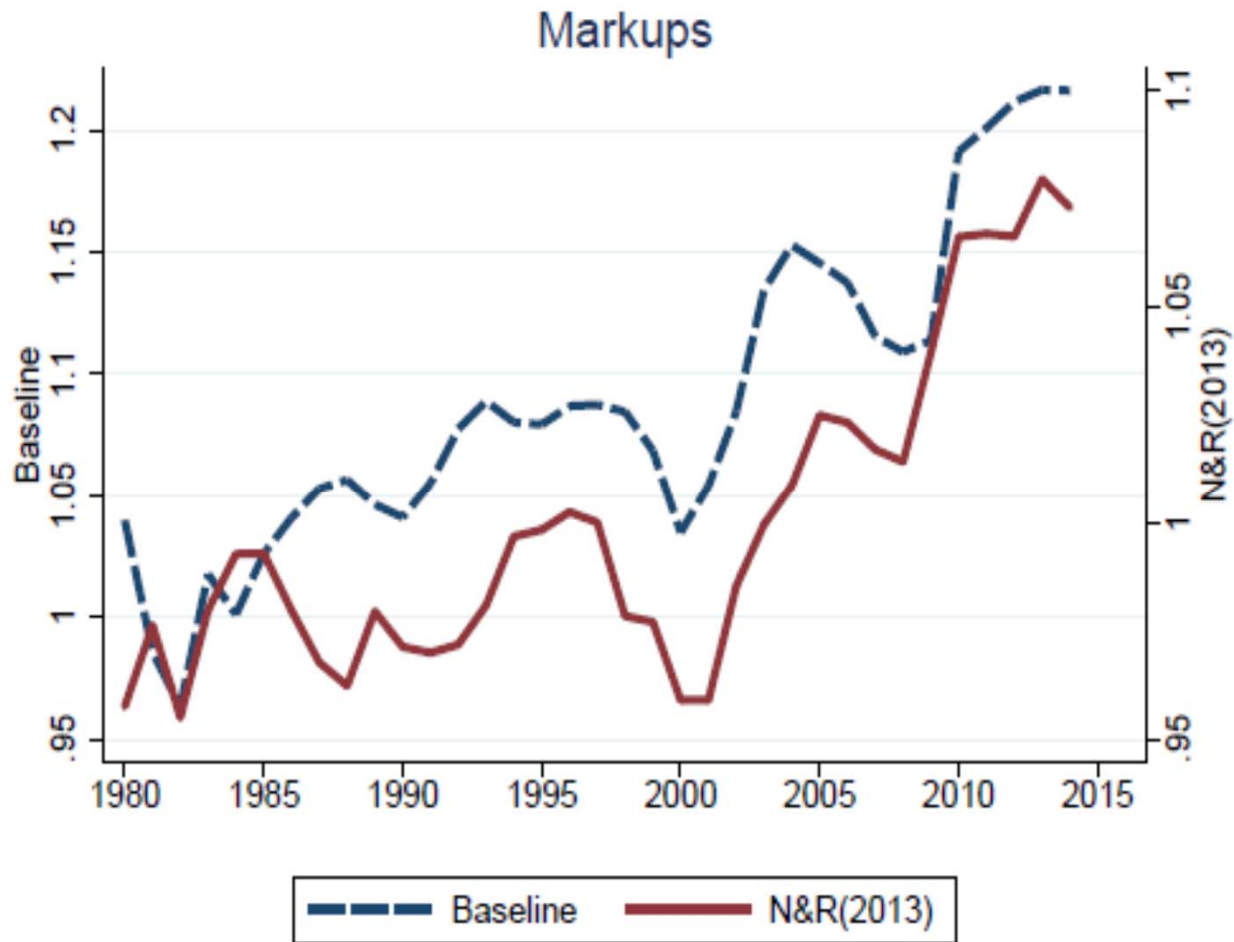
- Make your place better: smart specialization, reform institutions, invest...
- Move to the big city

Monopoly

- Increasing returns internal to firm
- Spatial characteristics
- Interaction with Marshallian externalities
- Amplification by financialization

Eggertsson et al. (2018), KALDOR AND PIKETTY'S FACTS: THE RISE OF MONOPOLY POWER IN THE UNITED STATES

- Financial wealth has increased rapidly despite no real increase in the amount of investment in the economy.
- The financial value of many firms now is permanently higher than the cost of their assets.
- Despite higher profits & lower interest rates, more valuable firms haven't invested in their own operations or workforces despite higher profits and low interest rates.
- The average rate of return on capital has stayed steady while interest rates have dropped.
- Falling labor share, rising profit share.



