

An Experiment on Screening When Employees Choose Their Productivity[†]

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Abstract

In the first stage, ex ante symmetrical agents can simultaneously invest into becoming highly productive. In the second stage, since an agent's productivity is his private information, a principal offers a menu of contracts to separate the two types of agents. This comes at the cost of paying an information rent to the highly productive types. The information rent is lower the more agents of high type are active and thus investment cost may not be covered. Therefore, the first stage constitutes a coordination game of who should invest in productivity.

We observe much more investment in productivity than expected. Nevertheless, the investments pay off for two reasons. First, efficiency is achieved as principal subjects frequently offer optimal contracts. Second, the principal subjects share profits with their employees rather than exploiting them. In addition, the higher the productivity, and the higher the (sunk) investment cost, the more generous the principal subjects are.

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