Programme on
Innovation and Diffusion

The Rise of Superstar Firms: Causes and Consequences

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THE LONDON SCHOOL OF ECONOMICS AND POLITICAL SCIENCE

Forbes

Apple Becomes 1st Company Worth $3 Trillion—Greater Than The GDP Of The UK

Forbes, Jan 3rd 2022

https://www.forbes.com/sites/zacharysmith/2022/01/03/apple-becomes-1st-company-worth-3-trillion-greater-than-the-gdp-of-the-uk/?sh=2468cc8d5603

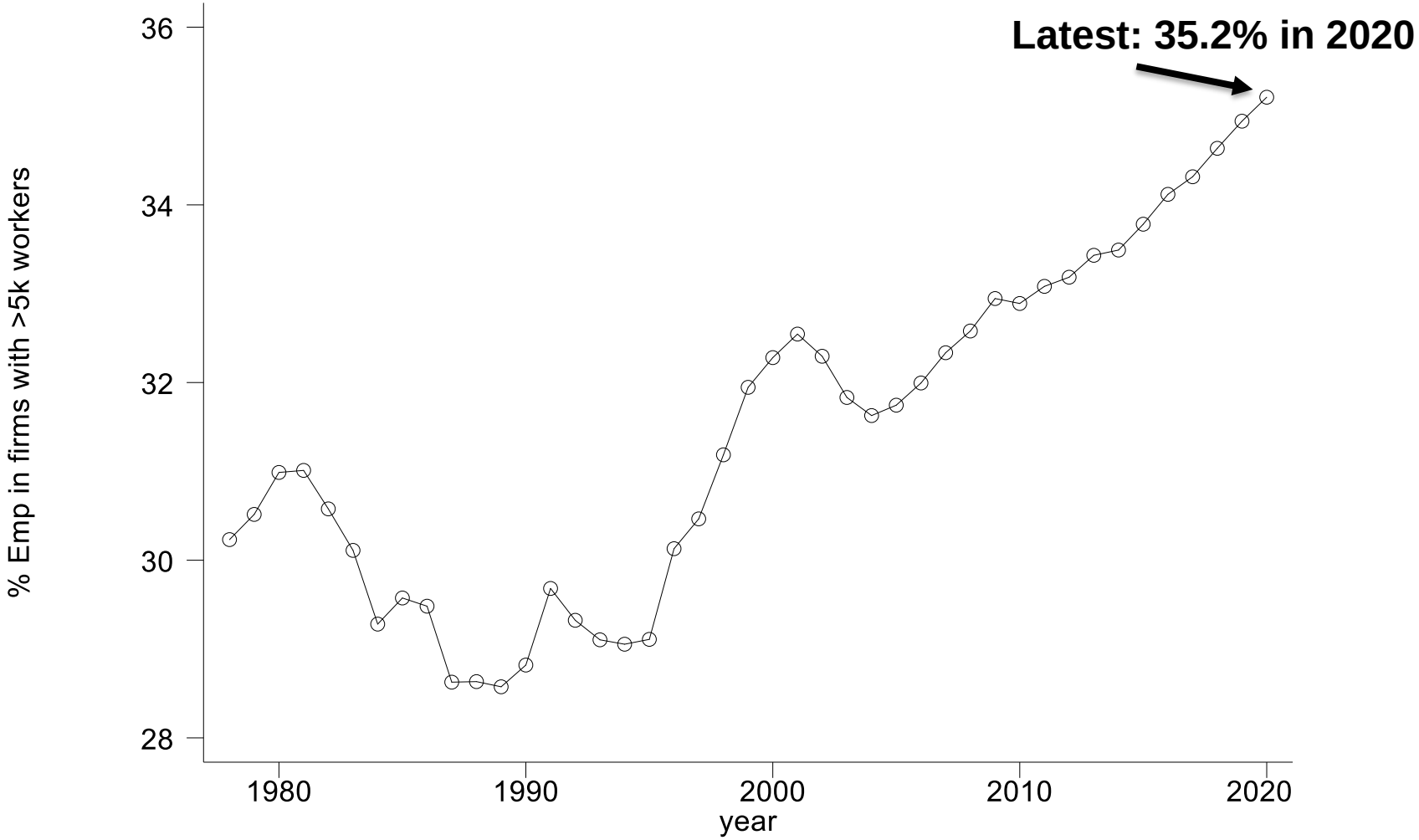
Market Valuation at Feb 24th 2023 (GAFAMs)

