

Abstract: We analyze equilibrium wage contracts in a competitive search model where a firm motivates workers to invest in a match-specific skill. If skill is not critical for production, the contract is first best. If critical, the contract coincides with an efficiency wage contract and cannot attain even second best. Unlike standard efficiency wage models, the wage plays a dual role, advertisement and motivation, which induces a novel source of inefficiency: the competition to attract workers forces a wage to be chosen that increases the ex ante utility of workers at the expense of ex post utility.