

Non-Neutral Technology and Monopsony Power in Foreign Input Markets

Xinhao Wang* Wenxiao Dong[†] Nan Zhi[‡]

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Abstract

This paper investigates monopsony power in foreign-input markets—the ability of downstream firms to pay prices below the marginal revenue product of imported intermediates. We develop a structural estimator that incorporates factor-biased (non-Hicks-neutral) technical change to recover firm-level markdowns. Using matched Chinese industrial firm and customs microdata from 2000–2007, we document economically large and persistent foreign-input markdowns. Over the same period, non-neutral technology expanded rapidly, reshaping effective input productivity. Ignoring this channel generates substantial bias in markdown estimates—overstating buyer power when technology is labor- or material-augmenting, and understating it when input-saving forces dominate. Monte Carlo simulations confirm that the proposed estimator performs well in finite samples. Empirically, we find that the median firm-level markdown corresponds to a market power measure of about 2.81, while the average growth rate of factor-biased technology is approximately 1.40. These results underscore the importance of incorporating non-neutral technical change in measuring input-market monopsony and provide a tractable empirical framework for its identification.

Keywords: Monopsony Power, Non-Hicks Neutral Technology, Foreign Input Market, nested CES demand, Production Function Estimation

JEL Codes: L13, F14, D24, O33, C15

*Corresponding author, Visiting Instructor, Department of Economics, Bates College. 4 Andrews Road, Lewiston, Maine 04240, USA. xwang4@bates.edu

[†]Postdoctoral Researcher, Institute of New Structural Economics and National School of Development, Peking University. Langrun Garden, Peking University, 5th Yiheyuan Road, Haidian District, Beijing, China. wenxiaodong@nsd.pku.edu.cn

[‡]Visiting Assistant Professor in the Department of Economics at the University of Florida, USA. nan.zhi@ufl.edu

1 Introduction

Over the past four decades, China’s manufacturing sector has become deeply integrated into the world economy, as evidenced by the rapid expansion of exports and imports and the tightening of links within global value chains.

Large buyers occupy a prominent position in many modern industries. Their ability to secure supplier prices below competitive benchmarks is particularly salient in international trade, where high entry costs deter rivalry and activity is concentrated among a small set of large or highly productive firms. In such environments, dispersion in the prices of imported intermediates is systematically related to market concentration and to the demand systems of individual importers. Transactions along global value chains therefore often occur in buyer-concentrated markets in which purchasers possess nontrivial market power. These features make concerns about dominant buyers especially salient in international input trade (Antras et al. (2017); Bernard et al. (2007)). Yet our understanding of the size and implications of importers’ buyer power remains limited, because canonical analyses of input trade typically treat buyers as price takers.

A central implication of open-economy models is that importer market power operates like an implicit tariff. It distorts production and trade volumes yet improves the terms of trade by shifting rents away from foreign suppliers. The net welfare effect is theoretically ambiguous: output contractions and higher prices reduce consumer surplus, whereas profit increases—reflecting the transfer of foreign rents—raise producer surplus. Countries that wield import market power may thus exploit it in the design of trade policy; even in the absence of statutory tariffs, large importers can secure terms-of-trade gains when they possess buyer power in input trade.

In China, the post-WTO expansion in firm scale endowed a subset of manufacturers with unprecedented purchasing leverage. Following China’s WTO entry, tariff reductions were accompanied by strong import growth: between 2000 and 2006, the value of intermediate imports rose by roughly 256 percent, and by 2007 about 7.1 percent of manufacturing firms used imported intermediates, which accounted for approximately 7.5 percent of total inputs in ordinary trade (Brandt et al. (2017)). Ignoring this heterogeneity when formulating policy can lead to biased predictions for pass-through, quantities, and welfare. Consequently, credible measurement of market power in imported-intermediate markets is essential, with careful separation of buyer-power wedges from technology-driven changes in input demand.

We document two facts for Chinese manufacturing in the 2000s. First, there is substantial cross-sectional heterogeneity in the foreign-input cost share across firms and within industries. Second, despite import liberalization, the sales-weighted foreign-input cost share **de-**

clines in several major sectors over 2000–2007. The magnitude and timing of these changes differ across industries and across firms, indicating nontrivial within-industry adjustment and composition effects.

This paper provides micro evidence that buyer power in foreign-input markets and non-Hicks-neutral technology, including its evolution over time, help explain both the dispersion and the decline of within-industry foreign-input cost shares. To our knowledge, this is the first study in a developing-country setting to document the downward trend in imported-input expenditure shares while jointly assessing the roles of buyer power (monopsony) and non-Hicks-neutral, input-biased technological change.

This study examines the role of non-Hicks-neutral, input-biased technology in driving the decline of imported-input cost shares and shaping the cross-sectional dispersion of imported-input shares across firms in Chinese manufacturing. When technology raises the effective productivity of imported intermediates, firms require fewer physical units per unit of output; with gross substitutability between domestic and foreign materials, the expenditure share on imported inputs can decline even as their efficiency rises. Concurrent developments—upgrading of domestic substitutes, movements in relative prices, and shifts in the composition of production toward firms or products less reliant on imports—reinforce this pattern. Hence, foreign-biased efficiency gains can coexist with, and in some cases contribute to, a declining imported-input cost share.

I estimate firm–time–specific foreign-input markdowns and non-Hicks-neutral technology using firm-level production data and variation in input prices. Firms minimize costs by choosing domestic and foreign materials conditional on technology and market conditions. Our approach focuses on variation in cost shares, which can be induced either by changes in markdowns or by factor-augmenting productivity. Because foreign-input–biased technology and buyer power both move cost shares, prices and quantities alone do not separately identify the two. To achieve identification, I combine a final-goods demand relationship, a production function that allows factor bias, and controls for the foreign-input supply curve.

The empirical procedure proceeds in three steps. First, I construct a markdown-adjusted foreign-input expenditure share using the firms’ first-order conditions. Second, I estimate a production function that allows factor bias by two-step GMM, following [Akerberg et al. \(2015\)](#) and [Doraszelski and Jaumandreu \(2018\)](#), which delivers output elasticities while disciplining timing and functional-dependence assumptions. Third, I adapt the double-ratio approach of [Brooks et al. \(2021a\)](#) to separate the foreign-input markdown from non-Hicks-neutral, input-biased technology by exploiting relative elasticities and relative cost shares for foreign versus domestic materials.

Buyer power (markdowns). We find economically large markdowns with substantial het-

erogeneity both across and within sectors. Distributions are right-skewed and heavy-tailed: means typically exceed medians and dispersion is sizable, indicating that a small set of firms with strong buyer power drives sectoral averages. Over 2000–2007, the revenue-weighted mean foreign-input markdown rises markedly—from about 4.0 to about 6.8 (roughly a 70 percent increase)—while the median increases more modestly, from roughly 2.2 to 3.1 (about 41 percent). The widening gap between the weighted mean and the median (from 1.8 to 3.7) shows that growth in markdowns is concentrated among larger firms rather than reflecting a uniform shift of the entire distribution.

Non-Hicks-neutral technology. By construction, the level of our estimated foreign-input–augmenting technology is not intrinsically interpretable, as it depends on normalization and units; what is informative is its trajectory over time. Our estimates show that the log of the foreign-input–augmenting technology rises from -3.86 in 2000 to -3.34 in 2007, implying roughly a 67 percent increase in the effective productivity embodied in imported intermediates—about 7.6 percent per year. This pattern documents pronounced foreign-biased technical change. The concurrent decline in the expenditure share of imported inputs does not contradict this result: as imported intermediates became more efficient, firms required fewer units for a given output, while rapid upgrading among Chinese suppliers compressed quality gaps and encouraged substitution toward domestic inputs. Taken together, these forces align with China’s 2000s structural transformation—deepening integration into global value chains, absorption of embodied foreign know-how, and the rise of competitive domestic producers—so that growth in the estimated foreign-input–augmenting technology captures technological upgrading associated with globalization even amid falling import cost shares.

Interpretation and link to misallocation. Our markdown measure can be understood as a relative wedge on foreign materials. In the spirit of the misallocation literature (e.g., (Hsieh and Klenow, 2009)), it captures distortions on imported inputs relative to domestic materials. Following the standard assumption that domestic materials are flexibly chosen at market prices, the recovered wedge is interpretable as a foreign-input-specific distortion. Importantly, allowing for non-Hicks-neutral technology shows that part of what would otherwise be attributed to distortions is in fact technology-driven variation in input requirements. In this sense, incorporating input-biased technology mitigates overstatement of misallocation that would arise from attributing all movements in expenditure shares to buyer power alone.

The rest of the paper is organized as follows. Section 2 reviews the related literature on production-based measures of market power, input-market wedges, and non-neutral technical change. Section 3 describes the data, industry background, and stylized facts. Section 4 develops the empirical framework and identification strategy. Section 5 reports the estimation results. Section 6 presents Monte Carlo simulations assessing finite-sample performance

and robustness. Section 7 concludes.

2 Literature Review

A substantial empirical literature measures firm-level market power from production data. Two approaches are central. The first infers *product-market markups* from firms’ first-order conditions under cost minimization, identifying the markup as the ratio of a flexible input’s output elasticity to its revenue share (De Loecker and Warzynski, 2012; De Loecker et al., 2016a, 2020). The second quantifies *factor-market markdowns*—the wedge between an input’s marginal revenue product and its purchase price—most prominently in labor markets (Dobbelaere and Mairesse, 2013; Brooks et al., 2021b). These methods inform analyses of pass-through, factor income shares, misallocation, and welfare in open economies (Restuccia and Rogerson, 2017). Under the production approach, the marginal revenue product of a variable input equals its price scaled by the markup; rearrangement yields the ratio of output elasticity to revenue share as the empirical object (De Loecker and Warzynski, 2012). Applications document substantial dispersion and nontrivial aggregate movements in markups in trade-exposed settings (De Loecker et al., 2016a, 2020). Two identification caveats recur. First, the estimator presumes *competitive input markets*; if firms exert buyer power, the statistic conflates output- and input-side wedges (Dobbelaere and Mairesse, 2013). Second, most implementations treat technology as *Hicks-neutral*, implying proportional movements of elasticities and cost shares across inputs. In practice, markups computed from different flexible inputs, notably labor versus materials, often diverge in levels and trends, consistent with input-market imperfections and non-neutral technology (Raval, 2019). Moreover, with sunk costs and irreversibility, persistently low or even sub-unity price–cost margins can be optimal because of option value (Dixit and Pindyck, 1994).

Markdowns capture buyer power by comparing marginal revenue products with observed input prices. In labor applications, markdowns map to the inverse of the firm-specific labor-supply elasticity under standard assumptions; large-sample evidence for China and India indicates economically meaningful wedges that depress wages and reduce the labor share (Manning, 2003; Brooks et al., 2021b; Rubens et al., 2024). Recent work extends the same logic to materials and imported intermediates. Using customs microdata and firm accounts, researchers construct *importer-level markdowns* by pairing revenue elasticities of imported inputs with their revenue shares, while allowing input prices to result from bargaining rather than perfect competition (Morlacco, 2020). Plant-level evidence that jointly estimates output markups and input markdowns shows that policy shocks, such as subsidies or movements in world prices, are partly absorbed through markdown adjustments, which limits pass-

through to targeted agents (Avignon and Guigue, 2023). The open-economy implication is distinctive: buyer power over foreign inputs carries terms-of-trade content akin to an implicit tariff (Morlacco, 2020; Avignon and Guigue, 2023).

Both strands inherit identification frictions from production-function estimation. The proxy-variable literature addressed simultaneity using investment or intermediate inputs (Olley and Pakes, 1996; Levinsohn and Petrin, 2003), and clarified timing and functional dependence conditions for identification (?). Unobserved input-price dispersion contaminates deflated expenditures; recovering quality-adjusted quantities using first-order conditions mitigates this bias (Grieco et al., 2016). General conditions for identifying heterogeneous productivity in flexible environments are now well understood (Gandhi et al., 2020). These pillars are preconditions for credible wedge measurement, particularly when wedges are constructed from imported-input data with quality, variety, and bilateral price dispersion.

Under Hicks neutrality, productivity scales output proportionally across inputs, leaving factor shares unchanged. If technology is factor-augmenting, cost shares and elasticities move even when wedges are stable. This generates attribution problems: a decline in the labor share may reflect labor-saving technical change rather than stronger monopsony; shifts in material shares may arise from input-augmenting efficiency rather than buyer power (?Raval, 2018). Evidence from U.S. manufacturing rejects Cobb–Douglas and neutrality, with the micro elasticity of substitution well below one and persistent dispersion in factor shares (Raval, 2018; Oberfield and Raval, 2014). Macro patterns further underscore the need to separate technology from wedges (Karabarbounis and Neiman, 2014; De Loecker et al., 2020).

Most empirical analyses focus on labor- and capital-augmenting components. For foreign-input buyer power, the relevant margin is materials-augmenting efficiency. Using Chinese steel, Zhang (2019) estimates a CES technology with three factor-specific efficiencies—labor, capital, and materials—finding $\sigma < 1$ (gross complementarity), rapidly rising labor-augmenting efficiency, more modest capital efficiency, and lagging materials efficiency; counterfactuals attribute a sizable share of the decline in labor’s revenue share to non-neutrality. Because materials efficiency is distinct from capital efficiency and exhibits its own dispersion and dynamics, input-side bias is economically meaningful rather than a residual of labor and capital trends (Zhang, 2019). Two identification consequences follow for importer markdowns: revenue elasticities of imported inputs respond to movements in materials efficiency, and expenditure shares shift with input-augmenting progress even when wedges are unchanged (Raval, 2018; ?, 2019).

Three points follow. First, wedge estimation should be joint: markups, markdowns, and factor-biased productivity ought to be identified within a unified framework rather than sequentially under neutrality (?Brooks et al., 2021b). Second, measurement must confront

input-price heterogeneity and variety and quality composition; treating deflated expenditures as quantities biases elasticities and shares (Grieco et al., 2016). Third, welfare analysis must be open-economy: importer buyer power resembles an implicit tariff, so incidence and welfare depend on demand curvature, foreign supply elasticities, and pass-through; wedges net of factor bias provide appropriate inputs for policy evaluation (Morlacco, 2020; Avignon and Guigue, 2023; De Loecker et al., 2016a). Overall, production-based methods enable measurement of product-side markups and factor-side markdowns at scale, and extensions to imported intermediates document economically large importer buyer power with distinctive open-economy implications (Morlacco, 2020; Avignon and Guigue, 2023). At the same time, robust evidence shows that productivity is non-neutral, with factor-augmenting components—including materials—that move elasticities and shares even when wedges are unchanged (Raval, 2018). Credible measurement in foreign input markets therefore requires joint estimation of wedges and factor-biased technology under production-function identification that corrects for input-price heterogeneity (Olley and Pakes, 1996; Levinsohn and Petrin, 2003; ?; Grieco et al., 2016; Gandhi et al., 2020).