Growing monopoly power in American business in the neoliberal era

source: Eggertsson et al. (2018), KALDOR AND PIKETTY'S FACTS: THE RISE OF MONOPOLY POWER IN THE UNITED STATES

Why the growth of monopoly?

- Institutional
 - Change in anti-trust doctrine (Chicago, Bork)
 - Deregulation (mostly of old network industries)
 - Expanded intellectual property rights
- Business structure
 - New network industries
- Financialization
 - Capital to feed the new monopoly sector

Network Externalities

Google and Facebook - 84% of global spending on digital advertising, excluding China (FT, 4/12/2017)

“The two companies’ hold on online spending has created a digital duopoly that is upending the advertising business.

Several analysts estimate that excluding Google and Facebook, the digital ad industry actually shrank in the first half of 2016.”

<https://www.ft.com/content/30c81d12-08c8-11e7-97d1-5e720a26771b>



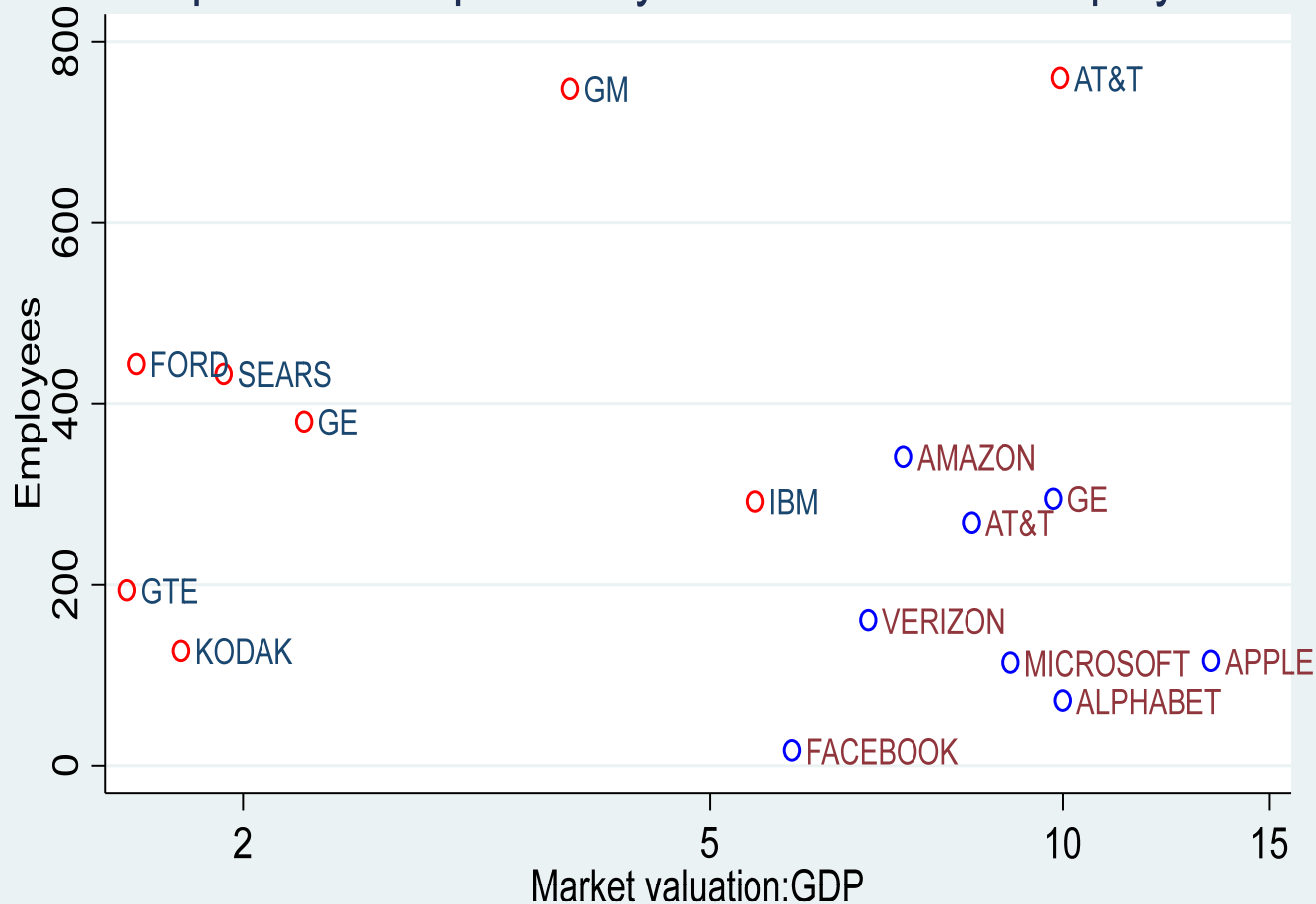
[As Amazon's dominance grows, suppliers are forced to play by its rules.](#) “At least 21 public companies [i.e., relatively large companies, with publicly traded shares] have disclosed they are generating 10 percent or more of their revenue through Amazon.”

