

Market Power and Public Policy
ECON 465-01 and PUBPOL 310-01
Allan Collard-Wexler
Social Sciences 136 Tuesday-Thursday 3:05-4:20
Spring 2015

Market Power and Public Policy

The purpose of antitrust laws is to control how firms attain and maintain their market position; presumably for the betterment of consumers, or at least for the benefit of society. In this class, using a rigorous set of tools from microeconomic and game theory, we will investigate the underpinnings of policies meant to deal with market power, such as antitrust laws, the regulation of public utilities, the regulation of financial markets, and antidumping rules.

This class will dive into the regulations used in industries with market power, such as antitrust laws and the regulation of natural monopolies. In addition, we will look into the economic theory that provides (or fails to provide) the intellectual foundation for these policies. Most of the theory background will thus be drawn from the field of Industrial Organization in economics. However, much of the substantive evidence for these policies will come from looking at the intersection of industry studies, legal decisions, and historical sources.

Evaluation: You will be evaluated based on three different components.

Midterm (20%) Tuesday March 3rd.

Final (30%) Thursday April 16th.

4 Problem Sets (20%).

Class Presentation (20%), 30 minute in class presentation of one of the antitrust cases.

Participation (10%).

Background: I expect all of you to have background in microeconomics that covers basic models of oligopoly such as Cournot and Bertrand competition, as well as asymmetric information. Some knowledge of linear regression will also come in handy for understanding empirical papers.

Reading List:

The required textbook for this class is:

Jean Tirole, *The Theory of Industrial Organization*, MIT, 1987 (dated, but the Bible of the field to some extent).

Classroom Etiquette:

I expect you to follow the basic rules of classroom etiquette, which is particularly important for a small class like this one. I expect to come to every class, on time. If you can't make it to class for one reason or another, please send me an email (I won't respond typically). My policy on anything with a screen (laptops, ipads, smartphones) is that they are not allowed unless I give you explicit permission to use them.

As well, I will expect from you (and myself) that we uphold the Duke Community Standard:

- I will not lie, cheat, or steal in my academic endeavors;
- I will conduct myself honorably in all my endeavors; and
- I will act if the Standard is compromised.

Tentative Outline

1. Introduction

- The story of the American Tobacco Company and the Sherman Act.
- Readings from “The Visible Hand” by Alfred Chandler on the rise of large corporations.

2. Antitrust Laws: Merger Policy

- a. Theory of Mergers (Tirole)
- b. Horizontal Mergers.
Readings from “Antitrust Revolution” on the proposed ATT T-mobile merger.
- c. Vertical Mergers and the double marginalization problem.

3. Antitrust Laws: Cartels

- a. Theory of Cartel Stability (Tirole).
- b. Price Fixing Cases:
ADM and Vitamin cases. Gasoline Cartels. Efficiency and operation of a cartel.
- c. Bid Rigging Cases:
John Asker American Economic Review Paper on Stamps.
- d. German pre-war and Scandinavia post-war: permissive cartel environments.

4. Antitrust Laws: Two-Sided Markets

Readings from:

- David S. Evans and Richard Schmalensee’s “Paying with Plastic”.
- Jean-Charles Rochet and Jean Tirole “Two-Sided Markets: A Progress Report” RAND Journal of Economics.

5. Predatory Pricing and International Trade Sanctions

- a. Predatory Pricing Theory: Role of financial constraints (Tirole)
- b. Predatory Pricing: Evidence from the Titanium Dioxide Industry (Pakaj Ghemawat).
- c. Dumping Cases in Steel.

6. Regulation of Monopolist

- a. Laffont and Tirole: Regulation of a Monopolist with unknown cost and the principle-agent problem.
- b. Case: Electrical Rate Regulation, and Telephone Regulation.
- c. Net Neutrality Regulations and Bilateral Oligopoly.

7. Monopsony Power and Countervailing Market Power
 - a. Bargaining in Bilateral Oligopoly.
 - b. A la carte pricing in Cable TV.
 - c. Regulation of Healthcare markets (Capps, Dranove, Satterwaite)

8. Regulation of Financial Markets
 - a. Over the counter versus exchange trading and market power.

Tentative Schedule:

January 8: Introduction and the Case of American Tobacco.

January 13: Theory of Homogenous Good Mergers Monopoly versus Competition.

January 15: Theory of Homegenous Good Mergers Cournot and Bertrand versus Competition.

January 20: Williamson Tradeoff: Cost Efficiencies in Mergers. Read ATT & T-Mobile paper on cost efficiencies.

Problem Set 1: Theory of Mergers

January 22: Double Marginalization and Supply Assurance: Vertical Mergers.

January 27: Vertical Mergers: Hortacsu and Syverson, Brown Shoe Decision.

January 29: Cartels; descriptive work. Shipping Cartel (Scott-Morton), Joint Executive Committee in Railroads (Porter). Anatomy of Cartels in Finland Paper.

February 3: Cartels: Theory of Cartel Stability (Tirole).

February 5: Cartels Examples: Stamps (Bid Rigging), Price Fixing Case on Vitamins, Quebec Gasoline Cartel.

February 10: Cartels: Scandinavian and German Legal Cartels.

Problem Set 2: Simple Cartel Models (Green Porter)

February 12: Two-Sided Market: Uber, Ebay, Credit Cards.

February 17: Two-Sided Market: Theory (Tirole-Rochet).

February 19: Two-Sided Market: Theory-Continued.

February 24: Two-Sided Market: Examples from “Paying with Plastic”.

February 26: Class Cancelled.

March 3: Midterm Exam.

March 5: Predatory Pricing: Examples from Bus Routes, Shipping Cartels, Titanium Dioxyde (Ghemawat).

March 17: Predatory Pricing: Theory – Long Purse Example, Gang of 4 Asymmetric Information.

March 19: Predatory Pricing: Theory – Dynamic Oligopoly Games.

March 24: Predatory Pricing: Connan Snider on American Airlines.

March 26: Predatory Pricing: Dumping Cases in Steel and Solar Panels in the International Trade Court.

Problem Set 3: Predatory Pricing

March 30: Regulation of a Monopolist: Examples from Electrical Utilities, Turnpike Authorities, Telecommunications.

April 2: Regulation of a Monopolist: Laffont-Tirole.

April 4: Regulation of a Monopolist: Laffont-Tirole part 2.

April 7: Electrical Rate Cases, Water Utilities (Timmins and Wolak).

Problem Set 4: Regulation of a Monopolist with unknown cost

April 9: Monopsony Power: Hospital-Health Insurance, Cable TV- Content Providers.

April 14: Over the counter markets and market power in finance.

April 16: Final Exam.

April 21: Discussion of Topics Left Over.