3 Data and Empirical Facts

3.1 Data

We construct the empirical sample by merging two longitudinal datasets. The primary source is the National Bureau of Statistics of China’s Annual Survey of Industrial Firms, which compiles firm reports from manufacturing enterprises and is maintained by the statistical authority. The resulting panel is unbalanced and covers two broad groups of manufacturers: state-owned enterprises and non-state-owned firms that satisfy the “above-scale” criterion, defined as annual sales of at least RMB 5 million (approximately US\$650,000) in the corresponding year.

The survey provides rich firm-year information on total revenue, expenditures on intermediate inputs, wage rates and wage bills, and a detailed set of firm characteristics—such as age, ownership status, and location—together with additional balance-sheet and income-statement variables. These features make the dataset well suited to production-function estimation and to the measurement of wedges on both the product side and the input side. For comprehensive documentation of coverage, construction rules, and known data issues, see (Brandt et al., 2014).

The second dataset consists of transaction-level customs records compiled by the General Administration of Customs of China. The data are highly disaggregated at the Harmonized

System eight-digit (HS8) level and record, for each firm-product transaction, the direction of trade (imports versus exports), the reported unit value, the physical quantity, and the total customs value. A distinctive feature of these records is the classification of processing-trade regimes. The database separates, among others, processing with imported materials and processing with supplied materials, together with closely related processing arrangements. This information permits a granular characterization of firms' participation in value-added trade and provides direct evidence on upstream sourcing strategies, including whether imported intermediates are tied to specific processing arrangements or used in ordinary trade. The transaction-level structure and product detail make the customs data complementary to the firm panel and well suited to studying input sourcing and pass-through in open-economy production settings.

We focus on six CIC two-digit industries—textiles (17), Textile and products (18), leather and products (19), electrical machinery and equipment (39), Communications, information and other electronic equipment (40), and Measuring instruments and office machinery (41)—for three reasons. First, these sectors exhibit a high intensity of imported intermediates and prominent processing-trade activity, which sharpens identification of buyer power in foreign input markets and provides informative variation in input prices and quantities. Second, the period surrounding China's WTO accession featured substantial tariff reductions together with export-oriented instruments—notably duty drawbacks and value-added tax rebates—which expanded firms' participation in international markets, reconfigured upstream sourcing toward foreign inputs, and coincided with pronounced productivity growth; this sequence provides policy-induced variation that is informative for production-function parameters and for wedge estimation on both the product and input sides. Third, these industries afford unusually detailed intermediate-input price information drawn from customs transaction records at the Harmonized System eight-digit level, which report values and quantities and permit the construction of high-granularity unit values; when linked to the firm survey, these data support the creation of quality-adjusted input quantities and enable credible estimation of non-Hicks-neutral, input-augmenting technology with an explicit focus on imported intermediates.

We build a panel dataset for 2000–2007 by linking the firm survey to customs transactions, harmonizing firm identifiers and industry codes, and deflating nominal variables with industry-specific price indices; imported-input prices are aggregated from HS6 unit values. After excluding observations with extreme values in core variables or missing lagged variables required by the estimator, the working sample contains 58,520 firm-year observations across the six industries. Appendix A.1 defines all variables; Table 1 reports summary statistics.

Table 1: Descriptive Statistics

(1) Variable	(2) Mean	(3) SD	(4) P25	(5) P50	(6) P75	(7) Min	(8) Max	(9) N
Capital stock (K)	55041.30	236033.42	3146.08	10076.76	34670.16	30.00	14809013.65	58520
Employment (L)	651.96	1673.19	144.00	296.00	629.00	8.00	188151.00	58520
Domestic input cost	17110605.75	1.22e+08	974354.72	2668856.63	8178027.50	2173.75	7.39e+09	58520
Foreign input cost	10656224.11	1.16e+08	312281.50	982999.50	3518031.50	531.00	1.61e+10	58520
Revenue (R)	34413670.41	2.43e+08	2282619.25	5656501.98	16643492.18	16793.93	2.45e+10	58520
Foreign input quantity (M^F)	16517494.66	1.49e+08	85902.50	421716.50	2126632.50	1.00	1.54e+10	58520
Wage (WL)	2374.20	13280.50	1254.42	1794.83	2626.10	0.00	3174890.00	58520
Labor cost	2374.20	13280.50	1254.42	1794.83	2626.10	0.00	3174890.00	58520
Gross fixed asset	6546691.00	28364486.32	371796.42	1193967.78	4111052.42	3624.50	1.78e+09	58520
Management fees	1246634.02	11559751.24	147641.60	328259.06	819948.82	120.82	1.73e+09	58520

Notes: Columns (1)–(9) report summary statistics for each variable: (1) Variable name; (2) Mean (sample mean); (3) SD (sample standard deviation); (4) P25 (25th percentile); (5) P50 (median/50th percentile); (6) P75 (75th percentile); (7) Min (sample minimum); (8) Max (sample maximum); (9) N (number of observations). Sample restricted to CIC2 industries 17, 18, 19, 39, 40, and 41. All monetary variables are reported in levels and measured in USD. Wage equals labor cost divided by employment. Statistics are computed variable-wise using available observations.

3.2 Heterogeneity and Declining of Foreign Input Share

We measure the firm-level foreign-input share as the ratio of expenditure on imported intermediates to total cost¹. To construct sectoral series, we take a sales-weighted average across firms within a CIC-2 industry. Figure 1 plots these sector-level shares for six industries over 2000–2007. Two facts emerge. First, there is a pronounced **downward trend** in foreign-input cost shares in several large sectors. Textile and products (18) and leather-related products (19) exhibit the clearest, near-monotonic declines; textiles (17) falls after substantial year-to-year volatility; communication and electronics (40) and instruments and office machinery (41) drift down after mid-sample plateaus; electrical machinery (39) follows an inverted-U, rising early and then retreating. Second, there is **marked heterogeneity** in levels, timing, and volatility, implying that both within-sector adjustments and shifts in the sales composition across sectors shape the aggregate.

¹ e_{fst}^F = (expenditure on foreign intermediates) / (total cost) for firm f in sector s and year t . The sector series plotted in Figure 1 we take a sales-weighted average of these firm shares:

$$E_{st}^F = \sum_{f \in s} \frac{\text{sales}_{ist}}{\sum_{j \in s} \text{sales}_{jst}} e_{fst}^F,$$

so that larger firms by sales carry greater weight in the sector-level series.

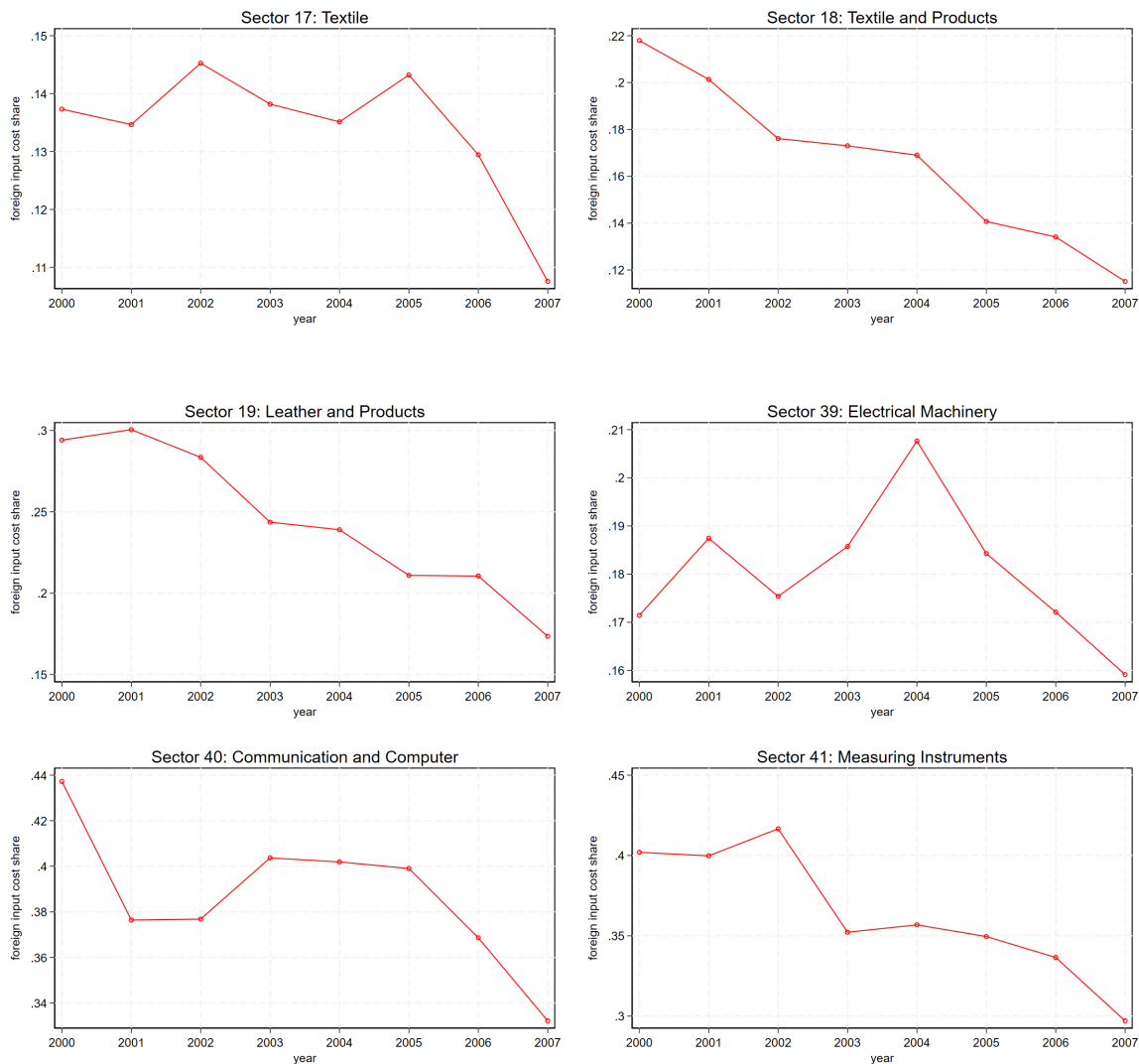


Figure 1: Change of Foreign Expenditure Share across Sectors

The observed decline in sectoral foreign-input shares is consistent with at least two distinct mechanisms that have very different structural implications. One interpretation is increased downstream buyer power or foreign-input markdowns: large buyers may obtain lower effective import prices or substitute away from imported intermediates, reducing observed expenditure on foreign inputs relative to total cost. An alternative (or simultaneous) explanation is input-biased technological change —technology that reduces the required imported intermediate input per unit of output (or otherwise changes cost shares) will also lower the imported input expenditure share.

Because both buyer-power markdowns and input-biased technological change affect the same observed series, attempting to compute a foreign-input markdown while ignoring input-biased technology is likely to yield biased and misleading inferences. Put simply: a falling

ratio of expenditure on imported intermediates to total cost could reflect bargaining effects, changes in input quantities driven by technology, or a mixture of both. Since we do not perform a structural decomposition here, any numeric “markdown” computed from these shares without accounting for input-biased technology risks conflating price and quantity channels and overstating the role of buyer power.

In light of these facts, empirical work that aims to measure foreign-input markdowns should either obtain additional data that separate prices from quantities for foreign inputs, or explicitly model input-biased technology so that price and productivity channels can be disentangled. Absent such steps, the descriptive patterns in Figure 2 motivate allowing technology to be factor- or input-biased in structural models that seek to interpret cross-sector heterogeneity and aggregate dynamics.

4 Empirical Model

Consider a firm f that produces a good Q using labor L , domestic intermediate input M_{ft}^D , foreign intermediate input ² M_{ft}^F and capital K at time t , according to a production function $G(\cdot)$. Firms differ not only in their Hicks-neutral productivity level Ω_{ft} , but also in foreign intermediate input-augmenting productivity A_{ft} . Finally, measurement error in log output is denoted ϵ_{ft} and is assumed to be mean independent to the inputs. In contrast, the set of production function coefficients β is assumed to be common across firms:

$$Q_{ft} = G(L_{ft}, M_{ft}^D, A_{ft}M_{ft}^F, K_{ft}; \beta)\Omega_{ft} \exp(\epsilon_{ft}) \quad (1)$$

Output and intermediate input can be traded across borders, so firms f in the industry face an inverse demand function. We assume demand function $G(\cdot)$ is twice differentiable in all variable inputs. Specifically, we assume domestic and foreign intermediate inputs are variable inputs and we denote the output elasticity of foreign intermediate foreign inputs and domestic inputs as θ_{ft}^F and θ_{ft}^D , respectively:

$$\theta_{ft}^F \equiv \frac{\partial G(\cdot)}{\partial M_{ft}^F} \frac{M_{ft}^F}{G(\cdot)} \quad \theta_{ft}^D \equiv \frac{\partial G(\cdot)}{\partial M_{ft}^D} \frac{M_{ft}^D}{G(\cdot)} \quad (2)$$

Firms pay variable input prices W_{ft}^F and W_{ft}^D face input supply curves with inverse supply elasticities $\psi_{ft}^F - 1$ and $\psi_{ft}^D - 1$ such that

²In terms of notations, superscript F denotes foreign inputs, D denotes domestic inputs, subscript f denotes firm.

$$\psi_{ft}^F \equiv \frac{\partial W_{ft}^F}{\partial M_{ft}^F} \frac{M_{ft}^F}{W_{ft}^F} + 1 \quad \psi_{ft}^D \equiv \frac{\partial W_{ft}^D}{\partial M_{ft}^D} \frac{M_{ft}^D}{W_{ft}^D} + 1 \quad (3)$$

4.1 Firm Behavior

Because we assume that domestic and foreign intermediate inputs are variable inputs, they are chosen in every period by the producer to minimize current variable costs. We denote marginal costs as λ_{ft} , and the cost minimization problem is given by the following equation:

$$\min_{\{M_{ft}^F, M_{ft}^D\}} [W_{ft}^D M_{ft}^D + W_{ft}^F M_{ft}^F - \lambda_{ft}(Q_{ft} - G(\cdot))] \quad (4)$$

From F.O.C. w.r.t. M_{ft}^F , we can get

$$W_{ft}^F + M_{ft}^F \frac{\partial W_{ft}^F}{\partial M_{ft}^F} = \lambda_{ft} \frac{\partial Q_{ft}}{\partial M_{ft}^F} \quad (5)$$

Multiply both sides by $\frac{M_{ft}^F}{Q_{ft}}$

$$W_{ft}^F \psi_{ft}^F \frac{M_{ft}^F}{Q_{ft}} = \lambda_{ft} \frac{\partial Q_{ft}}{\partial M_{ft}^F} \frac{M_{ft}^F}{Q_{ft}} = \lambda_{ft} \theta_{ft}^F \quad (6)$$

$$\frac{1}{\lambda_{ft}} = \frac{\theta_{ft}^F Q_{ft}}{W_{ft}^F M_{ft}^F \psi_{ft}^F} \quad (7)$$

