

Abstract

We develop a continuous-time model of career concerns that incorporates human capital accumulation throughout the working life. Workers are able to generate an output that follows a diffusion process with a drift that is the sum of effort and ability ("talent"). Talent corresponds to a hidden process that is partially endogenous as a consequence of on-the-job skills accumulation. We find that learning about ability through output observations creates a wedge between the rate at which talent keeps track of past productivity shocks and the corresponding rate at which talent estimates discount past performance. This generates inefficient provision of incentives in standard models of career concerns (exogenous talent) that is robust to the entire class of Gaussian processes in the diffusion-form. Nevertheless, it is precisely this wedge which makes human capital accumulation a channel for extracting additional informational rents from belief-distortions. Hence, effort levels are above the ones predicted by previous career concerns models, yet inefficiencies are far from being eliminated.