- ***Apple*** $2.32 Trillion
- ***Microsoft*** $1.86 Trillion
- ***Google/Alphabet*** $1.14 Trillion
- ***Amazon*** $0.95 Trillion
- ***Facebook/Meta*** $0.44 Trillion
- Growth has been supercharged by COVID's push to online, but has been going on long before the Pandemic

Overview

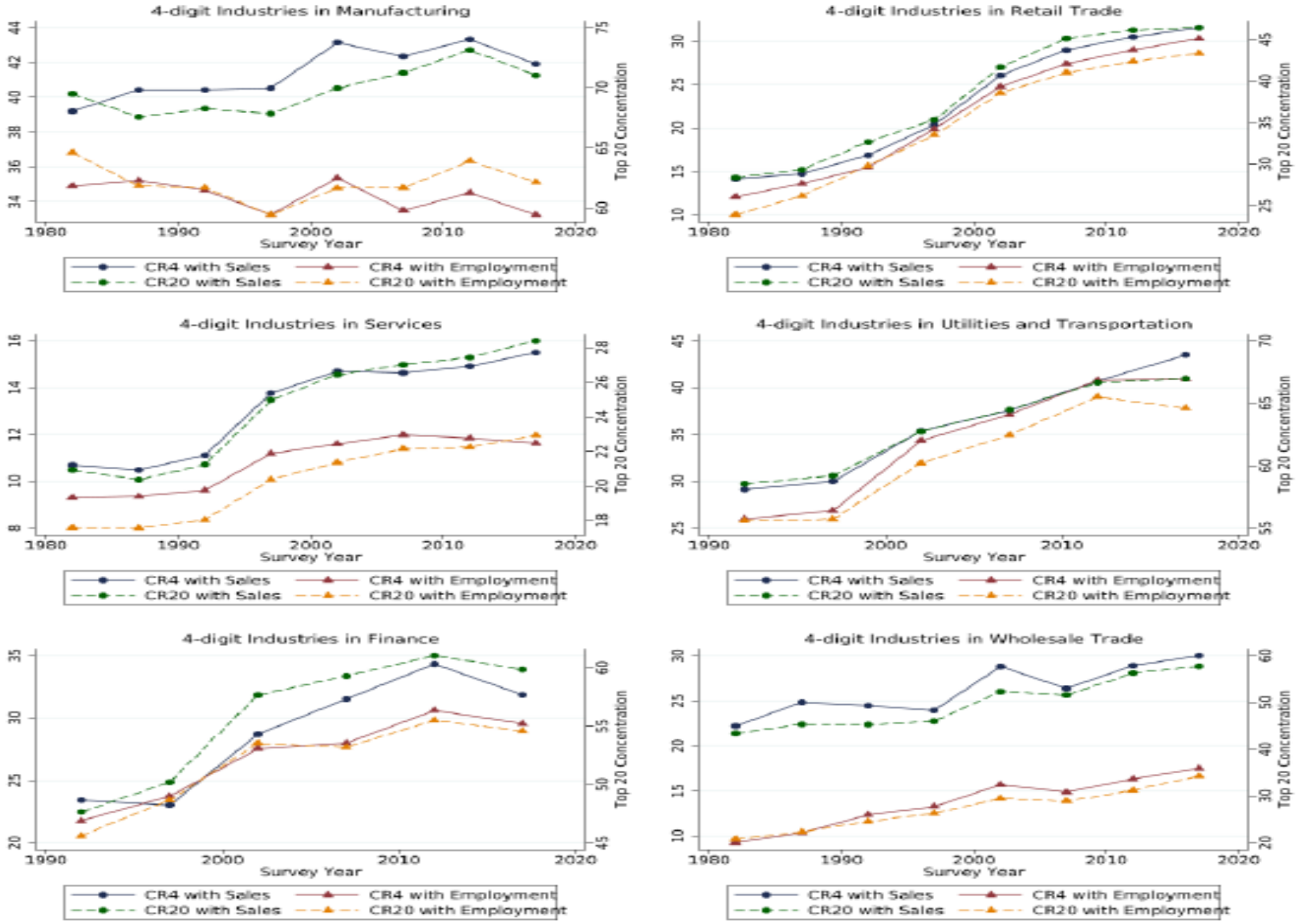
- **The rise of Superstar firms**
  - Firms getting larger on a number of dimensions (global trend)
- **Causes**
  - Technological rather than political
- **Consequences**
  - Caveat: Big isn't always bad.
  - In theory, less competition could help innovation
  - In practice, competition & innovation go together
  - Rise has coincided with global productivity slowdown: suggests not so benign
  - Even if superstar firms grew on merits, still risk of future abuse
- **Policy**
  - Focus on competition policy
  - Industrial policy; Labour market policy; Skills policy

