Driving the Drivers: Algorithmic Wage-Setting in Ride-Hailing*

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Abstract

Companies are increasingly using algorithms to manage their workers. Such algorithms often differentiate wages for workers based on their work schedules, thus restricting the work flexibility of gig workers and forcing them to undertake extended working hours. Using rich transaction data from a ride-hailing company in Asia, we document algorithmic wage-setting and study its impact on worker behavior. The algorithm profiles drivers based on their work schedules and favors drivers who work longer hours for the platform. Our data shows that drivers favored by the algorithm earn 8% more hourly than non-favored drivers. To quantify the welfare effects of such preferential algorithms, we construct and estimate a two-sided market model with time-varying demand and dynamic labor supply decisions. Our counterfactual shows that removing the preferential algorithm leads to a 7.79% increase in ride fares, hurting both consumers and the platform. On the other hand, an additional 10% of drivers would switch to flexible schedules, reducing their total work hours. We see a 3.51% surplus gain for drivers who keep flexible schedules. Among drivers, those who are young, male, and local benefit more.

Keywords: Two-Sided Market, Fair Pay, Work Schedule, Cross-Time Elasticity, Labor Supply, Market Power, Compensation Structure

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1 Introduction

Recent years have witnessed the rapid acceleration of algorithmic technologies. A prominent example is the ride-hailing market. A ride-hailing platform provides riders with an economical mode of transportation and allows drivers to create their own work schedules to best fit the job into their lives. However, the platform does not treat work schedules equally: some yield more revenue. The platform may find it profitable to "profile" its drivers based on their work schedules, and may reward "high-performing" drivers who work long hours for the benefit of the platform. In particular, algorithms grant preferential order assignment to drivers based on their profiles, thereby influencing their hourly earnings. We refer to this as *algorithmic wage-setting.* These algorithms frequently limit the work flexibility of gig workers, compelling them to take on longer working hours.[1]

This is an important issue and is not unique to ride hailing. Similar considerations arise in other industries. For example, Uber Eats' algorithm gives preference to full-time over part-time workers when assigning orders. Similarly, DoorDash's algorithm discourages workers from strategically choosing orders. If a worker declines a long-distance delivery, they may stop receiving further delivery requests. Meanwhile, Instacart exercises significant control over the labor process, thereby restricting workers' autonomy over their time and the work they can undertake.[2] Every platform referenced here employs a specific assignment algorithm to influence labor supply decisions. While existing research primarily focuses on the pricing aspects of algorithms, we focus on its order of assignment aspects. What is the efficiency of such assignment algorithms? What are the distributional consequences? Is there room for improvement? In this paper, we use rich transaction data from one leading ride-hailing company to study these questions. We aim to provide the first empirical study of algorithmic wage-setting and its impact on worker behavior and welfare.

First, we show that ride-hailing companies exercise algorithmic wage-setting, limiting driver utilization of schedule flexibility. In principle, a driver is free to choose whether or not to work for each hour of the day. However, a driver's hourly earnings depend not only on the specific hours during which they work, but also by their working hours in other parts of the day. For instance, at 7 AM, a driver who has also worked between 4 and 6 AM might have higher hourly earnings than a driver who only works at 7 AM, because the algorithm may prioritize the former driver in the order of assignments at 7 AM. To

[1] The documentary *The Gig Is Up* (2021) reveals how gig work promised freedom for workers but delivered lower wages and poor working conditions.

[2] News reports for Uber Eats: How Uber got almost everything it wanted in Ontario's Working For Workers Act; DoorDash: Apps like Uber and DoorDash use AI to determine pay. Workers say this makes it impossible to predict wages. Instacart: At The Mercy Of An App: Workers Feel The Instacart Squeeze.

understand why the platform's algorithm may prefer certain work schedules, we highlight one important channel the literature has overlooked: *cross-time* labor supply elasticity. Most platforms apply surge pricing to balance demand and supply, which leverages *real-time* labor supply elasticity by increasing fares when demand exceeds supply. However, steeper fares discourage demand and reduce transactions if demand is overly elastic. In contrast, we focus on preferential assignment algorithms that adjusts the labor supply in one time period by offering incentives in a different period, leveraging *cross-time* labor supply elasticity. In particular, such algorithms exploit the fact that drivers care about the total value of all hourly working decisions. Unlike the *real-time* rewarding of surge pricing, preferential algorithms may reward preferred drivers at any hour by prioritizing their trip assignments. Thus, even in hours when outside options are more attractive, some drivers may still prefer to work because they are rewarded at other hours. We provide a theoretical model in Section 2 to sharpen the intuition of when the adoption of a preferential algorithm is beneficial for the platform.

Second, we document significant wage differentials across workers due to work schedules. Using rich transaction data from one leading ride-hailing company in Asia, we show that three main factors drive the wage differential: high-performing drivers are given more ride requests per hour, wait fewer minutes for each request, and receive more requests from riders with lower cancellation rates. Here, labeling drivers as high- or low-performing is not a reflection of their efficiency or quality of work. It merely indicates that they have more or less committed work schedules and log more or fewer total hours on the platform. Due to the algorithmic wage-setting, drivers experience different hourly earnings, even if they are equally efficient and deliver the same quality of work. We also examine several alternative explanations documented in the literature about US ride-hailing markets (see, e.g., Cook, Diamond, Hall, List and Oyer, 2021). We rule out alternative explanations, such as drivers strategically choosing where to work, strategically accepting or canceling orders, driving faster, and having better knowledge of routes. Moreover, we show the robustness of our finding to endogeneity concerns by employing instrumental variables: the rate of change in precipitation and the air quality index in drivers' hometown cities. The large wage differential we identify is mainly due to algorithmic wage-setting, which penalizes low-performing drivers.

Third, to measure the impact of these preferential algorithms on consumer and driver welfare, and to determine who gains and who loses from such a system, we construct and estimate a two-sided market model with time-varying demand and dynamic labor supply decisions. We propose a dynamic equilibrium model of a ride-hailing market similar to Frechette, Lizzeri and Salz (2019), further incorporating the decisions of the platform in the two-sided market. The platform assigns orders and thus determines the hourly wage rate for drivers based on their overall work schedules. Our model accounts for riders' downward-sloping demand, drivers' dynamic labor supply with heterogeneous outside options, and the platform's fare and wage settings. Two market power sources drive the platform's pricing decisions: the driver faces alternative time-varying outside options, and the rider has alternative modes of transportation. Drivers choose first work schedule types and then hourly work schedules by solving finite-horizon dynamic discrete choice problems. While drivers can set their own work schedules, the platform rewards high-performing drivers by assigning them more frequent and rewarding trips, leading to wage differentials between work schedules.

Our labor supply model with unobserved heterogeneity is point-identified using conditional choice probabilities in drivers' dynamic labor supply. Regarding estimation, we first estimate rider demand for service time for each hour of the day. We consider each hour a different market and aggregate our data to the day-hour level. We use the number of cars in competing ride-hailing companies on the given day as our supply-side instrumental variable. Then, we calculate the conditional choice probabilities of working for each hour of the day, based on drivers' observed work schedules. Together with the observed wage sequences, we then estimate the parameters in the labor supply model. Combining the estimated labor supply model and the rider demand model, we show how the platform leverages cross-time labor supply elasticity using the preferential algorithm. When ride fares are held unchanged, eliminating the preferential algorithm will decrease labor supply, resulting in driver shortages for most hours. Our results show that the relation between wage differentials and labor shortages is not one-to-one. Instead, the platform smooths out the payment of high incentive wages by leveraging the variations in demand elasticity and the differing reservation values of drivers over time.

Next, we calculate the changes in consumer and driver welfare when one eliminates the preferential algorithm. Results show that eliminating the preferential algorithm will result in losses for both the platform and the riders. On the other hand, drivers will enjoy more flexibility in choosing a work schedule under "fair" pay. In aggregate, platform revenues will decrease by 12.16% and total surplus will decrease by 7.16% if we hold ride fares unchanged when we eliminate the preferential algorithm. The proportion of high-performing drivers will decrease by 11.48% as more drivers switch to being lower performing. For the switchers, the driver surplus will increase by 3.51%. If we allow the platform to re-optimize ride fares after eliminating the preferential algorithm, it will raise rider fares to re-balance demand and supply. As a result, ride fares will increase by 7.79%. We also look at how eliminating the preferential algorithm affects different driver demographics. We find that female and older drivers who choose to be high performing are more likely to suffer from this policy change. The effect for female drivers in general is ambiguous, because women are also more likely to prefer more flexible work schedules, and thus receive a larger welfare gain from eliminating the preferential algorithm. Individuals who are not local residents face limitations in purchasing homes and accessing schools, and they tend to work long hours for the platform even without a preferential algorithm. They suffer a welfare loss if we eliminate the preferential algorithm. Lastly, we investigate what factors determine the effectiveness of the preferential algorithm. We conduct counterfactuals by alternating key structural parameters and find that the platform benefits more from implementing a preferential algorithm when rider demand is more elastic or when warm-up cost is greater. Meanwhile, the loss of driver surplus with a preferential algorithm is smaller in the same conditions.

Related Literature

Our paper is one of the first to study how algorithms affect market outcomes. Asker, Fershtman and Pakes (2022) study how the design of artificial intelligences'(AIs) learning protocols can lead to competitive or supracompetitive price outcomes when competing in a simple Bertrand pricing game, and Asker, Fershtman and Pakes (2023) compare the prices generated by AIs that use different learning protocols. Calvano, Calzolari, Denicolò and Pastorello (2020) numerically simulate how algorithmic pricing leads to collusive strategies in an oligopoly model of repeated price competition. Assad, Clark, Ershov and Xu (2023) show that AI adoption has a significant effect on competition by studying Germany's retail gasoline market. Using rich transaction data from one of the leading ride-hailing companies in Asia, we provide the first empirical study of algorithmic wage-setting and its impact on worker behavior and welfare.

Our model builds on the literature on two-sided markets, focusing on how the platform sets prices for both sides. See Rysman (2009) for a comprehensive survey. We take this view to the ride-hailing market, allowing for two sources of market power: driver and rider outside options. While Rysman (2004) proposes a general setting with oligopolistic competition between platforms, we focus on one leading platform in Asia. This simplification approximates the industry structure well and allows us to incorporate important dynamics in drivers' labor supply. In estimating rider preferences, we employ an IV approach, similar to Kalouptsidi (2014), to deal with unobserved factors that may affect demand and rider fare schedules. In estimating drivers' preferences, we propose a GMM estimator that integrates the CCP estimator of Hotz and Miller (1993). We also account for unobserved driver heterogeneity in estimating the structural parameters in their dynamic discrete choices.

Our results add to the labor literature on compensation and incentives in the workplace. Economists have understood the importance of incentives for decades and made good progress in specifying how compensation and its form influence worker effort—see Lazear (2018) for an excellent summary. However, little is known about the compensation and incentives provided by new algorithmic technologies. Our paper provides the first empirical study of how algorithmic wage-setting manipulates pay structures and alters worker behavior. Such analysis is especially important in the context of a rise in the incidence of alternative work arrangements (Katz and Krueger, 2019). Our results also add to the discussion of wage differentials, a subject of which there has been extensive documentation based on demographics such as gender and race. Altonji and Blank (1999) provide a great overview of this literature, while Blau and Kahn (2017) survey the literature on the gender pay gap. Another small body of literature studies part-time and full-time wage differentials. For example, Aaronson and French (2004) study the joint determination of hours and wages, exploiting the variation in labor hours induced by social security rules. Our paper is one of the first to document wage differentials due to algorithmic wage-setting.

Some earlier papers have used taxi data to investigate individual labor-supply decisions. Farber (2008) and Crawford and Meng (2011) estimate a structural model of a taxi driver's stopping decision, allowing for reference-dependent preferences. However, they do not analyze the industry equilibrium. Instead, similar to Chen, Ding, List and Mogstad (2020), Frechette, Lizzeri and Salz (2019), and Buchholz (2022), our model studies the overall equilibrium of the ride-hailing market. We focus on understanding the effects of the platform and its preferential algorithms. To do this, we estimate a dynamic labor supply model with driver preferences about work schedules.

There is also a growing literature on the ride-hailing market. This literature documents that workers value alternative work arrangements (Mas and Pallais, 2017). Chen, Rossi, Chevalier and Oehlsen (2019) show that work schedule flexibility increases driver utility. Moreover, geolocation-based matching of drivers and riders creates substantial efficiency gains (Liu, Wan and Yang, 2019). Several papers specifically study surge pricing. For example, Castillo (2020) studies Uber's surge pricing using an empirical model of the two-sided market with riders, drivers, and the platform. Ming, Tunca, Xu and Zhu (2019) also demonstrate that surge pricing improves rider and driver welfare as well as platform revenues. Instead of surge pricing, our paper highlights another important channel: the platform's balancing of demand and supply through the *cross-time* labor supply elasticity by the implementation of preferential algorithms.

The remainder of this paper is organized as follows. In Section 2, we delve into the details of the preferential algorithm and introduce a theoretical model to explain why the platform has incentives to implement such an algorithm. Section 3 describes our data. Section 4 provides reduced-form evidence of algorithmic wage-setting that favors high-performing drivers. Section 5 describes an equilibrium model with a dynamic model of drivers' labor supply. Section 6 discusses our identification argument and estimation results, and Section 7 discusses our counterfactual experiments. Finally, Section 8 concludes. The Appendix contains all omitted details.

2 Preferential Algorithm

Worldwide, online platforms have been accused of implementing preferential algorithms to restrict the work flexibility of gig workers. Our paper aims to understand why platforms employ such algorithms, as well as the resulting wage differential and its implications for consumer surplus, driver surplus, and platform profit. Specifically, we study one of the leading ride-hailing platforms in Asia, which we refer to as "Platform X" to maintain confidentiality.[3] Platform X's algorithm grants preferential order assignment to drivers based on their total working time, particularly during incentivized hours. Below, we elaborate in detail on how Platform X's preferential algorithm works.

2.1 Preferential Algorithm in Ride-Hailing

Platform X typically distributes requests to drivers within three kilometers. Within this designated radius, Platform X gives priority to particular drivers based on their order assignment scores. Drivers earn points based on the time they spend and the duration for which they work for the platform. In the city we are investigating (as of 2018), Platform X's fare schedules segment a workday into six intervals: (1) morning, 7:00–10:00; (2) midday, 10:00–16:00; (3) afternoon, 16:00–19:00; (4) evening, 19:00–22:00; (5) night, 22:00–00:00; and (6) early morning, 00:00–6:59 (next day). The points earned per hour for drivers vary depending on the specific time intervals. Certain intervals are designated as incentivized hours, during which drivers receive higher points for their work. In the app, drivers have access to the point-earning formula, which provides them with precise information about the number of points they will earn at different times of the day. On average, drivers earn 0.3 points for each order they fulfill. The total score of a driver is computed by summing up all the points they have earned during the previous thirty days.

[3] The leading ride-hailing platforms in Asia include Uber, Lyft, Didi, Grab, Gojek, and Ola, among others. With the development of Asia's residential travel demands, the number of ride-hailing users in Asia grew to 800 million by the end of 2020. Platform X has millions of ride-hailing drivers and serves over one hundred million people globally, having collected an annual revenue of over $10 billion USD in 2020. Platform X offers several tiers of operations: express, premium, and luxury. Our study focuses on its express service. Like UberX in the US, express accounts for most of the service provided on Platform X in Asia.

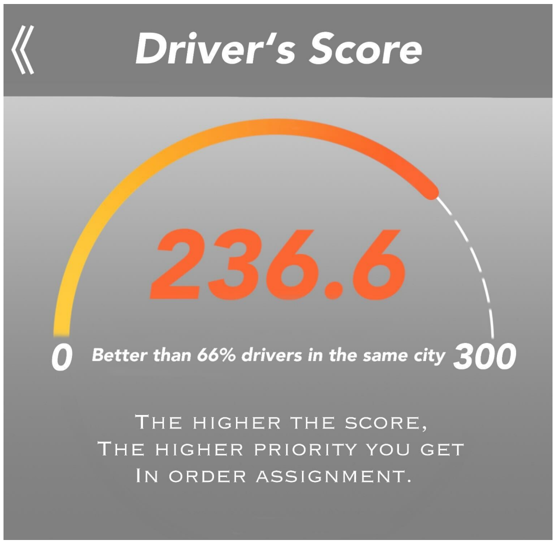


Figure 1: Information Displayed to Drivers

Figure 1 presents the information visible to the drivers.[4] The driver is presented with their current score, which in this case is 236.6. Next, there is a line indicating the percentile of their score, stating that the score is "better than 66% of drivers in the same city." At the bottom of the screen, there is a line that explains the usage of the score to the drivers, stating that "the higher the score, the higher priority you will have in order assignment." To summarize, drivers are provided with the formula for earning points, possess full knowledge of their current score, and also understand that the score directly impacts the priority of order assignment.

Regarding fare schedules, all drivers face the same fare schedules on Platform X. Thus, hourly wage differentials across drivers mainly come from systematic differences in order assignment. Riders pay a 10 CCY base fare, 0.38 CCY per minute, and 1.9 CCY per mile for each Platform X Express trip. During the morning hours (7:00–10:00), the per-mile rate increases to 2.5 CCY, while during the afternoon (16:00–19:00), night (22:00–0:00), and early morning (0:00–7:00) hours, the per-mile rate is 2.4 CCY. Drivers receive 79.1% of the rider fare.[5]

2.2 Why Implement a Preferential Algorithm?

We will now elaborate on why the platform is motivated to introduce a preferential algorithm. First, if the platform can apply first-degree price discrimination to both consumers and

[4]For confidentiality reasons, we exclude all specific firm information. Instead, we present a generic illustration that precisely replicates the information displayed to drivers on the platform.

[5]This information comes from Platform X's annual report.

drivers, it can maximize its profits to the fullest extent. In such a scenario, the platform captures the entire surplus from both consumers and drivers, and introducing a preferential algorithm will not increase the platform's profit. The preferential algorithm is effective only in situations where the platform cannot achieve perfect price discrimination among drivers. In reality, the platform may be able to extract consumer surplus through mechanisms like surge pricing. However, extracting the entire surplus from drivers is challenging due to factors such as labor laws and the design of the wage scheme. For instance, countries like France have regulations requiring a minimum payment for drivers per ride, resulting in a surplus for drivers.

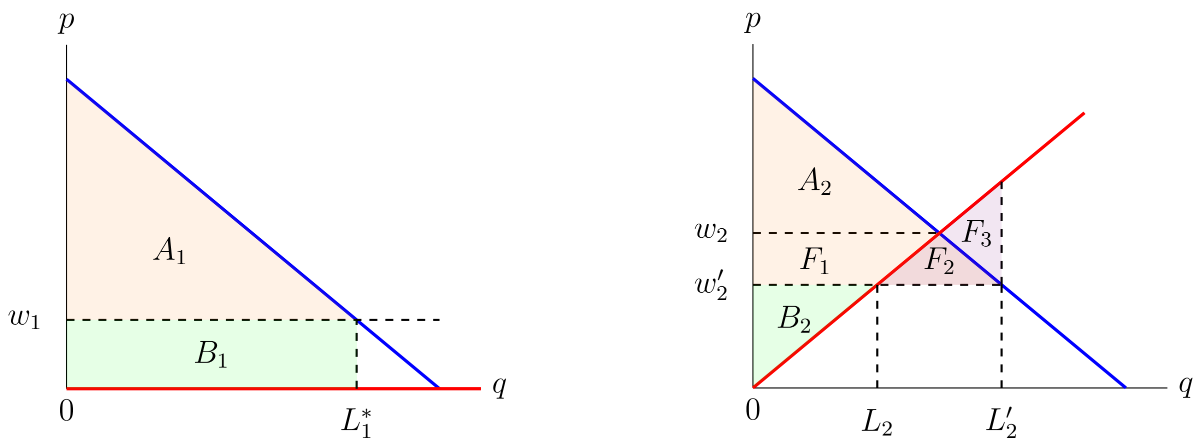


Figure 2: Cross-Time Labor Supply Elasticity

Notes: The red lines represent the labor supply curve in each time period, while the blue lines represent the demand curve. The light green area displays the surplus of drivers, whereas the light yellow area displays the surplus of the platform during each time period.

