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On the firms' component of wage dispersion:  
endogenous effort versus search frictions.

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**Abstract**

This paper presents an environment in which firms' productive heterogeneity passes through to wage dispersion via sequential search and endogenous worker effort levels. Despite small gains from trade, the model is able account for more than two thirds of the measured firm component of wage dispersion. The implied narrow range of worker utility effectively pins down the lowest wage in the distribution and higher wages simply compensate workers for their extra effort.

**JEL codes:** E24, J64

**Keywords:** Wage dispersion, sequential search

## 1 Introduction

It has been well established that substantial wage dispersion exists among otherwise similar workers (Acemoglu [2002], Lemieux [2006], Autor et al [2008]). Of that wage dispersion, Abowd and Kramarz [1999] attribute about one third to firm effects. This paper investigates the importance of

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