Since mid ’80s, Big Firms get bigger: % domestic jobs in US firms with 5,000+ workers rose ~28% in ‘87 to ~35% in 2020



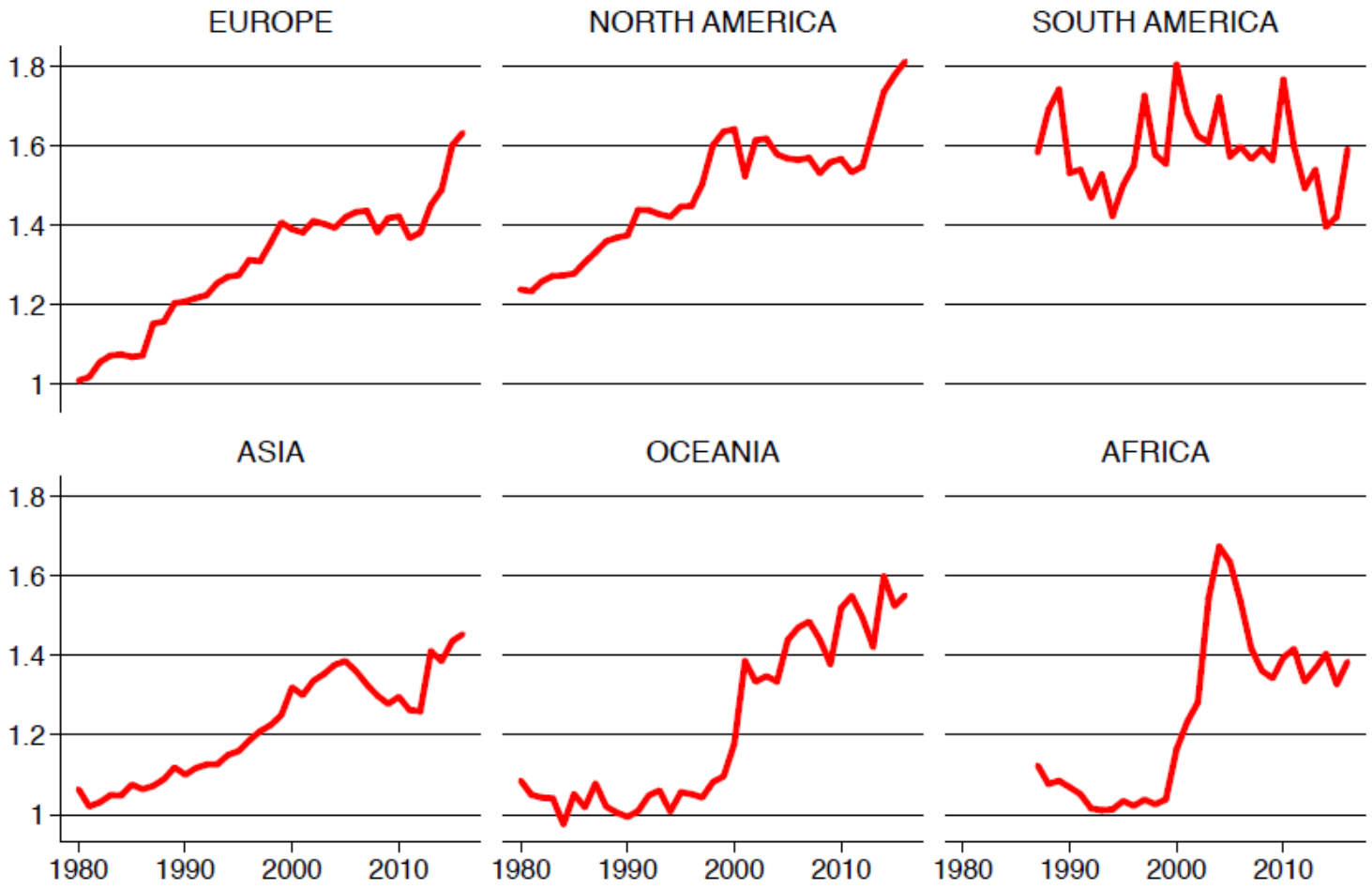
Source: US Business Dynamics Statistics (2022), https://www.census.gov/data/datasets/time-series/econ/bds/bds-datasets.html