Figure 2 presents a scenario in which the implementation of a preferential algorithm is profitable for the platform. Panels (a) and (b) represent two distinct time periods, t_1 and t_2. In both periods, the platform captures the entire consumer surplus by employing surge pricing, while providing drivers with a constant wage throughout each time period. The red lines represent the labor supply curve in each time period, while the blue lines represent the demand curve. Assuming, without loss of generality, that the alternative outside option for drivers has a value of zero at t_1. At time period t_1, the platform compensates drivers with a wage rate of w_1, leading to a surplus of B_1 for the drivers. The platform is unable to further decrease the wage rate at t_1 because of the minimum wage requirement. At t_1, there is an abundance of drivers willing to work at the wage rate w_1. However, in equilibrium, only L_1^*

drivers are able to receive orders and earn a surplus. The platform has the authority to select which drivers among the available pool will receive these orders. This ability to choose drivers necessitates the implementation of a preferential algorithm, which the platform utilizes to extract additional surplus from the drivers.

Without a preferential algorithm, the equilibrium wage rate at t_2 is w_2, determined by the point of intersection between the demand and supply curves. At time period t_1, the platform earns a profit of A_1, while at time period t_2, it earns a profit of A_2. Therefore, the total profit for the platform in the absence of a preferential algorithm is $A_1 + A_2$, while the driver surplus amounts to $B_1 + B_2 + F_1$.

With a preferential algorithm, the platform communicates to drivers that if they work during time period t_2, they will be given priority and receive an order during time period t_1. Hence, the platform can motivate drivers to work during time period t_2 without offering substantial incentive wages. This allows the platform to lower the wage rate to w_2' during time period t_2 and still sustain the desired level of labor supply, denoted as L_2'. Therefore, with the implementation of a preferential algorithm, the total profit for the platform becomes $A_1 + A_2 + F_1 + F_2$, while the driver surplus is $B_1 + B_2 - F_2 - F_3$.

Typically, the platform needs to offer high incentive wages to motivate drivers to work more. For instance, at the wage rate w_2' during t_2, if the platform intends to increase the labor supply from L_2 to L_2', it must provide additional compensation of $F_2 + F_3$ to motivate more drivers to work. Nevertheless, with the implementation of a preferential algorithm, the platform no longer needs to offer such incentive wages. Instead, it can prioritize drivers who work during time period t_2 for order assignment during time period t_1. Drivers who choose to work during t_2 are now compensated by earning a surplus during t_1. As a result, during time period t_1, the preferential algorithm will create a wage differential between drivers who exclusively work during t_1 and drivers who work during both t_1 and t_2. The power of implementing a preferential algorithm arises from the excess supply of drivers during time period t_1 and the platform's ability to select which drivers will receive orders in such situations. The effectiveness of the preferential algorithm depends on the disparity in demand elasticity and reservation values of drivers across different time periods.

This simple theoretical model highlights the incentive for using a preferential algorithm. The preferential algorithm allows the platform to extract additional driver surplus in situations where it is unable to conduct first-price discrimination for drivers. The preferential algorithm leverages cross-time labor supply elasticity to extract additional driver surplus, while surge pricing utilizes real-time elasticity to maximize the platform's profit. Despite their different mechanisms, the platform achieves higher profit from both surge pricing and the preferential algorithm. In Appendix A, we use our theoretical model to illustrate the contrasting ways surge pricing and the preferential algorithm operate, as well as to highlight their potential complementarity. Specifically, we compare the equilibrium outcomes in four scenarios: without surge pricing and the preferential algorithm, with only surge pricing, with only the preferential algorithm, and with both surge pricing and the preferential algorithm.

3 Data

To study the wage differential resulting from the preferential algorithm, we acquire transaction-level data from the Transportation Bureau of a major city in Asia. We observe all completed transactions of all ride-hailing platforms in December 2018 for that city.[6] We also observe drivers' attributes, such as age, gender, and place of birth.

For each transaction, we observe the trip's origin, destination, and distance, as well as the duration spent on passenger pickup and transportation, and the corresponding payment the driver receives. The transaction-level data allow us to observe the detailed work schedules of the drivers and have in-depth information on the orders they received. Furthermore, the order details, encompassing origin, destination, wait time, pickup time, and drive time, enable us to assess the quantity and quality of orders received by different drivers. Therefore, we can investigate the underlying factors contributing to drivers' wage differentials. While we have data on completed transactions from all ride-hailing platforms, our main analysis focuses exclusively on Platform X for two key reasons. First, Platform X holds a dominant position in the city under study, accounting for more than 90% of the market share. Second, our data indicate that drivers rarely multi-home or switch between different platforms, suggesting that platform competition is almost negligible in our city of study.[7]

Table 1 summarizes our data set. The unit of observation is at the driver-hour level.[8] A driver serves, on average, 1.9 orders per hour and earns 50 CCY. The number of orders ranges from 1 to 9 between the 25$^{\text{th}}$ percentile and the maximum value, demonstrating a significant variation in the number of orders fulfilled by drivers within an hour. For each hour worked, drivers generally only spend half the time transporting riders, devoting 10 minutes of their time to picking up riders and another 19 minutes to waiting for orders, on average. Considering that drivers spend a substantial amount of time on these latter two tasks, having a higher priority in order assignment plays a significant role in improving a

[6]The city we study has a population of around eleven million.

[7]Appendix F shows a detailed analysis of multi-homing.

[8]The unit of observation in our raw database is at the driver-rider-order level. We primarily concentrate on weekdays (a total of 21 days) due to variations in supply, demand, and fee schedules between weekdays and weekends. Following the literature, we conduct our main demand estimation and counterfactual analysis at the driver-hour level. For more details on how we derive the driver-hour level data from the raw data, please refer to Appendix E.

driver's hourly wage.

Table 1: Summary Statistics (Driver-Hour)

	Mean	Std. Dev.	Min	25 Pctl	Median	75 Pctl	Max
Hourly Wage (CCY)	49.98	24.52	0	32.83	47.42	62.74	286.86
Earning Time (minutes)	30.60	12.01	0	21	31	40	60
Pickup time (minutes)	10.62	6.67	0	6	10	15	60
Idle Time (minutes)	18.78	14.32	0	6	17	29	60
Number of Orders	1.89	1.11	0	1	2	3	9
Distance (km)	14.11	7.41	0	8.78	13.1	18.2	94.13
Number of Observations				4,182,318			

Table 2 summarizes the driver characteristics. There are $40,104$ unique drivers in our data, of which 2.7% are female and 37.4% are local. We define local drivers as drivers with local household registration permits.[9] Household registration permits have a profound impact on residents' capacity to buy houses and access schools and childcare facilities, thereby influencing their available opportunities in the job market. Table 2 shows that drivers work a median of 13 of the 21 workdays. There is considerable heterogeneity across the number of days each driver works, ranging from 5 to 19 days between the 25$^{\text{th}}$ and 75$^{\text{th}}$ percentiles. Moreover, there is also substantial variation in the number of work hours per day, with the 25$^{\text{th}}$ percentile driver working 4.8 hours, while the 75$^{\text{th}}$ percentile driver works 10.5 hours.

Table 2: Summary Statistics of Driver Characteristics

Characteristic	Mean	Std. Dev.	Min	25 Pctl	Median	75 Pctl	Max
Age	37.29	8.24	21	31	37	43	61
Work Days	12.02	7.03	1	5	13	19	21
Daily Work Hours	7.61	3.59	1	4.75	8.09	10.47	18

The summary statistics of drivers working for Platform X in our city of study are substantially different from Uber data from the US market. For instance, according to Cook, Diamond, Hall, List and Oyer (2021), 27.3% of Uber drivers are women, whereas just 2.7% of the drivers in our data are female. Additionally, our drivers dedicate significantly more time to their work, averaging around 7.6 hours per day, while Uber drivers usually work approximately 3 hours per day. The substantial difference in working hours may be attributable to the preferential algorithm discussed in this study.

[9]Household registration permits are issued by the government and indicate the particular area a person is from; in this area, the registrant is entitled to benefits such as hospitals, schools, or land-purchasing rights.

High-Performing and Low-Performing Drivers

Section 2.1 provides a comprehensive explanation of the preferential algorithm used by Platform X. While the platform's assigned driver scores are not directly observable in our data, we can infer the historical driving performance of each driver from the transaction data, since we have access to all completed transactions.

We first verify whether working longer periods, particularly during incentivized hours, leads to increased order assignment priority and subsequently higher hourly wages, as explained in Section 2.1. We regress the hourly wage of a driver on the total number of hours worked in a month and the percentage of incentivized hours worked, controlling for day, hour, and operation area fixed effects. According to interviews with drivers and engineers at Platform X, during our study period, midday and night hours (starting from 7 PM) were identified as incentivized hours. Table 3 shows the results. Generally, drivers who work more, especially during incentivized hours, earn a higher hourly wage than other drivers. Column (2) of Table 3 shows that working one additional hour in a month increases a driver's hourly wage by 0.3 cents. Given that the 25^{th} to 75^{th} percentiles of drivers work 27 to 172 hours, their hourly wage gap is 0.435 CCY or 0.87% of the average hourly wage. A more important feature of the higher hourly wages is the percentage of incentivized hours worked. Allocating 1% more work time to incentivized hours increases the hourly wage by 0.187 CCY. Given that the 25^{th} to 75^{th} percentile drivers spend 55% to 72% of their work time on incentivized hours, respectively, their hourly wage gap is 3.2 CCY or 6.4% of the average hourly wage. These findings indicate that the preferential algorithm employed by Platform X aligns with its description: drivers who put in longer hours and work more during incentivized hours are indeed given priority in order assignments, resulting in a higher hourly wage. In Section 4, we thoroughly investigate how the preferential algorithm drives this wage differential and eliminate alternative explanations.

One computational challenge arises from the fact that, for each hour, a driver has the option to choose whether to work. As a result, the number of potential driver work schedules on any given day reaches 2^{24}. This vast number of possible driver statuses is computationally impractical to track in our analysis. Based on our interviews with drivers, it appears there are mainly two types of drivers. The first type comprises high-performing drivers, who can also be perceived as committed or full-time. The second type are low-performing drivers, who can also be perceived as uncommitted or part-time. Hence, we proceed to validate the possibility of categorizing drivers into two types based on their historical work performance. Additionally, limiting the driver types to two will make our dynamic labor supply model more tractable.

We implement machine learning algorithms to cluster drivers based on their hourly wages,

Table 3: Factors Correlated with Hourly Wage

Hourly Wage	(1)	(2)
# of Work Hours in month	0.003***	0.003***
	(0.000)	(0.000)
% Incentivized Hours		18.724***
		(0.170)
Constant	54.918***	39.201***
	(0.126)	(0.190)
Observations	4,182,318	4,182,318
R-squared	0.040	0.043

Notes: We control for day-hour fixed effects, origin district fixed effects, and destination district fixed effects. Standard errors are in parentheses. *** p<0.01.

work schedule, and other observed characteristics. Our findings indicate that we can primarily classify drivers into the two distinct types, and this result is robust to various specifications.[10] Based on the analysis, we formally classify the two types of drivers as follows: A driver is considered high-performing if they worked for at least two consecutive hours during incentivized hours (midday or night) on a minimum of 8 out of the 21 workdays. Conversely, a driver is classified as low-performing if they do not meet these criteria.[11] Throughout all our subsequent analyses, we use the terms "H-type" and "L-type" to represent the status of drivers as high-performing and low-performing, respectively.

Table 4 summarizes the characteristics of high- and low-performing drivers. There are $23,712$ high-performing drivers and $16,392$ low-performing drivers. Panel I reports the drivers' characteristics. High-performing drivers are more likely to be non-local and male. Women account for 2.2% of the high-performing drivers and 3.5% of the low-performing ones. Non-locals account for 69% of the high-performing drivers and only 53% of the low-performing ones. The average age is comparable between high- and low-performing drivers. Panels II and III report driver performance. On average, high-performing drivers work more, averaging 17 out of 21 workdays, while low-performing drivers, on average, work 5 out of

[10]Online Appendix G describes the machine learning algorithm we use to cluster drivers.

[11]We performed various robustness checks by changing the threshold for identification as a high-performing driver. For example, we changed the required number of days from 8 to 9, 10, 11, etc., out of 21 workdays, and we put further restrictions on the total number of hours worked per month at various levels. Reduced-form results in Section 4 are robust to these definitions. As explained in the main context, the key feature of high-performing drivers is the percentage of hours worked consecutively in incentivized hours. Because of the high fixed cost of starting to work, consecutively worked hours during incentivized hours are highly correlated with the total number of hours worked. This may help explain why the two criteria we use in the main context are robust to all the variations mentioned here.

Table 4: High/Low-performing Driver Characteristics

	High-performing (1)	Low-performing (2)
Panel I: Driver/Vehicle Characteristics		
% female	2.2%	3.5%
% non-local	69%	53%
Age	37.2	37.4
Panel II: Performance (in a month)		
Work Days	17	5
Work Hours	159	26
# of orders	301	46
Monthly Revenue	7,985	1,202
Panel III: Performance (in an hour)		
Work Time	30.7	29.3
Pickup time	10.7	10.2
Idle Time	18.6	20.4
# of orders	1.90	1.76
Hourly Revenue	50.4	46.5
# of drivers	23,712	16,392
Share of Drivers	59.1%	40.9%

21 workdays. In any given hour, conditional on working, high-performing drivers have more passenger-service time (30.7 minutes versus 29.3 minutes) and spend less time waiting for orders (18.6 minutes versus 20.4 minutes). High-performing drivers also finish more orders (1.9 orders versus 1.74 orders) and earn more (50.4 versus 46.5 CCY per hour) than low-performing drivers.

4 Reduced-Form Evidence

In this section, we first provide evidence that high-performing drivers earn a higher hourly wage, then investigate the factors driving this wage differential. Lastly, we rule out alternative explanations for the observed wage differential between high- and low-performing drivers, including strategically choosing where to work, strategically selecting and canceling orders, driving faster, and having a better knowledge of routes.

4.1 Wage Differential

First, conditional on working in the same hour, we test whether high-performing drivers earn more than low-performing ones. We regress the hourly wage of a driver on an indicator of being high-performing and control for day-hour, origin, and destination fixed effects. Table 5 shows a significant difference in hourly wage between high- and low-performing drivers. High-performing drivers earn 3.8 CCY, or 8.2% more per hour, than their low-performing counterparts. The result is very robust, with or without controlling for various fixed effects.

Table 5: Wage Differential: High-performing versus Low-performing

Dependent Variables	Hourly Wage		
	(1)	(2)	(3)
High-performing	3.886***	3.794***	3.851***
	(0.0397)	(0.0393)	(0.0391)
Constant	46.49***	46.57***	47.24***
	(0.0376)	(0.0372)	(0.0701)
Day-Hour FE		Y	Y
Origin FE			Y
Destination FE			Y
Observations	4,182,318	4,182,318	4,182,318
R-squared	0.002	0.039	0.050

Notes: Standard errors in parentheses. *** p<0.01

Given that high-performing drivers earn significantly higher hourly wages, we investigate what factors drive this wage differential. To this end, we study the characteristics of the orders that high- and low-performing drivers receive. For example, we evaluate the number of orders they receive and how often a rider cancels their order. We also compare the the amount of idle time and the time spent serving the customer for the two types of drivers. Table 6 shows the results. Column (1) shows that conditional on working in the same hour, high-performing drivers receive more orders than low-performing ones. On average, high-performing drivers receive 0.125 more orders or 7.1% more every hour. Second, orders assigned to high-performing drivers are 2.8% less likely to be canceled by riders (column 2).[12] Because high-performing drivers get assigned more orders every hour, they also drive 0.748

[12] Our main analysis throughout this paper uses data on completed transactions. Our data include information on canceled orders in the first ten days (from December 1 to December 10, 2018). We use data on completed transactions and canceled orders for all regressions involving cancellation rates. Therefore, the number of observations differs from that of other regressions.

more kilometers and spend 5.4% more time carrying riders in an hour (column 4).[13] More importantly, high-performing drivers spend 10.5% less time waiting for orders (column 5). This result is consistent with the descriptions in Section 2 of how the algorithm prioritizes high-performing drivers for better order assignments.

Table 6: Driving Forces of Wage Differential

Dependent Variables	# Orders	Cancellation Rate (Rider)	Drive Dist	Earning Time	Idle Time
	(1)	(2)	(3)	(4)	(5)
High-performing	0.125***	-0.0023***	0.748***	1.579***	-2.140***
	(0.0018)	(0.0004)	(0.0003)	(0.0187)	(0.0221)
Constant	1.468***	0.0894***	12.85***	32.35***	17.04***
	(0.00313)	(0.0005)	(0.0212)	(0.0334)	(0.0395)
Mean of Low-performing	1.76 (orders)	8.2%	13.4 (km)	29.3 (min)	20.4 (min)
High-performing compared to Low-performing	7.1%	-2.8%	5.6%	5.4%	-10.5%
Observations	4,182,318	4,815,026	4,182,318	4,182,318	4,182,318
R-squared	0.080	0.006	0.045	0.100	0.115

Notes: In all columns except column (2), our analysis uses completed transactions, which are available from Dec. 1, 2018, to Dec. 31, 2018. In column (2), we also include canceled orders to compute rider cancellation rates. Information on canceled order is available from Dec. 1, 2018, to Dec. 10, 2018. Standard errors are in parentheses. All specifications control for day-hour fixed effects, origin district fixed effects, and destination district fixed effects. *** p<0.01

In summary, Table 6 shows that three main factors are driving the wage differentials between high- and low-performing drivers. The former are given more rides from the platform, waste less idle time waiting for orders, and receive more orders from higher quality riders (those with a lower probability of rider-initiated cancellation). As the platform's algorithm determines the assignment of orders, we hereafter term the systematic difference in the quantity and quality of order assignments based on work schedule (high-performing versus low-performing) algorithmic preferential wage-setting.

4.2 Rule Out Alternative Explanations

There could, of course, be alternative explanations for the wage differentials between high- and low-performing drivers. Rather than having the algorithm prioritize different work schedules when assigning orders, some may argue that drivers make decisions endogenously, resulting in the observed wage difference. For example, Cook, Diamond, Hall, List and Oyer (2021) find that the gender earnings gap amongst drivers can be entirely attributed to three factors: experience on the platform (learning-by-doing), preferences and constraints about

[13] Gaineddenova (2021) shows that drivers prefer more expensive trips with a shorter pickup distance, using data from a decentralized ride-hailing platform.

where to work (driven largely by where drivers live and, to a lesser extent, by safety), and preferences about driving speed. To provide a robustness check for our findings, we consider four alternative explanations and use our data to prove that such alternative explanations are unlikely to be true in our context. First, high-performing drivers may have better knowledge of the popular rider pickup areas (hot spots) and get more orders. Second, high-performing drivers may learn how to reject and cancel rides strategically. Third, high-performing drivers may drive faster than others and earn a higher hourly rate. Fourth, high-performing drivers may know the streets better and choose better routes than their low-performing counterparts.