As shown in [De Loecker et al. \(2016b\)](#), the markup of the final goods P_{ft} over marginal costs λ_{ft} , $\mu_{ft}^P \equiv P_{ft}/\lambda_{ft}$, is defined in the following equation:

$$\mu_{ft}^P = \frac{\theta_{ft}^F}{\gamma_{ft}^F \psi_{ft}^F} \quad (8)$$

From F.O.C. w.r.t. M_{ft}^D , we can get

$$\mu_{ft}^P = \frac{\theta_{ft}^D}{\gamma_{ft}^D \psi_{ft}^D} \quad (9)$$

where γ_{ft}^j denotes the cost of input j ($j = D, F$) as a share of gross revenues of firm f in year t , such that $\gamma_{ft}^F = \frac{W_{ft}^F M_{ft}^F}{P_{ft} Q_{ft}}$ and $\gamma_{ft}^D = \frac{W_{ft}^D M_{ft}^D}{P_{ft} Q_{ft}}$. Following [Morlacco \(2019\)](#) and [Brooks et al. \(2021a\)](#), from Eq. (8) and Eq. (9), the ratio of ψ_{ft}^F to ψ_{ft}^D equals the ratio of γ_{ft}^D to γ_{ft}^F

multiplied by the ratio of their output elasticities (i.e., $\frac{\theta_{ft}^F}{\theta_{ft}^D}$). And because we assume firms are price takers in domestic input market (i.e., $\psi_{ft}^D = 1$), we can get the following equation:

$$\psi_{ft}^F = \frac{\theta_{ft}^F \gamma_{ft}^D}{\gamma_{ft}^F \theta_{ft}^D} \psi_{ft}^D = \frac{\theta_{ft}^F \gamma_{ft}^D}{\gamma_{ft}^F \theta_{ft}^D} \quad (10)$$

Thus, the inverse supply elasticity of foreign intermediate inputs is the ratio of the foreign input's output elasticity to the domestic input's output elasticity, multiplied by the ratio of the domestic to foreign input expenditure shares. By definition, the foreign intermediate inputs markdown are defined as the ratio of marginal revenue product and factor price, $\mu_{ft}^F \equiv \frac{MRPM_{ft}^F}{W_{ft}^F}$. Therefore, from F.O.C., the foreign intermediate inputs markdown can be expressed as a function of this inverse foreign intermediate input supply elasticity:

$$\mu_{ft}^F = \frac{\theta_{ft}^F \gamma_{ft}^D}{\gamma_{ft}^F \theta_{ft}^D} = \psi_{ft}^F \quad (11)$$

where the marginal revenue product of foreign input is defined as:

$$MRPM_{ft}^F = P_{ft} \frac{\partial Q_{ft}}{\partial M_{ft}^F} \quad (12)$$

We define ψ_{ft}^F as the foreign input markdown (i.e., the buyer power in the foreign input market). Its calculation requires knowing the cost shares and output elasticities of both foreign and domestic intermediate inputs. Accordingly, from [Brooks et al. \(2021a\)](#), equation (11) implements this using a double-ratio approach.

4.2 Identification Challenge

Moreover, from (1), we can rewrite (5) as:

$$W_{ft}^F + M_{ft}^F \frac{\partial W_{ft}^F}{\partial M_{ft}^F} = \lambda_{ft} \frac{\partial G(L_{ft}, M_{ft}^D, A_{ft} M_{ft}^F, K_{ft}; \beta)}{\partial M_{ft}^F} \Omega_{ft} A_{ft} \quad (13)$$

We can also rewrite F.O.C. w.r.t. M_{ft}^D as:

$$W_{ft}^D = \lambda_{ft} \frac{\partial G(L_{ft}, M_{ft}^D, A_{ft} M_{ft}^F, K_{ft}; \beta)}{\partial M_{ft}^D} \Omega_{ft} \quad (14)$$

If we take the ratio of (13) and (14), we can get

$$\frac{W_{ft}^F + M_{ft}^F \frac{\partial W_{ft}^F}{\partial M_{ft}^F}}{W_{ft}^D} = \frac{\frac{\partial G(L_{ft}, M_{ft}^D, A_{ft} M_{ft}^F, K_{ft}; \beta)}{\partial M_{ft}^F}}{\frac{\partial G(L_{ft}, M_{ft}^D, A_{ft} M_{ft}^F, K_{ft}; \beta)}{\partial M_{ft}^D}} A_{ft} \quad (15)$$

From (15), we can see that if firm has no buyer power in foreign input market, (i.e. $\frac{\partial W_{ft}^F}{\partial M_{ft}^F} = 0$), we can recover A_{ft} directly. But from (15), we now have two unknowns $\frac{\partial W_{ft}^F}{\partial M_{ft}^F}$ and A_{ft} , so it is difficult to identify ψ_{ft}^F and A_{ft} separately as shown in Rubens et al. (2024). Therefore, this paper uses a new approach to identify markdown ψ_{ft}^F when there exists foreign input-biased technology A_{ft} .

4.3 Production Function

We implement the general framework in the context of the Chinese manufacturing industries. On the production side, we assume a Cobb–Douglas production function in which output depends on labor L_{ft} , intermediate inputs M_{ft} , and capital K_{ft} , with respective output elasticities β_l , β_m , and β_k . We further decompose intermediate inputs into domestic and foreign components and aggregate them through a CES production function, where the elasticity of substitution between domestic inputs (M_{ft}^D) and foreign inputs (M_{ft}^F) is denoted by γ . We denote ω_{ft} and a_{ft} as the logarithms of Hicks-neutral (Ω_{ft}) and foreign intermediate input-augmenting productivity (A_{ft}), respectively. Hicks-neutral and foreign-input-augmenting productivity are $\Omega_{ft} = e^{\omega_{ft}}$ and $A_{ft} = e^{a_{ft}}$.

$$Q_{ft} = e^{(\omega_{ft} + \varepsilon_{ft})} K_{ft}^{\beta_k} L_{ft}^{\beta_l} M_{ft}^{\beta_m} \quad (16)$$

$$M_{ft} = \left[(M_{ft}^D)^{\frac{\gamma-1}{\gamma}} + (A_{ft} M_{ft}^F)^{\frac{\gamma-1}{\gamma}} \right]^{\frac{\gamma}{\gamma-1}} \quad (17)$$

Taking logs on both sides of equation (16), and applying a second-order Taylor expansion of equation (17) around $\gamma = 1$ and denoting ω_{ft} and a_{ft} as the logarithms of Hicks-neutral, foreign intermediate inputs augmenting productivity, respectively, one can write the firm's production function as

$$q_{ft} = \beta_k k_{ft} + \beta_l l_{ft} + \beta_F (m_{ft}^F + a_{ft}) + \beta_D m_{ft}^D + \frac{1}{2} \beta_{FF} (m_{ft}^F + a_{ft})^2 + \frac{1}{2} \beta_{DD} (m_{ft}^D)^2 + \beta_{FD} (m_{ft}^F + a_{ft}) m_{ft}^D + \omega_{ft} + \varepsilon_{ft} \quad (18)$$

We define $m_{ft}^F + a_{ft} = m_{ft}^{F*}$ and impose homogeneity of degree $\beta_F + \beta_D$ in M_{ft}^F and M_{ft}^D

by setting $-\beta_{FF} = -\beta_{DD} = \beta_{FD} \equiv \beta$. Then the production function becomes

$$q_{ft} = \beta_k k_{ft} + \beta_l l_{ft} + \beta_F m_{ft}^{F*} + \beta_D m_{ft}^D - \frac{1}{2} \beta (m_{ft}^D - m_{ft}^{F*})^2 + \omega_{ft} + \varepsilon_{ft} \quad (19)$$

Therefore, the output elasticity of foreign input can be expressed as:

$$\theta_{ft}^F = \frac{\partial Q_{ft}}{\partial M_{ft}^F} \frac{\partial M_{ft}^F}{\partial Q_{ft}} = \frac{\partial q_{ft}}{\partial m_{ft}^F} = \beta_F + \beta(m_{ft}^D - m_{ft}^{F*}) = \beta_F + \beta(m_{ft}^D - m_{ft}^F - a_{ft}) \quad (20)$$

Similarly, the output elasticity of domestic input can be expressed as:

$$\theta_{ft}^D = \frac{\partial Q_{ft}}{\partial M_{ft}^D} \frac{\partial M_{ft}^D}{\partial Q_{ft}} = \frac{\partial q_{ft}}{\partial m_{ft}^D} = \beta_D - \beta(m_{ft}^D - m_{ft}^{F*}) = \beta_D - \beta(m_{ft}^D - m_{ft}^F - a_{ft}) \quad (21)$$

Using the definition of m_{ft}^{F*} , we can then express the ratio of output elasticity between foreign input and domestic input as:

$$\frac{\theta_{ft}^F}{\theta_{ft}^D} = \frac{\beta_F + \beta(m_{ft}^D - m_{ft}^{F*})}{\beta_D - \beta(m_{ft}^D - m_{ft}^{F*})} \quad (22)$$

From the F.O.C. of firm's cost minimization problem, we have the following conditions:

$$\frac{\partial Q_{ft}}{\partial M_{ft}^F} = \psi_{ft}^F \frac{W_{ft}^F}{\lambda_{ft}}, \quad \frac{\partial Q_{ft}}{\partial M_{ft}^D} = \frac{W_{ft}^D}{\lambda_{ft}}$$

Using the definition of output elasticity and rearrange the first-order conditions for foreign and domestic inputs, we can get

$$\frac{\partial Q_{ft}}{\partial M_{ft}^D} = \frac{\partial q_{ft}}{\partial m_{ft}^D} \frac{Q_{ft}}{M_{ft}^D} = \frac{W_{ft}^D}{\lambda_{ft}} = [\beta_D - \beta(m_{ft}^D - m_{ft}^{F*})] \frac{Q_{ft}}{M_{ft}^D}$$

$$\frac{\partial Q_{ft}}{\partial M_{ft}^F} = \frac{\partial q_{ft}}{\partial m_{ft}^F} \frac{Q_{ft}}{M_{ft}^F} = \psi_{ft}^F \frac{W_{ft}^F}{\lambda_{ft}} = [\beta_F + \beta(m_{ft}^D - m_{ft}^{F*})] \frac{Q_{ft}}{M_{ft}^F}$$

Using the definition of foreign input inverse supply elasticity ψ_{ft} , we can then express the ratio of output elasticity between foreign input and domestic input as a function of ψ_{ft}^F and input expenditures:

$$\frac{\theta_{ft}^F}{\theta_{ft}^D} = \frac{\beta_F + \beta(m_{ft}^D - m_{ft}^{F*})}{\beta_D - \beta(m_{ft}^D - m_{ft}^{F*})} = \frac{\psi_{ft}^F W_{ft}^F M_{ft}^F}{W_{ft}^D M_{ft}^D}$$

We can define the markdown-adjusted foreign input expenditure share S_{ft}^{FD} as the fraction of a firm's total variable input spending that goes to foreign inputs after those foreign-input expenditures have been adjusted by the markdown:

$$S_{ft}^{FD} \equiv \frac{\psi_{ft}^F W_{ft}^F M_{ft}^F}{\psi_{ft}^F W_{ft}^F M_{ft}^F + W_{ft}^D M_{ft}^D} \quad (23)$$

From (20) and (23), we can get

$$m_{ft}^D - m_{ft}^{F*} = -\frac{\beta_F}{\beta} + \frac{\beta_F + \beta_D}{\beta} S_{ft}^{FD}$$

From (21) and (23), we can get

$$m_{ft}^F + a_{ft} = \frac{\beta_F}{\beta} - \frac{\beta_F + \beta_D}{\beta} S_{ft}^{FD} + m_{ft}^D \quad (24)$$

We can then express the output elasticity of foreign and domestic inputs as a function of S_{ft}^{FD} , β_F and β_D :

$$\theta_{ft}^F = \beta_F + \beta(m_{ft}^D - m_{ft}^{F*}) = (\beta_F + \beta_D) S_{ft}^{FD} \quad (25)$$

$$\theta_{ft}^D = \beta_D - \beta(m_{ft}^D - m_{ft}^{F*}) = (\beta_F + \beta_D)(1 - S_{ft}^{FD}) \quad (26)$$

Using (25) and (26), we can get the sum of the output elasticity of the foreign and domestic input as:

$$\theta_{ft}^F + \theta_{ft}^D = \beta_F + \beta_D$$

From (25),(26) and (18), we can rewrite the production function as:

$$q_{ft} = \beta_k k_{ft} + \beta_l l_{ft} + \beta_D m_{ft}^D + \beta_F \left(\frac{\beta_F}{\beta} - \frac{\beta_F + \beta_D}{\beta} S_{ft}^{FD} + m_{ft}^D \right) - \frac{1}{2} \beta \left(\frac{\beta_F}{\beta} + \frac{\beta_F + \beta_D}{\beta} S_{ft}^{FD} \right)^2 + \omega_{ft} + \varepsilon_{ft} \quad (27)$$

Further simplifying the above equation, we can get

$$q_{ft} = \beta_k k_{ft} + \beta_l l_{ft} + (\beta_D + \beta_F) m_{ft}^D + \frac{1}{2} \frac{(\beta_F)^2}{\beta} - \frac{1}{2} \frac{(\beta_D + \beta_F)^2}{\beta} (S_{ft}^{FD})^2 + \omega_{ft} + \varepsilon_{ft} \quad (28)$$

4.4 Final Good Market

Regarding the final good market, we follow Zhang (2019) and assume the monopolistic competition (Morlacco, 2019).

$$Q_{ft} = \Delta_{ft} P_{ft}^{-\eta} \quad (29)$$

Where P_{ft} is the output price endogenously chosen by the firm, and η is the constant demand elasticity. Δ_{ft} is a time-specific demand shifter observed by the firm before choosing domestic and foreign inputs in each period. Δ_{ft} is further decomposed to be a time dummy Δ_t common to all firms, an unexpected i.i.d. shock ξ_{ft}^D , and the effects of other observed firm characteristics, such as firm size, age, and ownership. Assume that Δ_{ft} can be written in the following form:

$$\ln \Delta_{ft} = \Delta_t + \alpha_{\text{size}} \cdot \text{firm size}_{ft} + \alpha_{\text{age}} \cdot \text{firm age}_{ft} + \alpha_{\text{own}} \cdot \text{firm ownership}_{ft} + \xi_{ft}^D.$$

Consider the firm's profit maximization problem:

$$\pi_{ft} = \max_{P_{ft}} \{ P_{ft} Q_{ft}(P_{ft}) - C_{ft}(Q_{ft}(P_{ft})) \}$$

From the F.O.C., we can get

$$MR_{ft} = MC_{ft}$$

From final good demand function (29), we can have

$$MR_{ft} = P_{ft} + Q_{ft} \frac{dP_{ft}}{dQ_{ft}} = P_{ft} + Q_{ft} \left(-\frac{1}{\eta} \frac{P_{ft}}{Q_{ft}} \right) = P_{ft} \frac{\eta - 1}{\eta} = MC_{ft}$$

Then the final good markup μ_{ft}^P can be expressed as

$$\mu_{ft}^P = \frac{P_{ft}}{MC_{ft}} = \frac{\eta}{\eta - 1} \quad (30)$$

4.5 Foreign Input Markdown Calculation

In this section we show that identifying the foreign-input markdown is equivalent to identifying S_{ft}^{FD} . Identification is achieved by combining the final-good demand function and the production function with appropriate controls for the foreign-input supply side. We then identify non-neutral technology.