Figure 5: Top-4 and Top-20 Concentration by Industry Segment



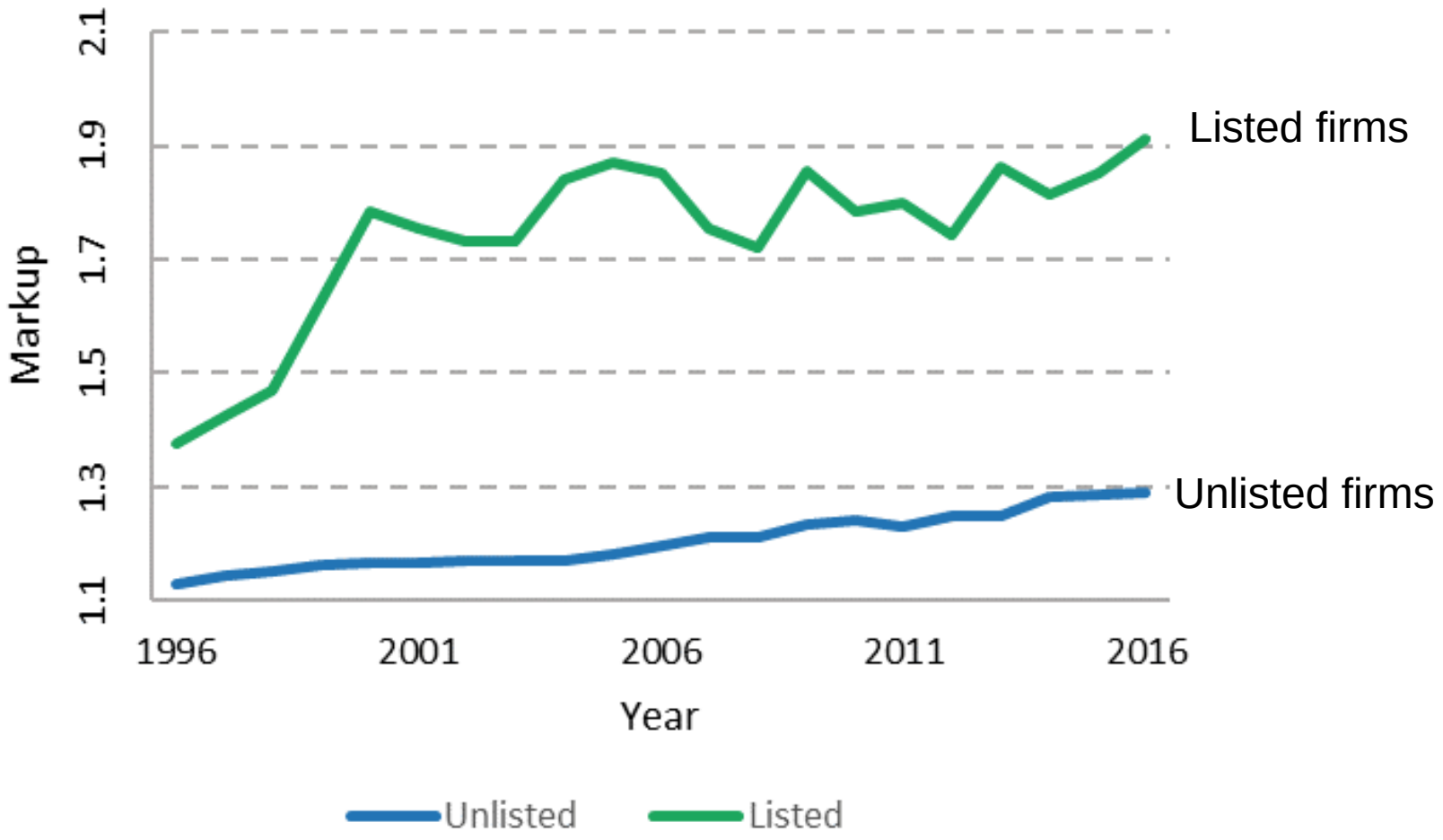
Source: Autor, Patterson and Van Reenen (2023)
Notes: US Economic Census 1982-2017