High-Performing Drivers Strategically Choose Where to Work

First, we explore whether high-performing drivers have better knowledge of hot spots, and hence are strategically choosing where to work in order to earn more hourly.[14] There are eight districts in the city we study. We first examine where the high- and low-performing drivers work and whether they tend to pick up or drop off clients in different areas. Table 7 suggests no substantial difference between the origin or destination districts where high- and low-performing drivers work.

Table 7: Active Area for High-performing and Low-performing Drivers

District	Origin		Destination	
	Low-performing	High-performing	Low-performing	High-performing
1	7%	7%	7%	7%
2	9%	8%	9%	8%
3	20%	22%	21%	23%
4	7%	7%	7%	7%
5	16%	15%	15%	14%
6	10%	11%	10%	11%
7	16%	15%	16%	15%
8	16%	15%	15%	13%
Total	100%	100%	100%	100%

To better control for location-fixed effects, we manually divide the eight districts into even finer 1km × 1km grids. Because we observe the coordinates of each pickup and drop-off location, we can accurately place trip origins and destinations into one square on the fine grids. Column (2) of Table 8 reports the results of re-running our main regression with

[14] For example, Haggag, McManus and Paci (2017) find that New York taxi drivers accumulate neighborhood-specific experience, which helps them find riders.

day-hour and grid fixed effects, which are close to the benchmark result in column (1).[15] This shows that the wage differential between high- and low-performing drivers cannot be explained by high-performing drivers picking up or dropping off passengers from certain locations or neighbourhoods. We further divide each hour into four 15-minute intervals as a robustness check. Instead of controlling for day-hour fixed effects, we now control for day-hour-15-minute fixed effects. With a finer measure of both location- and time-fixed effects, we are essentially comparing drivers who work in the same location at the same time. The only difference between the drivers is their performance level, which depends on their past work schedules. Column (3) reports the result after controlling for day-hour-15-minute and grid fixed effects, and column (4) reports the result controlling for day-hour-15-minute-grid fixed effects. The results in all robustness checks are close to our benchmark result in column (1). Thus, a knowledge of hot spots and strategically choosing where to work are unlikely explanations for the wage differential between high- and low-performing drivers.

Table 8: Wage Differentials with Finer Grids

Dependent Variables	Hourly Wage (OLS)				IV
	(1)	(2)	(3)	(4)	(5)
High-Performing	2.742***	2.704***	2.705***	2.731***	8.99***
	(0.0391)	(0.0453)	(0.0448)	(0.0448)	(0.9614)
Constant	47.98***	21.38	23.90	47.56***	41.85***
	(0.0701)	(22.75)	(22.51)	(0.0427)	(0.8755)
Time Controls:					
Day-Hour	Y	Y			
15Minute			Y		
Location Controls:					
Origin/Destination	Y				
Grid		Y	Y		
Grid-15Minute				Y	Y
Observations	3,160,528	3,160,528	3,160,528	3,160,528	3,160,528
R-squared	0.053	0.075	0.094	0.097	(omitted)

Notes: Standard errors are in parentheses. *** p<0.01, ** p<0.05, * p<0.1
We restrict our sample to drivers who were active in the last hour.

To mitigate potential biases in driver selection based on unobservable characteristics, we have employed instrumental dummy variables (IVs): the rate of change in precipitation

[15] Column (1) of Table 8 has the same specification as column (3) of Table 5, where we control for origin, destination, and day-hour fixed effects. The two results differ because we restrict our sample to drivers who were active in the last hour in Column (1) of Table 8.

and air quality index (AQI) in the driver's hometown city between 2017 and 2018. These weather variables satisfy the two conditions required for valid IVs. Firstly, the occurrence of precipitation and changes in air pollution may be correlated with a driver's decision to become a high-performing driver. For instance, alterations in precipitation and air pollution might affect the benefits of farming, potentially motivate more drivers to leave their hometowns and become full-time drivers in the focal city under study, as suggested by (Miguel et al., 2004). Second, the variation in weather conditions in a driver's hometown should not directly impact the driver's hourly rate or order distribution in the city being studied. The IV results are presented in column (5), revealing a more significant wage differential between high- and low-performing drivers. We include additional IV results in Appendix H.

High-Performing Drivers Strategically Cancel Orders

Second, the literature shows that more experienced drivers can learn how to strategically reject and cancel rides, hence earning more. To examine whether such a mechanism exists in our data, we regress the probability of a driver canceling an order on driver type and control for day-hour, origin, and destination fixed effects. The results in column (1) of Table 9 show that, if anything, high-performing drivers have a lower cancellation rate than low-performing ones in our data. The robustness check results, controlling for finer location and time-fixed effects, remain consistent with these findings. It is very difficult for drivers to cancel an order on Platform X , which may help explain why Platform X drivers behave differently from the Uber drivers described in Cook, Diamond, Hall, List and Oyer (2021). Because high-performing drivers are less prone to cancelling an order, it is unlikely, in our case, that the higher hourly wage of high-performing drivers is caused by drivers strategically rejecting and choosing rides.

High-Performing Drivers Drive Faster

Third, some drivers may drive faster than others, hence completing more trips and earning a higher hourly wage. We examine whether high-performing drivers drive faster than their low-performing counterparts by regressing the average driving speed per hour on an indicator of being high-performing. We continue to control for day-hour, origin, and destination fixed effects. Column (2) of Table 9 shows the results. While we do find that high-performing drivers drive slightly faster (0.5%) than low-performing ones, the 0.5% faster driving speed is insufficient to explain the 8% wage differential we find in our main analysis. This 0.5% faster driving speed only converts into an extra 0.24 CCY per hour,[16] thus explaining very

[16]The average driving speed for a low-performing driver is 24.63 km/h. Thus, by driving 0.5% faster, high-performing drivers drive 0.12 km more per hour. The average ride fare is about 2 CCY/km. Therefore,

Table 9: Driver Cancellation and Driver Speed

Dependent Variables	Probability of Cancellation (by Driver)	Driving Speed
	(1)	(2)
High-performing	-0.0062***	0.1313***
	(0.0002)	(0.0194)
Constant	0.0365***	0.410***
	(0.0003)	(0.0006)
Mean of Low-performing	3.4%	24.63 (km/h)
High-performing compared to Low-performing	-18.2%	0.5%
Observations	4,815,026	4,168,889
R-squared	0.004	0.089

Notes: Standard errors are in parentheses. We control for day-hour fixed effects, origin district fixed effects, and destination fixed effects. *** p<0.01

little of the 3.8 CCY (or 8%) wage differential between high- and low-performing drivers.

High-Performing Drivers Know the Routes Better

Lastly, some may argue that high-performing drivers know the streets better and may hence use shortcuts or less congested routes to their benefit. As our dataset contains only the origin and destination of each ride, we cannot observe the exact route chosen by the driver. However, based on our interviews with Platform X drivers and engineers, we find that drivers mostly follow the GPS-recommended route given by the Platform X app, as riders may file complaints to Platform X if drivers do not do so. Therefore, drivers have little incentive to deviate from the recommended route.

To summarize, we examine four alternative explanations for the wage differential between high- and low-performing drivers: that high-performing drivers may strategically choose where to work, strategically select and cancel orders, drive faster, or have a better knowledge of routing. However, upon more in-depth analysis of our data, we can rule out all four of these as likely explanations of the observed wage differential between high- and low-performing drivers.

assuming that the extra 0.12 km is entirely used in carrying a rider, without any time wasted to wait for and pick up customers, then $0.12 * 2 = 0.24$ CCY. Therefore, this 0.5% faster driving speed only converts into an extra 0.24 CCY per hour.

5 Model

Given that the preferential algorithm prioritizes specific drivers based on their work schedule for order assignments, the labor supply decision is now subject to the rules specified by the preferential algorithm. To understand who benefits and who loses under such a preferential algorithm, we propose a dynamic equilibrium model of a ride-hailing market, similar to Frechette, Lizzeri and Salz (2019). In our model, each driver decides when and how long to work, depending on the wage rates and reservation values.

We model the decisions of market participants for one day. At each hour of the day, there is a demand curve for rides, $D_t(P_t)$. Given this demand curve, the platform makes two types of decision. First, it determines the price to charge riders, P_t. We allow for dynamic pricing and thus let prices vary across different times of the day. Second, the platform's algorithm allocates ride orders to each driver. The algorithm distinguishes between two types of drivers: high-performing and low-performing. The former commit to working consecutively for at least 2 hours during incentivized hours, 10 AM–4 PM and 7 PM–6 AM the next day. The latter make no work schedule commitments. Driver i first decides whether to be high performing or low performing $\tau \in \{H, L\}$. We assume that drivers choose their type (H or L) at the start of the day, and drivers cannot change their worker type throughout the day. Conditioning on the choice of being an H-type or L-type, each driver chooses whether to work for each hour of the day. The problem is dynamic, because whenever a driver starts working or resumes working after a break, there is a fixed "warm-up" cost. If the driver chooses to be high performing, the dynamic problem is under the constraint that working hours need to satisfy certain work schedules. Otherwise, the problem is unconstrained.

Our model prioritizes within-day dynamics over day-to-day dynamics to emphasize the major trade-off involved in drivers' standard decision-making process. According to our interviews with drivers, they tend to maintain consistent working habits from day to day. This may be attributed to the fact that the initial introduction of ride-hailing in the focal market took place as early as 2014, allowing drivers to have established their daily patterns by the time of our study in 2018. Our data also validate this consistency in hourly driving patterns. While it is technically feasible to incorporate day-to-day dynamics into our existing one-day model, doing so presents significant challenges due to data limitations and computational complexities. As a result, we leave this to future research. Investigating day-to-day dynamics could offer interesting insights into how drivers make choices among platforms and whether they opt to become ride-hailing drivers. As per our interviews with drivers, day-to-day dynamics are typically established within a short period. For individuals who have not yet settled into a consistent routine, choosing full-time ride-hailing work requires making arrangements with family members, such as finding suitable daycare for their children. Once drivers have settled into their day-to-day dynamics, they revert to the within-day dynamics, as described in our study.

We use a bold typeface to denote vectors containing values for each hour of the day. For example, $\boldsymbol{P}$ denotes prices for all $t = 1, \cdots, 24$. The sequence of wage rates is $\boldsymbol{W^{\tau}}$, which is determined by the platform's pricing decisions $\boldsymbol{P}$ and the algorithm deciding which driver receives an order.

5.1 Drivers' Dynamic Labor Supply

Drivers first choose to be either high performing or low performing. Low-performing drivers solve an unconstrained dynamic discrete choice problem of when to work. As per our discussion in Section 3, high-performing drivers are required to work consecutively for at least 2 hours during incentivized hours, between 10 AM–4 PM and 7 PM–6 AM the next day. Besides fulfilling the required working hours, a high-performing driver also makes an hourly choice of whether to work. A driver who chooses to be high performing must choose which minimum requirement to satisfy in advance. For example, driver A may choose to be a high-performing driver by committing to work between 10 AM and 12 PM. Between 10 AM and 12 PM, driver A will be active on the app with probability 1; at any other time of the day, driver A can freely choose whether to work. We assume that drivers choose their work type (H or L) at the start of the day, and that drivers cannot change their type during that day. A low-performing driver B does not commit to any work schedule. *Ex post*, even if driver B ends up working long hours, including from 10 AM to 12 PM, they would still be considered a low-performing type.

Sixteen possible work schedules satisfy the high-performing requirement.[17] Work status is summarized by different work schedules, $\mathcal{L} \equiv \{0\}$ and $\mathcal{H} \equiv \{1, \cdots, 16\}$. The choice of work schedule is a simple logit model,

$$N^j = N \cdot \frac{\exp(EV^j)}{\sum_{k=0}^{16} \exp(EV^k)},$$

where N is the total number of potential drivers and EV^j represents the expected value of choosing work schedule j.[18] Therefore, the total number of high-performing drivers is $N^H = \sum_{k=1}^{16} N^k$, and the total number of low-performing drivers is $N^L = N^0$.

[17] For example, if a driver chooses to satisfy the high-performing requirement by working 10 AM–12 PM, then they are categorized as schedule 1. If a driver chooses to satisfy the high-performing requirement by working 11 AM–1 PM, then they are categorized as schedule 2, etc.

[18] We use the number of unique drivers in the 21 workdays as the number of potential drivers in our model.

After deciding whether to be H-type, drivers then find the optimal solution to their dynamic discrete choice problem by choosing whether to work at each time t. Drivers observe the warm-up cost κ, sequence of hourly wages $\boldsymbol{W^\tau}$, and reservation values $\boldsymbol{O}$. At each time t, low-performing drivers compare the hourly wage plus the difference in expected future values to the value of their outside option before deciding whether to work at time t. This is a dynamic problem because if the driver chooses to work at time t and continues working at $t+1$, they would not need to pay an extra warm-up cost at $t+1$. Hence, the expected future value at time t is higher if the driver chooses to work than if they choose not to work at time t. High-performing drivers have to work with probability 1 during committed hours. At any other time of day, high-performing drivers solve the same dynamic discrete choice problem by comparing their hourly wage plus the difference in expected future values to their outside option, then decide whether to work at each time t.

Specifically, at the beginning of hour t, a driver receives a random draw from the wage distribution and another draw from the outside option:

$$\begin{aligned} U_{1t}^\tau &= \underbrace{W_t^\tau}_{\text{preferential wage rate}} + \sigma \cdot \epsilon_{1t}, \\ U_{0t}^\tau &= \underbrace{O_t^\iota}_{\text{outside option value}} + \sigma \cdot \epsilon_{0t}, \end{aligned} \tag{1}$$

where U_{1t}^τ corresponds to the utility associated with working during time period t, while U_{0t}^τ represents the utility of not working during the same period. O_t^ι represents the reservation value from working on something else, and $\epsilon_{\cdot t}$ represents the error term, which is Type-I extreme value distributed. Differences in reservation values among various groups of drivers may impact their labor supply decisions. To account for this, we consider the presence of unobserved heterogeneity in drivers' reservation values. Specifically, we have $O_t^\iota = O_t + \eta_{\iota,t}$, where O_t is the average reservation value per hour, $\eta_{\iota,t}$ is driver-specific unobserved heterogeneity representing their preference for certain parts of the day, and ι is the unobserved heterogeneity type. According to our survey of drivers, these preferred parts often closely align with the intervals on Platform X's fare schedule.[19] Therefore, we consider seven unobserved heterogeneity types that align with these intervals. For the benchmark driver group 0, the unobserved heterogeneity term η_{0t} is set to 0 for all time periods t. In contrast, driver group 1 has an unobserved heterogeneity term η_{1t}, equal to η_1, during the time period from 7 AM to 10 AM and 0 for all other time periods. Similarly, driver group 2 shows an unobserved heterogeneity term η_{2t}, equal to η_2, during the period from 10 AM to 4 PM.

If the driver took the outside option in the previous hour, there is a fixed warm-up cost

[19] Section 2.1 offers details of the fare schedules.

$\kappa > 0$ to start work. This is to rationalize the fact that drivers often drive for consecutive hours. The value function for the low-performing driver at any time t that is not the first or the last period is

$$V_t^L = \begin{cases} W_t^L + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^L & \text{if } a_t = 1 \ \& \ a_{t-1} = 1, \\ W_t^L - \kappa + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^L & \text{if } a_t = 1 \ \& \ a_{t-1} = 0, \\ O_t^\iota + \sigma \cdot \epsilon_{0t} + \beta EV_{0t+1}^L & \text{if } a_t = 0. \end{cases}$$

Here, W_t^L represents the wage rate for the low-performing driver at time t, κ is the warm-up cost, and σ is the scale parameter. The terms EV_{1t+1}^L and EV_{0t+1}^L denote the expected values if the driver chooses to work or not to work, respectively, at time t. The labor supply decision of the driver is denoted by a_t, where $a_t = 0$ indicates not working at time t. The value functions for all time periods, for both low- and high-performing drivers, appear in Appendix B. We solve the dynamic discrete choice problems through backward induction.

Individual driver choices, in turn, generate the aggregate labor supply for each hour by driver type:

$$N_t^H = \sum_{j=1}^{16} N^j \times \text{Pr(work in hour t|work schedule j)},$$
$$N_t^L = N^0 \times \text{Pr(work in hour t|work schedule 0)},$$

where the conditional choice probabilities $\Pr(\cdot|\cdot)$ are the solutions to the above-mentioned dynamic discrete choice problems. We denote the type-specific labor supply as

$$N_t^H = \mathcal{N}_t^H(\boldsymbol{W^H}; \boldsymbol{\theta}) = \mathcal{N}_t^H(\boldsymbol{P}, \boldsymbol{s}; \boldsymbol{\theta}),$$
$$N_t^L = \mathcal{N}_t^L(\boldsymbol{W^L}; \boldsymbol{\theta}) = \mathcal{N}_t^L(\boldsymbol{P}, \boldsymbol{s}; \boldsymbol{\theta}).$$

5.2 Demand for Rides and the Platform's Problem

Riders only demand driver-earning hours. The number of earning hours they demand is $D_t(P_t)$, where P_t is the hourly serving rate that the platform posts at hour t. For simplicity, we assume that the demand for rides is downward-sloping and iso-elastic:

$$Q_t = D_t(P_t) = \delta_t P_t^{-\epsilon}, \tag{2}$$

where ϵ is the constant demand elasticity. The demand shifter δ_t includes daily weather indices, such as precipitation and temperature.

The platform takes demand shifter δ_t and demand elasticity ϵ as given and chooses prices and assignments to balance the demand and supply of rides so as to maximize platform profit. Let s_t be the percentage of orders assigned to high-performing drivers at time t, where $s_t \in [0,1]$. The platform's choice of $(\boldsymbol{P}, \boldsymbol{s})$ maximizes its own payoff:

$$\begin{aligned} \max_{(\boldsymbol{P},\boldsymbol{s})} \quad & r \sum_t P_t D_t(P_t) \\ \text{s.t.} \quad & D_t(P_t) s_t \leq \lambda_t^H \mathcal{N}_t^H(\boldsymbol{P}, \boldsymbol{s}; \boldsymbol{\theta}) \\ & D_t(P_t)(1-s_t) \leq \lambda_t^L \mathcal{N}_t^L(\boldsymbol{P}, \boldsymbol{s}; \boldsymbol{\theta}). \end{aligned} \tag{3}$$

Here, r represents the platform's commission rate, while drivers receive a $1-r$ portion of the ride fare. $D_t(P_t)$ is the demand for rides, measured in earning hours, and $\mathcal{N}_t^\tau$ represents the total number of working hours (active app hours) that the drivers provide. λ_t^τ is the technological constraint restricting the relationship between working hours and earning hours, where $\lambda_t^\tau \in [0,1]$. For example, $\lambda_t^\tau = 0.5$ means that for every 15 minutes driving with a rider, a typical driver spends another 15 minutes on pickup, payment, etc. If $\lambda_t^\tau = 1$, there is no time spent on pickup.[20] We have idle drivers waiting for trip requests when one of the two inequalities is unbounded. In our empirical analysis, we set the commission rate r equal to 20%.[21]

Given the choice of prices and assignments $(\boldsymbol{P}, \boldsymbol{s})$, the platform effectively determines the sequence of wages $(\boldsymbol{W^H}, \boldsymbol{W^L})$. Each high- or low-performing driver expects to receive a wage rate

$$\begin{aligned} W_t^H &= (1-r) P_t D_t(P_t) s_t \frac{1}{N_t^H}, \\ W_t^L &= (1-r) P_t D_t(P_t)(1-s_t) \frac{1}{N_t^L}, \end{aligned} \tag{4}$$

where $1-r$ is the revenue share that the driver receives, while s_t represents how the algorithm favors high-performing drivers (the proportion of orders assigned to high-performing drivers).

