

Econ 123, fall 2001

Lecture notes on oligopoly/collusion: week 2.

Mainly meant to help my memory as I lecture, but if it's helpful to students that's great too. Just be aware that it's *not meant to be read in isolation*.

1. Reprise of firm-specific elasticity and the Lerner equation. Confirm formula for dominant firm with fringe; VVH page 164. Illustrate with GP-FJ merger CIS, to be found at: <http://www.usdoj.gov/atr/cases/f7300/7364.htm>. What critical elasticity do we know is important even without knowing cost details?

2. High-price equilibrium in repeated oligopoly game. Unlike VVH, trace through the Bertrand case, which is simpler.

Within the model, lessons: role of n (or min s); role of r (cartels break down in recessions).

Remarks on capacity limits (simple case: no firm essential to serve the market at $p=c$). Is the limit on n realistic? Renegotiation?

Leniency policy.

3. Imperfect collusion. Is it hard to reach an equilibrium? Is it much harder if you can't talk?

4. Remarks on some cases (some cited in VVH).

a. *Railroads*. Dr Strangelove.

b. *Nasdaq*. Best-price rule ("preferencing"). If you're interested in this one, you should be able to access a short article in the *Journal of Economic Perspectives* 1995 (in library or check www.jstor.org from Berkeley domain).

c. *AA-Braniff*.

Mr. Putman: Do you have any suggestions for me?

Mr. Crandall: Yes, I have a suggestion for you. Raise your [blank] fares 20 percent. I'll raise mine the next morning.

Mr. Putman: Robert, we...

Mr. Crandall: You'll make more money and I will, too.

Mr. Putman: We can't talk about pricing!

Mr. Crandall: Oh [blank], Howard. We can talk about any [blank] thing we want to talk about.

The taped conversation found its way to the U.S. Justice Department. Ironically, Mr. Crandall's suggestion did not violate Section 1 of the Sherman Act because Mr. Putman rejected the proposal. American agreed to "cease and desist" from any discussions of prices with competitors.

d. *Tetracycline*. Were they in fact setting a monopoly price? ("demand was inelastic..."). If so, what about the patent? More relevance than just barrier to entry: monopoly outcome is viewed as acceptable. Licensing arrangements versus price agreements: policy and patent-holder interests.

e. *Christie's/Sotheby's*. Should one worry that only the seller side was subject to agreement?

5. Conscious parallelism. Should it be treated the same as collusion? Argument that it's *not* enough to say they have the same outcome (even if they do). Facilitating practices can sometimes be attacked: Airlines' pricing pre-announcements. Auto makers' 1950s-60s deal on pollution control technology (?). Price-matching offers. GE-style price protection plan: your advice for GE?

6. For Thursday: Read the *Addyston Pipe* decision at the back of VVH chap.5. Be prepared to discuss the following in class:

- a. If you were debating against the defendants and they made the arguments sketched in Judge Taft's words on p.140, do you have a "gotcha"?
- b. What light is cast on the statement in VVH page 127 that "cost savings are quite unlikely without actual integration"?
- c. What do you think about the affidavits from buyers that prices were reasonable?

7. For next week: Read VVH chapter 7 (skip 6 for now), to p.213. **Also read** the DOJ/FTC *Horizontal Merger Guidelines*, at <http://www.ftc.gov/bc/docs/horizmer.htm>. **Prepare to discuss:** How would you have analyzed the Staples-Office Depot merger? If you were an FTC Commissioner, would you have voted to block the merger?