Price-Cost Markups around the world (publicly listed firms)



Source: Eeckhout and de Loecker (2018) using Worldscope

Aggregate Price-cost Markups in UK



Source: de Loecker, Obermeier and Van Reenen (2022), Deaton Inequality Review

Some Potential Causes

1. ***Increase in exogenous sunk costs: "Wal-Mart Story" e.g.*** larger firms have advantages in using **intangible capital such as software (**Besson ’17; Eberly & Crouzet ’21)
2. ***Increase in endogenous sunk costs "Google/Apple Story”*** Increased importance of **platform competition** (network effects, especially in **digital** markets)
3. **Globalization:** Allocates more market share to more productive firms; Global value chains advantage multinationals
4. Weaker **anti-trust enforcement** (Philippon ’19). Unlikely, given broadly similar trends in EU and US
5. **Falling diffusion** of technology between leaders and followers (Akcigit & Ates, ’21)

- Likely to be different stories across industries

Competition Policy

- Knee-jerk restraints on superstar firm growth or breaking them up is likely to be very costly
- Even if superstar firm success not due to weaker institutions, in our “winner take most world”, important to modernize **anti-trust policy** to reduce risks of harm:
  - **Ex ante regulation**: EU Digital Markets Act, UK DMU, etc. Interoperability, data portability/access
  - Key role for **innovation/future competition** in assessing anti-trust enforcement
  - **Standards of proof** to shift more towards acquirers instead of government regulators
  - Finding ways to increase **structural competition** (e.g. EU Single Market for Services; trade agreements)

Conclusions

- Growing differences between superstar firms and rest of economy: e.g. increased concentration & markups
- Technology is dominant factor, esp. in digital producing sectors and industries/firms using ICT intensively
- Does not imply size/market power always confers an innovation advantage
- Important implications for labor markets
- Need to modernize competition and labor market policy

Thank you!