[20] We obtain the value of the technological constraint from the data. We compute the driving time as a percentage of driver work time in each day-hour for both high- and low-performing drivers. Then, we calculate the maximum as the technological restriction.

[21] According to Platform X's IPO document, the national average commission rate is 20.9%. In our survey, most drivers suggest that the commission rate is about 20%. Therefore, we use $r = 0.2$ in our empirical analysis.

6 Estimation

6.1 Demand Estimation

We first estimate rider demand for service time for each hour h. We consider each hour a different market and aggregate our data to the day-hour level. Based on the logarithm of total earning time (Q_t) and the logarithm of average hourly ride fare (P_t), we estimate demand parameters as follows:

$$\log Q_t = \log \delta_h - \epsilon \log P_t + e_h. \tag{5}$$

Our demand estimation suffers from classic supply-demand endogeneity: the platform may set a higher price when there is a higher demand shock in the market, so our OLS estimates may be biased. Similar to Kalouptsidi (2014), we use the number of cars in competing ride-hailing companies on a given day as our supply-side instrumental variable. Suppose the hourly demand shock e_h is instantaneous, with an expected value of zero *ex ante*. In this case, the number of cars in competing ride-hailing companies is not correlated with hour-level demand shocks. On the other hand, the number of cars competitors operate is negatively correlated with the ride fare that the platform can charge. Therefore, the number of cars in competing ride-hailing companies is a valid instrument.

Table 10: Demand Estimation

Dependent Variables	ln(Service Hours)			
	(1) OLS	(2) OLS	(3) OLS	(4) IV
ln(Hourly Wage)	-5.151***	-5.158***	-0.767***	-1.186**
	(0.0743)	(0.0737)	(0.152)	(0.553)
Rain		-0.0020	-0.0005	-0.0006
		(0.002)	(0.0007)	(0.0007)
Temperature		0.0127***	0.0094***	0.0098***
		(0.0033)	(0.0011)	(0.0012)
Constant	32.12***	32.06***	10.62***	12.69***
	(0.350)	(0.348)	(0.752)	(2.736)
Hour FE			Y	Y
Day of Week FE			Y	Y
Observations	744	744	744	744
R-squared	0.866	0.869	0.988	0.988

Notes: Standard errors are in parentheses. *** p<0.01, ** p<0.05, * p<0.1

Table 10 reports demand estimates for the city of study. Column (1) reports the estimates without fixed effects. Column (2) reports estimates with the weather as a demand shifter. Column (3) further includes day and hour fixed effects. Column (4) reports our IV estimates. After controlling for hourly fixed effects and day-of-the-week fixed effects, column (3) reports a demand elasticity of -0.767. The estimated demand elasticity is much smaller with fixed effects than the estimates in the naïve OLS regression. Our IV estimates in column (4) are similar to those with fixed effects in column (3), and show that when the hourly ride fare increases by 1%, the total demand for service time decreases by 1.2%. We use these IV estimates as the demand elasticity in our counterfactual analysis. Our estimated demand elasticity of -1.186 is comparable to the values estimated in the literature. For example, Frechette, Lizzeri and Salz (2019) estimate an elasticity of -1.225 for New York City's taxi market, while Cohen, Hahn, Hall, Levitt and Metcalfe (2016) rely on the surge pricing algorithm and estimate a smaller price elasticity for UberX (between -0.4 and -0.6).

6.2 Identification and Estimation of Supply Parameters

Our model with unobserved heterogeneity is point-identified using conditional choice probabilities in drivers' dynamic labor supply. Appendix C.1 contains the details of our identification arguments. We follow our identification argument closely in estimating the model and estimate the following structural parameters: $\theta \equiv (\{O_t^\iota\}, \kappa, \sigma)$. $\{O_t^\iota\}$ is the reservation value at each time t, which includes the average reservation value O_t and the unobserved heterogeneity $\eta_{\iota,t}$. κ is the warm-up cost of starting to work, and σ is the normalization term of the EVT1 errors (the scale parameter). We explain the details of our estimation procedure in Appendix C.2.

Table 11 shows the estimation results. The first row shows the estimated population density of each driver group. Three main driver groups clearly dominate: group 3 with probability 0.42, group 2 with probability 0.18, and group 4 with probability 0.18. The second row of Table 11 shows the probability of being high-performing for each driver group. Driver groups 2 and 4 are 96.5% and 93.4% likely to be high performing, respectively, while driver groups 2 and 4 have the lowest average reservation values.

Table 11: Estimation Results for Unobserved Heterogeneity

	Group 0	Group 1	Group 2	Group 3	Group 4	Group 5	Group 6
Population density of each group	0.07	0.06	0.18	0.42	0.18	0.04	0.05
Probability of H-Type	76.7%	78.7%	96.5%	49.6%	93.4%	82.8%	81.0%
Average Reservation Value	46.2	45.6	36.5	50.9	40.6	45.1	44.8

Figure 3 shows the estimated reservation values with unobserved driver heterogeneity.

The average estimated reservation value is 49 CCY. The black line shows the estimated reservation values for group 0 drivers. Reservation values are lowest during morning hours, around 25 CCY, and highest at late night, around 68 CCY. For context, the minimum hourly wage in the city under study was 18.5 CCY in 2018. From the estimated results, we can see that drivers have higher reservation values during incentivized hours between 10 AM—2 PM and 7 PM—5 AM. This helps explain why the ride-hailing platform wants to implement algorithmic preferential wage-setting and convince drivers to work more during those incentivized hours. In terms of driver heterogeneity, driver groups 2 and 4 exhibit low reservation values during midday and early night periods, respectively. The estimated warm-up cost is 124 CCY, or around 2.5 times the average hourly reservation value. The high warm-up cost helps explain why drivers usually choose to drive consecutive hours.

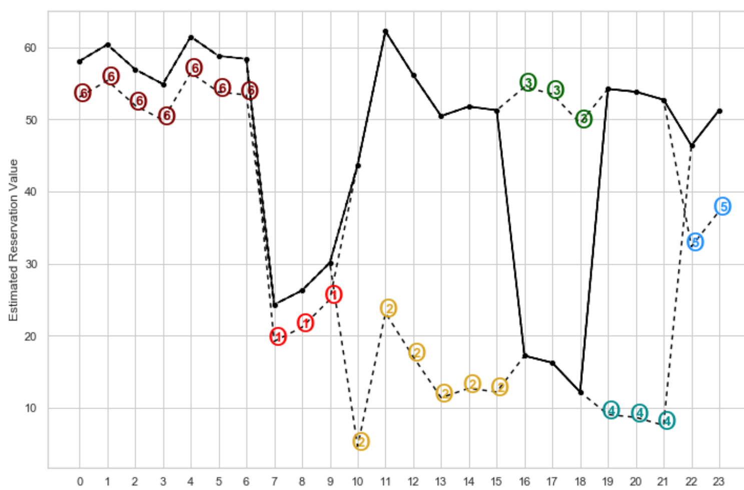


Figure 3: Estimated Reservation Values with Unobserved Driver Heterogeneity

Table 11 shows that three main driver groups dominate: the benchmark drivers (group 3), drivers with low midday reservation values (group 2), and those with low early night reservation values (group 4). To better understand the estimated driver groups, we associate the observed driver characteristics with the respective driver groups. Because driver group 2 has a low midday reservation value and a high probability of being high-performing, observed high-performing drivers who choose to work midday are more likely to be in driver group 2. Similarly, observed high-performing drivers who work early nights are more likely to be in driver group 4. Based on this definition, we divide observed high-performing drivers into several groups according to their working hours. The *OnlyDay* group comprises drivers who work at least 2 consecutive hours in the daytime for at least 8 of 21 workdays.[22] The

[22]This is consistent with our definition of high-performing drivers, who we require to satisfy the condition

OnlyNight group refers to drivers working at least 2 consecutive hours at night for at least 8 of 21 workdays. Drivers who satisfy both criteria belong to the *BothDay&Night* group. The three groups (*OnlyDay*, *OnlyNight*, *BothDay&Night*) are mutually exclusive. The remaining high-performing drivers are grouped into the *Rest* group.

Table 12 compares the driver characteristics of different driver groups in the data, with several interesting findings. First, the *OnlyDay* group has a higher proportion of female drivers (3.5%) than the *OnlyNight* group (1.2%). Second, the average age in the *OnlyDay* group (38.3) is higher than that of the *OnlyNight* group (36.5). Third, non-locals are more likely to be high-performing drivers. For instance, 76% of the drivers in the *BothDay&Night* group are non-local, as compared to 62% of those in the *OnlyNight* or *OnlyDay* group. Therefore, the results suggest that driver groups 2 and 4 are more likely to consist of older, non-local, and female drivers. On the other hand, driver group 3 is more likely to include younger, local, and male drivers. By associating observed driver demographics with estimated driver groups through unobserved heterogeneity, the counterfactual analysis allows us to better understand which individuals may benefit or suffer from the implementation of a preferential algorithm.

Table 12: Observed Driver Characteristics

Type	Low-Performing	High-Performing			
Group		Only Night	Only Day	Both Day & Night	Rest
Female	3.5%	1.2%	3.5%	1.7%	1.6%
Age	37.4	36.5	38.3	36.8	36.4
Non-local	53%	62%	63%	76%	62%
# of Drivers	16,392	3,073	6,659	11,939	2,041

Lastly, we validate our model by checking its goodness of fit. Specifically, we examine whether the simulated values fit the observed CCPs well. Figure D.1 shows the model's goodness of fit, and indicates that overall, the simulated values do indeed fit the observed CCPs.

7 Counterfactual Analysis

We conduct two main counterfactual experiments. First, we show the welfare effects of eliminating the preferential algorithm. To this end, we break down how using a preferential

in at least 8 of the 21 workdays.

algorithm affects the balance between demand and supply over time, as well as how it influences passenger fares. Second, we investigate what factors determine the effectiveness of the preferential algorithm.

7.1 Elimination of Preferential Algorithm ("Fair" Pay)

In the first counterfactual analysis, we study changes in welfare if the preferential algorithm based on work schedules is eliminated. In this case, orders would be randomly assigned to nearby active workers. Effectively, the hourly wage each driver earns will become

$$\widetilde{W}_t = \frac{\eta P_t D_t(P_t)}{N_t}.$$

Given the new sequence of hourly wages $\{\widetilde{W}_t\}$, drivers solve the unconstrained dynamic discrete choice problem for each hour t:

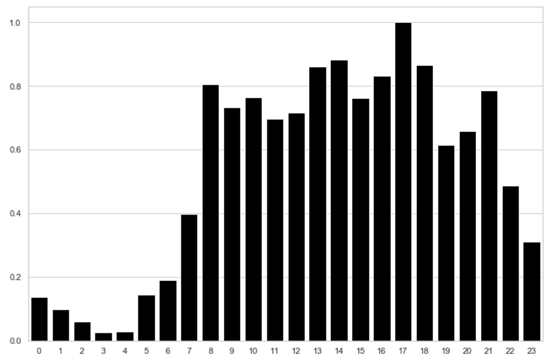
$$\begin{aligned} U_{1t} &= \underbrace{\widetilde{W}_t}_{\substack{\text{non-preferential} \\ \text{wage rate}}} \quad + \quad \sigma \cdot \epsilon_{1t}, \\ U_{0t} &= \underbrace{O_t^{\iota}}_{\text{outside option value}} \quad + \quad \sigma \cdot \epsilon_{0t}, \end{aligned}$$

where we have replaced the preferential wage rates W_t^H and W_t^L by the "fair" rate $\widetilde{W}_t$.

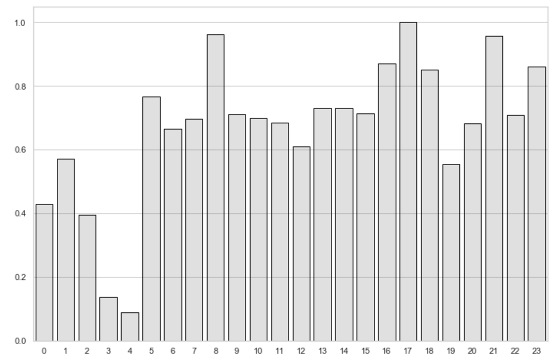
First, we show how the platform leverages cross-time labor supply elasticity using the preferential algorithm. We maintain the ride fares at the same level as when using a preferential algorithm, but we eliminate the wage differential among drivers. While keeping the ride fares unchanged, eliminating the preferential algorithm will decrease labor supply, resulting in labor shortages for most hours. Panel (a) of Figure 4 shows the level of labor shortage.[23] Upon eliminating the preferential algorithm, we can see a severe labor shortage during midday and in the late afternoon. Panel (b) shows the wage differential between high- and low-performing drivers when the preferential algorithm is present. A high wage differential in a particular hour means a high incentive wage for that hour. These results show that the relation between wage differentials and labor shortages is not one-to-one. For example, there is a severe labor shortage at 1 PM and 2 PM, even though the platform does not directly provide high incentive wages specifically at 1 PM and 2 PM, instead doing so from 5 AM to 8 AM. Panel (a) shows that the labor shortage is very mild in the early morning from 5 AM to 7 AM. Therefore, the platform does not necessarily provide direct

[23] To better illustrate the results, we normalize the maximum labor shortage and the maximum wage differential to 1 in Figure 4.

high incentive wages to mitigate labor shortages in a given hour, but instead smooths out the payment of high incentive wages by leveraging the variations in demand elasticity and the differing reservation values of drivers over time.



(a) Labor Shortage



(b) Wage Differential (W_t^H - W_t^L)

Figure 4: Illustration of Leveraging Cross-time Labor Supply Elasticity

To further illustrate the idea of cross-time labor supply elasticity, we eliminate the wage differential between high- and low-performing drivers in only one hour (the treatment hour) and study the implied elasticity of labor supply. More precisely, we calculate the elasticity as

$$\mathcal{E}_t^\tau(h) = \frac{\left(N_t^\tau(\widetilde{\boldsymbol{W}}^H, \widetilde{\boldsymbol{W}}^L) - N_t^\tau(\boldsymbol{W}^H, \boldsymbol{W}^L)\right) / N_t^\tau(\boldsymbol{W}^H, \boldsymbol{W}^L)}{(\widetilde{W}_h^\tau - W_h^\tau)/W_h^\tau},$$

where h is the chosen hour during which we eliminate the wage differential between high- and low-performing drivers. Figure 5 shows the absolute value of the elasticity of labor supply corresponding to the elimination of the wage differential at 12 PM. The blue line represents the low-performing drivers, while the red line represents the high-performing ones. The former are much more responsive to the elimination of the wage differential than the latter. This is because, on the one hand, high-performing drivers' labor supply is inelastic in all hours (less than 0.7). On the other, low-performing drivers' labor supply elasticities are higher than 0.9 in all hours and even higher than 1 in the hours near the treated hour. The absolute elasticity value generally decreases for hours further away from the treatment hour. This is because there is a high warm-up cost for starting to work, and adjacent hours of the treatment hour will thus be affected more. However, the absolute elasticity value does not monotonically decrease with respect to the distance to the treatment hour because of the variation in reservation values across the different hours of the day. Given that multiplehour labor supply responds to the wage differential at one particular hour, the platform can strategically choose when to provide high incentive wages. In Appendix I, we replicate this exercise by changing the treatment hour from 7 AM to 6 PM.

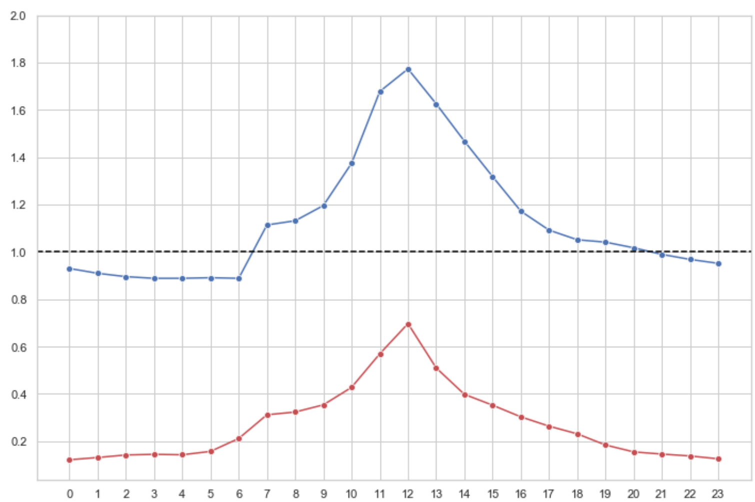


Figure 5: Elasticity of Labor Supply When Eliminating Wage Differential at 12 PM

Next, we show the welfare effects of eliminating the preferential algorithm. To examine how a preferential algorithm impacts passenger fares, we study two scenarios. First, we eliminate the wage differential among drivers but maintain the ride fares at the same level as when using a preferential algorithm. Second, we allow the platform to re-optimize its pricing strategy and change ride fares when the preferential algorithm is eliminated:[24]

$$\begin{aligned} \max_{\vec{P}} \quad & (1-\eta)\sum_t P_t D_t(P_t) \\ \text{s.t.} \quad & D_t(P_t) \leq \widetilde{\lambda}_t \mathcal{N}_t(\boldsymbol{W_t}; \boldsymbol{\theta}) \end{aligned} \tag{6}$$

Using the estimated parameters, we solve for the new equilibrium outcome if the platform can no longer implement algorithmic preferential wage-setting based on the work schedule. Then, we calculate the changes in platform revenue, consumer surplus, and driver surplus by comparing the outcome without the preferential algorithm to the outcome with it. We calculate consumer welfare as $\sum_t \int_{P_t}^{\infty} \delta_t x^{-\epsilon} dx$ and the driver surplus of each schedule j as

$$EV_0^j = \sigma \left[\ln \Big(\exp((\widetilde{W}_1 - \kappa + \beta EV_{12})/\sigma) + \exp((O_1 + \beta EV_{02})/\sigma) \Big) + \gamma \right],$$

[24]Note that the two feasibility constraints in equation 3 become one because all drivers have the same likelihood of receiving a task; $\widetilde{\lambda}_t$ is the technology restriction without algorithmic preferential wage-setting. Under "fair" pay, there is only one group, so $s = 1$.

where EV_0^j represents the expected value from choosing each work schedule type j.[25] Table 13 shows the results. In the first scenario, on the one hand, eliminating the preferential algorithm will result in a massive loss for both the platform and the rider because of a driver shortage. On the other, drivers enjoy more flexibility in choosing a work schedule under "fair" pay. Hence, there will be a 0.14% increase in driver surplus. High-performing drivers suffer a loss of 0.63% because there is no longer a bonus for being high-performing. Low-performing drivers see an increase in hourly wage, hence a 0.69% increase in surplus. In aggregate, the total surplus will decrease by 7.16% if we eliminate the preferential algorithm.