“The bigger concern is that Amazon — not the suppliers — have a direct relationship with consumers because they're the ones selling the products. That means Amazon owns the customer data and knows what sells well on its site — and if needed, it can go make those products themselves at a lower cost, supplanting the larger brand almost immediately.”

(CNBC, 21/12/2017)



1976 vs 2016 Top 8 US Companies by Mkt Valuation & Employees



Excluding finance & oil companies
Market valuation scaled by GDP per capita x 1,000,000
Data: Compustat, World Bank

The giants in 2016: fewer employees, higher market valuations

- In 2016, seven of the eight are based on network products
- In 1976, the two with highest market valuation (AT&T and IBM) were both based on network products

Walled gardens: some monopoly models of the information age

Interface standards

- Microsoft: document formats & Windows APIs. Has prevented competing (often free) desktop applications & PC operating systems
- Apple maintains similar control of its system (which is, ironically, built on top of the open source operating system BSD Unix)
- Google uses Android (built on open-source Linux) as gate-keeper for phone apps

Sale to advertisers of personal information from search or social networks

- What Google & Facebook do
- Also, any social network (Twitter, Instagram...) – the others just aren't as successful as the big two

Tollgate for market access by other businesses

- Amazon
- Alibris
- Trip Advisor
- Booking.com
- Airbnb
- Uber

Simple intellectual property

- Pharma
- Biotech – Monsanto's seeds
- Academic publishing
- Hollywood

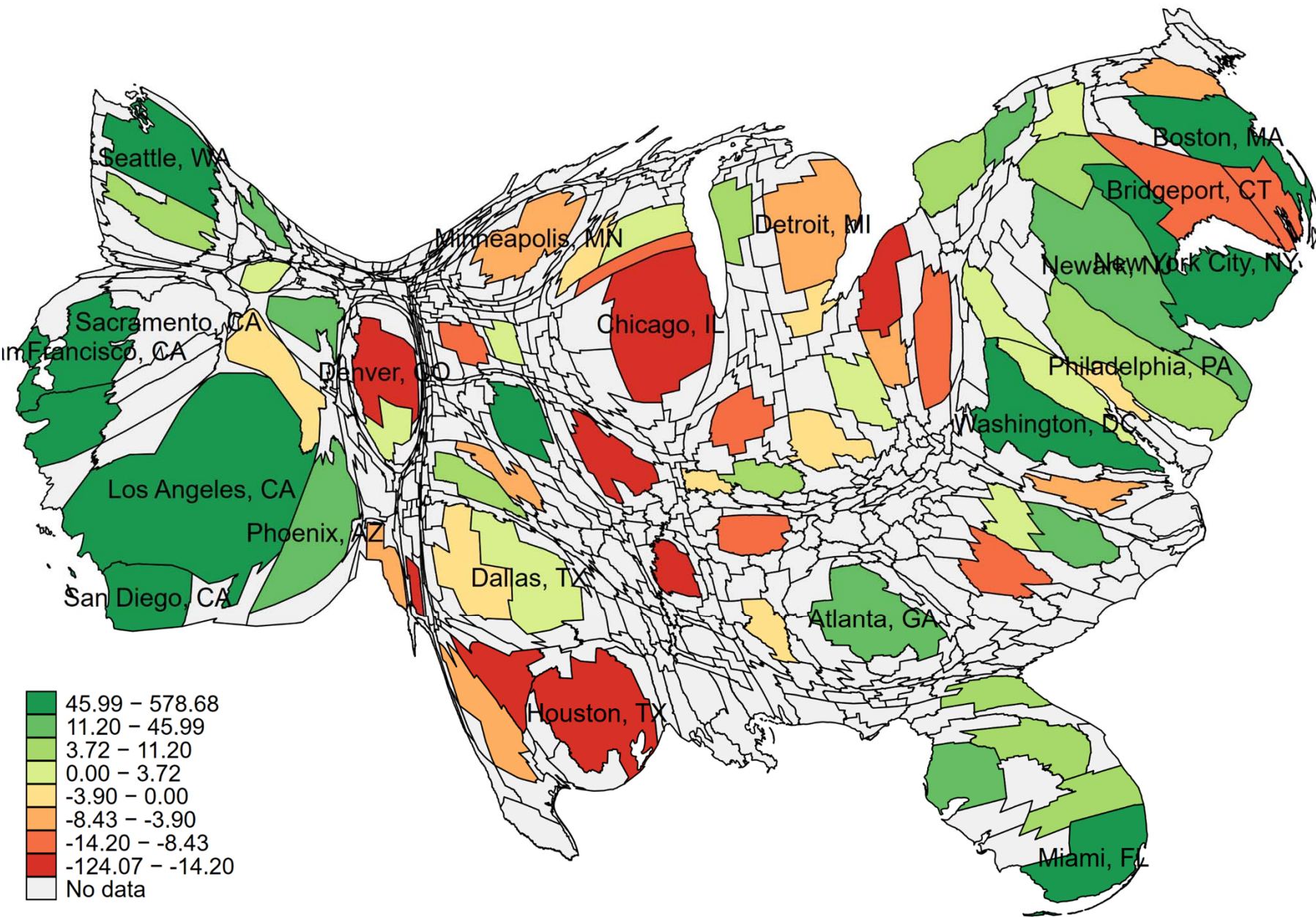
Note: in most cases, a network aspect to the monopoly

Note: we've been here before - network industries before the internet

- Historically, roads, water, sewage
- mid-19th to early 20th centuries, vast expansion of old networks & of new ones: postal service, railroads, electric power, domestic gas, telephone