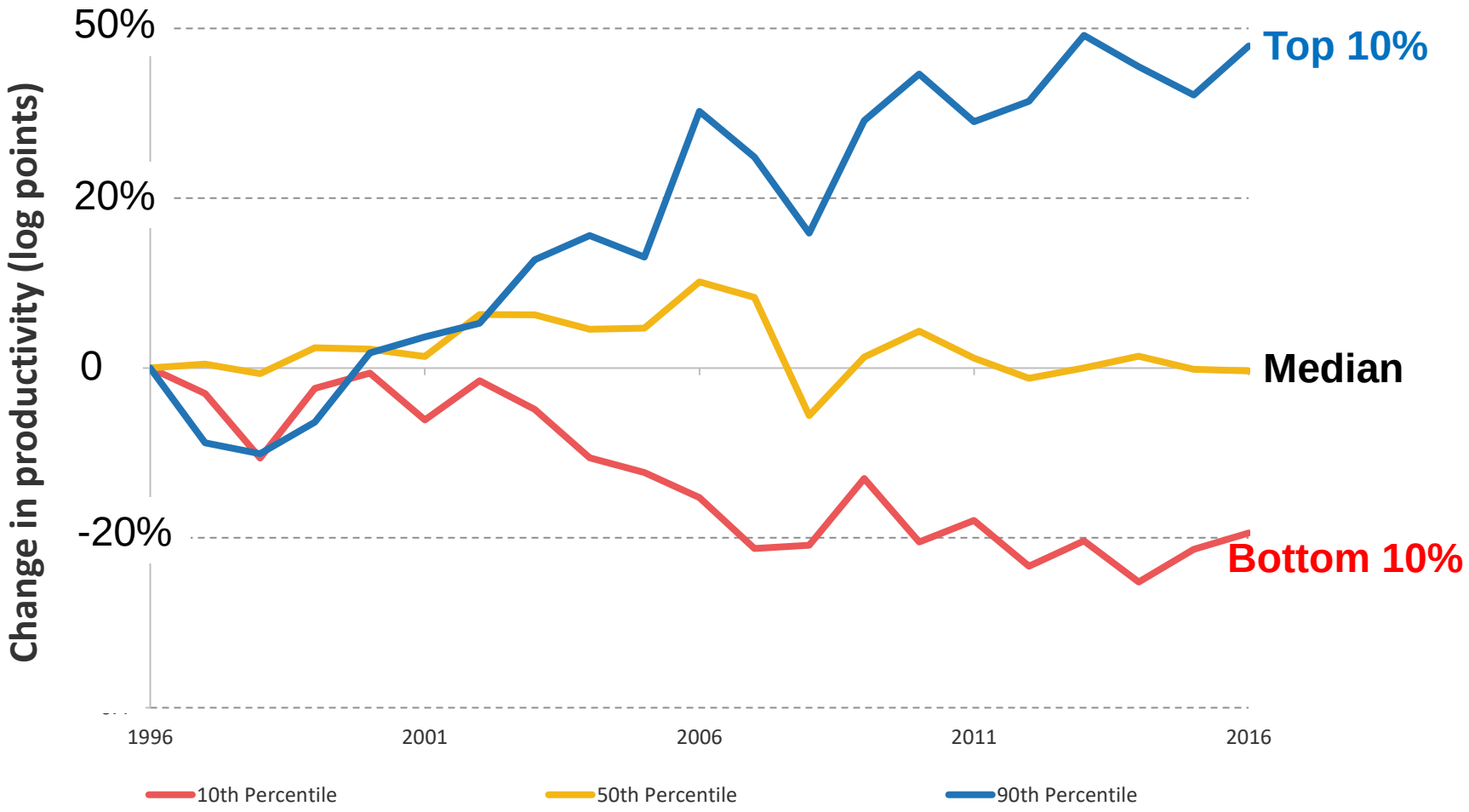
Further reading

- Griffith and Van Reenen (2023) “Product Market Competition, Creative Destruction and Innovation” Forthcoming in *Economics of Creative Destruction* (edited by Ufuk Akcigit and John Van Reenen) POID Discussion Paper 22
- de Loecker, Obermeier and Van Reenen (2022) “Firms and Inequality” IFS *Deaton Inequality Review* *https://poid.lse.ac.uk/PUBLICATIONS/abstract.asp?index=9154*
- Autor, Dorn, Katz, Patterson and Van Reenen “The Fall of the Labor Share and the Rise of Superstar Firms” (2020) Quarterly Journal of Economics
- Bloom, Sadun, Schuh and Van Reenen (2021) “Management as Technology” http://cep.lse.ac.uk/pubs/download/dp1433.pdf
- Scur, Sadun, Van Reenen, Lemos & Bloom (2021) “The World Management Survey at 18, *Oxford Review of Economic Policy* https://poid.lse.ac.uk/textonly/publications/downloads/poidwp002.pdf
- Van Reenen (2018)“Increasing Difference Between Firms” *Changing Market Structures and Implications for Monetary Policy*, Jackson Hole Symposium 19-65 http://cep.lse.ac.uk/pubs/download/dp1576.pdf NYT NPR

Market Valuation at start of 2022 (GAFAMs)

- ***Apple*** $3 Trillion
- ***Microsoft*** $2.53 Trillion
- ***Google/Alphabet*** $1.92 Trillion
- ***Amazon*** $1.69 Trillion
- ***Facebook/Meta*** $0.93 Trillion
- Growth has been supercharged by COVID's push to online, but has been going on long before the Pandemic

UK Productivity growth by firm: Superstar firms pull away from the rest



Source: de Loecker, Obermeier and Van Reenen (2022)
Notes: Historical ORBIS, ln(value added/employee), quantiles weighted by firm employment; values indexed to zero in 1996; Changes in log points, so 0.05 = about 5% growth; 0.4 = $(e^{0.04} - 1)*100 = 50\%$

Policy: Labor Markets (2/2)

- Counter-balancing power through **labor market policy**

- Institutions such as
  - Minimum wages
  - Collective bargaining
  - Labor standards (e.g. Gig economy)

- Strengthen job mobility (stopping non-competes; non-competes, etc.)

- Increasing human capital (especially through education and training)