Table 13: Changes in Welfare

Changes in	The first scenario: Maintain ride fares unchanged	The second scenario: The platform re-optimizes ride fares
Platform revenue	-12.16%	-1.42%
Consumer surplus	-12.16%	-1.42%
Driver surplus	0.14%	0.49%
Total surplus	-7.16%	-0.64%
Decomposition of Per-Driver Surplus		
High-performing driver (non-switcher)	-0.63%	-0.16%
Low-performing driver (non-switcher)	0.69%	0.99%
Switcher (from H-type to L-type)	3.51%	3.81%
Change in Probability of being H-type	-11.48%	-9.98%

Notes: We calculate changes in welfare by measuring the results without a preferential algorithm minus the results with a preferential algorithm. In the first scenario, ride fares without a preferential algorithm are held the same as ride fares with a preferential algorithm. In the second scenario, the platform re-optimizes its pricing strategy without a preferential algorithm.

In the second scenario, the platform will re-optimize its pricing strategy, increasing ride fares to reduce the driver shortage that we see in the first scenario after eliminating the preferential algorithm. Ride fares, on average, increase by 7.79% across different hours of the day, with the highest increase being 12.16%. This increase in fares helps alleviate the driver shortage. As a result, the losses of the platform and riders will be smaller than in the first scenario, resulting in a total 1.42% decrease in surplus. Driver surplus will increase further, because drivers benefit in the second scenario from the increased ride fares. Total

[25] Note that consumer surplus $\sum_t \int_{P_t}^{\infty} \delta_t x^{-\epsilon} dx = \sum_t \frac{\delta_t}{\epsilon-1}(P_t)^{1-\epsilon} = \frac{1}{(\epsilon-1)(1-\eta)} \times$ platform revenue. In the first scenario, when ride fares are unchanged, the total number of riders served equals $\min\{D_t(P_t), \widetilde{\lambda}_t \mathcal{N}_t(\boldsymbol{W_t}; \boldsymbol{\theta})\}$.

driver surplus will hence increase by 0.49% if we eliminate the preferential algorithm. Low-performing drivers have a 1% increase in surplus because they benefit from more flexibility in working and a higher ride fare. Regarding the extensive margin, the probability of being high-performing decreases by 11.48 percentage points in the first scenario and 9.98 percentage points in the second. After we eliminate the preferential algorithm, the probability of being a high-performing driver slightly increases in the second scenario, as compared to the first. The total surplus will decrease by 0.64% if we eliminate the preferential algorithm.

Table 14: Change in Driver Surplus, by Groups of Drivers

Changes in Driver Surplus	Driver Group						
	Group 0	Group 1	Group 2	Group 3	Group 4	Group 5	Group 6
Panel I: Maintain ride fares unchanged							
Total	0.08%	0.05%	-0.36%	0.20%	-0.22%	0.00%	0.07%
H-Schedule	-0.41%	-0.43%	-0.50%	-0.14%	-0.44%	-0.38%	-0.42%
L-Schedule	0.35%	0.38%	0.86%	0.12%	0.57%	0.37%	0.36%
Panel II: The platform re-optimizes ride fares							
Total	0.29%	0.28%	-0.02%	0.22%	0.08%	0.23%	0.29%
H-Schedule	-0.14%	-0.15%	-0.17%	-0.04%	-0.13%	-0.12%	-0.14%
L-Schedule	0.54%	0.58%	1.19%	0.16%	0.86%	0.57%	0.56%

Notes: We calculate changes in welfare by results without a preferential algorithm minus results with a preferential algorithm. We characterize driver groups by unobserved heterogeneity.

Lastly, we look at how different groups of drivers are affected if we eliminate the preferential algorithm. We characterize driver groups by the unobserved heterogeneity types described in Section 6.2. Table 14 shows the results. First, we can see both winners and losers from eliminating the preferential algorithm. From the elimination of the preferential algorithm, driver groups 2 and 4 experience a decrease in their surpluses of 0.36% and 0.22%, respectively, in the first scenario, while all other driver groups experience an increase. The welfare loss of driver groups 2 and 4 occurs because they are more likely to be high-performing, and high-performing drivers will no longer earn extra hourly wages without the preferential algorithm. Previous results showed that drivers in groups 2 and 4 are likely to be high-performing with probabilities of 96.5% and 93.4%, respectively. Previous results also showed that among high performers, female or older drivers are more likely to fall into groups 2 and 4. Therefore, the counterfactual results indicate that women and older drivers who choose to be high-performing are more likely to suffer from eliminating the preferential algorithm. The general effect for female drivers is ambiguous, because women are also more likely to be low-performing, with a larger welfare gain from the elimination of the preferential algorithm. Non-locals are more likely to suffer a welfare loss if we eliminate the preferential algorithm because they are more likely to be high-performing. All other driver groups (younger, local, male) will benefit from its elimination.

In summary, the platform benefits from implementing a preferential algorithm by leveraging the cross-time labor supply elasticity. Without a change in ride fares, eliminating the preferential algorithm results in a significant welfare loss for both the platform and riders due to driver shortages. Drivers, on the other hand, experience an increase in surplus because of the increased flexibility when choosing their work schedule. If we allow the platform to re-optimize pricing, ride fares will significantly increase without a preferential algorithm. However, the driver shortage will also be mitigated, and welfare loss will be smaller for both the platform and riders. Drivers, meanwhile, will have an even greater increase in welfare because of increased ride fares. Among the different groups of drivers, those who are male, young, and local are more likely to benefit from the elimination of the preferential algorithm. Older drivers, conversely, are likely to experience a welfare loss. The net effect for female drivers is ambiguous, with a welfare loss for high-performing female drivers and a welfare gain for low-performing ones.

7.2 Factors Determining Preferential Algorithm Effectiveness

To further investigate what factors determine the effectiveness of the preferential algorithm, we conduct counterfactuals by alternating key structural parameters. We specifically focus on the demand elasticity ϵ and warm-up cost κ. Table 15 shows the results when we alter the value of demand elasticity. When demand is more elastic, the platform benefits more from utilizing the cross-time labor supply elasticity by implementing the preferential algorithm. Therefore, in column (1) of Table 15, we see a larger increase in platform revenue, from 1.44% to 2.89%, if the platform implements the preferential algorithm. On the other hand, drivers suffer less from the preferential algorithm if demand elasticity increases. Total driver surplus will decrease by 0.32% when demand is more elastic, compared to a decrease of 0.49% when demand is less elastic. Our intuition is that when demand is very elastic, the platform is less willing to incentivize labor supply by increasing ride fares; otherwise, there would be a large decrease in rider demand. Therefore, drivers will experience a smaller increase in wage rate when the platform eliminates the preferential algorithm. Equivalently, this means that drivers will experience a smaller decrease in wage rate, and hence driver surplus, when the platform implements a preferential algorithm. Column (4) of Table 15 confirms this intuition by showing that the average decrease in wage is smaller (5.03% versus 7.26%) when demand is more elastic. As a result, the loss of low-performing drivers decreases from 0.98% to 0.17%.

Table 15: Varying the Value of Demand Elasticity ϵ

	Changes in (With - Without)			
Demand Elasticity	Platform Revenue/ Consumer Surplus	Driver Surplus	Driver Surplus (Low-performing)	Average Wage
Benchmark	1.44%	-0.49%	-0.98%	-7.26%
$\epsilon \times 1.1$	2.13%	-0.47%	-0.52%	-6.55%
$\epsilon \times 1.2$	2.60%	-0.40%	-0.29%	-5.78%
$\epsilon \times 1.3$	2.89%	-0.32%	-0.17%	-5.03%

Next, we examine the effect of the warm-up cost κ. Table 16 shows the results when we vary the value of this factor. When the warm-up cost is higher, the platform must pay higher wages to incentivize drivers to work. Hence, it is more profitable for the platform to avoid paying such high incentive wages by implementing the preferential algorithm. On the other hand, saving these high incentive wages reduces the ride fare, and hence more riders can be served. Serving more riders also generates more hourly revenues for the drivers. As a result, the loss in driver surplus from the preferential algorithm will be smaller when the warm-up cost is larger. Column (4) of Table 15 confirms this intuition by showing that the change in the number of served riders is greater (9.76% versus 9.55%) when the warm-up cost is larger.[26]

Table 16: Varying the Value of Warm-up Cost κ

	Changes in (With - Without)			
Warm-up Cost	Platform Revenue/ Consumer Surplus	Driver Surplus	Driver Surplus (Low-performing)	Consumers Served
Benchmark	1.44%	-0.49%	-0.98%	9.55%
$\kappa \times 1.1$	1.45%	-0.49%	-0.93%	9.64%
$\kappa \times 1.2$	1.46%	-0.49%	-0.86%	9.71%
$\kappa \times 1.3$	1.47%	-0.48%	-0.79%	9.76%

[26]In the second case, when we alter the value of the warm-up cost κ, showing the change in average wage will not directly reveal how driver surplus changes, because driver utility depends on both the warm-up cost and the average wage. Instead, when demand elasticity is fixed in this case, the surplus of low-performing drivers will monotonically increase with respect to the number of riders served. Similarly, in the first case, when we alter the value of demand elasticity η, showing the change in the number of riders served will not directly reveal how driver surplus changes, because the number of riders served is determined by both the labor supply decision and demand elasticity. In this case, when the warm-up cost is fixed, the surplus of low-performing drivers will monotonically increase with respect to the average wage rate. This is why we report different variables in the last columns of Tables 15 and 16.

To summarize, the platform benefits more from implementing a preferential algorithm when the demand is more elastic or when the warm-up cost is greater. Meanwhile, the loss of driver surplus with a preferential algorithm is also smaller given these two conditions.

8 Conclusion

The rapid acceleration of algorithmic technologies has changed the relationship between workers and employers, and there is an urgent need to better understand the emerging challenges posed by these technologies. Our paper aims to provide the first empirical study of algorithmic wage-setting and its impact on worker behavior and welfare. Using rich transaction data from a leading ride-hailing company in Asia, we first document significant wage differentials due to work schedules between high-performing drivers who work long and consecutive hours and their low-performing counterparts. Here, labeling drivers as high- or low-performing is not a reflection of their efficiency or quality of work. It merely indicates that they have more or less committed work schedules and log more or fewer total hours on the platform. We show that three main factors drive the wage differential: high-performing drivers are given more ride requests per hour, wait fewer minutes for each request, and receive more requests from riders with lower cancellation rates. Next, we exclude alternative explanations for the wage differentials, such as drivers strategically choosing where to work, strategically selecting and canceling orders, driving faster, and having better knowledge of routes. The large wage differential we identify is mainly due to algorithmic wage-setting, which penalizes low-performing drivers. Our arguments highlight one important channel the literature has overlooked: a platform can balance demand and supply through utilizing the *cross-time* labor supply elasticity.

We then propose a dynamic equilibrium model of a ride-hailing market to quantify the welfare effects of such a preferential algorithm. Results show that platform revenues will decrease by 12.16%, while the total surplus will decrease by 7.16%, if ride fares are held constant when we eliminate the preferential algorithm. The probability of drivers being high-performing will decrease by 11.48% without a preferential algorithm. For the switchers, driver surplus will increase by 3.51%. If we allow the platform to re-optimize ride fares after eliminating the preferential algorithm, it will raise rider fares to re-balance demand and supply, resulting in minimal welfare loss. Moreover, an additional 10% of drivers would switch to flexible schedules. Among drivers, those who are young, male, and local benefit more from the elimination of the preferential algorithm. Lastly, our simulations show preferential algorithms benefit the platform more and hurt drivers less when rider demand is more elastic or when the warm-up cost is higher.

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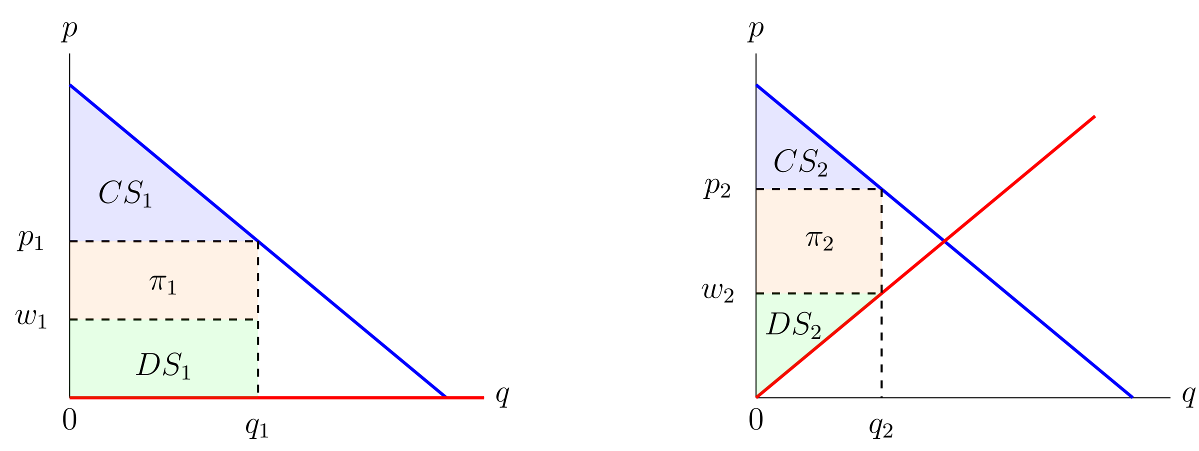
Appendix

A Preferential Algorithm and Surge Pricing

The platform benefits from both surge pricing and a preferential algorithm, although their mechanisms differ. To illustrate the contrasting ways surge pricing and the preferential algorithm operate and to showcase their potential complementarity, we use our theoretical model to solve equilibrium outcomes in the following four scenarios:

1. Without surge pricing or a preferential algorithm
2. With only surge pricing
3. With only the preferential algorithm
4. With both surge pricing and the preferential algorithm

As discussed in section 2, we consider a scenario with two time periods, denoted as t_1 and t_2. For both periods, we the demand to be $P_t^d = 10 - q$. During time period t_1, drivers have a reservation value of 0. During time period t_2, drivers have positive and heterogeneous reservation values, and the supply curve is defined as $P_{t_2}^s = q$.

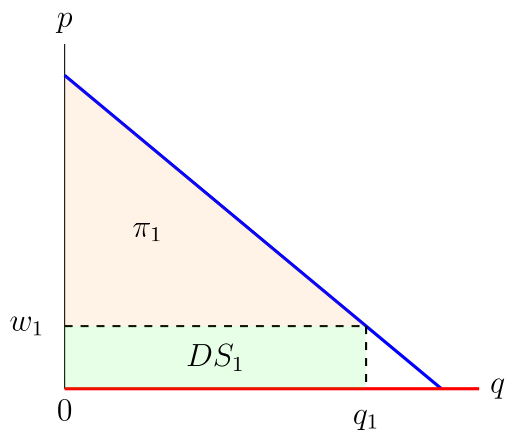


(a) t_1 (b) t_2

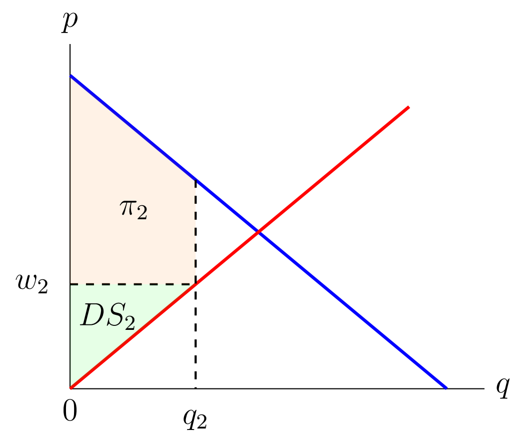
Figure A.1: Case 1, without surge pricing and preferential algorithm

In the baseline case, with neither surge pricing nor a preferential algorithm, the platform sets a price p_t for time period t, and drivers earn $w_t = (1 - \eta) * p_t$, where η represents the fractional commission fee. The platform's earnings in this case are $\eta * p_t * q_t$. For this numerical example, we assume $\eta = 0.5$. Figure A.1 shows the results for case 1. In both periods, the platform chooses the optimal ride fare p_t to maximize its profit. For the numerical example, the platform sets ride fares at $p_1^* = 5$ and $p_2^* = 6.67$, leading to wage rates of $w_1^* = 2.5$ and $w_2^* = 3.33$ for the drivers. The blue area in Figure A.1 represents the consumer surplus, the orange area represents the platform's profit, and the green area shows the drivers' surplus.

Figure A.2 shows the results for case 2, in which only surge pricing is implemented. With surge pricing, the platform captures the entire consumer surplus while offering a constant wage rate to the drivers in each period.[27] Consequently, in this scenario, the platform optimizes the wage rate to pay the drivers. In the given numerical example, the optimal wage rate is set at $w_1^* = w_{min} = 2$,[28] and $w_2 = 3.33$. The implementation of surge pricing results in a complete elimination of consumer surplus in both periods.



(a) t_1



(b) t_2

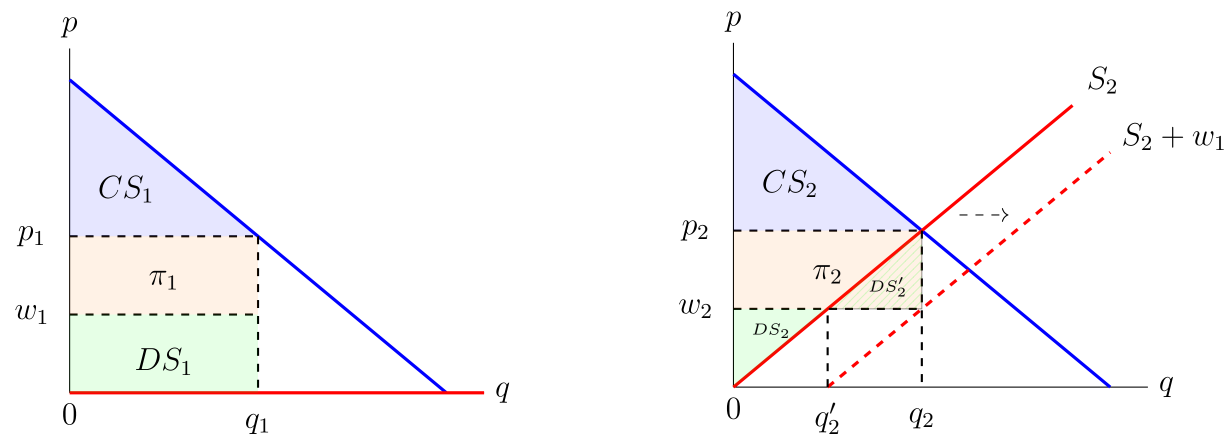
Figure A.2: Case 2, with only surge pricing

Figure A.3 shows the results for case 3, in which only the preferential algorithm is implemented. With a preferential algorithm, the platform communicates to drivers that if they work during time period t_2, they will be given priority and receive an order during time period t_1. Hence, the platform can motivate drivers to work during time period t_2 without

[27] Alternatively, we can use the same wage scheme as in case 1, where drivers receive a constant percentage of the ride fare as their payment. This would lead to a higher surplus for the drivers. However, to highlight the key trade-off and to simplify the model here, we opt for a constant wage rate in this context.