Taking natural log of the demand function, we can get

$$p_{ft} = \frac{1}{\eta} \ln(\Delta_{ft}) - \frac{1}{\eta} q_{ft} \quad (31)$$

From the cost minimization problem and $\lambda_{ft} = MC_{ft}$, we can get

$$W_{ft}^F \psi_{ft}^F = \lambda_{ft} \frac{\partial Q_{ft}}{\partial M_{ft}^F} = MC_{ft} \frac{\partial Q_{ft}}{\partial M_{ft}^F} \quad (32)$$

Using the output elasticity of foreign input, we have

$$W_{ft}^F \psi_{ft}^F = MC_{ft} \frac{\partial q_{ft}}{\partial m_{ft}^F} \frac{Q_{ft}}{M_{ft}^F} \quad (33)$$

Using the final good markup (30), we can express the F.O.C of foreign input as:

$$W_{ft}^F \psi_{ft}^F = \frac{\eta - 1}{\eta} P_{ft} \theta_{ft}^F \frac{Q_{ft}}{M_{ft}^F} \quad (34)$$

Similarly, we can express the F.O.C of domestic input as:

$$W_{ft}^D = \frac{\eta - 1}{\eta} P_{ft} \theta_{ft}^D \frac{Q_{ft}}{M_{ft}^D} \quad (35)$$

From (34) and (35) and using the double-ratio approach, we can express foreign input markdown as:

$$\psi_{ft}^F = \frac{W_{ft}^D M_{ft}^D}{W_{ft}^F M_{ft}^F} \frac{S_{ft}^{FD}}{1 - S_{ft}^{FD}} \quad (36)$$

From (36), we show that calculate markdown is equal to identifying S_{ft}^{FD} as $\frac{W_{ft}^D M_{ft}^D}{W_{ft}^F M_{ft}^F}$ can be observed from data.

4.5.1 Identify Markdown-Adjusted Foreign Input Expenditure Share

To identify S_{ft}^{FD} , we first rearrange (35) and from (26), we can get

$$\frac{P_{ft} Q_{ft}}{W_{ft}^D M_{ft}^D} = \frac{\frac{\eta}{\eta-1}}{(\beta_D + \beta_F)(1 - S_{ft}^{FD})} \quad (37)$$

From the cost minimization problem, one can use (37) and the definition of revenue $R_{ft} = P_{ft} Q_{ft}$ to identify S_{ft}^{FD} . Specifically, we can get:

$$\ln \left(\frac{R_{ft}}{W_{ft}^D M_{ft}^D} \right) = \ln \frac{\eta}{\eta-1} - \ln(\beta_D + \beta_F) - \ln(1 - S_{ft}^{FD}) + \varepsilon_{ft} \quad (38)$$

where ε_{ft} is the pure disturbance term at the production end of the firm. In order to identify

S^{FD} , we can run the following regression:

$$\ln\left(\frac{R_{ft}}{W_{ft}^D M_{ft}^D}\right) = \alpha_0 + X_{ft} \sigma + \varepsilon_{ft} \quad (39)$$

Here, the control variable X_{ft} is used to absorb heterogeneity on the foreign input-supply side and the combined effects of demand price elasticity and variable-input output elasticities. Specifically, X_{ft} includes firm capital, labor and domestic inputs, firm age, management cost, firm location, ownership type, year and industry dummy variables. After removing the stochastic disturbance ε_{ft} , the expression becomes:

$$\ln\left(\frac{\widehat{R}_{ft}}{W_{ft}^D M_{ft}^D}\right) = \hat{\alpha}_0 + X_{ft} \hat{\sigma} \quad (40)$$

We let $\widehat{s}_{ft}^R$ be the fitted value of the dependent variable from the regression equation $\ln\left(\frac{\widehat{R}_{ft}}{W_{ft}^D M_{ft}^D}\right)$. We use this expression as a constraint in the production-function estimation. After removing ε_{ft} , S_{ft}^{FD} can be expressed as:

$$S_{ft}^{FD} = 1 - \frac{\eta}{\eta - 1} \frac{1}{\beta_D + \beta_F} e^{-\widehat{s}_{ft}^R} \quad (41)$$

Equation (41) shows that the estimated adjusted foreign-domestic input share S_{ft}^{FD} is a function of the ratio of sales revenue to domestic input cost $\widehat{s}_{ft}^R = \frac{\widehat{R}_{ft}}{W_{ft}^D M_{ft}^D}$

4.5.2 Production Function Estimation

After we identify S_{ft}^{FD} , the production function (28) can be rewritten as:

$$q_{ft} = \beta_k k_{ft} + \beta_l l_{ft} + (\beta_D + \beta_F) m_{ft}^D + \frac{1}{2} \frac{\beta_F^2}{\beta} - \frac{1}{2} \frac{(\beta_D + \beta_F)^2}{\beta} \left(1 - \frac{\eta}{(\eta - 1)(\beta_D + \beta_F)} e^{-\widehat{s}_{ft}^R}\right)^2 + \omega_{ft} + \varepsilon_{ft} \quad (42)$$

We know revenue (in natural log) can be expressed as $r_{ft} = p_{ft} + q_{ft}$ and substitute the expressions of p_{ft} (31) and q_{ft} (42) into r_{ft} , we can get

$$\begin{aligned} r_{ft} = p_{ft} + q_{ft} = & \frac{1}{\eta} \ln(\Delta_{ft}) + \frac{\eta - 1}{\eta} \beta_k k_{ft} + \frac{\eta - 1}{\eta} \beta_l l_{ft} + \frac{\eta - 1}{\eta} (\beta_D + \beta_F) m_{ft}^D - \frac{\eta - 1}{\eta} \frac{\beta_D^2 + 2\beta_D \beta_F}{2\beta} \\ & + \frac{\eta - 1}{\eta} \frac{(\beta_D + \beta_F)\eta}{\beta(\eta - 1)} e^{-\widehat{s}_{ft}^R} - \frac{\eta - 1}{\eta} \frac{\eta^2}{2\beta(\eta - 1)^2} e^{-2\widehat{s}_{ft}^R} + \frac{\eta - 1}{\eta} \omega_{ft} + \frac{\eta - 1}{\eta} \varepsilon_{ft} \end{aligned} \quad (43)$$

Substitute the expression of $\ln(\Delta_{ft})$ into (43) and if we assume $\epsilon_{ft} \equiv \frac{1}{\eta}\xi_{ft}^D + \frac{\eta-1}{\eta}\epsilon_{ft}$, we can get

$$\begin{aligned} r_{ft} = p_{ft} + q_{ft} = & \frac{\eta-1}{\eta}\beta_k k_{ft} + \frac{\eta-1}{\eta}\beta_l l_{ft} + \frac{\eta-1}{\eta}(\beta_D + \beta_F)m_{ft}^D - \frac{\eta-1}{\eta}\frac{\beta_D^2 + 2\beta_D\beta_F}{2\beta} \\ & + \frac{\eta-1}{\eta}\frac{(\beta_D + \beta_F)\eta}{\beta(\eta-1)}e^{-\hat{s}_{ft}^R} - \frac{\eta-1}{\eta}\frac{\eta^2}{2\beta(\eta-1)^2}e^{-2\hat{s}_{ft}^R} + \frac{\eta-1}{\eta}\omega_{ft} \\ & + \frac{1}{\eta}(\Delta_t + \alpha_{\text{size}} \cdot \text{firm size}_{ft} + \alpha_{\text{age}} \cdot \text{firm age}_{ft} + \alpha_{\text{own}} \cdot \text{firm ownership}_{ft}) + \epsilon_{ft} \quad (44) \end{aligned}$$

Following [Akerberg et al. \(2015\)](#); [Doraszelski and Jaumandreu \(2018\)](#), we use two-stage approach to estimate the above production function. At first stage, we estimate

$$r_{ft} = h(l_{ft}, k_{ft}, m_{ft}^D, m_{ft}^F, w_{ft}^l, w_{ft}^F, e^{-\hat{s}_{ft}^R}, p_{ft}) + \nu_{ft},$$

via OLS with $h(\cdot)$ as a third-order polynomial, yielding $\hat{r}_{ft}$.

$$\begin{aligned} \frac{\eta-1}{\eta}\omega_{ft} = \hat{r}_{ft} - & \frac{\eta-1}{\eta}\beta_k k_{ft} - \frac{\eta-1}{\eta}\beta_l l_{ft} - \frac{\eta-1}{\eta}(\beta_D + \beta_F)m_{ft}^D + \frac{\eta-1}{\eta}\frac{\beta_D^2 + 2\beta_D\beta_F}{2\beta} \\ & - \frac{\eta-1}{\eta}\frac{(\beta_D + \beta_F)\eta}{\beta(\eta-1)}e^{-\hat{s}_{ft}^R} + \frac{\eta-1}{\eta}\frac{\eta^2}{2\beta(\eta-1)^2}e^{-2\hat{s}_{ft}^R} \\ & - \frac{1}{\eta}(\Delta_t + \alpha_{\text{size}} \cdot \text{firm size}_{ft} + \alpha_{\text{age}} \cdot \text{firm age}_{ft} + \alpha_{\text{own}} \cdot \text{firm ownership}_{ft}) \end{aligned}$$

We define the above parameters as: $\frac{\eta-1}{\eta}\frac{\beta_D^2 + 2\beta_D\beta_F}{2\beta} \equiv \alpha_0$, $\frac{\eta-1}{\eta}\beta_k \equiv \alpha_k$, $\frac{\eta-1}{\eta}\beta_l \equiv \alpha_l$, $\frac{\eta-1}{\eta}(\beta_D + \beta_F) \equiv \alpha_m^D$, $\frac{\eta-1}{\eta}\frac{(\beta_D + \beta_F)\eta}{\beta(\eta-1)} \equiv \alpha_{s1}$, $\frac{\eta-1}{\eta}\frac{\eta^2}{2\beta(\eta-1)^2} \equiv \alpha_{s2}$ and we can get

$$\begin{aligned} \frac{\eta-1}{\eta}\omega_{ft} = r_{ft} + & \alpha_0 - \alpha_k k_{ft} - \alpha_l l_{ft} - \alpha_m^D m_{ft}^D - \alpha_{s1} e^{-\hat{s}_{ft}^R} - \alpha_{s2} e^{-2\hat{s}_{ft}^R} \\ & - \frac{1}{\eta}(\Delta_t + \alpha_{\text{size}} \cdot \text{firm size}_{ft} + \alpha_{\text{age}} \cdot \text{firm age}_{ft} + \alpha_{\text{own}} \cdot \text{firm ownership}_{ft}) \end{aligned}$$

At second stage, we introduce law of motion of the Hicks-neutral productivity,

$$\frac{\eta-1}{\eta}\omega_{ft} = g\left(\frac{\eta-1}{\eta}\omega_{ft-1}\right) + \mu_{ft} \quad (45)$$

, where we approximate $g(\cdot)$ as a first order polynomial in all its argument. Then the innovation $\mu_{ft} = \frac{\eta-1}{\eta}\omega_{ft} - \frac{\eta-1}{\eta}\omega_{ft-1}$ depends only on observables and all parameters to be estimated, and we use the GMM method proposed by ? to estimate vector of parameter α

from the following moment condition:

$$\mathbb{E}[\mu_{ft}(\alpha) Z_{ft}] = 0, \quad (46)$$

where instrument variable vector Z_{ft} contains lags of domestic input, labor, markdown-adjusted cost share $e^{-\hat{s}_{ft}^R}$ and current capital as well as their interaction terms.

4.5.3 Foreign Input Markdown and Non-Neutral Technology Calculation

After identifying $\hat{s}_{ft}^R$, from (41), we can get

$$S_{ft}^{FD} = 1 - \frac{1}{\hat{\alpha}_m^D} e^{-\hat{s}_{ft}^R}$$

From (36), foreign input markdown can be expressed as:

$$\psi_{ft}^F = \frac{W_{ft}^D M_{ft}^D (1 - \frac{1}{\hat{\alpha}_m^D} e^{-\hat{s}_{ft}^R})}{W_{ft}^F M_{ft}^F \frac{1}{\hat{\alpha}_m^D} e^{-\hat{s}_{ft}^R}} \quad (47)$$

From (24), the foreign input-biased technology can be expressed as

$$a_{ft} = \frac{\beta_F}{\beta} - \frac{\beta_F + \beta_D}{\beta} S_{ft}^{FD} + m_{ft}^D - m_{ft}^F$$

After removing the mean, we obtain an estimate of foreign input-augmenting productivity

$$\hat{a}_{ft} = -\frac{(\hat{\alpha}_{s1})^2}{2\hat{\alpha}_{s2}\hat{\alpha}_m^D} S_{ft}^{FD} + m_{ft}^D - m_{ft}^F$$

where $-\frac{(\hat{\alpha}_{s1})^2}{2\hat{\alpha}_{s2}\hat{\alpha}_m^D} \equiv -\frac{\hat{\beta}_F + \hat{\beta}_D}{\hat{\beta}}$

5 Estimation Results

The estimation results for the non-neutral production functions are reported in the table 2.

The table 2 reports the estimated results for the main parameters. Among these, the production-side parameters are the ones this paper cares about most. Therefore, although some of the parameters do not have an immediate, intuitive economic interpretation, the short-run returns-to-scale parameter α_m^D represents their short-run revenue scale returns. Table 2 shows α_m^D ranges from 0.79 to 0.99, and the industry average of the short-run

scale parameter is 0.89. These findings are very close to estimates reported in the existing literature. In addition, based on the parameter estimates, the average income elasticities for labor and capital are 0.07 and 0.01, respectively. The above estimates closely match existing results and lie within a reasonable range.

To show the relationship between estimated parameters and short-run returns-to-scale as well as revenue elasticity of different inputs, we can show the following:

$$\begin{aligned}
\theta_{ft}^{RF} &= \frac{\partial R_{ft}}{\partial M_{ft}^F} \frac{M_{ft}^F}{R_{ft}} = \frac{\partial(P_{ft}Q_{ft})}{\partial M_{ft}^F} \frac{M_{ft}^F}{P_{ft}Q_{ft}} \\
&= \left[Q_{ft} \frac{\partial P_{ft}}{\partial Q_{ft}} + P_{ft} \right] \frac{\partial Q_{ft}}{\partial M_{ft}^F} \frac{M_{ft}^F}{P_{ft}Q_{ft}} \\
&= \left[\frac{Q_{ft}}{P_{ft}} \frac{\partial P_{ft}}{\partial Q_{ft}} + 1 \right] \frac{M_{ft}^F}{Q_{ft}} \frac{\partial Q_{ft}}{\partial M_{ft}^F} = \frac{\theta_{ft}^F}{\mu_{ft}^P} \\
&= \frac{(\beta_F + \beta_D) S_{ft}^{FD}}{\mu_{ft}^P} = \alpha_M^D S_{ft}^{FD}
\end{aligned}$$

$$\theta_{ft}^{RD} = \frac{\partial R_{ft}}{\partial M_{ft}^D} \frac{M_{ft}^D}{R_{ft}} = \frac{\partial(P_{ft}Q_{ft})}{\partial M_{ft}^D} \frac{M_{ft}^D}{P_{ft}Q_{ft}} = \alpha_M^D (1 - S_{ft}^{FD})$$

$$\theta_{ft}^{RL} = \frac{\partial R_{ft}}{\partial L_{ft}} \frac{L_{ft}}{R_{ft}} = \frac{\partial(P_{ft}Q_{ft})}{\partial L_{ft}} \frac{L_{ft}}{P_{ft}Q_{ft}} = \alpha_l$$

$$\theta_{ft}^{RK} = \frac{\partial R_{ft}}{\partial K_{ft}} \frac{K_{ft}}{R_{ft}} = \frac{\partial(P_{ft}Q_{ft})}{\partial K_{ft}} \frac{K_{ft}}{P_{ft}Q_{ft}} = \alpha_k$$

If we only consider domestic intermediate input and foreign intermediate input as variable inputs, then the short-run revenue scale returns can be expressed as $\theta_{ft}^{RD} + \theta_{ft}^{RF} = \alpha_M^D$.

