

Review of: "The Impact of Entrepreneurial Risk Aversion on Wages in General Equilibrium"

Friedrich L. Sell¹

¹ Universität der Bundeswehr München

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Friedrich L. Sell, Universität der Bundeswehr München

Brief review of:

The Impact of Entrepreneurial Risk Aversion on Wages in General Equilibrium. By Ying Feng, National University of Singapore, and James E. Rauch, UC San Diego, NBER, and CESifo.

I confess (and I know: Qeios wants us to be friendly reviewers): if you read such a pregnant title of a paper as the authors present here, then you almost expect something like the “liquidity trap” of John Maynard Keynes and not – sorry – a “note,” which is what it is ultimately about, of just under 8 pages. Why not: “a short supplement to Kihlstrom and Laffont (1979). . . .”?

And in fact, “In this note. . . .” (page 2), the authors later truly acknowledge their genre.

Central hypothesis of Kihlstrom and Laffont (1979): “an increase in risk aversion lowers the equilibrium wage. This result is intuitive: greater risk aversion causes agents to prefer wage work over entrepreneurship, and also causes entrepreneurs to hire fewer workers” (page 2). Already in a simple supply-demand framework of the labour market, this result is replicable: supply increases, demand decreases, which leads to a lower wage rate, ceteris paribus. Do we truly need all that math to sort of “prove” this result?

The authors: “We hope to increase the usefulness of KL for other researchers and to facilitate improvement in its exposition for the many graduate courses in which it is taught” (page 2).

I am not sure whether this aim is accomplished in the note. The lack of simple numerical examples, illustrating graphs, etc., etc., is evident. This applies foremost to section 4!

The formal generalisation, extension, and clarification of the Kihlstrom and Laffont (1979) results presented by the authors is creditable.

Literature: I would like to refer the authors to H.-W. Sinn’s “Risiko als Produktionsfaktor” (Risk as a Factor of Production), *Jahrbücher für Nationalökonomie und Statistik*, 1986, Vol. 201/6, <https://doi.org/10.1515/jbnst-1986-0602>, in which the impact of risk on entrepreneurial decisions is carefully addressed and from which further arguments supplementary to Kihlstrom and Laffont (1979) can be won.

Sinn, who earlier and later published widely in international journals, is a sort of victim of the “lost in translation problem” (see, for example: Sauer, B./Sell, F. L, Lost in Translation - a revival of Wolfgang Stützel’s Balances Mechanics. In: *European Journal of the History of Economic Thought*, Vol. 25, Nr. 3, 2018, S. 401-427). Many of his far-reaching theoretical results have therefore not been received enough in the international community of economists.

I make this remark also because one of the authors “recalls” his affiliation to CESifo (Sinn, for that matter, was president of this institution during the period of 1999-2016)!