

“Entry and Profits in an Aging Economy: The Role of Consumer Inertia”

Abstract: Over the past thirty years, the share of young firms in the US has declined while the share of profits in GDP has increased. This paper explores the role of consumer inertia as a driver of these twin phenomena. Using detailed micro-data, I document that consumer inertia has gone up due to the aging of the US population. Empirical evidence based on variation across different product categories and temporal variation across US states indicate a negative relation between consumer inertia and firm formation. I develop a model of entry, exit, and firm dynamics with consumer inertia. The model implies that more consumer inertia makes it more difficult for entrants to establish a customer base and incentivizes large incumbents to raise markups. I calibrate the model using micro-estimates of consumer inertia and data on firm dynamics. According to the model, the rise in consumer inertia accounts for a substantial proportion of the twin phenomena