Table 2: Non-Neutral Production Function Estimates

(1) Code	(2) Industry	(3) α_l	(4) α_k	(5) α_m^D	(6) α_{s1}	(7) α_{s2}	(8) N
17	Textile	0.0757 (0.3337)	0.0169 (0.0848)	0.8565 (0.3143)	-1.7785 (3.9825)	0.4586 (3.3273)	3423
18	Textile and Products	0.0833 (0.0383)	0.0220 (0.0159)	0.8033 (0.1227)	-9.9465 (3.6977)	8.3320 (3.7560)	4015
19	Leather and Products	0.0895 (0.0481)	-0.0279 (0.0197)	0.9458 (0.0773)	-10.0451 (4.6588)	8.3571 (4.4319)	2416
39	Electrical Machinery	0.0569 (0.0997)	-0.0137 (0.0406)	0.9878 (0.3360)	-1.3100 (6.6030)	-0.3096 (6.0578)	3706
40	Communication and Computer	0.0795 (0.1405)	0.0028 (0.0249)	0.9706 (0.3029)	-0.6182 (8.2199)	-0.8466 (8.1785)	6067
41	Measuring Instruments	0.0575 (0.0795)	-0.0239 (0.0273)	0.7935 (0.1789)	-11.3693 (5.5840)	9.8667 (5.7113)	1396

Note: Standard errors are shown in parentheses on the line below each estimate; they were calculated from 200 bootstrap replications.

From Eq. (47), the foreign input markdown under non-neutral technology are reported in table 3.

Table 3: Sector-Level Buyer Power, Non-Neutral, by CIC-2 Sector

(1) Code	(2) Industry	(3) N	(4) Mean	(5) Median	(6) SD
17	Textile	9590	5.61	3.05	6.94
18	Textile and Products	12293	5.57	2.62	7.21
19	Leather and Products	6460	6.67	3.10	9.11
39	Electrical Machinery	9992	6.51	3.50	8.19
40	Communication and Computer	16277	5.65	2.60	8.41
41	Measuring Instruments	3842	4.03	1.94	5.94
Total		58454	5.78	2.81	7.87

Notes: Col. (3) gives the number of observations (N); Cols. (4)–(6) report mean, median, and standard deviation (SD) of firm-level buyer power.

The table 3 shows that markdowns exist and that substantial heterogeneity is present both across sectors and within sectors. The frequent occurrence of means exceeding medians and the sizable standard deviations point to right-skewed, heavy-tailed distributions—a small subset of firms with very large buyer power drives sectoral averages.

Furthermore, we also illustrate the change of markdown under non-neutral technology over sample period 2000-2007.

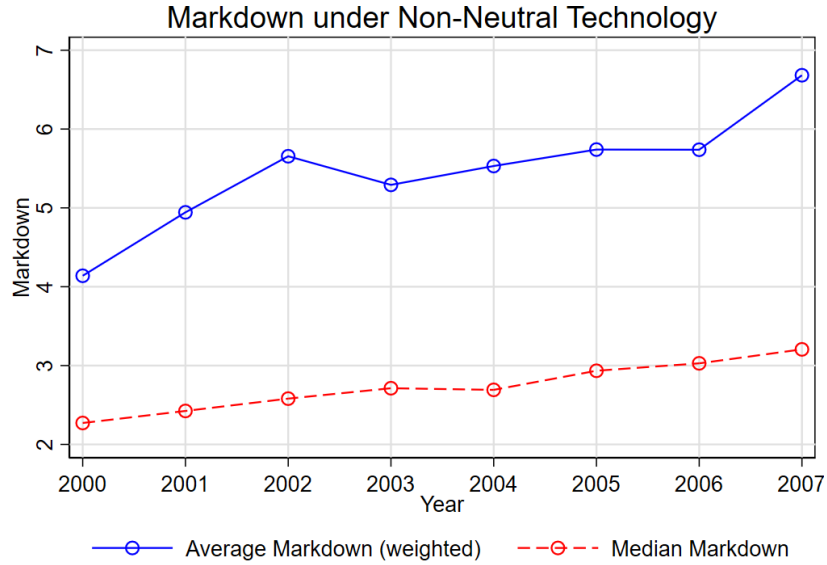


Figure 2: Change of Markdown over Time under Non-Neutral Technology

Across the selected sectors from 2000 to 2007 the revenue-weighted (“average”) foreign-input markdown rises substantially while the median markdown increases more slowly. The weighted average climbs from approximately 4.0 in 2000 to about 6.8 in 2007 (an increase of $6.8 - 4.0 = 2.8$, i.e. a 70% increase), whereas the median moves from roughly 2.2 to 3.1 (an increase of 0.9, i.e. $\approx 40.9\%$). Because the weighted mean is consistently and increasingly larger than the median (the gap widens from 1.8 to 3.7, an absolute rise of 1.9, or $\approx 105.6\%$), the pattern indicates that the growth in markdowns is driven disproportionately by larger firms (or higher-revenue observations) rather than a uniform shift across the firm distribution.

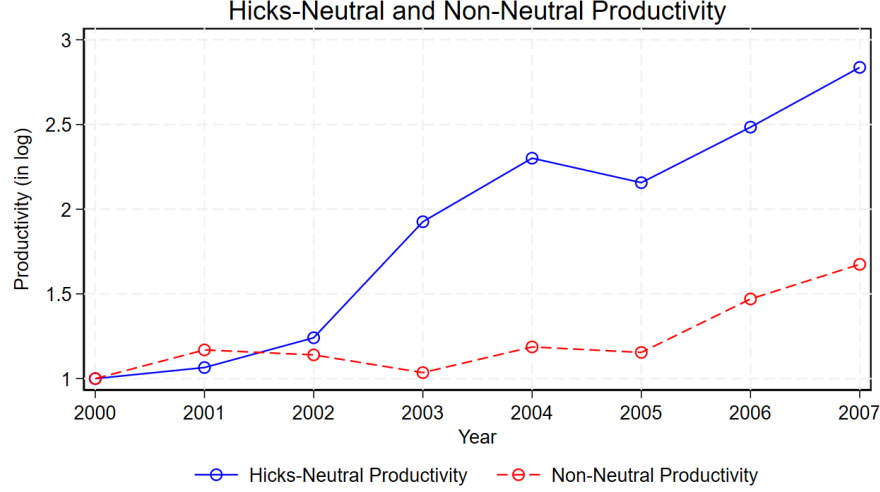


Figure 3: Dynamics of Hicks-neutral and non-Hicks technology

Furthermore, Figure 3 demonstrates the dynamics of sector-level Hicks-neutral technology and non-neutral technology from 2000 to 2007. Solid blue line represents revenue-weighted Hicks-neutral (total factor) productivity, normalized to 1 in 2000. Dashed red line represents revenue-weighted non-neutral productivity, normalized to 1 in 2000.

The non-neutral productivity rises relatively quickly in the early 2000s technology (blue) remains close to 1 through 2002, accelerates after 2002–2003, overtakes the non-neutral measure following the 2004 peak, and reaches roughly 1.33 by 2007.

Because these are revenue-weighted series, the plotted movements primarily reflect changes among higher-revenue firms. Descriptively, non-neutral (foreign input biased) productivity gains appear earlier in the sample while Hicks-neutral gains are more sustained later; this description is intended as a factual summary of the plotted trends rather than a causal claim.

One plausible interpretation is that initial adoption of foreign input biased technologies or improved sourcing raised the marginal productivity of foreign inputs first (captured by red line), and these gains later diffused into wider productivity-enhancing adjustments.

And the Table 4 shows the Hicks-neutral and non-neutral technology growth rate for each selected sector.

Table 4: Growth Rate of Hicks-neutral and Non-Neutral Productivity

Code	Industry	Hicks-neutral (%)	Non-neutral (%)
17	Textile	2.97	0.92
18	Textile and Products	2.87	7.48
19	Leather and Products	-0.68	8.72
39	Electrical Machinery	-1.44	10.90
40	Communication and Computer	-3.56	4.97
41	Measuring Instruments	-2.17	2.52

Across the sectors shown, non-neutral (foreign input-biased) productivity growth exceeds Hicks-neutral (TFP) growth in five sectors (18, 19, 39, 40, 41). The largest non-neutral gains are concentrated in electrical machinery (39, 10.90%) and leather and related products (19, 8.72%), while the Hicks-neutral growth rate is positive and comparatively larger only in the Textile sector (17, 2.97% vs 0.92%). Several sectors (19, 39, 40, 41) display negative Hicks-neutral productivity growth alongside positive non-neutral technology growth, indicating that measured improvements in productivity tied to imported intermediates can be large even when aggregate (Hicks-neutral) TFP is flat or declining.

This pattern is descriptive: revenue-weighted growth rates emphasize outcomes for higher-revenue firms, so the reported magnitudes primarily reflect what happens at larger firms within each sector. A cautious interpretation is that input-specific (non-neutral) productivity improvements are an important component of measured productivity dynamics in these sectors, particularly in machinery and leather-related manufacturing, while broad-based Hicks-neutral gains are modest and concentrated in textiles.

We also examine three determinants of firm-level foreign-input markdown: size, foreign-input-biased technology, and ownership. Size is proxied by the firm’s revenue. Foreign-input-biased technology is represented by a_{ft} and used in natural-log form, $\ln a_{ft}$. Ownership is captured by a dummy variable FOE that equals 1 if the firm has any positive foreign ownership share (majority or minority) and 0 otherwise.

We then run the following regression:

$$\ln \psi_{ft}^F = \alpha + \beta_1 \text{size} + \beta_2 \ln a_{ft} + \beta_3 \ln \text{FOE} + \text{FE}_{ft} + \varepsilon_{ft}$$

Table 5: Impact of Firm Size on Firm’s Buyer Power

	(1)	(2)	(3)
Dependent Variable		$\ln \psi_{ft}^F$	
$\ln(\text{size})$	0.290*** (0.009)	0.167*** (0.007)	0.167*** (0.007)
a_{ft}		0.458*** (0.003)	0.458*** (0.003)
FOE			0.462*** (0.110)
Observations	51,997	51,997	51,997
FE	FY	FY	FY
Adj. R^2	0.66	0.79	0.79

Notes: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.10$. FY denote firm and year fixed effects. Size is measured as firm’s total revenue and results are robust if we use total employment as an alternative measure. Standard errors are reported in parentheses.

The table reports OLS estimates where the dependent variable is the natural log of the firm-level foreign-input markdown (log buyer power), $\ln \psi_{ft}^F$. Model (1) reports the baseline association between firm size (logged revenue) and markdown; Model (2) adds the foreign-input-biased technology measure a_{ft} ; Model (3) further adds the FOE ownership dummy. All specifications include firm and year fixed effects (FY). Standard errors are shown in parentheses and significance stars indicate conventional p-value thresholds.

Firm size is positively and highly significantly associated with larger markdowns: the coefficient on $\ln(\text{size})$ falls from 0.29 in (1) to 0.17 in (2)–(3) after adding technology and ownership controls, indicating that a 1% increase in revenue is associated with roughly a 0.17–0.29% higher markdown, conditional on fixed effects. The foreign-input-biased technology coefficient is 0.458 and precisely estimated; if a_{ft} is entered in natural-log form, this is interpreted as an elasticity (a 1% increase in the input-biased productivity measure corresponds to 0.46% higher markdown). The FOE dummy in (3) is positive and significant: FOE firms have substantially larger markdowns, about $\exp(0.462) - 1 \approx 0.59$ (59%) higher on average relative to purely domestic firms, conditional on the included controls.

Model fit improves when adding the technology and ownership variables (adjusted R^2 rises from 0.66 to 0.79). The sample covers 51,997 firm–year observations. Results are reported with standard errors in parentheses and are robust to using employment instead of revenue as the size measure (see notes). These estimates are descriptive associations conditional on fixed effects and covariates; they document that larger firms, firms with higher measured

foreign-input-biased productivity, and foreign-owned firms tend to exhibit systematically larger buyer power as measured by the log markdown.