[28] The platform is unable to further decrease the wage rate at t_1 because of the minimum wage requirement, as explained in 2. Otherwise, the platform would charge $w_1^* = 0$ at t_1, resulting in no driver surplus during that period. Consequently, the implementation of the preferential algorithm on top of surge pricing would no longer be feasible. In this particular scenario, to enable a meaningful comparison between case 2 and case 4, it is necessary to ensure a positive drivers' surplus at t_1.

offering extra incentive wages. As a result, the labor supply curve is shifted outwards at t_2, as illustrated by the dashed red line. In this scenario, the optimal prices are $p_1^* = 5$ and $p_2^* = 5$, leading to $w_1^* = 2.5$ and $w_2^* = 2.5$, with the number of orders served being $q_1^* = 5$ and $q_2^* = 5$. However, with a wage rate of $w_2^* = 2.5$, some drivers actually earn a negative surplus at t_2. For drivers falling within the range of q_2' to q_2, the wage at t_2 is insufficient to cover their reservation values. Despite this, they are willing to work during this time period because they anticipate earning a positive surplus at t_1 with prioritized order assignment. The platform's profit at t_2 is represented by the orange rectangle π_2 in panel (b) of Figure A.3, which is $(p_2 - w_2) * q_2$. The driver surplus is equivalent to the green area $DS_2 - DS_2'$. The preferential algorithm serves to assist the platform in extracting additional driver surplus.



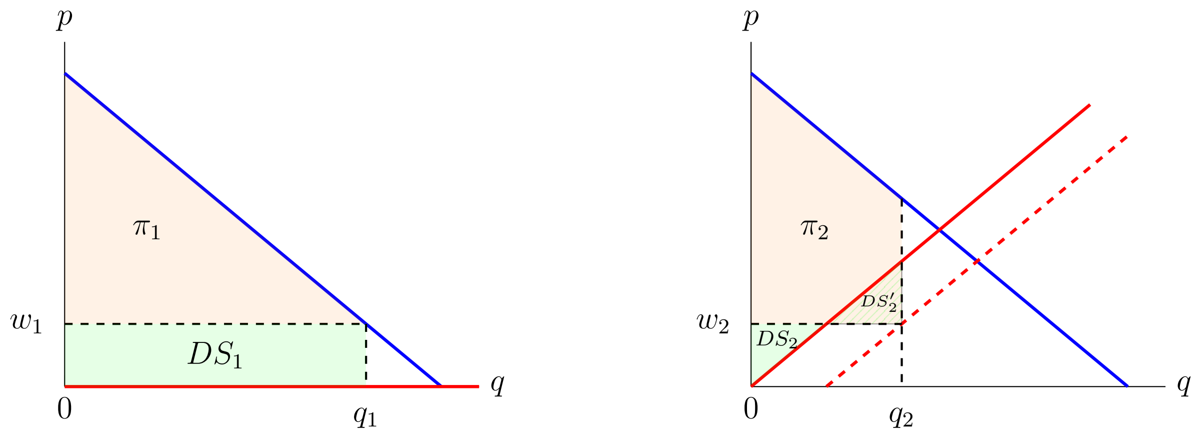
(a) t_1

(b) t_2

Figure A.3: Case 3, with only preferential algorithm

Figure A.4 shows the results for case 4, with both surge pricing and the preferential algorithm. First, similar to case 2, surge pricing allows the platform to capture the entire consumer surplus. Additionally, in case 4, the platform further leverages the preferential algorithm to incentivize drivers to work more. In Figure A.4, the platform's profit is denoted as π_1 and π_2, respectively, for time periods t_1 and t_2, while driver surplus is DS_1 during time period t_1 and $DS_2 - DS_2'$ during time period t_2.

We proceed to compare the equilibrium outcomes in each scenario. Table A.1 provides a summary of the equilibrium profit of the platform, the ride fare, the wage rate, and the quantity served for each scenario. On the other hand, Table A.2 shows the consumer surplus, driver surplus, and total surplus for the respective scenarios. We refer to the scenario with neither the preferential algorithm nor surge pricing as the benchmark case (case 1). When comparing the results of case 2 with the benchmark case, we can see that by implementing



(a) t_1 (b) t_2

Figure A.4: Case 4, with both surge pricing and preferential algorithm

surge pricing, the platform serves more consumers during t_1. While drivers experience a lower wage rate at t_1, the total drivers' surplus increases from 12.5 to 16 due to the higher number of orders served. Consequently, with the implementation of surge pricing, although the entire consumer surplus is captured by the platform, drivers also benefit from a higher driver surplus.

Table A.1: Equilibrium Outcomes

	Platform's profit		Price		Wage rate		Quantity	
	t_1	t_2	t_1	t_2	t_1	t_2	t_1	t_2
Case 1: No algorithm, no surge	12.50	11.11	5.00	6.67	2.50	3.33	5.00	3.33
Case 2: Only surge pricing	32.00	16.67	/	/	2.00	3.33	8.00	3.33
Case 3: Only algorithm	12.50	12.50	5.00	5.00	2.50	2.50	5.00	5.00
Case 4: Both surge and algorithm	32.00	24.00	/	/	2.00	2.00	8.00	4.00

Table A.2: Comparing Surplus

	Driver Surplus		Consumer Surplus		Total Surplus
	t_1	t_2	t_1	t_2	$t_1 + t_2$
Case 1: No algorithm, no surge	12.50	5.56	12.50	5.56	59.72
Case 2: Only surge pricing	16.00	5.56	0.00	0.00	70.22
Case 3: Only algorithm	12.50	0.00	12.50	12.50	62.50
Case 4: Both surge and algorithm	16.00	0.00	0.00	0.00	72.00

When comparing case 3, where only the preferential algorithm is implemented, with the benchmark case, we can see that the platform now charges lower ride fares and pays lower wage rates during t_2. Consequently, the driver surplus is reduced upon the introduction of the preferential algorithm. However, consumers also benefit from the lower ride fares during t_2, resulting in an increase in consumer surplus.

Lastly, in case 4, we examine the outcomes when both surge pricing and a preferential algorithm are implemented. When comparing case 4 with case 2, we observe that the platform not only captures the entire consumer surplus but also further extracts driver surplus by introducing the preferential algorithm. As a consequence, the total driver surplus decreases from 21.56 to 16. On the other hand, when comparing case 4 with case 3, we observe that after implementing the preferential algorithm, the additional introduction of surge pricing actually leads to an increase in driver surplus. This is because the platform serves more consumers, leading to drivers benefiting from the increased demand. Consequently, the total driver surplus increases from 12.5 to 16 between case 3 and case 4.

In summary, the findings show that both surge pricing and the preferential algorithm help increase the platform's profit, but they operate through distinct mechanisms. By implementing surge pricing, the consumer surplus is reduced as compared to the baseline scenario; however, both the platform's profits and the drivers benefit from this strategy. On the other hand, implementing the preferential algorithm may decrease driver surplus as compared to the baseline scenario, but it also leads to improved profitability for the platform and greater benefits for consumers. The results from case 4 demonstrate the complementarity between surge pricing and the preferential algorithm. When both methods are implemented, the platform's profit is the highest, and the total surplus is also maximized. This highlights the strong synergy between surge pricing and the preferential algorithm in achieving the best overall outcomes for the platform. However, this combination also results in a significant distributional effect, leading to a reduction in both consumer and driver surplus when compared to the baseline scenario.

B Drivers' Finite-Horizon Dynamic Problem

This appendix describes in detail drivers' finite-horizon dynamic choices. For each hour t, the utility of working and not working are specified as

$$\begin{aligned} U_{1t}^{\tau} &= \underbrace{W_t^{\tau}}_{\text{preferential wage rate}} + \sigma \cdot \epsilon_{1t}, \\ U_{0t}^{\tau} &= \underbrace{O_t^{\iota}}_{\substack{\text{outside option value,} \\ O_t^{\iota} = O_t + \eta_{\iota,t}}} + \sigma \cdot \epsilon_{0t}, \end{aligned} \tag{B.1}$$

Drivers first observe random shocks ϵ, then decide whether to work. To keep things straightforward, we leave out the hyperscript ι when referring to O_t^{ι} in the derivations below.

B.1 Low-Performing Drivers

For the final period, $t = T$,

$$V_T^L = \begin{cases} W_T^L + \sigma \cdot \epsilon_{1T} & \text{if } a_T = 1 \ \& \ a_{T-1} = 1, \\ W_T^L - \kappa + \sigma \cdot \epsilon_{1T} & \text{if } a_T = 1 \ \& \ a_{T-1} = 0, \\ O_T + \sigma \cdot \epsilon_{0T} & \text{if } a_T = 0. \end{cases}$$

So, the expected utility for the last period T is

$$\begin{aligned} EV_{1T}^L &= \sigma \left[\ln \Big(\exp(W_T^L/\sigma) + \exp(O_T/\sigma) \Big) + \gamma \right], \\ EV_{0T}^L &= \sigma \left[\ln \Big(\exp((W_T^L - \kappa)/\sigma) + \exp(O_T/\sigma) \Big) + \gamma \right]. \end{aligned}$$

Throughout our model, EV's subscript 1 represents $a_{t-1} = 1$. In this case, EV_{1T}^L represents the expected value of a low-performing driver at time T if $a_{T-1} = 1$.

At any time $t \in [T-1, 2]$,

$$V_t^L = \begin{cases} W_t^L + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^L & \text{if } a_t = 1 \ \& \ a_{t-1} = 1, \\ W_t^L - \kappa + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^L & \text{if } a_t = 1 \ \& \ a_{t-1} = 0, \\ O_t + \sigma \cdot \epsilon_{0t} + \beta EV_{0t+1}^L & \text{if } a_t = 0. \end{cases}$$

So, the expected utility of period t is

$$EV_{1t}^{L} = \sigma\left[\ln\left(\exp((W_t^L + \beta EV_{1t+1}^{L})/\sigma) + \exp((O_t + \beta EV_{0t+1}^{L})/\sigma)\right) + \gamma\right],$$
$$EV_{0t}^{L} = \sigma\left[\ln\left(\exp((W_t^L - \kappa + \beta EV_{1t+1}^{L})/\sigma) + \exp((O_t + \beta EV_{0t+1}^{L})/\sigma)\right) + \gamma\right].$$

For the first period, $t = 1$,

$$V_1^L = \begin{cases} W_1^L - \kappa + \sigma \cdot \epsilon_{11} + \beta EV_{12}^L & \text{if } a_1 = 1, \\ O_1 + \sigma \cdot \epsilon_{01} + \beta EV_{02}^L & \text{if } a_1 = 0. \end{cases}$$

The expected value of being a low-performing driver is then

$$EV^L = \sigma\left[\ln\left(\exp((W_1^L - \kappa + \beta EV_{12}^L)/\sigma) + \exp((O_1 + \beta EV_{02}^L)/\sigma)\right) + \gamma\right]. \tag{B.2}$$

B.2 High-Performing Drivers

High-performing drivers are required to work at T_0 and for at least 2 consecutive hours. T_0 can be any hour between 10AM–2PM or 7PM–5AM. There are 16 possible work schedules to choose from. For schedule $j \in \{1, \cdots, 16\}$, with committed working hours $[T_0, T_0+1]$,

if $T_0 + 2 < T$, then for the last period T,

$$V_T^j = \begin{cases} W_T^H + \sigma \cdot \epsilon_{1T} & \text{if } a_T = 1 \ \& \ a_{T-1} = 1, \\ W_T^H - \kappa + \sigma \cdot \epsilon_{1T} & \text{if } a_T = 1 \ \& \ a_{T-1} = 0, \\ O_T + \sigma \cdot \epsilon_{0T} & \text{if } a_T = 0. \end{cases}$$

The expected utility of period T is

$$EV_{1T}^{j} = \sigma\left[\ln\left(\exp(W_T^H/\sigma) + \exp(O_T/\sigma)\right) + \gamma\right],$$
$$EV_{0T}^{j} = \sigma\left[\ln\left(\exp((W_T^H - \kappa)/\sigma) + \exp(O_T/\sigma)\right) + \gamma\right].$$

At $t \in [T_0 + 3, T - 1]$,

$$V_t^j = \begin{cases} W_t^H + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^j & \text{if } a_t = 1 \ \& \ a_{t-1} = 1, \\ W_t^H - \kappa + \sigma \cdot \epsilon_{1t} + \beta EV_{1t+1}^j & \text{if } a_t = 1 \ \& \ a_{t-1} = 0, \\ O_t + \sigma \cdot \epsilon_{0t} + \beta EV_{0t+1}^j & \text{if } a_t = 0. \end{cases}$$

The expected utility of period $t \in [T_0+3, T-1]$ is

$$EV_{1t}^j = \sigma \left[\ln \Big(\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma) \Big) + \gamma \right],$$
$$EV_{0t}^j = \sigma \left[\ln \Big(\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma) \Big) + \gamma \right].$$

At time T_0+2, because the driver commits to work at T_0 and T_0+1, $a_{T0+1} = 1$ with probability 1,

$$V_{T_0+2}^j = \begin{cases} W_{T_0+2}^H + \sigma \cdot \epsilon_{1T_0+2} + \beta EV_{1T_0+3}^j & \text{if } a_{T_0+2} = 1, \\ O_{T_0+2} + \sigma \cdot \epsilon_{0T_0+2} + \beta EV_{0T_0+3}^j & \text{if } a_{T_0+2} = 0. \end{cases}$$

At T_0+1, the high-performing driver has to work. The expected value at any T_0+1 is

$$EV_{1T_0+1}^j = W_{T_0+1}^H + \beta EV_{1T_0+2}^j + \sigma\gamma.$$

At period T_0, the expected value is

$$EV_{1T_0}^j = W_{T_0}^H + \beta EV_{1T_0+1}^j + \sigma\gamma,$$
$$EV_{0T_0}^j = W_{T_0}^H - \kappa + \beta EV_{1T_0+1}^j + \sigma\gamma.$$

At any time before T_0, $t \in [2, T_0-1]$, the expected utility is

$$EV_{1t}^j = \sigma \left[\ln \Big(\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma) \Big) + \gamma \right],$$
$$EV_{0t}^j = \sigma \left[\ln \Big(\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma) \Big) + \gamma \right].$$

For period 1,

$$V_1^j = \begin{cases} W_1^H - \kappa + \sigma \cdot \epsilon_{11} + \beta EV_{12}^j & \text{if } a_1 = 1, \\ O_1 + \sigma \cdot \epsilon_{01} + \beta EV_{02}^j & \text{if } a_1 = 0. \end{cases}$$

The expected value of being a high-performing driver is then

$$EV^j = \sigma \left[\ln \Big(\exp((W_1^H - \kappa + \beta EV_{12}^j)/\sigma) + \exp((O_1 + \beta EV_{02}^j)/\sigma) \Big) + \gamma \right]. \tag{B.3}$$

C Identification and Estimation

C.1 Identification

We start with the case without UH, so that $O_t^\iota = O_t$. Denote $P_t^\tau(a_T = a|a_{T-1} = b) = P_t^\tau(a|b)$, where $a, b = 0, 1$ and $\tau = L, H$. We have

$$\log P_T^L(1|1) - \log P_T^L(0|1) = \frac{W_T^L - O_T}{\sigma}, \tag{C.1}$$

$$\log P_T^L(1|0) - \log P_T^L(0|0) = \frac{W_T^L - O_T - \kappa}{\sigma}, \tag{C.2}$$

which implies that

$$\frac{\kappa}{\sigma} = [\log P_T^L(1|1) - \log P_T^L(0|1)] - [\log P_T^L(1|0) - \log P_T^L(0|0)]. \tag{C.3}$$

Similarly, H-type drivers have

$$\log P_T^H(1|1) - \log P_T^H(0|1) = \frac{W_T^H - O_T}{\sigma}, \tag{C.4}$$

$$\log P_T^H(1|0) - \log P_T^H(0|0) = \frac{W_T^H - O_T - \kappa}{\sigma}. \tag{C.5}$$

Combining (C.1) and (C.4) gives

$$\sigma = \frac{W_T^H - W_T^L}{[\log P_T^H(1|1) - \log P_T^H(0|1)] - [\log P_T^L(1|1) - \log P_T^L(0|1)]}, \tag{C.6}$$

which implies that κ is identified by following (C.3)

$$\kappa = (W_T^H - W_T^L)\frac{[\log P_T^L(1|1) - \log P_T^L(0|1)] - [\log P_T^L(1|0) - \log P_T^L(0|0)]}{[\log P_T^H(1|1) - \log P_T^H(0|1)] - [\log P_T^L(1|1) - \log P_T^L(0|1)]}$$

and O_T is identified by following (C.1) or (C.4)

$$O_T = W_T^L - (W_T^H - W_T^L)\frac{\log P_T^L(1|1) - \log P_T^L(0|1)}{[\log P_T^H(1|1) - \log P_T^H(0|1)] - [\log P_T^L(1|1) - \log P_T^L(0|1)]}.$$

When there is no UH, we have three unknown parameters O_T, σ, κ and four equations that capture the observed CCPs $P_T^\tau(1|a_{T-1})$, where $a_{T-1} = 0, 1$ and $\tau = L, H$. Note that $P_T^\tau(1|a_{T-1})$ and the above defined odd ratios $P_T^\tau(1|a_{T-1})/P_T^\tau(0|a_{T-1})$ capture the same amount of identifying information because $P_T^\tau(1|a_{T-1}) + P_T^\tau(0|a_{T-1}) = 1$. The system is overidentified using just the last period, which is clear because our identification steps do not involve (C.5).

When there is UH, we assume that

$$O_t^\iota = O_t + \eta_{\iota,t},$$

where $\eta_{\iota,t}$ represents time-interval-specific preference. Considering data from the last period, we have five unknown parameters $O_T, \eta_{(5)}, p_{(5)}, \sigma, \kappa$, where (5) denotes the 5-th UH type, and again four equations that capture the observed CCPs $P_T^\tau(1|a_{T-1})$, where $a_{T-1} = 0, 1$ and $\tau = L, H$. Obviously, data from the last period are insufficient for point identification. Combining the last two periods, we have six unknown parameters $O_T, O_{T-1}, \eta_{(5)}, p_{(5)}, \sigma, \kappa$ and eight equations. More specifically, the eight equations represent the observed CCPs $\overline{P}_t^\tau(1|a_{t-1}) = (1 - p_{(5)})P_t^\tau(1|a_{t-1}) + p_{(5)}P_{t,(5)}^\tau(1|a_{t-1})$, where $a_{t-1} = 0, 1$, $t = T - 1, T$, and $\tau = L, H$, relate to the unknown parameters. In particular,

$$\overline{P}_T^\tau(1|a_{T-1}) =(1 - p_{(5)})\frac{\exp(\frac{W_T^\tau - \kappa 1(a_{T-1}=0)}{\sigma})}{\exp(\frac{W_T^\tau - \kappa 1(a_{T-1}=0)}{\sigma}) + \exp(\frac{O_T}{\sigma})} \tag{C.7}$$

$$+ p_{(5)}\frac{\exp(\frac{W_T^\tau - \kappa 1(a_{T-1}=0)}{\sigma})}{\exp(\frac{W_T^\tau - \kappa 1(a_{T-1}=0)}{\sigma}) + \exp(\frac{O_T + \eta_{(5)}}{\sigma})}, \tag{C.8}$$

$$\overline{P}_{T-1}^\tau(1|a_{T-2}) =(1 - p_{(5)})\frac{\exp(\frac{W_{T-1}^\tau - \kappa 1(a_{T-2}=0) + \beta EV_{1T}^\tau}{\sigma})}{\exp(\frac{W_{T-1}^\tau - \kappa 1(a_{T-2}=0) + \beta EV_{1T}^\tau}{\sigma}) + \exp(\frac{O_{T-1} + \beta EV_{0T}^\tau}{\sigma})} \tag{C.9}$$

$$+ p_{(5)}\frac{\exp(\frac{W_{T-1}^\tau - \kappa 1(a_{T-2}=0) + \beta EV_{1T}^{\tau,(5)}}{\sigma})}{\exp(\frac{W_{T-1}^\tau - \kappa 1(a_{T-2}=0) + \beta EV_{1T}^{\tau,(5)}}{\sigma}) + \exp(\frac{O_{T-1} + \eta_{(5)} + \beta EV_{0T}^{\tau,(5)}}{\sigma})}, \tag{C.10}$$

where the expected utility for the last period T is given by

$$EV_{a_{T-1}T}^\tau = \sigma\left[\ln\Big(\exp(\frac{W_T^\tau - \kappa 1(a_{T-1} = 0)}{\sigma}) + \exp(\frac{O_T}{\sigma})\Big) + \gamma\right],$$
$$EV_{a_{T-1}T}^{\tau,(5)} = \sigma\left[\ln\Big(\exp(\frac{W_T^\tau - \kappa 1(a_{T-1} = 0)}{\sigma}) + \exp(\frac{O_T + \eta_{(5)}}{\sigma})\Big) + \gamma\right].$$

Note that $\overline{P}_t^\tau(0|a_{t-1}) = 1 - \overline{P}_t^\tau(1|a_{t-1})$ does not provide additional identification power.

