Frank and Cook: Winner Take All

What do Placido Domingo, Alex "A-Rod" Rodriguez, Sanjay Jha, Tom Hanks, and Danielle Steel have in common? They all compete successfully in what Frank and Cook (1995) call "winner-take-all markets"—fields in which rewards are heavily concentrated in the hands of a few top performers. The key to their extraordinary success is relative rather than absolute ability: They are a little better than the competition. For example, probably hundreds of the world's opera tenors are almost as talented as Placido Domingo, but they will never play major opera houses, get lucrative recording contracts, or appear on television. Like the hundreds of actors who are almost as talented as Tom Hanks, these tenors will be lucky if they can even support themselves as performers.

Frank and Cook assert that the winner-take-all phenomenon, well established in the entertainment industry and in professional sports, is rapidly spreading to other fields, such as business, law, journalism, medicine, and academia. They point to executives like Sanjay Jha, CEO of Motorola, whose total compensation in 2008 came to $104 million. For reasons we do not have space to describe here, the authors are convinced that the extreme outcomes in winner-take-all competition have negative consequences for individuals and the economy as a whole.

The key question for Frank and Cook is, why are winner-take-all markets proliferating? Some writers point to the cozy relationships between CEOs and the corporate boards that set their compensation. Others emphasize the emergence in the 1980s of "a culture of greed," tolerant of excessive rewards for those at the top. Frank and Cook stress technological and economic factors. They note that mass production, large-scale organization, and vast markets favor large relative rewards at the top. For example, few authors can claim the millions Danielle Steel gets for one of her (less than profound) novels. But a publisher who commits large sums to producing and promoting mass-market fiction might be ill-advised to sign a writer who is *almost* as popular as Steel. The largest corporations operate on a scale that even 25 years ago would have seemed extraordinary.

With so much money riding on every decision, boards of directors are not inclined to hire someone *almost* as able as Jha for a lot less. Improvements in communications and transportation, along with growing international trade, expand the arena in which winner-take-all markets can flourish. Yet, they are by no means universal. Frank and Cook cite evidence that the large relative rewards flowing to

CEOs in the United States are exceptional. The pay gap between European and Japanese chief executives and their workers is modest by American standards. The authors suggest that what makes the United States different is the open competition for top slots in American corporations. In Europe and Japan—as in the United States until recently—executives typically spend their entire careers with a single firm and are promoted from within. Their corporate employers are not compelled to bid against one another for CEOs.

Much of Frank and Cook's argument rests on the idea that barriers to market competition have been falling. Corporations, sports teams, TV networks, universities, and other well-financed organizations are much more willing to raid one another's talent than they have been in the past. Federal deregulation of commercial aviation, trucking, banking, communications, the securities industry, and other sectors increases competition between firms and raises the bidding for top managers and professionals. Falling barriers to international trade and investment probably have the same effect.

Frank and Cook illuminate some of the market forces that are polarizing earnings, but their central concept of winner-take-all remains problematic. The notion works well enough for opera singers and CEOs, but how much does it tell us about the more general phenomenon of rising inequality? The authors attempt to extend the idea to people they call "minor-league superstars"—successful doctors, dentists, lawyers, stockbrokers, accountants, and others who earn hundreds of thousands of dollars a year. They show that inequality of earnings among people in these occupations has been growing. But winner-take-all assumes that a few top players suck up a large share of the available rewards, leaving little for the less talented. It is difficult to imagine that this is the case among people in large, varied professions like law and accounting. On the other hand, the singers, CEOs, and doctors do have this much in common: growing competition has raised the stakes and widened the compensation in their fields.

Another problem is this: Frank and Cook focus entirely on occupational earnings, as we have generally done in this chapter. But, as we will learn in the next chapter, where we broaden our perspective on inequality, those with the highest incomes typically depend more on investments than on jobs or professions.