- “Natural monopolies”:
 - Strong increasing returns
 - Economically essential
- By mid-20th century, brought **either** into public ownership **or** under public regulation in **almost every** country of the world, regardless of political/economic complexion
- NB in many of those cases, the location of the monopoly business's assets was co-extensive with its market (e.g. electric power grid): different politics of regulation from e.g. Facebook

What does monopoly do?

- Harm consumer? (Bork test)
- Levy tax on other businesses / places.
 - Google, Facebook ads
 - Consider business models of AirBnB, Uber, Monsanto
- Deprive individuals / businesses of use of tools
 - Microsoft and software development / customization
- These effects are **spatial**



Headquarters of market power:
Change in the ratio of market value to book value of assets, 1980-2016

(CZs with 5 or more non-financial firms in Compustat dataset)

Interaction of monopoly and Marshall

Why locate a monopoly firm in a Marshallian cluster?

- Amplification of Marshallian productivity advantages
 - Winner-takes-all, you want the best programmers & the latest information
- Market for start-ups
 - Start-up objective: sell to bigger company
 - Google, Apple, Facebook objective: acquire or kill
 - Both strategies benefit from co-location
 - Proximity to venture capital

Finance for monopoly

- Agency problem and corporate governance: insider-outsider struggle over “free cash flow” – assets which are more valuable if separated from firm (Jensen 1986, 1989)
- Reforms to pensions, corporate governance, banking aimed at empowering outsiders.
- With growing monopoly sector, all liquid or liquidatable assets in competitive sector look like free cash flow: strip assets, invest in promising start-up.
- See O’Sullivan (2000), Appelbaum & Batt (2014), and papers in Martin & Pollard (2017)