We can continue the identification process backward and identify all the remaining parameters. In summary, we can identify the model with UH as long as each type involves at least two periods.

C.2 Estimation

We follow our identification argument closely in estimating the model. For each hour t, the utility of working and not working are

$$
\begin{aligned}
U_{1t}^{\tau} &= W_t^{\tau} + \sigma \cdot \epsilon_{1t}, \\
U_{0t}^{\tau} &= O_t^{\iota} + \sigma \cdot \epsilon_{0t} \\
&= O_t + \eta_{\iota,t} + \sigma \cdot \epsilon_{0t}.
\end{aligned}
$$

We use π_ι to denote the probability of individual driver i being the unobserved type ι. We make use of observed conditional choice probabilities to estimate the structural parameters. First, we derive the conditional choice probability of working for each type of driver. To keep things straightforward, we leave out the hyperscript ι when referring to O_t^{ι} in the derivations below.

Low-performing Drivers

For the final period T, the conditional probability of working for each unobserved type ι is

$$
\begin{aligned}
P^L(a_T = 1 | a_{T-1} = 1, \iota) &= \frac{\exp(W_t^L/\sigma)}{\exp(W_t^L/\sigma) + \exp(O_T/\sigma)}, \\
P^L(a_T = 1 | a_{T-1} = 0, \iota) &= \frac{\exp((W_t^L - \kappa)/\sigma)}{\exp((W_t^L - \kappa)/\sigma) + \exp(O_T/\sigma)}.
\end{aligned}
$$

For any $t \in [2, T-1]$,

$$
\begin{aligned}
P^L(a_t = 1 | a_{t-1} = 1, \iota) &= \frac{\exp((W_t^L + \beta EV_{1t+1}^L)/\sigma)}{\exp((W_t^L + \beta EV_{1t+1}^L)/\sigma) + \exp((O_t + \beta EV_{0t+1}^L)/\sigma)}, \\
P^L(a_t = 1 | a_{t-1} = 0, \iota) &= \frac{\exp((W_t^L - \kappa + \beta EV_{1t+1}^L)/\sigma)}{\exp((W_t^L - \kappa + \beta EV_{1t+1}^L)/\sigma) + \exp((O_t + \beta EV_{0t+1}^L)/\sigma)}.
\end{aligned}
$$

For $t = 1$,

$$
P^L(a_1 = 1, \iota) = \frac{\exp((W_1^L - \kappa + \beta EV_{12}^L)/\sigma)}{\exp((W_1^L - \kappa + \beta EV_{12}^L)/\sigma) + \exp((O_1 + \beta EV_{02}^L)/\sigma)}.
$$

Therefore, at any t, the conditional probability for low-performing drivers is

$$\begin{aligned} P^L(a_t = 1|a_{t-1} = 0) &= \sum_\iota \pi_\iota \cdot P^L(a_t = 1|a_{t-1} = 0, \iota), \\ P^L(a_t = 1|a_{t-1} = 1) &= \sum_\iota \pi_\iota \cdot P^L(a_t = 1|a_{t-1} = 1, \iota). \end{aligned} \tag{C.11}$$

High-performing Drivers

For any schedule $j \in \{1, \cdots, 16\}$, the conditional probability of working in the final period T is

$$\begin{aligned} P^j(a_T = 1|a_{T-1} = 1, \iota) &= \frac{\exp(W_t^H/\sigma)}{\exp(W_t^H/\sigma) + \exp(O_T/\sigma)}, \\ P^j(a_T = 1|a_{T-1} = 0, \iota) &= \frac{\exp((W_t^H - \kappa)/\sigma)}{\exp((W_t^H - \kappa)/\sigma) + \exp(O_T/\sigma)}. \end{aligned}$$

For any $t \in [T_0 + 3, T - 1]$, we have

$$\begin{aligned} P^j(a_t = 1|a_{t-1} = 1, \iota) &= \frac{\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma)}{exp((W_t^H + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma)}, \\ P^j(a_t = 1|a_{t-1} = 0, \iota) &= \frac{\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma)}{\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma)}. \end{aligned}$$

At $t = T_0 + 2$, we have

$$P^j(a_t = 1|a_{t-1} = 1, \iota) = \frac{\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma)}{\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma)}.$$

At $t = T_0 + 1$, we have

$$P^j(a_t = 1|a_{t-1} = 1, \iota) = 1.$$

At $t = T_0$, we have

$$\begin{aligned} P^j(a_t = 1|a_{t-1} = 1, \iota) &= 1, \\ P^j(a_t = 1|a_{t-1} = 0, \iota) &= 1. \end{aligned}$$

For any $t \in [2, T_0 - 1]$, we have

$$P^j(a_t = 1|a_{t-1} = 1, \iota) = \frac{\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma)}{\exp((W_t^H + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma)},$$
$$P^j(a_t = 1|a_{t-1} = 0, \iota) = \frac{\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma)}{\exp((W_t^H - \kappa + \beta EV_{1t+1}^j)/\sigma) + \exp((O_t + \beta EV_{0t+1}^j)/\sigma)}.$$

At $t = 1$, we have

$$P^j(a_1 = 1, \iota) = \frac{\exp((W_1^H - \kappa + \beta EV_{12}^j)/\sigma)}{\exp((W_1^H - \kappa + \beta EV_{12}^j)/\sigma) + \exp((O_1 + \beta EV_{02}^j)/\sigma)}.$$

Therefore, at any t, the conditional probability for high-performing drivers is

$$\begin{aligned} P^H(a_t = 1|a_{t-1} = 0) &= \sum_{\iota} \sum_{j=1}^{16} \pi_\iota \cdot \widetilde{P}^j(\iota) \cdot P^j(a_t = 1|a_{t-1} = 0, \iota), \\ P^H(a_t = 1|a_{t-1} = 1) &= \sum_{\iota} \sum_{j=1}^{16} \pi_\iota \cdot \widetilde{P}^j(\iota) \cdot P^j(a_t = 1|a_{t-1} = 1, \iota), \end{aligned} \tag{C.12}$$

where $\widetilde{P}^j$ is the probability of choosing each high-performing schedule, and

$$\widetilde{P}^j(\iota) = \frac{\exp(EV^j(\iota))}{\sum_{k=1}^{16} \exp(EV^k(\iota))}.$$

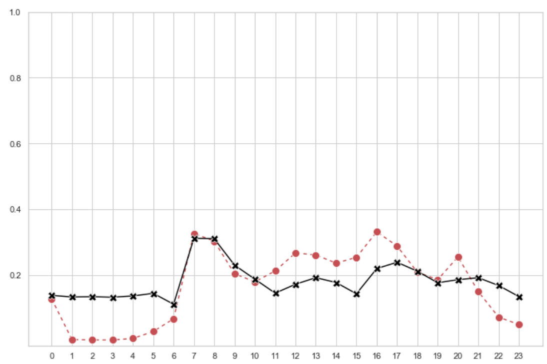
We estimate the model by minimizing the weighted distance between the data moments and the simulated moments of the finite mixture model:

$$\{\hat{\theta}, \hat{\pi}\} = arg \min_{\theta, \pi} \quad [\boldsymbol{P^\tau} - \widehat{\boldsymbol{P}}^{\boldsymbol{\tau}}(\theta, \pi)]' W [\boldsymbol{P^\tau} - \widehat{\boldsymbol{P}}^{\boldsymbol{\tau}}(\theta, \pi)].$$

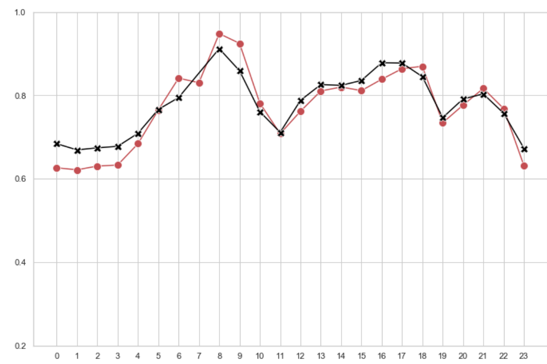
Here, W represents a positive definite matrix. The vector $\boldsymbol{P^\tau}$ contains the actual conditional choice probabilities (CCPs) derived from the data. This vector is of dimension 96-by-1 and includes the conditional probabilities of the different choices for each time period t. Specifically, $P^H(a_t = 1|a_{t-1} = 0), P^H(a_t = 1|a_{t-1} = 1), P^L(a_t = 1|a_{t-1} = 0), P^H(a_t = 1|a_{t-1} = 0)$. Additionally, $\widehat{\boldsymbol{P}}^{\boldsymbol{\tau}}$ denotes a vector containing simulated conditional choice probabilities, calculated based on equations C.11 and C.12.

D Model Validation

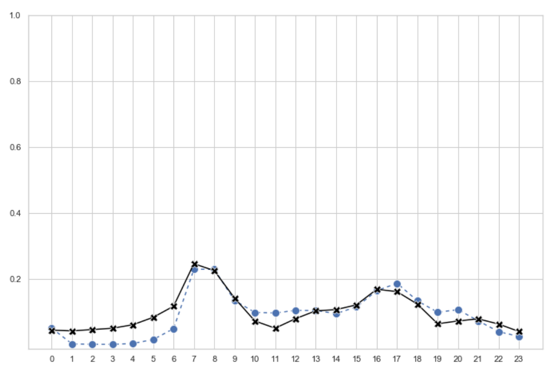
Figure D.1 illustrates the model's goodness of fit. The simulated conditional choice probabilities (CCPs) reasonably align with the observed CCPs for both high- and low-performing drivers. However, there is a slight discrepancy in the fit of high-performing drivers at $a_{t-1} = 0$ during early morning hours. This discrepancy could be attributable to the relatively low number of transactions occurring during this period, as compared to other working hours.



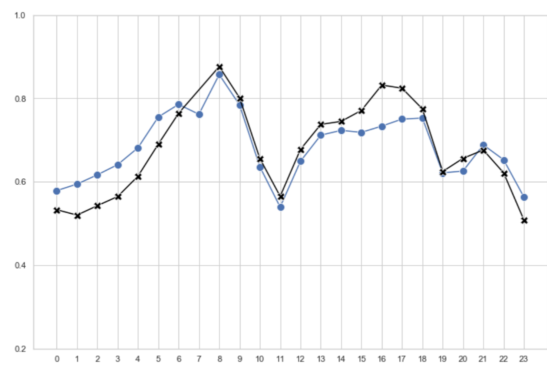
(a) High-performing Drivers, State = 0



(b) High-performing Drivers, State = 1



(c) Low-performing Drivers, State = 0



(d) Low-performing Drivers, State = 1

Figure D.1: Model Goodness of Fit

Note: Figure D.1 shows the model's simulated values against the empirically observed CCPs. The black lines represent the model's simulated values.

Online Appendices: Not for Publication

E Data Description

For the working dataset, we are interested in driver operation and wage information, and we construct several important variables for each driver-hour:

- **Earning time** is the trip duration, measured as the amount of time a driver spends with the rider. A driver can transport riders and collect revenue only during their earning time.
- **Drive Distance** measures the distance over which a driver serves a rider in an hour.
- **Driver's Hourly Wage** measures the revenue of a driver in an hour.[29] Given that the platform fee is around 20% of revenue, the driver income is roughly 80% of the ride fare.
- **Pickup Time** measures the time a driver spends on the way to pick up riders.
- **Idle Time** is the time a driver spends waiting for orders in an hour, given by the following relationship: Idle time = 60 - Work time - Pickup time.
- **Number of Orders** measures the number of orders a driver receives in an hour.[30]

Below, we discuss our algorithm for how to construct a driver-hour level dataset from the driver-rider-order level dataset:

- **Drop Outliers.** We keep all orders with a departure and arrival in the urban area (eight districts) within the city, and drop orders with a price of zero, those with a price above 200, or those that span over four hours. In total, we drop less than 0.5% of the observations.
- **Construct Work Schedules.** Following Chen et al. (2019), we define a driver as working during an hour t if he works at least ten minutes out of that hour. At night (22PM–6AM), when orders are sparse, we define a driver as working during hour t if they work at hour $t-1$ and hour $t+1$. All a driver's working hours comprise their work schedule.

[29] Our definition is different from that of Chen et al. (2019), who define "wage rate" as a driver's total earnings in an hour, divided by minutes worked, multiplied by sixty. In other words, they study the wage rate when the driver is driving a rider, and we focus on the wage rate when the driver is active on the platform.

[30] In rare cases, an order may span several hours, which we attribute to the hour of departure.

- **Match Order to Hour.** Suppose an order spans x hours. We divide this order into x sub-orders, with each sub-order corresponding to an hour. The hourly wage rate and driving distance are defined as proportional to each hour. For instance, suppose an order starts at 8:50 and finishes at 9:20, yielding a revenue of 60 CCY. We say that $\frac{10}{10+20} = \frac{1}{3}$ of the order belongs to the 8 AM operations, and the rest contributes to the 9 AM operations. By doing so, we divide this order into two sub-order operations: The driver drives 10 minutes and earns 20 CCY at 8 AM and drives 20 minutes (10 miles) and makes 40 CCY at 9 AM. After matching orders to hours, we aggregate all sub-orders in an hour and obtain the given driver's earning time, ride prices, pickup time, idle time, and number of orders during this hour.

F Summary Statistics: Orders and Transactions

Table F.1 summarizes orders and transactions; the unit of observation is at the order level. There are around 15 million total order transactions in our sample period, with an average route length of 6.9 km and drive time of 17 minutes. The average price per order is 25.31 CCY (about $4 USD).

Table F.1: Summary Statistics: Orders and Transactions

Variable	Mean	Std. Dev.	Min	Max
Price	25.31	26.44	0	3,387
Drive Distance (km)	6.92	6.85	0	727
Drive Time (minutes)	17.36	13.14	0	1,458
Number of Observations		14,471,573		

Multi-Homing versus Single-Homing. In our main analysis, we focus on Platform X, because it accounts for more than 90% of China's mainland ride-hailing market. Nonetheless, there is a concern that drivers may switch between working for different platforms if they pay different hourly wages. To address such concerns, we document the number of vehicles/drivers that are multi-homed versus those that are single-homed in our data. First, we look at the number of vehicles that are multi-homed based on registration data. Panel (a) of Table F.2 shows that 85% of vehicles are registered to only one platform, while only 1.8% of vehicles are registered to more than two platforms. Therefore, multi-homing is not very common, based on vehicle registration information. Then, we look at how common multi-homing is directly from actual transactions. Panel (b) of Table F.2 shows that among all the vehicles that conducted business in December 2018, 92.5% used a single platform and never switched to another platform within the month. Only 0.3% of vehicles used more than two platforms in this month. The evidence shows that the majority of vehicles/drivers are single-homed.

Table F.2: Multi-Homing versus Single-Homing

Number of Registered Platforms	Number of Vehicles	Percent
1	86,422	84.6%
2	13,838	13.5%
3	1,866	1.8%

(a) Based on Vehicle Registration Data

Number of Used Platforms	Number of Vehicles	Percent
1	49,213	92.5%
2	3,836	7.2%
3	141	0.3%

(b) Based on Transactional Data

Among the multi-homed drivers, we further study how these drivers switch between different ride-sharing platforms, as well as calculating the number of multi-homed and single-homed drivers within a whole day, based on actual transactions. In any given day of December, only about 1% of drivers used more than one platform. This suggests that drivers in our data are mostly single-homed and rarely switch between platforms.

Orders, Transactions, Precipitation, and Temperature. Figure F.1 reports the daily number of orders and transactions during our sample period (10 days of order data and 31 days of transaction data). We compare these with daily precipitation and average temperatures. From December 6 to 10, the precipitation increases and the temperature decreases, resulting in more ride orders (customer demand). However, the number of completed transactions across days remains the same throughout our sample period. We use information about precipitation and temperature in our demand estimation.

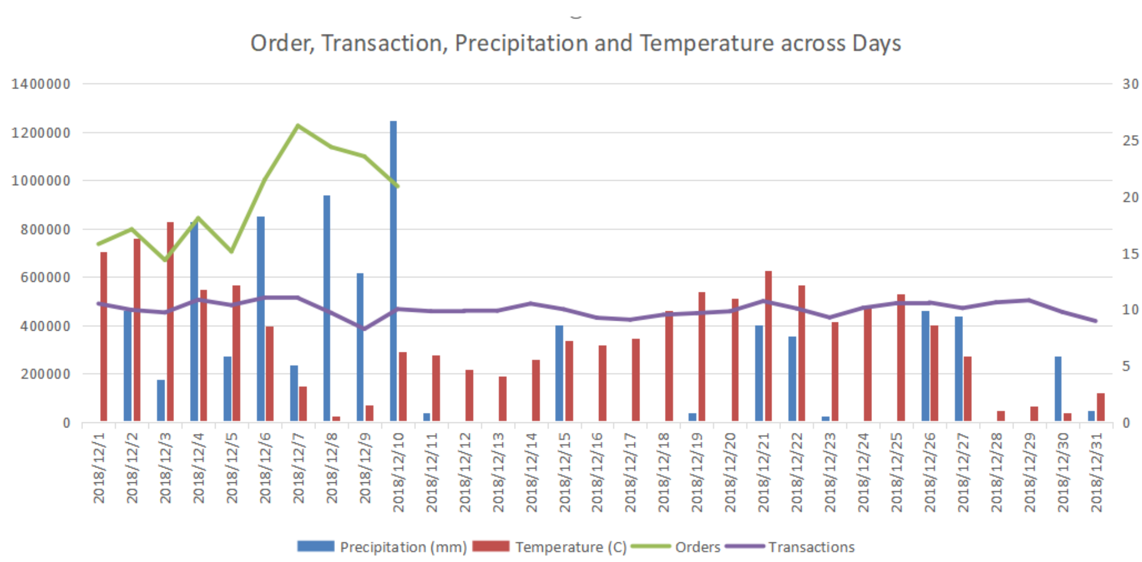


Figure F.1: Orders, Transactions, Precipitation, and Temperature across Days

G Cluster Schedules and Hourly Rates

This online appendix describes how we cluster drivers using their work schedule and hourly wage rate data. We use the data that contain driver schedules and hourly revenue for all drivers on Dec. 3, 2018. Our sample includes 23,689 drivers (observations).