5.1 Robustness Check

We estimate Hicks-neutral production function to calculate markdown as robustness check. To do it, we take logs on both sides of equation (16), and use a second-order Taylor expansion of equation (17) around $\gamma = 1$. One can write the firm's production function as

$$q_{ft} = \beta_k k_{ft} + \beta_l \ell_f + \beta_F m_{ft}^F + \beta_D m_{ft}^D + \beta_{FF} (m_{ft}^F)^2 + \beta_{DD} (m_{ft}^D)^2 + \beta_{FD} m_{ft}^F m_{ft}^D + \omega_{ft} + \varepsilon_{ft}, \quad (48)$$

Therefore, the output elasticity of foreign input can be expressed as:

$$\theta_{ft}^F = \beta_F + 2\beta_{FF} m_{ft}^F + \beta_{FD} m_{ft}^D$$

Similarly, the output elasticity of domestic input can be expressed as:

$$\theta_{ft}^D = \beta_D + 2\beta_{DD} m_{ft}^D + \beta_{FD} m_{ft}^F$$

And we can also get:

$$\frac{\theta_{ft}^F}{\theta_{ft}^D} = \frac{\beta_F + 2\beta_{FF} m_{ft}^F + \beta_{FD} m_{ft}^D}{\beta_D + 2\beta_{DD} m_{ft}^D + \beta_{FD} m_{ft}^F}$$

We first do the input-demand inversion. From the first-order conditions of cost minimization, foreign and domestic intermediate input quantities satisfy

$$M_{ft}^F = \delta(W_{ft}, V_{ft}/M_{ft}^F, K_{ft}, P_{ft}, e^{\omega_{ft}}), \quad (49)$$

$$M_{ft}^D = \mu(W_{ft}, V_{ft}/M_{ft}^D, K_{ft}, P_{ft}, e^{\omega_{ft}}). \quad (50)$$

Here W_{ft} is the vector of input prices, V_{ft} the vector of input quantities, P_{ft} the output price, and $e^{\omega_{ft}}$ productivity. Monotonicity in prices allows us to invert (50):

$$W_{ft}^D = \mu^{-1}(W_{ft}/W_{ft}^D, V_{ft}, K_{ft}, P_{ft}, e^{\omega_{ft}}) \quad (51)$$

Substituting (51) into (49) yields

$$M_{ft}^F = \tilde{\delta}(W_{ft}/W_{ft}^D, V_{ft}/M_{ft}^F, K_{ft}, P_{ft}, e^{\omega_{ft}}), \quad (52)$$

which in turn can be inverted for productivity:

$$e^{\omega_{ft}} = \tilde{\delta}^{-1}(V_{ft}, K_{ft}, W_{ft}/W_{ft}^D, P_{ft}). \quad (53)$$

Although P_{ft} is unobserved, we proxy it with firm-level output deflators $\tilde{P}_{ft}$. The above production function becomes

$$\begin{aligned} \tilde{q}_{ft} = & \beta_k k_{ft} + \beta_l l_{ft} + \beta_F m_{ft}^F + \beta_D \bar{m}_{ft}^D + \beta_{FF} (m_{ft}^F)^2 + \beta_{DD} (\bar{m}_{ft}^D)^2 + \beta_{FD} m_{ft}^F \bar{m}_{ft}^D \\ & + \tilde{\delta}^{-1}(\ell_{ft}, k_{ft}, \bar{m}_{ft}^D, m_{ft}^F, w_{ft}^F, w_{ft}^\ell, p_{ft}) + u_{ft} \end{aligned} \quad (54)$$

where $u_{ft} = \varepsilon_{ft} + \beta^D h(w_{st}^D - w_{ft}^D)$

We use two-stage approach to estimate the above production function. At first stage, we estimate

$$q_{ft} = \phi(l_{ft}, k_{ft}, m_{ft}^D, m_{ft}^F, w_{ft}^F, w_{ft}^l, p_{ft}) + \varepsilon_{ft},$$

via OLS with $\phi(\cdot)$ as a third-order polynomial, yielding $\hat{q}_{ft}$. At Second stage, we introduce a law of motion for productivity:

$$\omega_{ft} = \rho(\omega_{ft-1}) + \xi_{ft}, \quad \rho(\cdot) \text{ is a first-order polynomial}, \quad (55)$$

⁴ and we can get

$$\omega_{ft}(\beta) = \hat{q}_{ft} - (\beta_k k_{ft} + \beta_l l_{ft} + \beta_F m_{ft}^F + \beta_D \bar{m}_{ft}^D + \beta_{FF} (m_{ft}^F)^2 + \beta_{DD} (\bar{m}_{ft}^D)^2 + \beta_{FD} m_{ft}^F \bar{m}_{ft}^D) \quad (56)$$

Then we can get

$$\xi_{ft}(\beta) = \omega_{ft}(\beta) - \rho(\omega_{ft-1}(\beta))$$

Then the innovation ξ_{ft} depends only on observables and parameter vector β , and we estimate β from the following moment condition:

$$\mathbb{E}[\xi_{ft}(\beta) Z_{ft}] = 0, \quad (57)$$

where instrument variable vector Z_{ft} contains lags of domestic and foreign input, current capital and labor, and their interaction terms.

Using double-ratio approach, we can derive the foreign input markdown under Hicks-neutral productivity $\psi_{ft}^{FHN} = \frac{\beta_F + 2\beta_{FF} m_{ft}^F + \beta_{FD} m_{ft}^D}{\beta_D + 2\beta_{DD} m_{ft}^D + \beta_{FD} m_{ft}^F} \cdot \frac{W_{ft}^D M_{ft}^D}{W_{ft}^F M_{ft}^F}$

Under Hicks-neutral production function, we estimate production function using 2-step

⁴Results are robust if we assume $\rho(\cdot)$ is a second-order polynomial in all its arguments.

GMM methods proposed by [Akerberg et al. \(2015\)](#). Table 3 reports the estimated parameters. The output elasticity of labor and capital is defined as β_k and β_l respectively. And output elasticity for foreign input and domestic input are given as following $\theta_{ft}^F = \beta_F + 2\beta_{FF}m_{ft}^F + \beta_{FD}m_{ft}^D$ and $\theta_{ft}^D = \beta_D + 2\beta_{DD}m_{ft}^D + \beta_{FD}m_{ft}^F$, respectively.

The median output elasticity of foreign input across sectors is 0.30 whereas median output elasticity of domestic input is 0.38. The median output elasticity of labor is 0.12 and output elasticity of capital is 0.06. The full estimation results are reported in table 3.

Table 6: Estimation Results for Hicks-neutral Production Function

(1) Code	(2) Industry	(3) β_k	(4) β_l	(5) β_D	(6) β_F	(7) β_{DD}	(8) β_{FF}	(9) β_{FD}	(10) N
17	Textile	0.0439 (0.0197)	0.0693 (0.0402)	-0.0333 (0.0583)	0.1731 (0.0642)	0.0637 (0.0141)	0.0225 (0.0044)	-0.0544 (0.0127)	8579
18	Textile and Products	-0.0569 (0.0231)	-0.1048 (0.0459)	-0.0123 (0.0812)	0.2539 (0.0564)	0.1027 (0.0105)	0.0221 (0.0057)	-0.0724 (0.0107)	9871
19	Leather and Products	0.0380 (0.0209)	0.1189 (0.0271)	0.0183 (0.0983)	0.1937 (0.0369)	0.0364 (0.0158)	0.0225 (0.0033)	-0.0379 (0.0111)	5032
39	Electrical Machinery	0.0774 (0.0245)	0.1110 (0.0412)	0.0364 (0.0749)	0.1742 (0.0410)	0.0328 (0.0117)	0.0121 (0.0040)	-0.2464 (0.1143)	8106
40	Communication and Computer	0.0803 (0.0178)	0.1789 (0.0330)	-0.0360 (0.0546)	0.1453 (0.0326)	0.0284 (0.0210)	0.0149 (0.0062)	-0.2262 (0.0209)	11559
41	Measuring Instruments	0.0109 (0.0233)	0.0456 (0.0644)	-0.3106 (0.1039)	0.1648 (0.0547)	0.0621 (0.0180)	-0.0023 (0.0103)	-0.0082 (0.2152)	2975

Note: Standard errors are shown in parentheses on the line below each estimate; they were calculated from 200 bootstrap replications.

Using the double-ratio approach, the foreign input markdown under Hicks-neutral technology are reported in the table 7.

Table 7 indicates that foreign-input markdowns under a Hicks-neutral technology are present: the economy-wide mean buyer power is 3.98 (median 2.22), implying that firms on average obtain non-negligible markdowns on foreign intermediates. There is clear sectoral heterogeneity. Textile and related sectors (CIC-2 codes 17–19) display substantially higher buyer power (means: 3.32, 6.50, 4.58; medians: 2.38, 4.10, 2.59) and larger dispersion (SDs up to 8.87) than machinery and electronics sectors (codes 39–41), which show lower means (3.1, 2.95, 3.10) and lower medians (1.5–1.7).

Table 7: Sector-Level Buyer Power, Hicks-Neutral, by CIC-2 Sector

(1) Code	(2) Industry	(3) N	(4) Mean	(5) Median	(6) SD
17	Textile	9612	3.32	2.38	8.53
18	Textile and Products	12360	6.50	4.10	8.87
19	Leather and Products	6504	4.58	2.59	6.76
39	Electrical Machinery	10015	3.13	1.71	3.87
40	Communication and Computer	16347	2.95	1.48	6.75
41	Measuring Instruments	3852	3.10	1.63	5.75
Total		58690	3.98	2.22	7.27

Notes: Col. (3) gives the number of observations (N); Cols. (4)–(6) report mean, median, and standard deviation (SD) of firm-level buyer power.

5.2 Change of Buyer Power over Time

This section analyzes the markdowns on foreign intermediate inputs across selected Chinese manufacturing sectors between 2000 and 2007. Figure 4 demonstrates the six panels plot the median firm-level buyer power over time under two specifications: the blue lines representing the Hicks-neutral specification and the red dashed lines representing the Non-Hicks specification. A clear, general pattern is that the Non-Hicks estimates are typically larger and show stronger upward trends over 2000–2007 than the Hicks-neutral estimates. This visual gap indicates that the assumed technology (Hicks-neutral vs. non-Hicks) materially affects the level and time path of inferred buyer power.

Within the textile and leather group (CIC 17–19) the dynamics are heterogeneous. Sector 17 (Textile) shows a widening gap with Non-Hicks medians substantially above the Taylor medians and increasing more rapidly. Sector 18 (Textile and Products) is the notable exception: the Hicks-neutral lies above the Non-Hicks series and rises toward the end of the sample, suggesting that Hicks-neutral assumptions allocate relatively more buyer power to this sub-sector. Sector 19 (Leather and Products) exhibits rising buyer power in both specifications, but much more sharply under Non-Hicks. In short, the textile cluster (sectors 17–19) shows within-group reallocation when technology assumptions change—one sub-sector (18) moves opposite to the other two.

The other cluster (CIC 39–41: Electrical Machinery; Communication and Computer; Measuring Instruments) presents a more uniform story. For these sectors the Non-Hicks medians are consistently higher and generally increasing, while the Taylor medians remain low and roughly flat (or slightly rising). Sector 39 and 40 show especially persistent gaps, and sector 41 has a sharp early spike in the Non-Hicks series before stabilizing. That uniform

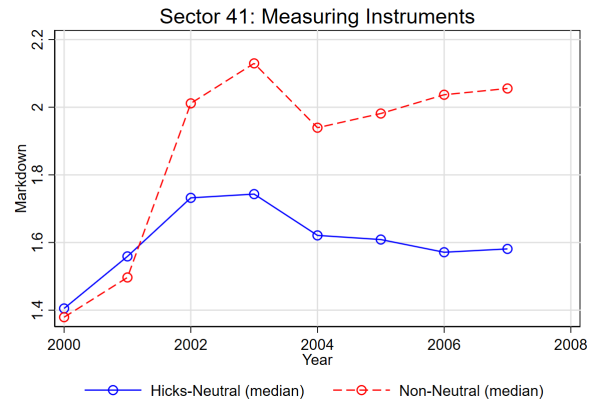
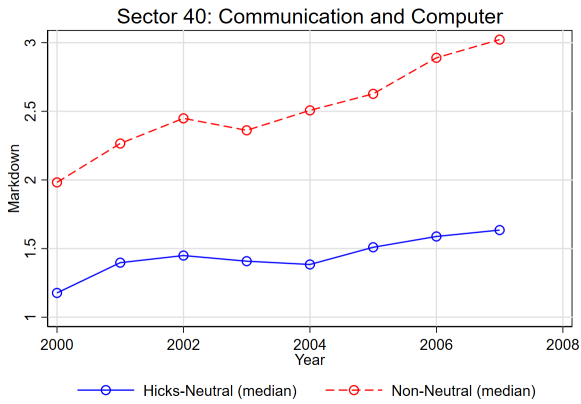
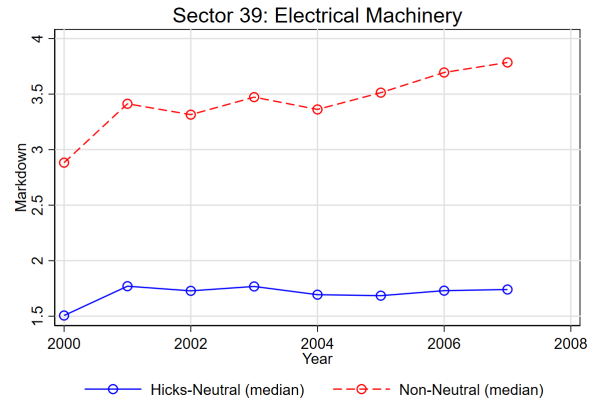
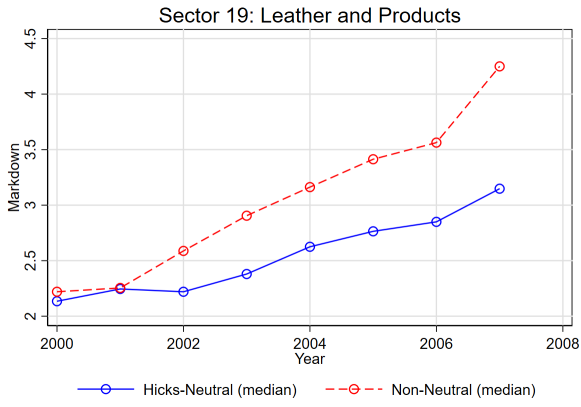
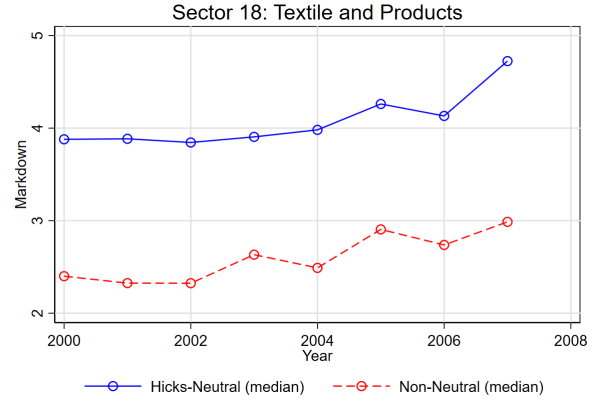
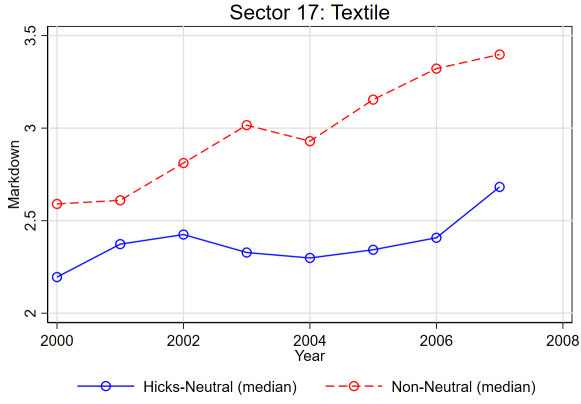


Figure 4: Median buyer power under non-neutral and Hicks-neutral technology

downward shift under Hicks-neutral assumptions suggests the Hicks-neutral technology restriction underestimated buyer power across these capital- and technology-intensive industries.

These patterns imply that estimated foreign-input buyer power is sensitive to the production-technology assumption. Non-Hicks specifications tend to deliver higher and more volatile buyer-power medians, whereas Hicks-neutral specifications often yield lower and smoother medians —though the effect is heterogeneous across sub-sectors. Because multiple channels (e.g., input substitution patterns) can produce these differences.

6 Monte Carlo Simulation

6.1 Non-Neutral Technology

We conduct a Monte Carlo experiment to evaluate the performance of our estimation method described in Section 4. The data-generating process (DGP) is based on Equation (43). Specifically, we simulate a panel dataset of 30 independent markets, each containing 50 firms observed over 10 years. Thus, the simulated dataset contains 1,500 firms and 15,000 firm-year observations in total.

