

Dynamische Wirtschaftsanalysen – erste Ergebnisse aus Forschungsprojekten mit AFiD-Daten

Donnerstag 20. Mai 2010
13:15 bis 14:45 Uhr

INDUSTRIE

Product Differentiation and Profitability in German Manufacturing Firms

Prof. Dr. Joachim Wagner und Dr. Nils Braakmann

Leuphana Universität Lüneburg

We use a unique rich newly built data set for German manufacturing enterprises that combines data from the cost structure survey, the survey of products produced, and the monthly report of manufacturing establishments (aggregated over all months, and all establishments belonging to an enterprise) to investigate the product differentiation – firm performance relationship. We find that an increase in the degree of product diversification has a negative impact on profitability when observed and unobserved firm characteristics are controlled for. The effects are statistically significant and large from an economic point of view. This helps to understand the – at least, at a first glance – surprising fact that nearly 40 percent of all manufacturing enterprises with at least 20 employees in Germany are single-product firms according to a detailed classification of products, and that multi-product enterprises with a large number of goods are a rare species.

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Empiricism meets Theory – Is the Boone-Indicator applicable?

Alexander Schiersch und Jens Schmidt-Ehmcke

Deutsches Institut für Wirtschaftsforschung, Berlin

Assessing the degree of competition in industries is a crucial challenge for both researchers and decision-makers in politics and antitrust authorities. Indicators are needed to identify a lack of competition or the results of policy changes that are intended to intensify competition. In order to meet these needs several competition indicators have been put forward. Unfortunately, all of them are flawed.

Boone (2008) extended the existing set of competition measures by creating an indicator that applies relative profits. It is based on the idea that competition rewards efficiency. Hereby, efficiency is defined as ability to produce the same output with lower marginal costs. In industries with increasing competition inefficiently operating firms are punished more harshly than relatively more efficient ones. Thus, comparing the relative profits between some arbitrary efficient firm and a firm with higher efficiency provides information on the level of competition in an industry.

The existing literature compares the Boone-Indicators (BI) with traditional measures as the price-cost-margin (PCM) or the Herfindahl index (HI) in order to prove its superiority and robustness. This is usually done by simple correlation analysis or by counting the direction the indicators point to. Moreover, deviations in the performance of PCM and BI are sometimes taken as a proof for the practical importance of theoretical concerns about the price cost margin (Boone et al., 2004). But as Boone et al. (2004) noticed: "Without a priori information about the 'true' degree of competition in an industry it is difficult to say whether the relative profits measure is empirically better than the price cost margin". Consequently, whether BI is superior to traditional competition measures or not, remains an open question.

This paper tries to fill this research gap. We use legal cartel cases to evaluate the performance of competition measures before and after a case. Hence, even without knowing the "true" degree of competition, we have events that should be mirrored by each competition measure. This gives us the opportunity to test whether (i) the Boone Indicator is correctly indicating changes in competition and whether (ii) the theoretical concerns about PCM can be confirmed.