

Wage Markdowns and FDI Liberalization*

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This version: March 2020

First version: December 2016

Abstract

This paper examines whether liberalization of inward foreign direct investment (FDI) reduces firms' monopsony power in labor markets. We estimate firm-level wage markdown, wage over marginal revenue of labor, from China's production data and identify the causal effect of FDI liberalization on wage markdown, using China's regulation changes upon its accession to the World Trade Organization. Large and productive firms, state-owned firms, exporters, and foreign firms exercise less monopsony power. FDI liberalization increased monopsony power and decreased labor share in value-added. These findings are contrast to classical theory based on concentration but consistent with modern theory based on search frictions.

Keywords: Foreign direct investment, Monopsony, Wage, Search, Firm heterogeneity

*We thank comments from Matilde Bombardini, Arnaud Costinot, Anna Gumpert, Hiroyuki Kasahara, Daiji Kawaguchi, Kohei Kawaguchi, Lin Ma, Tomohiro Machikita, Andreas Moxnes, Kensuke Teshima, Francesco Trebbi, Miaojie Yu, Xiwei Zhu, and participants at Hitotsubashi conferences in 2016 and 2018, Sogang-HSE workshop, Keio U, IDE-JETRO, APTS, SWET, JISE meetings, GRIPS, PKU-HSE, U Tokyo, Diatobunka U, Nankai U, Chukyo U and Kobe U. We gratefully acknowledge financial supports from JSPS Kakenhi (26220503, 19H01477, 17H00986, 18K12769, 15H05728 and 15H05392).

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