We use a 24×1 vector for each driver to describe their working schedule and hourly wage rate. The n^{th} element represents hourly revenue at n o'clock. If the driver does not work during this hour, we set the element value to 0. For instance, if the driver worked at 7 AM and earned 18 CNY, the 7th element is 18 for this vector. In addition, we construct the following variables to measure the driver's working schedule and include them in our study:

- **earlyMorning**: driver's working hours during the early morning (0–7)
- **morning**: driver's working hours during the morning peak (7–10)
- **midday**: driver's working hours during the midday period (10–16)
- **afternoon**: driver's working hours during the afternoon (16–19)
- **evening**: driver's working hours during the evening (19–22)
- **night**: driver's working hours during the night (22–24)
- **workHour**: driver's working hours in one day
- **start**: the hour during which the driver starts work
- **end**: the hour during which the driver ends work
- **consecutive**: driver's consecutive working hours in a day
- **consecutive1/2/3**: We divide 24 hours into 3 parts. Consecutive1/2/3 indicates a driver's consecutive working hours in each part of the day.
- **consecutive4**: driver's consecutive working hours during the evening (19–22)
- **morningCon/afternoonCon**: driver's consecutive working hours during the morning and afternoon
- **hourlyRate**: driver's average hourly wage rate in a day

We apply the k-means method and cluster the drivers in our working database in order to explore how different work schedules can affect a driver's hourly revenue. The k-means clustering method divides observations into a certain number (k) of groups according to their similarity. We do not know the number of groups to define *ex ante*. Therefore, we try $k = 2, 3, 4$ different clusters.

Table 1 illustrates the results when $k = 2$. Drivers are divided into low hourly rates (cluster 1) and high hourly rates (cluster 2). High hourly rate drivers are more likely to work longer and consecutive hours. Tables 2 and 3 report cluster results for $k = 3$ and $k = 4$, respectively. Though we pre-set more clusters, drivers can always be separated into two groups. When $k = 3$, we have low hourly rate drivers (cluster 1) and high hourly rate drivers (clusters 2 and 3). When $k = 4$, we have low hourly rate drivers (cluster 1) and high hourly rate drivers (clusters 2, 3, and 4). Moreover, no matter which k we choose, the characteristics of the lower-income schedules are similar: they work shorter and fewer consecutive hours.

Table G.1: Clustering results for k=2

	cluster1	cluster2
count	11,226	12,472
earlyMorning	0.59	0.29
morning	1.2	2.15
midday	1.61	4.86
afternoon	0.93	2.71
evening	0.87	2.16
night	0.7	1.46
workHour	5.62	13.01
start	9.21	7.4
end	16.59	20.92
consecutive	4.56	11.59
consecutive1	1.3	1.61
consecutive2	2.16	6.24
consecutive3	1.91	4.75
consecutive4	1.29	2.98
morningCon	1.56	2.95
afternoonCon	1.22	3.52
hourlyRate	40.03	46.91

Table G.2: Clustering results for k=3

	cluster1	cluster2	cluster3
count	8,912	7,745	7,041
earlyMorning	0.51	0.52	0.27
morning	1.21	1.43	2.51
midday	1.46	3.42	5.38
afternoon	0.76	2.58	2.48
evening	0.6	2.89	1.43
night	0.43	2.51	0.59
workHour	4.79	12.37	12.34
start	9.36	8.07	7.14
end	15.57	22.51	19.35
consecutive	3.92	10.36	11.35
consecutive1	1.24	1.34	1.83
consecutive2	1.98	4.4	6.91
consecutive3	1.34	6.16	3.27
consecutive4	0.84	4.41	1.7
morningCon	1.56	1.98	3.42
afternoonCon	0.98	3.52	3.11
hourlyRate	38.28	47.73	46.12

Table G.3: Clustering results for k=4

	cluster1	cluster2	cluster3	cluster4
count	7,921	6,246	5,328	4,203
earlyMorning	0.48	0.24	0.27	0.82
morning	1.32	2.59	2.36	0.3
midday	1.41	4.73	5.37	2.11
afternoon	0.72	2.79	2.33	2.16
evening	0.46	2.9	0.98	2.75
night	0.28	2.26	0.23	2.46
workHour	4.55	14.55	11.4	9.67
start	9.12	6.87	7.32	9.77
end	14.93	22.27	18.54	22.47
consecutive	3.71	12.44	10.53	8.16
consecutive1	1.29	1.82	1.72	0.96
consecutive2	1.94	6.09	6.85	2.76
consecutive3	1.09	6.04	2.51	5.74
consecutive4	0.62	4.19	1.06	4.26
morningCon	1.69	3.51	3.25	0.47
afternoonCon	0.91	3.74	2.85	3.02
hourlyRate	37.54	46.78	45.77	48.05

H Control For Unobservable Selection: IV results

To mitigate potential biases in driver selection based on unobservable characteristics, we employ instrumental dummy variables: the rate of change in precipitation and air quality index (AQI) in the driver's hometown city between 2017 and 2018. The selection of drivers based on these variables is not influenced by the drivers' unobserved characteristics.

These weather variables satisfy the two conditions required for valid instrumental variables (IVs). First, the occurrence of precipitation and changes in air pollution may be correlated with a driver's decision to become a high-performing driver, as suggested by (Miguel et al., 2004). For instance, alterations in precipitation and air pollution might motivate more drivers to leave their hometowns and become high-performing drivers in the city under study. Second, the variation in weather conditions in a driver's hometown should not directly impact the driver's hourly rate or order distribution in the city being studied. The IV results appear in column (5), revealing a more significant wage differential between high- and low-performing drivers.

Table H.1: Wage Differential: First Stage

	High-performing					
	(1)	(2)	(3)	(4)	(5)	(6)
Change in Precipitation	-0.157***	-0.155***	-0.154***	-0.159***	-0.157***	-0.155***
	(0.00131)	(0.00129)	(0.00130)	(0.00134)	(0.00132)	(0.00132)
Change in AQI				-0.0270***	-0.0231***	-0.0206***
				(0.00322)	(0.00318)	(0.00318)
Constant	0.898***	0.898***	0.886***	0.895***	0.896***	0.884***
	(0.000148)	(0.000146)	(0.000450)	(0.000327)	(0.000324)	(0.000529)
Controls:						
Day-Hour FE		Y	Y		Y	Y
Origin/Dest FE			Y			Y
Observations	4,182,318	4,182,318	4,182,318	4,182,318	4,182,318	4,182,318
R-squared	0.003	0.023	0.024	0.003	0.023	0.024

Standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1

The first stage results appear in Table H.1. We regress the High-performing dummy on

Table H.2: Wage Differential: IV results

	Hourly Wage					
	(1)	(2)	(3)	(4)	(5)	(6)
High-performing	8.908***	9.480***	5.599***	9.268***	9.813***	5.759***
	(0.679)	(0.676)	(0.677)	(0.678)	(0.675)	(0.676)
Constant	41.98***	47.28***	49.47***	41.65***	46.97***	49.32***
	(0.611)	(1.192)	(1.186)	(0.609)	(1.191)	(1.185)
Day-Hour FE		Y	Y		Y	Y
Origin FE			Y			Y
Destination FE			Y			Y
IV (2017-2018)						
Change in Precipitation	Y	Y	Y	Y	Y	Y
Change in AQI				Y	Y	Y
Observations	4,182,318	4,182,318	4,182,318	4,182,318	4,182,318	4,182,318
R-squared	0.024	0.034	0.050	0.024	0.034	0.050

Standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1

the weather conditions, with F-values exceeding 1000 for all specifications. In column (1), we regress the High-performing dummy on the precipitation change without any fixed effects. In column (2), we include day-hour fixed effects, and in column (3), we include day-hour, origin, and destination fixed effects. Columns (4)–(6) are replicates of (1)–(3), except that we include both precipitation change and AQI change as explanatory variables.

Our analysis reveals a robust negative correlation between precipitation and driver performance. Specifically, we find a one percent increase in precipitation in a driver's hometown to be associated with a 0.154% decrease in the probability of a driver attaining high-performance status. More precipitation is usually associated with higher agricultural output (Miguel et al., 2004) and may inadvertently diminish drivers' incentives to move to the city we study and become a high-performing driver. Moreover, we identify a negative impact of air quality on driver performance. A one percent increase in the Air Quality Index (AQI), reflecting elevated pollution levels, corresponds to a 0.02% decrease in the likelihood of drivers achieving high-performance status. This observation aligns with the hypothesis that heightened pollution levels, often linked to increased industrial output in drivers' hometowns, may undermine their motivation to move to the city we study and become high-performing drivers.

The instrumental variable (IV) results appear in Table H.2. Column (1) presents the results without any fixed effects, while column (2) includes day-hour fixed effects. In column (3), we include day-hour fixed effects, origin fixed effects, and destination fixed effects. Columns (4)–(6) are replicates of (1)–(3), except that we include both precipitation change and AQI change as instruments.

Our findings demonstrate that high-performing drivers outearn their low-performing counterparts. Specifically, when examining column (3)/(6), we observe that high-performing drivers earn 5.6/5.8 CCY more per hour than low-performing drivers. This wage differential is notably higher than that indicated by our main ordinary least squares (OLS) findings.

We conjecture that low-performing drivers exhibit a higher level of strategic behavior. For instance, they may strategically select optimal times and locations to work, which contributes to their comparatively lower number of working hours. This aligns with the fact that their working decisions are more discerning and selective. In summary, our OLS estimates underestimate the wage disparity due to algorithmic preferences.

I Results from Eliminating the Wage Differential

To understand the effect of eliminating wage differentials between high- and low-performing drivers, Figure I.1 shows the equilibrium labor supply decision in panel (a) and the equilibrium wage rate in panel (b). In this scenario, we maintain the ride fares at the same level as when the platform uses a preferential algorithm. When we eliminate the wage differential between high- and low-performing drivers, drivers will switch from being high performing because it no longer provides any bonus. Because we fix the ride fares, and hence rider demand, there will be a labor shortage because of the lack of high-performing drivers. As a result of the excess demand, the equilibrium wage rate without a preferential algorithm will be higher than the wage rate of low-performing drivers when there is a preferential algorithm. The equilibrium wage rate without a preferential algorithm lies between the former wage rates of the high- and low-performing drivers.

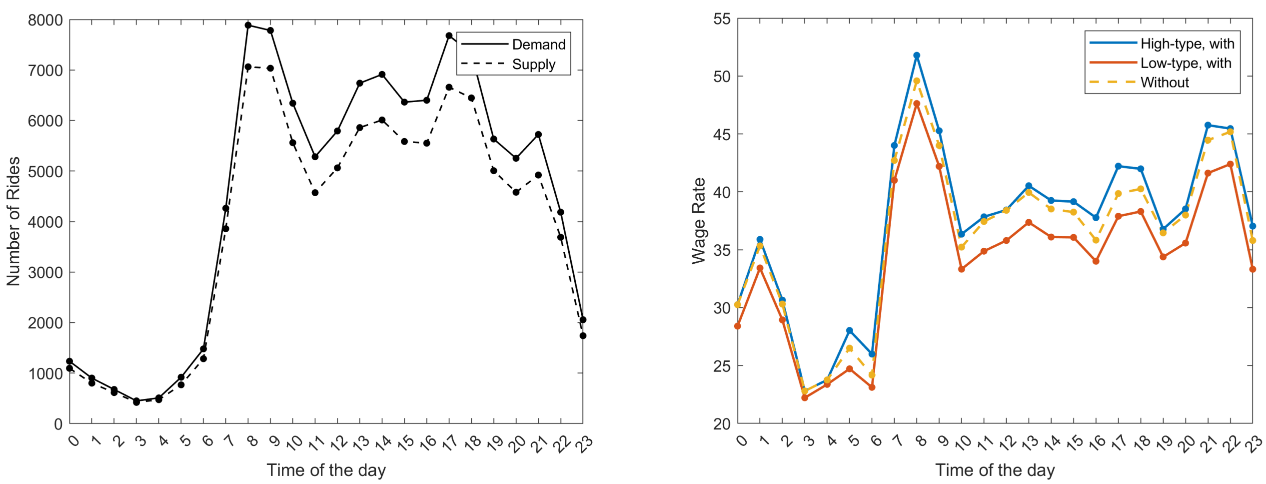
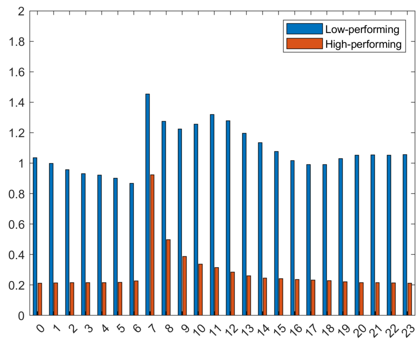
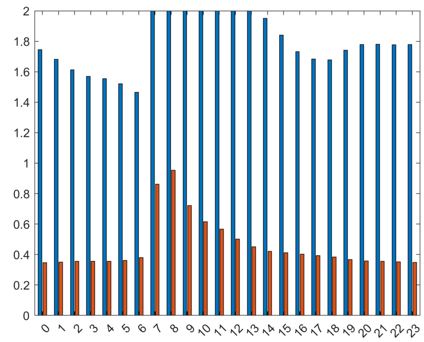


Figure I.1: Results from Eliminating the Wage Differential between W^H and W^L

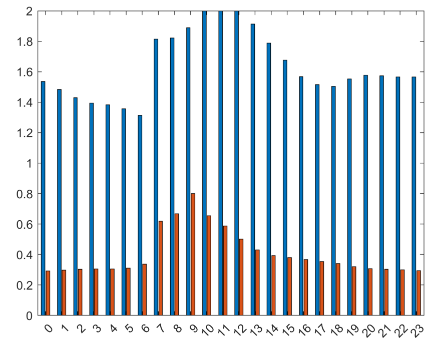
Next, we study the counterfactual results of eliminating the wage differential between high- and low-performing drivers only in the treatment hour h. When we eliminate this wage differential in one particular hour, drivers will switch from being high performing because the benefit for doing so is now smaller. Because we fix the ride fares, and hence rider demand, there will be a labor shortage because of the lack of high-performing drivers. As a result, the equilibrium wage rate for low-performing drivers without a preferential algorithm will be higher than the wage rate when there is a preferential algorithm. Figure I.2 shows the elasticity of labor supply corresponding to the elimination of the wage differential in treatment hour h.



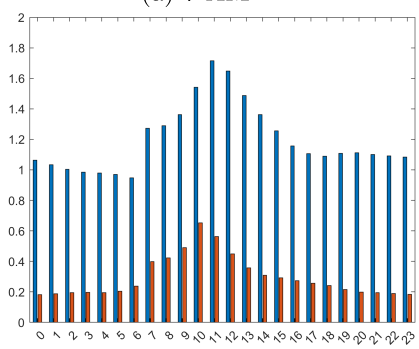
(a) 7 AM



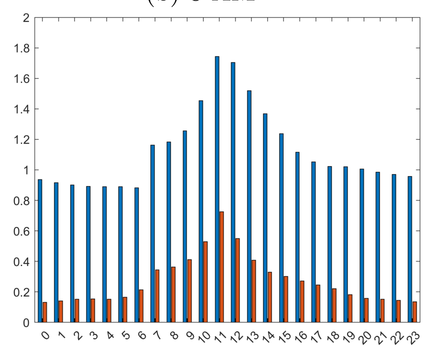
(b) 8 AM



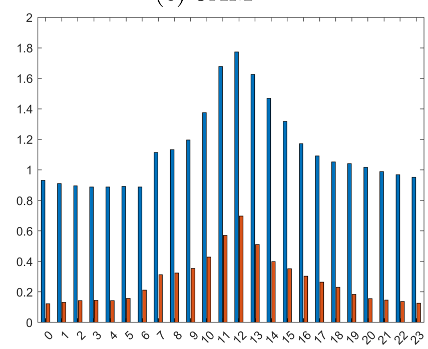
(c) 9AM



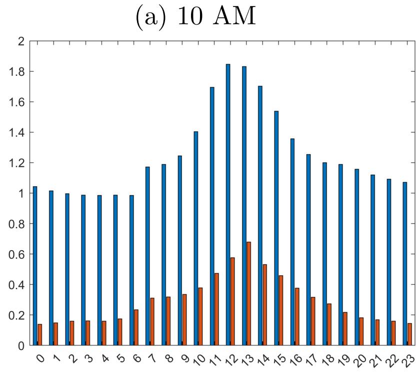
(a) 10 AM



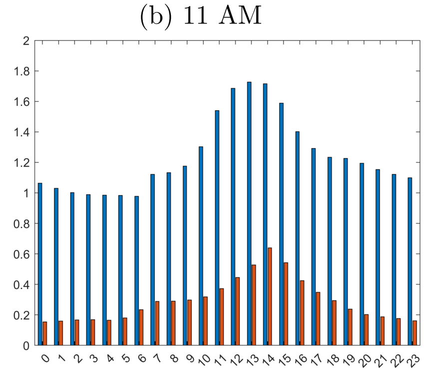
(b) 11 AM



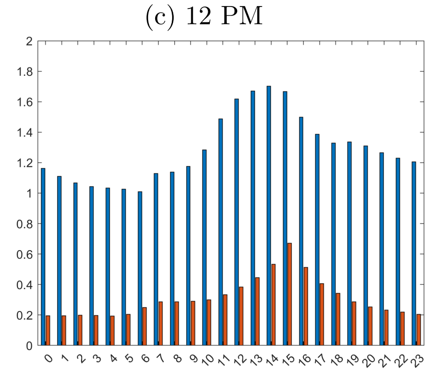
(c) 12 PM



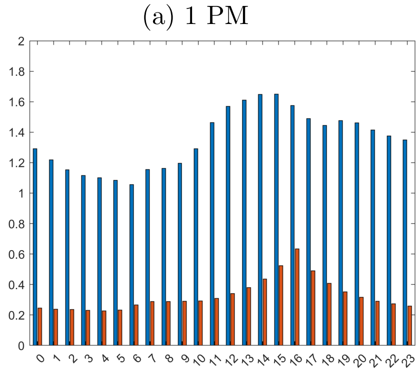
(a) 1 PM



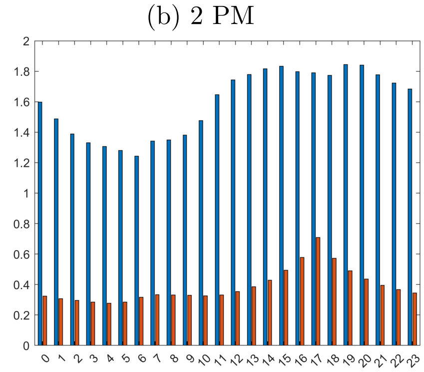
(b) 2 PM



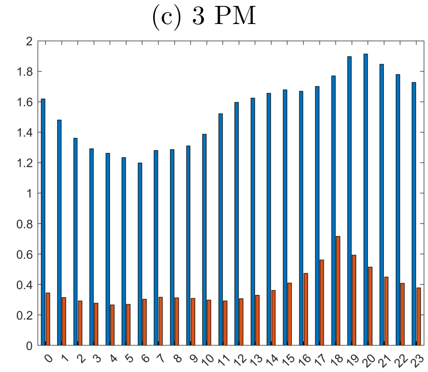
(c) 3 PM



(a) 4 PM



(b) 5 PM



(c) 6 PM

Figure I.2: Absolute Elasticity of Low-Performing and High-performing Drivers