CHAZEN INSTITUTE RESEARCH BRIEF

The Startup Pay Premium

KEY TAKEAWAYS

- ✓ Young firms, on average, pay about 25 percent less than older, more established firms.
- ✓ Low-paid workers at young firms tend to be low-paid even when employed elsewhere, and most young firms never end up paying really well.
- ✓ Higher wages at startups compensate workers for higher risk, resulting in a hidden pay premium.
- ✓ The future survival probability and growth rate of a startup can be predicted by the characteristics of its initial workforce.

Startups are known for having low-paying jobs. They are also known for offering employees attractive non-monetary perks, such as flexible office hours and stock options, to compensate for their inability to offer higher wages. But new research suggests that who gets hired and how much they get paid at the outset of a new company really matters.

In "Pay, Employment, and Dynamics of Young Firms," **Christian Moser**, **Chazen Senior Scholar at Columbia Business School**, and co-authors Tania Babina of Columbia Business School, Wenting Ma of the University of Massachusetts, Paige Ouimet of the University of North Carolina, and Rebecca Zarutskie of the Federal Reserve Board of Governors examined pay differences between workers at newly established firms and older companies – and found that those companies that invest early in higher wages ultimately have better survival and growth prospects.

Research

Using data from the U.S. Census Bureau that span nearly two decades, the researchers were able to track millions of workers' earnings across employers. Controlling for firm age and size, and other differences in organizational characteristics, they identified a positive pay premium among young startups.

The study overturns conventional wisdom about startup behavior, often characterized by flexible working environments but lower pay, and offers a new understanding of the relationship between young firms' pay levels and long-term outcomes.

23% MORE

Average pay of workers whose startups survive 10 or more years*

25% LESS

Average earnings of workers at startups*

*compared to the overall worker pool

Results

According to the research, jobs at young firms pay considerably less than those at older, more established firms. Indeed, the data reveal that workers at startups, on average, earn about 25 percent less. The bulk of those lower wages are due to young firms' hiring of lower-ability workers and a greater likelihood the firm will fold. Interestingly, the researchers found that workers commonly employed by young, lower-paying firms tend to occupy lower-paid positions, even when employed elsewhere.

However, the research also shows that companies that manage to attract more capable workers at the time of founding are more likely to succeed in the future. In addition, higher pay at firm birth correlates with the ability level of the workers hired. For example, newly established companies that survive for 10 or more years are shown to have started with workers who are, on average, paid 23 percent more compared to the overall worker pool. This pay premium may reflect the fact that young firms need to compensate for a less-stable employment environment.

The researchers conclude that the human capital of young firms significantly relates to firm survival rates and future employment growth.

Download the full paper.

Read about the scholar.

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