Monopoly *of* finance

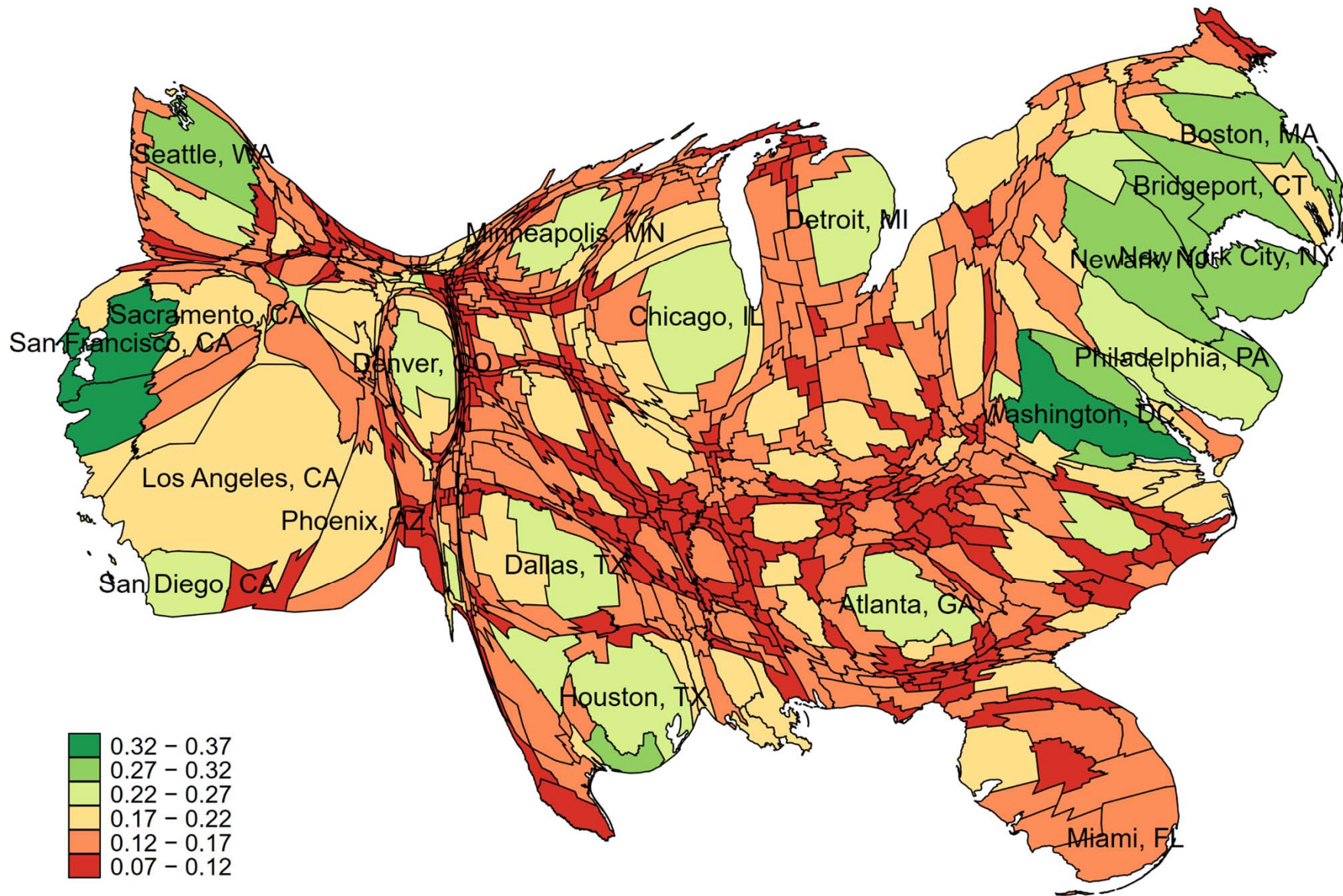
- Four biggest banks in the U.S. have a combined \$8.5 trillion in assets
 - nearly \$4 trillion more than the combined total of the next 100 biggest banks
 - Smaller regional banks are healthier
- Post- Recession bank closures
 - disproportionate in small & medium sized cities & rural areas
 - Banking Deserts
- Long-term decline in new firm formation tied to 1930s bank closures (Babina and Berger 2017)

Concentration of US banking system

Total assets of top three US banks
as % of total commercial banking sector assets



