Abstract

Agents choose to acquire skills ranging from simple and transparent tasks to complex and opaque ones. While potentially more productive, the latter generate more severe agency problems. In our overlapping generations model, agents compete with their predecessors. With dynamic contracts, long horizons help principals incentivize agents. Agents with short horizons are more difficult to incentivize than agents with long horizons. Hence, old agents are imperfect substitutes for young ones. This reduces competition between generations. As a result, young managers can opt for more opaque and complex technologies, and therefore larger rents, than their predecessors. Thus, in equilibrium, complexity and rents rise over time. Our theoretical results are in line with the increase in complexity and rents observed in the finance sector.

Keywords: Agency rents, moral hazard, finance sector, dynamic contracts, opacity.

JEL codes: D8, G2, G3.

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