Abstract

In this paper we investigate the degree of market power in U.S. manufacturing industries and whether that power is affected by fluctuations in demand. The key feature of our contribution is that it imposes on a model with adjustment costs the minimum structure necessary to recover a measure of the markup of output price over marginal cost. The markup is allowed to vary with fluctuations in demand, and its estimate is obtained using the Euler equation approach. The paper also presents evidence on the degree of returns to scale. We conduct the empirical investigation for U.S. two-digit manufacturing industries using annual data covering 1952 through 1985. Significant departures from perfect competition characterize a large number of U.S. industries. However, our estimates suggest that the markups are smaller than those found in studies that abstract from adjustment costs. In general, fluctuations in demand do not have a powerful effect on the degree of market power. In a few industries markups are significantly lower when the level of industry demand is above normal, while in a few others markups are higher when the aggregate economy is expanding.