2016



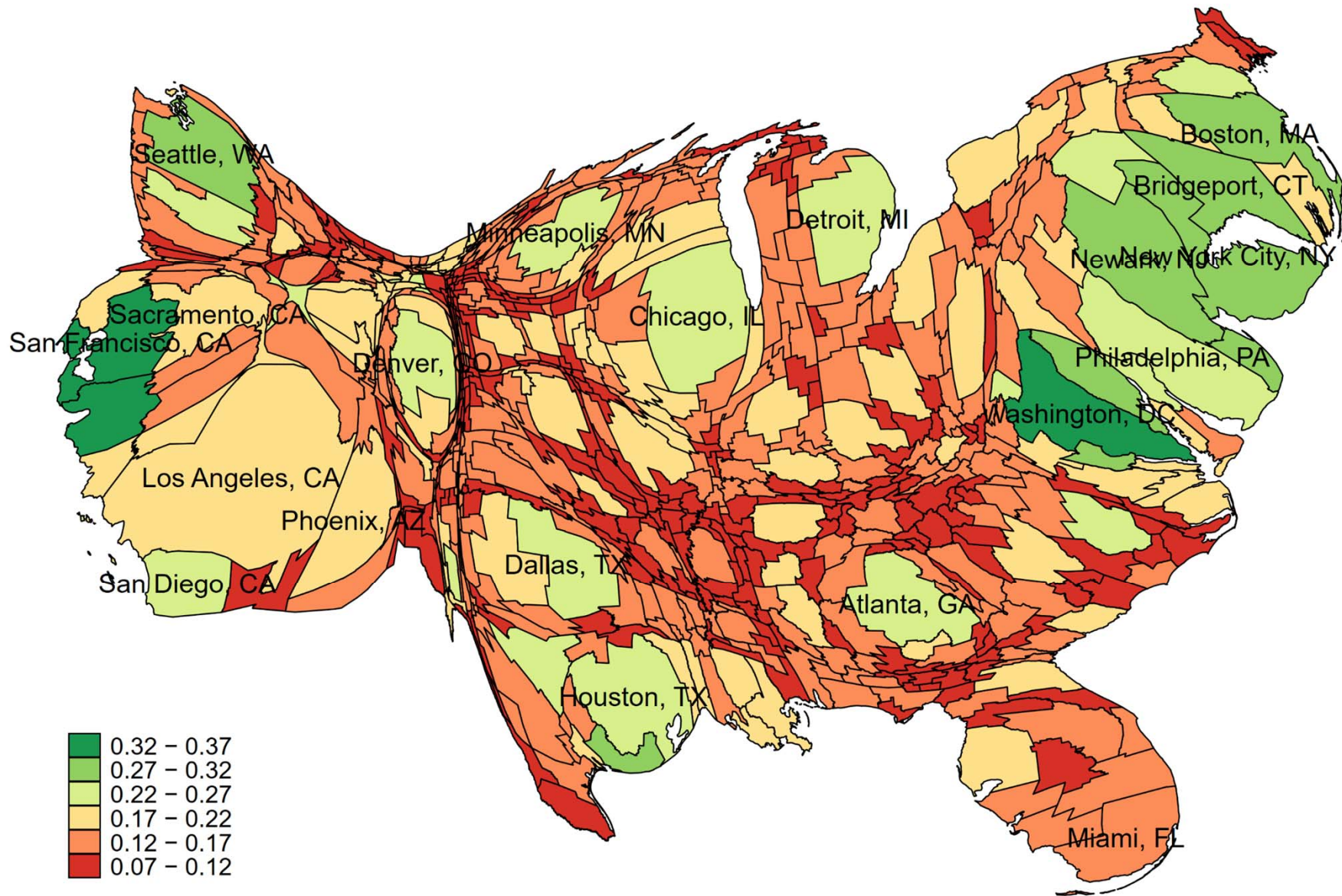
At time of Clinton/Trump (2016): Proportion of employed people earning more than national 80th percentile

By commuting zone (CZ); areas scaled by population

The top 20%

- ... work for the 0.01%
- ... for monopolies
- ... for the banks & private equity firms that finance monopolies
- ... for the lobbyists regulators and law firms which make the world safe for the monopolies and the banks

2016



At time of Clinton/Trump (2016): Proportion of employed people earning more than national 80th percentile

By commuting zone (CZ); areas scaled by population

Earnings data: IPUMS micro-data, US Census Bureau
Market valuation & company accounts: Compustat
Maps by Andreas Diemer

More work is going on...

Thank you!

