

Oligopolies

Damien Neven, Chief Economist*
DG COMP, European Commission

*The views expressed are those of the authors and do not necessarily reflect those of DG COMP or the European Commission

Introduction



- Oligopolies extract market power
 - In the presence of capacity constraints and significant market shares
 - When firms control a sufficiently large number of close substitutes (mind the gap)
 - When firms coordinate their behaviour through repeated interactions
- Networks of contracts
 - Prices contingent on those of competitors
 - Roaming
 - Distribution of online music
 - Information exchange

Contingent prices



- Price matching clauses
- Commitment to sell all products at the lowest price that a consumer can find in competing outlets
- In the context of coordination
 - Enhance detection
 - Commitment to respond aggressively
 - But contracts needs to be widespread
 - Typically found in retail sectors (coordination unlikely ?)
- Price discrimination
 - Active buyers use it to obtain rebates
 - Passive buyers pay high prices
 - Not widely used...

Contingent prices



- Signalling to uninformed consumers
 - By low cost retailers
 - High cost would not do it as it would induce the informed consumers to obtain the prices of low cost retailers
- Most favoured customer (commitment to reimburse current purchasers if the price falls)
- Makes deviation more costly (low prices apply to past buyers)
- But it is not clear that firms would want to adopt it ex ante
- Meet or release clauses
 - Reduces the incentive to cheat : customers attracted during a deviation will be able to obtain low prices during the punishment phase
- Overall : probably only a relatively minor + factor in the context of coordination

Roaming



- Provision of mobile services to foreign operators
- Perception that both wholesale and retail price are high
- In the early days : no traffic direction techniques
- Each host network is « an essential facility »
- With traffic direction techniques, local hosts could compete
- But initially did not..

Roaming



- High prices can be sustained by a network of contracts such that
 - Contracts are bilateral
 - Operators commit to offer the same contract to all foreign hosts
- In equilibrium, all contracts feature high wholesale prices
- High costs are supported by high revenues in the other direction
- And largely passed on to the final consumers
- Prices started to fall when some operators acquired foreign networks

Roaming



- Do we have the appropriate instruments ?
- Contracts have a vertical dimension but it is not the only essential feature that allow for the extraction of market power
- Collective dominance under Art 82 (the web of contracts is a « structural link »)
- Under Art 81 ?
 - With a collective dimension but outside the framework of coordination
 - With both horizontal and vertical components

Distribution of on line music



- I tunes is a common (distribution) agent for all majors (60 – 70 %)
- Common agents affect the incentive to undercut rivals
 - Principals fix the final price
 - The agent has a franchise contract; get all revenues in exchange for a fixed fee
 - Consider a contract by one firm; collusive price and a fixed fee (corresponding half the monopoly profit)
 - Incentive for its competitor : undercut ? It will reduce the profit of the agent – and the agent's profit is effectively his own profit through the fixed fee. Best reply is the monopoly price

Distribution of on line music



- Agent effectively suffers the external effect associated with competition
- Works if prices and contracts are set at the same time ; which is the case for on line distribution of music
- I tunes gets the full benefit of its effort, in terms of higher sales of a complement (i pods)
- Rents are extracted by the majors
- Competition between multiple common agents ?
- Application to joint ventures

Information exchange



- A number of recent cases in members states
- Palaces Parisiens
 - Information exchange prohibited almost per se
 - Exchange of information on occupancy rates and average price per room
- Iama (Italy)
 - Database of public information on insurance contracts
 - Distinction between data in the public domain which known or unknown
 - Available to consumers, large number of companies
- Fedicine (Spain)
- Private schools (UK)
 - Details of current fee levels and future plans
 - In time for the annual round of price fixing What is the “right” MIF, in the presence of platform competition ?
- Supermarkets (Norway)
 - Exchange of very detailed prices weekly
 - With a 5-8 days delay

Information exchange



- Ex ante to establish a focal point
 - But transparency can be useful for buyers
- Ex post to monitor deviations
- But an exchange of information is a commitment to renegotiate
 - which makes deviation more attractive in the first place
- And current information can also be used to improve the design of deviation strategies (old data may be more harmful)
- In the absence of coordination, incentive to share information is unclear (improves the design of strategies but also those of competitors)
- Information exchanges are probably often harmless but yield little benefit
 - Only as part of wider “coordination” case ?
 - Exceptionally ex ante ?

Conclusion



- Networks of contracts
- Central coordination
- Signalling in auctions