The true structural parameters are set to $\alpha_0 = 7$, $\alpha_l = 0.07$, $\alpha_k = 0.02$, $\alpha_m^D = 0.9$, $\alpha_{s1} = -6$, and $\alpha_{s2} = 4$. The logarithms of labor input l_{ft} , capital input k_{ft} , and domestic intermediate input m_{ft}^D are independently drawn from normal distributions with means 10, 5, 3, respectively, and unit variance. The exponential form of domestic input cost $e^{-s_{ft}}$ is drawn from a normal distribution: $e^{-s_{ft}} \sim N(2.5, 1)$. After that, we generate the quadratic term of $e^{-s_{ft}}$. We simulate the logarithms of Hicks-neutral ω_{ft} be normally distributed: $\omega_{ft} \sim N(0, 0.5)$. The logarithms of Hicks-neutral also follows an AR(1) process with serial correlation parameter $\rho = 0.9$. Measurement error ε_{ft} is drawn from a normal distribution $N(0, 0.1)$.

6.2 Estimation

For estimation, we implement a two-step GMM procedure to estimate the vector of parameters

$$\theta = (\alpha_0, \alpha_l, \alpha_k, \alpha_m^D, \alpha_{s1}, \alpha_{s2}, \rho)$$

from the moment condition Equation (57). We use the same set of instruments contains lags of domestic and foreign input, and current capital and labor as in our empirical analysis.

We conduct $R = 200$ Monte Carlo replications and summarize the distribution of estimates by their mean, standard deviation, finite-sample bias, and root mean squared error (RMSE).

6.3 Results

Table 8 presents the Monte Carlo results for non-neutral technology productivity. We find that the non-neutral technology estimator yields precise and consistent estimates. As summarized in table 8, the parameter of α_l , α_k , α_m^D , α_{s1} , α_{s2} are estimated at their true values 0.07, 0.02 0.9, -6 , and 4, with the standard deviation of these estimates across 200 replications being very small, at 0.0011, 0.0008, 0.0015, 0.0220 and 0.0044. The estimator successfully recovers the true parameter values with high accuracy. Both bias and RMSE remain negligible across all coefficients.

To illustrate the finite-sample distribution of the estimates, Figure 5 plots their distribution. Red dashed lines indicate the true parameter values, while blue dotted lines indicate the Monte Carlo means. The distributions are tightly centered around the truth, suggesting that the estimator performs well in finite samples.

These findings demonstrate that our non-neutral technology estimator is consistent and reliable under the DGP we consider. In particular, the inclusion of lagged instruments effectively addresses endogeneity stemming from the autoregressive error component.

6.4 Cobb-Douglas Production and Hicks-neutral Technology

As a robustness check, we also conduct Monte Carlo simulations under a Cobb–Douglas production function and under Hicks-neutral technology. In both cases, we simulate panel dataset of 30 markets with 50 firms observed over 10 years, and conduct 200 replications.

For the Cobb–Douglas specification, we follow the estimation method outlined in the Appendix, with the data-generating process defined by Equation (58). The true structural parameters are set to $\beta_l = 0.01$, $\beta_k = 0.01$, $\beta_D = 0.91$ and $\beta_F = 0.07$. The logarithms of labor input l_{ft} , capital input k_{ft} , domestic intermediate input m_{ft}^D and foreign intermediate input m_{ft}^F are independently drawn from normal distributions with means 10, 5, 3, 2, respectively, and unit variance. We simulate a Hicks-neutral productivity shock ω_{ft} be normally distributed: $\omega_{ft} \sim N(0, 0.5)$. The logarithms of production function follows an AR(1) process with serial correlation parameter $\rho = 0.9$. Measurement error ε_{ft} is drawn from a normal distribution $N(0, 0.1)$. Table 9 summarizes the Monte Carlo results while Figure 5 plots their distribution.

For Hicks-neutral specification, DGP follows Equation (48). The true structural parameters are set to $\beta_l = 0.13$, $\beta_k = 0.06$, $\beta_D = 0.14$, $\beta_F = 0.12$, $\beta_{DD} = 0.04$, $\beta_{FF} = 0.03$ and $\beta_{FD} = -0.05$. The logarithms of labor input l_{ft} , capital input k_{ft} , domestic intermediate input m_{ft}^D and foreign intermediate input m_{ft}^F are independently drawn from normal distributions with means 10, 5, 3, 2, respectively, and unit variance. After that, we generate the quadratic term of domestic intermediate input m_{ft}^D and foreign intermediate input m_{ft}^F , as well as their interaction term. We simulate a Hicks-neutral productivity shock ω_{ft} be normally distributed: $\omega_{ft} \sim N(0, 0.5)$. The logarithms of production function follows an AR(1) process with serial correlation parameter $\rho = 0.9$. Measurement error ε_{ft} is drawn from a normal distribution $N(0, 0.1)$. The corresponding results are reported in Table 10 and Figure 7.

In both the Cobb–Douglas and Hicks-neutral specifications, the estimated means are close to the true values, with small standard deviations, bias, and RMSE. The distributions are tightly centered around the truth. These findings confirm that our estimation method performs well in finite samples and remains consistent and reliable under alternative production function specifications.

Table 8: Monte Carlo Simulation: Non-neutral Technology Estimates

Parameter	True	Mean Estimate	Std. Dev.	Bias	RMSE
a_l	0.07	0.0700	0.0011	0.0000	0.0011
a_k	0.02	0.0200	0.0008	-0.0000	0.0008
a_m^D	0.90	0.8999	0.0015	-0.0001	0.0015
a_{es}	-6.00	-6.0006	0.0220	-0.0006	0.0219
a_{es^2}	4.00	4.0001	0.0044	0.0001	0.0044

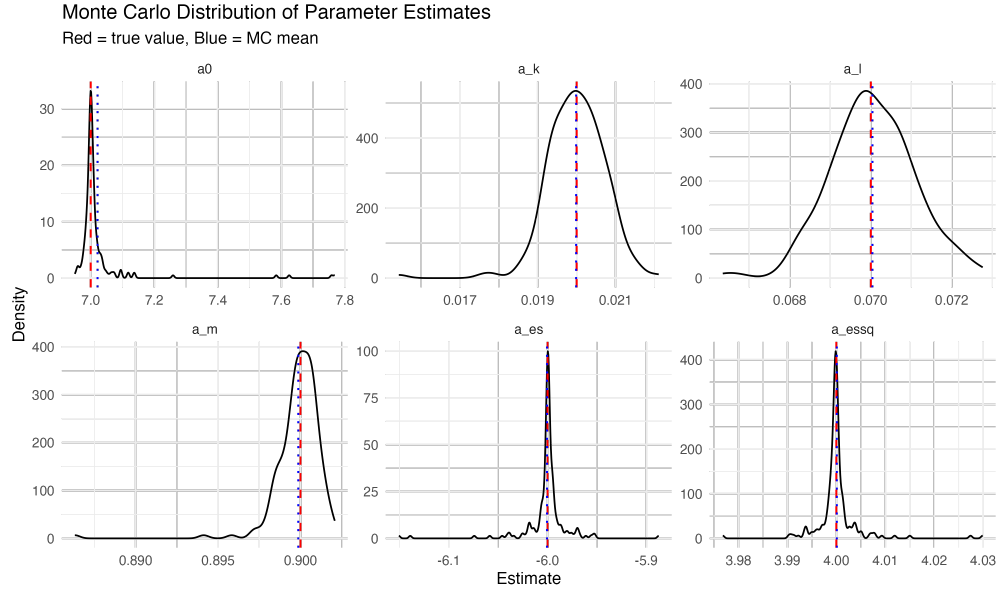


Figure 5: Monte Carlo Simulation: Non-neutral Technology Estimates

Table 9: Monte Carlo Simulation: Cobb-Douglas Production Estimates

Parameter	True	Mean Estimate	Std. Dev.	Bias	RMSE
β_l	0.01	0.010125	0.002055	0.000125	0.001843
β_k	0.01	0.010173	0.001519	0.000173	0.001369
β_D	0.91	0.910015	0.001212	0.000015	0.001084
β_F	0.07	0.069724	0.001468	-0.000276	0.001342

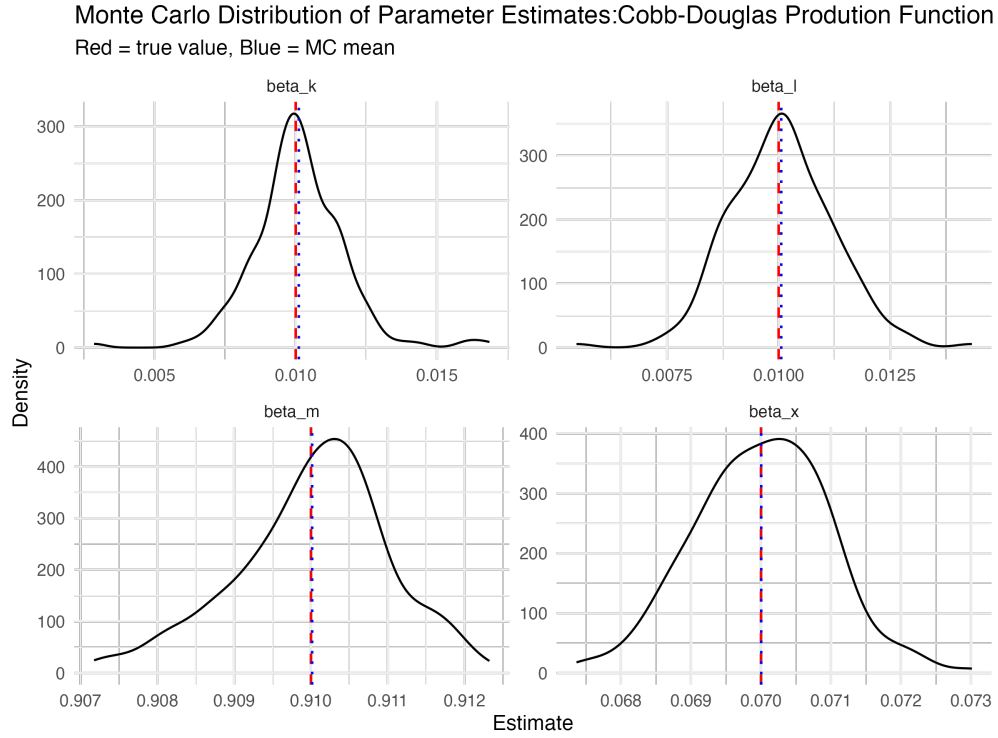


Figure 6: Monte Carlo Simulation: Cobb-Douglas Production Estimates

Table 10: Monte Carlo Simulation: Hicks-neutral Technology Estimates

Parameter	True	Mean Estimate	Std. Dev.	Bias	RMSE
β_k	0.06	0.060083	0.000669	0.000083	0.000673
β_l	0.13	0.130055	0.001256	0.000055	0.001254
β_D	0.14	0.143041	0.024295	0.003041	0.024424
β_F	0.12	0.124258	0.027972	0.004258	0.028225
β_{DD}	0.04	0.039068	0.008718	-0.000932	0.008746
β_{FF}	0.03	0.029202	0.005954	-0.000798	0.005992
β_{FD}	-0.05	-0.049758	0.004549	0.000242	0.004544

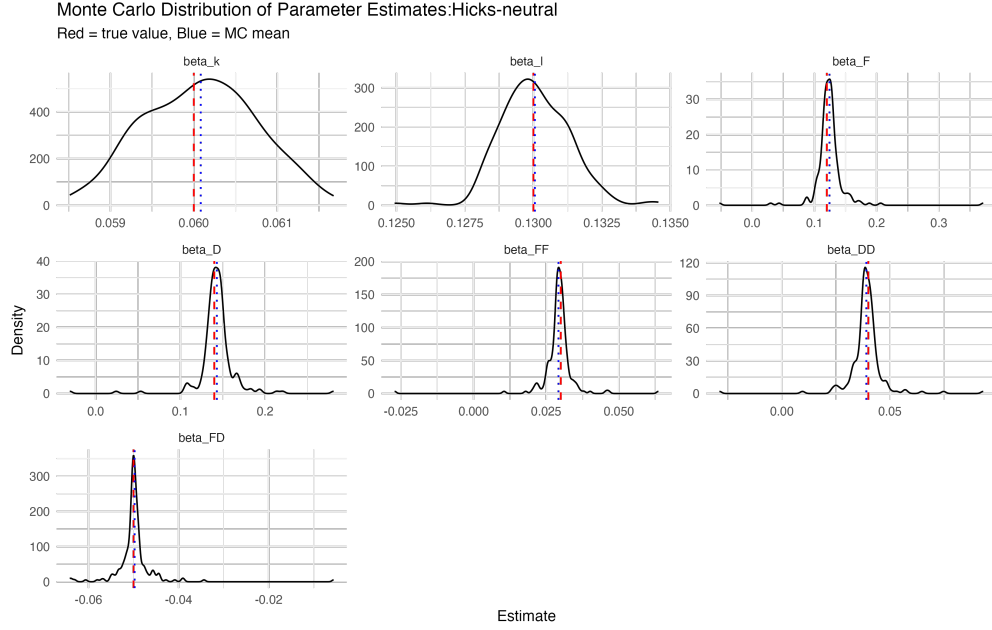


Figure 7: Monte Carlo Simulation: Hicks-neutral Technology Estimates

7 Conclusion

we begin by documenting the declining trend in selected Chinese manufacturing sectors' foreign-input cost share (CIC 17–19 and 39–41) over 2000–2007. This paper provides empirical evidence of buyer power in the foreign-input market and quantifies the buyer power of these sectors using firm-level data for 2000–2007 while allowing production technology to be foreign-input-biased rather than Hicks-neutral. By explicitly incorporating factor-biased technology, the analysis recovers firm-level foreign-input markdowns and compares them to Hicks-neutral benchmarks, showing that treating technology as Hicks-neutral when it is not leads to biased estimates of buyer power.

Specifically, we develop a framework to identify a firm's foreign input buyer power by jointly conditioning on determinants of foreign-input supply, final-good demand, and production-side technology. Under the factor-biased technology assumption, markdowns are pinned down by the equilibrium relationships among supply, demand, and production. Using this approach, we find that Revenue-weighted average markdowns rise over the sample period under both the Hicks-neutral and foreign-input-biased productivity specifications, and that the foreign-input-biased interpretation systematically affects both the level and the evolution of measured markdowns.

However, the empirical implementation controls for exporter responses rather than fully parametrizing an exporter-side supply function; consequently, foreign-input supply elasticities

ties are not structurally recovered.

These limitations suggest straightforward extensions to strengthen identification and policy relevance. Access to foreign-input supplier price and quantity data would allow joint estimation of foreign-input supply elasticities, which, combined with an explicit model of downstream bargaining, would recover supply elasticities and welfare shares and would enable credible structural counterfactuals that decompose the contributions of factor-biased technology and firm buyer power to the decline in foreign-input cost shares. Implementing decomposition exercises and counterfactual reweighting that hold firm composition fixed would clarify the mechanisms driving aggregate markdown and cost-share dynamics. Expanding sectoral, cross-country, and temporal coverage beyond the six sectors and the 2000–2007 window would test the generality of the findings and their relevance for current policy debates about global value chains and buyer power. A natural future direction is to undertake a welfare analysis of markdowns and factor-biased technology change on the economy.

