Occupational Choice and the Spirit of Capitalism

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Macroeconomics Reading Group

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Outline

1. Introduction

2. The Model

3. Conclusion
Question

- Why the landed class has been unable to maintain their status as élite?

- Explain important features of the Industrial Revolution:
  1. The decline of the aristocracy
  2. The rise and decline of industrial dynasties ("Buddembrooks" Theory)

- Model of cultural transmission and class dynamics
Contribution

1. General model of preferences transmission in a growth setting

2. Explains relation bt. class-specific preferences and socioeconomic outcomes
   - The Weberian Hypothesis

3. Explains socioeconomic transformation during the Industrial revolution
   - From landlords élite to industrials élite
Parents can instill **patience** and **test for leisure** in the offsprings.

Determinant of preferences:

1. Source of income: **wage** or **rent**
2. Steepness of the income profile
The Model

- OLG model: **altruistic** parents invest in preferences of the kids

- Preferences "production function":
  - \( A'(A, l_A) = \psi \bar{A} + (1 - \psi)A + g(l_A) \)
  - \( B'(B, l_B) = \psi \bar{B} + (1 - \psi)B + f(l_B) \)

- **Wage Earners:**

\[
V^W(A, B) = \max_{i \in I, l_A, l_B, n_1, n_2} \{(1 - B)(\log(w_{i,1}n_1) + A(1 - n_1)) \\
+ B(\log(w_{i,2}n_2) + A(1 - n_2)) - l_A - l_B + zV_c(A', B')\}
\]
**Wage earners:**

- Complementarity between investment in patience and income profile steepness
- Patience level determines occupational choice (uniquely) and investment in patience (single valued)
- Supply of labour depends on test for leisure $A$: $n = \min\{A^{-1}, 1\}$

**Rentiers:**

- Income derived by rent as function of supervision effort
- Do not invest in patience
• The landed class problem

\[ V^L(A, B) = \max_{l_A, n} \{ \log(r x + (r - r)xn) + A(1 - n)) - l_A + zV_c(A') \} \]

• Optimal labour supply

\[ n = \max \left\{ \min \left\{ A^{-1} - \frac{r}{r - r}, 1 \right\}, 0 \right\} \]

• For a given A labour supply is lower for rentier then wage earner
Pre - Industrial General Equilibrium:

- **Technology**
  - Agricultural technology: \( Y_F = L^\alpha Z^{1-\alpha} \rightarrow \text{flat income} \)
  - Artisan technology: \( Y_A = qH \), \( n_1 = n \) and \( n_2 = \gamma n \) \( \rightarrow \text{steep income} \)
  - Land rents are constant over time

- **Equilibrium**
  - \( q \) very low, all workers in the agricultural sector, \( l_B = 0 \)
  - \( q \) rise, wages adjust to make workers indifferent
  - ”endogenous” division: preferences stratification follows
Industrial Revolution

- New Technology for capital accumulation
  - Rate of return of capital: $R(n) = R + (\bar{R} - R)n^\eta$ and depreciation $\delta$
  - Capital income on top of wage: $(1 - \delta + R(n1, i))K$
  - Capital is irreversible and bequeathed to the childrens

- Equilibrium
  - More patient agents have higher propensity to invest
  - Low test for leisure $\rightarrow$ higher return $\rightarrow$ more investment
  - Artisans are the ideal investors
The Buddenbrooks

- Descendants of entrepreneurs as landlord
- Consumption becomes less elastic to labour effort
- Increases test for leisure
Conclusion

- Relevance of class dynamics for socioeconomic changes
- Culture and Institutions
- Relationship between growth and culture
- Explain the demise of aristocracy as ruling class