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A Appendix

A.1 Cobb-Douglas Production Function

Because we do not observe firm-level output prices P_{ft} directly, we construct a proxy firm-level output deflator $\tilde{P}_{ft}$ by combining the two-digit industry output deflator P_{st} with a firm-specific deviation $\hat{P}_{ft}$. Following [Morlacco \(2019\)](#), we define the firm-level output deflator

$$\tilde{P}_{ft} = P_{st} \hat{P}_{ft}$$

If we denote each variable's logarithm by its corresponding lowercase letter, then we can get

$$\hat{p}_{ft} = \ln \tilde{P}_{ft} - \ln P_{st} = \tilde{p}_{ft} - p_{st}.$$

Here, $\hat{p}_{ft}$ represents the unobserved firm-level deviation from the industry average output price. Since $\hat{p}_{ft}$ is not directly observable, we infer it from firm-level export prices. For each destination market c , we observe

$$\hat{p}_{fct} = p_{fct} - p_{Ict},$$

where p_{fct} is the log export price of firm f in market c , and p_{Ict} is the corresponding industry-level export price to country c (industries defined at the two-digit level).

Let X_{fct} be the export value of firm f to country c and $X_{ft} = \sum_c X_{fct}$ be its total export value. Define weights

$$w_{fct} = \frac{X_{fct}}{X_{ft}},$$

i.e., the share of firm f 's export value to country c relative to its total export value. Aggregating across destinations with these weights, we obtain

$$\hat{p}_{ft} = \sum_c w_{fct} \hat{p}_{fct}.$$

Substituting back gives the firm-level output price deflator in logs,

$$\tilde{p}_{ft} = p_{st} + \hat{p}_{ft},$$

which we use to deflate revenue and thereby control for firm-level output price bias in our estimations.

We apply an analogous procedure to construct a firm-specific foreign input deflator for imported inputs. Let W_{st}^F denote the 2-digit sector input deflator for foreign intermediate inputs. First, we define firm-level foreign input deflator as:

$$\tilde{W}_{ft}^F = W_{st}^F \hat{W}_{ft}^F,$$

and if we take logs of both sides, we can get:

$$\hat{w}_{ft}^F = \ln \tilde{W}_{ft}^F - \ln W_{st}^F = \tilde{w}_{ft}^F - w_{st}^F.$$

Here, $\hat{w}_{ft}^F$ represents the firm-level deviation from the industry average imported-input price. For each destination c , let W_{fct}^F and W_{Ict}^F be firm-level and industry-level imported-input prices, respectively, and define

$$\hat{w}_{fct}^F = w_{fct}^F - w_{Ict}^F.$$

Similarly, let Y_{fct} be the import value of firm f from country c and $Y_{ft} = \sum_c Y_{fct}$ be its total import value. Define weights

$$\eta_{fct} = \frac{Y_{fct}}{Y_{ft}},$$

i.e., the share of firm f 's import value from country c relative to its total import value. Aggregating with weights η_{fct} as above, we can get

$$\hat{w}_{ft}^F = \sum_c \eta_{fct} \hat{w}_{fct}^F,$$

we construct the firm-level foreign input price deflator (in natural log)

$$\tilde{w}_{ft}^F = w_{st}^F + \hat{w}_{ft}^F.$$

To estimate the Cobb–Douglas production function under non-competitive foreign-input markets, we follow the two-step GMM procedure of [Akerberg et al. \(2015\)](#) as implemented by [Morlacco \(2019\)](#). Moreover, since we do not have firm-level price data for output and domestic input, we use price bias control approach following [De Loecker \(2011\)](#). Following [Morlacco \(2019\)](#), we use the following log-linear production function for firm f at time t :

$$q_{ft} = f(l_{ft}, k_{ft}, m_{ft}^D, m_{ft}^F; \beta) + \omega_{ft} + \varepsilon_{ft}, \quad (58)$$

where lower-case denotes natural logs, ω_{ft} is a Hicks-neutral productivity shock, and ε_{ft}

denotes measurement error. The parameter vector β is constant within each two-digit manufacturing sector over our sample. Lowercase letters (e.g., l, k, m, w) denote input quantities or prices in natural logarithms; for example, l_{ft} is the natural logarithm of firm f 's total employment in year t and w_{ft}^l is the natural logarithm of firm f 's wage in year t . We treat capital and labor as dynamic inputs subject to adjustment frictions.

We first do the input-demand inversion. From the first-order conditions, foreign and domestic intermediate input quantities satisfy

$$M_{ft}^F = \delta(W_{ft}, V_{ft}/M_{ft}^F, K_{ft}, P_{ft}, e^{\omega_{ft}}), \quad (59)$$

$$M_{ft}^D = \mu(W_{ft}, V_{ft}/M_{ft}^D, K_{ft}, P_{ft}, e^{\omega_{ft}}). \quad (60)$$

Here W_{ft} is the vector of input prices, V_{ft} the vector of input quantities, P_{ft} the output price, and $e^{\omega_{ft}}$ productivity. Monotonicity in prices allows us to invert (45):

$$W_{ft}^D = \mu^{-1}(W_{ft}/W_{ft}^D, V_{ft}, K_{ft}, P_{ft}, e^{\omega_{ft}}). \quad (61)$$

Substituting this into (44) yields

$$M_{ft}^F = \tilde{\delta}(W_{ft}/W_{ft}^D, V_{ft}/M_{ft}^F, K_{ft}, P_{ft}, e^{\omega_{ft}}), \quad (62)$$

which in turn can be inverted for productivity:

$$e^{\omega_{ft}} = \tilde{\delta}^{-1}(V_{ft}, K_{ft}, W_{ft}/W_{ft}^D, P_{ft}). \quad (63)$$

Although P_{ft} is unobserved, we proxy it with firm-level output deflators $\tilde{P}_{ft}$.

In particular, we outline the procedure of estimating Cobb–Douglas production function. Combining these steps, the Cobb–Douglas specification becomes

$$q_{ft} = \beta_l l_{ft} + \beta_k k_{ft} + \beta_D \bar{m}_{ft}^D + \beta_F m_{ft}^F + \tilde{\delta}^{-1}(l_{ft}, k_{ft}, \bar{m}_{ft}^D, m_{ft}^F, w_{ft}^F, w_{ft}^l, p_{ft}) + u_{ft}, \quad (64)$$

where $u_{ft} = \varepsilon_{ft} + \beta_D(w_{st}^D - w_{ft}^D)$.

We use two-stage approach to estimate Cobb–Douglas production function. At first stage, we estimate

$$q_{ft} = \phi(l_{ft}, k_{ft}, m_{ft}^F, m_{ft}^D, w_{ft}^F, w_{ft}^l, p_{ft}) + \varepsilon_{ft},$$

via OLS with $\phi(\cdot)$ as a third-order polynomial, yielding $\hat{q}_{ft}$. At Second stage, we introduce

⁵ $\bar{m}_{ft}^D$ is the natural logarithm of the deflated domestic quantity, where the deflator is the two-digit sector-specific input deflator.

a law of motion for productivity:

$$\omega_{ft} = \rho(\omega_{ft-1}) + \xi_{ft}, \quad \rho(\cdot) \text{ is a first-order polynomial,} \quad (65)$$

⁶ and we can get

$$\omega_{ft}(\beta) = \hat{q}_{ft} - (\beta_l l_{ft} + \beta_k k_{ft} + \beta_D \bar{m}_{ft}^D + \beta_F m_{ft}^F) \quad (66)$$

Then we can get

$$\xi_{ft}(\beta) = \omega_{ft}(\beta) - \rho(\omega_{ft-1}(\beta))$$

Then the innovation ξ_{ft} depends only on observables and β , and we estimate β from the following moment condition:

$$\mathbb{E}[\xi_{ft}(\beta) Z_{ft}] = 0, \quad (67)$$

where Z_{ft} contains lags of domestic and foreign input, and current capital and labor. We therefore report sector-level estimates of β and use the double-ratio approach to estimate firm-level foreign intermediate input markdown under the Cobb-Douglas specification:

$$\psi_{ft}^F = \frac{\theta_{fg}^F \gamma_{ft}^D}{\gamma_{fg}^F \theta_{ft}^D}$$

where γ_{ft}^F denotes the cost of foreign input bundle F as a share of gross revenues of firm f in year t , such that $\gamma_{ft}^F = \frac{W_{ft}^F M_{ft}^F}{P_{ft} Q_{ft}}$. θ_f^F denotes the output elasticity of foreign input bundles. Since we already estimated the output elasticity (β vector), then the firm-level markdown under Cobb-Douglas production function can be expressed as

$$\psi_{ft}^{FCD} = \frac{\beta_F \gamma_{ft}^D}{\gamma_f^F \beta_D}$$

The estimated output elasticity under Cobb-Douglas and resulting sector-level foreign input markdown are reported in table 11 and table 12.

⁶Results are robust if we assume $\rho(\cdot)$ is a second-order polynomial in all its arguments.

Table 11: Non-Neutral Production Function Estimates

(1) Code	(2) Industry	(3) β_l	(4) β_k	(5) β_D	(6) β_F	(7) N
17	Textile	0.0020 (0.0159)	-0.0025 (0.0106)	0.8418 (0.0235)	0.1260 (0.0093)	5574
18	Textile and Products	-0.0100 (0.0174)	0.0278 (0.0092)	0.8484 (0.0208)	0.1699 (0.0098)	6865
19	Leather and Products	0.0329 (0.0223)	0.0203 (0.0134)	0.8635 (0.0296)	0.0707 (0.0112)	3880
39	Electrical Machinery	0.0444 (0.0195)	0.0051 (0.0128)	0.9968 (0.0233)	0.0256 (0.0071)	5989
40	Communication and Computer	0.0254 (0.0149)	0.0327 (0.0085)	0.9294 (0.0149)	0.0350 (0.0053)	9887
41	Measuring Instruments	0.0244 (0.0277)	-0.0186 (0.0188)	1.0078 (0.0261)	0.0210 (0.0108)	2278

Note: Standard errors are shown in parentheses on the line below each estimate; they were calculated from bootstrap replications.

Table 12: Sector-Level Buyer Power, Cobb-Douglas, by CIC-2 Sector

(1) Code	(2) Industry	(3) N	(4) Mean	(5) Median	(6) SD
17	Textile	10690	1.61	0.57	2.27
18	Textile and Products	13593	1.67	0.47	2.60
19	Leather and Products	6980	1.14	0.32	1.94
39	Electrical Machinery	10893	0.55	0.18	0.85
40	Communication and Computer	17109	0.58	0.15	1.13
41	Measuring Instruments	4148	0.86	0.21	1.52
Total		63413	1.06	0.37	1.90

Notes: Col. (3) gives the number of observations (N); Cols. (4)–(6) report mean, median, and standard deviation (SD) of firm-level buyer power under Cobb-Douglas production.

A.2 Variable Definitions

Unless otherwise specified, all variables are measured at the plant–year level in the merged production–customs dataset. Output is proxied by nominal value of industrial output of each firm. Total intermediate expenditures capture total intermediate inputs for production, while domestic intermediate inputs are defined as total intermediate expenditures minus the value of imported intermediates. Imported intermediates are constructed from customs

records as the sum of shipments not classified as “final consumption” or “capital goods” under the Broad Economic Classification (BEC); our findings remain robust when foreign intermediates are alternatively defined using only those BEC-coded as intermediate goods⁷. Labor input is measured by full-time-equivalent employment, and the implied average wage is computed by dividing total salary costs by total employment. Capital stock is proxied by the gross book value of fixed assets, including both movable and immovable assets. Following [Morlacco \(2019\)](#), we infer a date of purchase from the installment quota given a proxy lifetime duration of equipment (20 years) to obtain the current value of capital stock. We deflate the initial nominal capital stock with the investment deflator from [Perkins and Rawski \(2008\)](#). This deflator is a chain-linked price deflator based on separate price indices for equipment, machinery, and building structures.⁸ We construct this alternative series via $K_t = (1 - \delta_s) K_{t-1} + I_t$, where I take the book value of capital in the firm’s first year of activity as the initial level, and set the depreciation rate δ_s (which may vary by sector s). All nominal variables (domestic inputs, foreign inputs, and nominal output), except nominal capital, are deflated using four-digit industry price deflators⁹ from [Brandt et al. \(2012\)](#): output deflators rely on “reference price” series from the China Statistical Yearbooks, and input deflators are derived by combining these output deflators with the 2002 national input–output table. We derive two-digit industry price deflators as a weighted average of the corresponding four-digit industry deflators, where the weights are given by each four-digit industry’s output share within the corresponding two-digit industry. Firm age: the difference between the data year and the year in which the firm started up.

A.3 Dynamics of Import Value

During the sample period 2000–2007 we observe a general upward trend in total imported intermediates across Chinese manufacturing sectors.

⁷To isolate intermediate inputs, we then apply the United Nations’ Broad Economic Categories (BEC) Revision 4 specification—also defined on the 1996 HS6 basis—thereby yielding a consistent and reproducible set of intermediate-goods codes for our analysis. Results are robust if use this narrow definition of intermediate goods

⁸Results are robust to using an alternative measure of capital, which we construct using a perpetual-inventory method.

⁹The four-digit output and input deflator values are aggregated to the two-digit sector level.

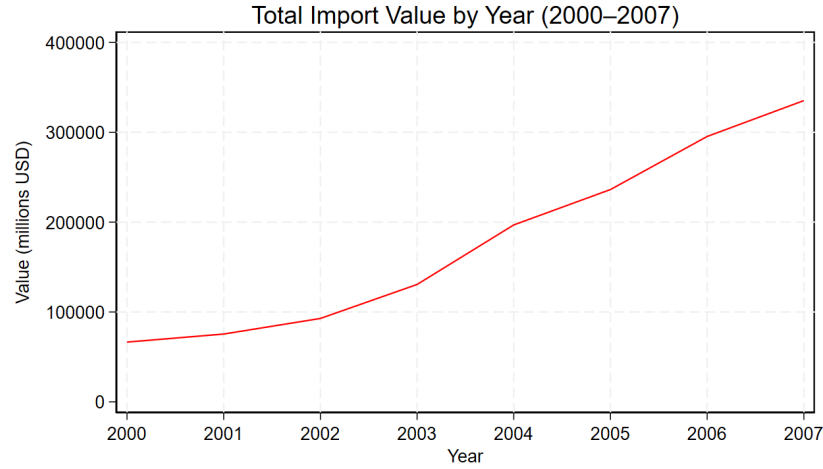


Figure 8: Total value of foreign inputs

Specifically, figure 8 plots total import value of Chinese intermediate inputs aggregated across CIC 2-digit sectors 13–42 for 2000–2007 and shows a clear upward trend: imports rise modestly from roughly 65,000 million USD in 2000 to about 90,000 million USD by 2002, then increase sharply after 2003 to approximately 340,000 million USD by 2007, indicating sustained and accelerating growth in imported intermediates over the period.