

Slides should be viewed in *slide show mode*.

Two-Sided Markets: What have we really learned for competition policy?

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It's déjà vu all over again.

**COMPETITION POLICY
IN TWO-SIDED MARKETS**



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and

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Prepared for the conference “Advances in the Economics of Competition Law”, Rome, June 23-25, 2005

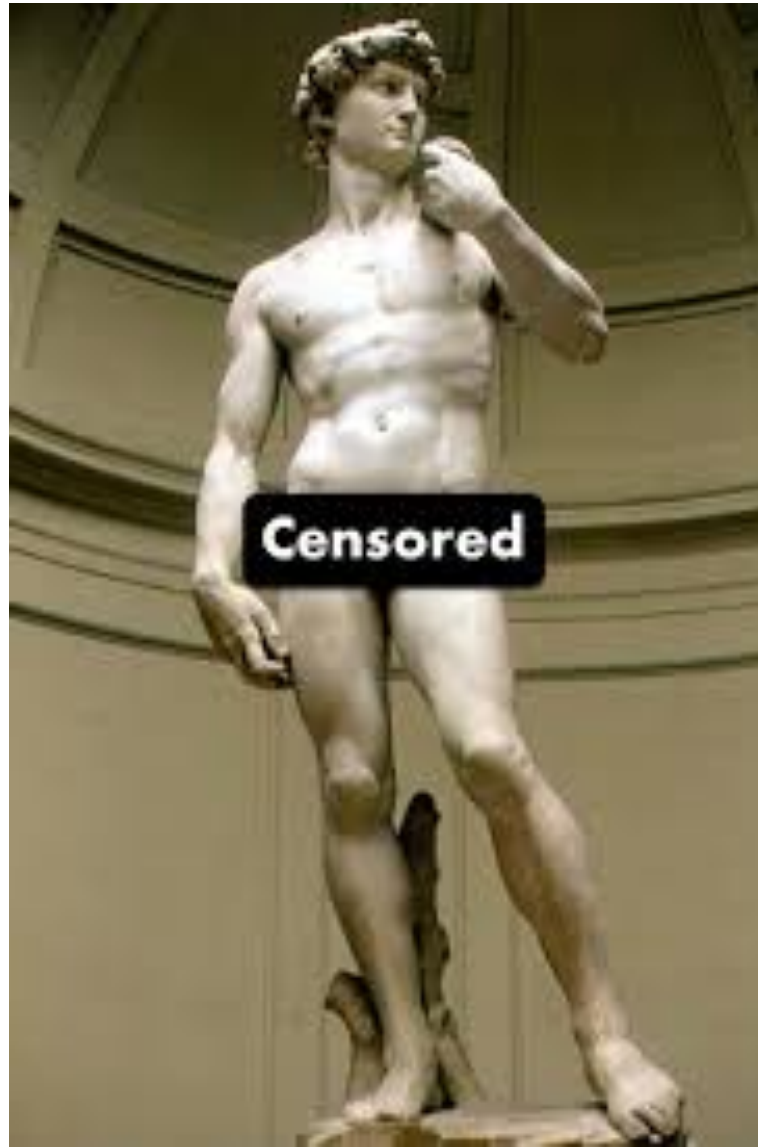
The Old New Learning

4. CONCLUSION: ANTI-TRUST ASPECTS

Need to renew anti-trust analysis for two-sided markets:

- high price-cost margin on one side does not imply market power (even with low fixed costs).
- Conversely price below cost on one side does not imply predatory behavior.
- Merger on one side increases competition on other side.
- Tying has rebalancing benefits.

A Platform?





Merchants and their customers jointly determine which payment instruments to use.

Merchant chooses which payment instruments to accept.

Customer chooses which payment instruments to use among those that merchant accepts (or goes to another merchant).



PREDATORY & EXCLUSIONARY BEHAVIOR

Aberdeen Herald & Post

Enough already with the warnings
of false positives.



Predatory pricing and exclusionary behavior may be a problem.

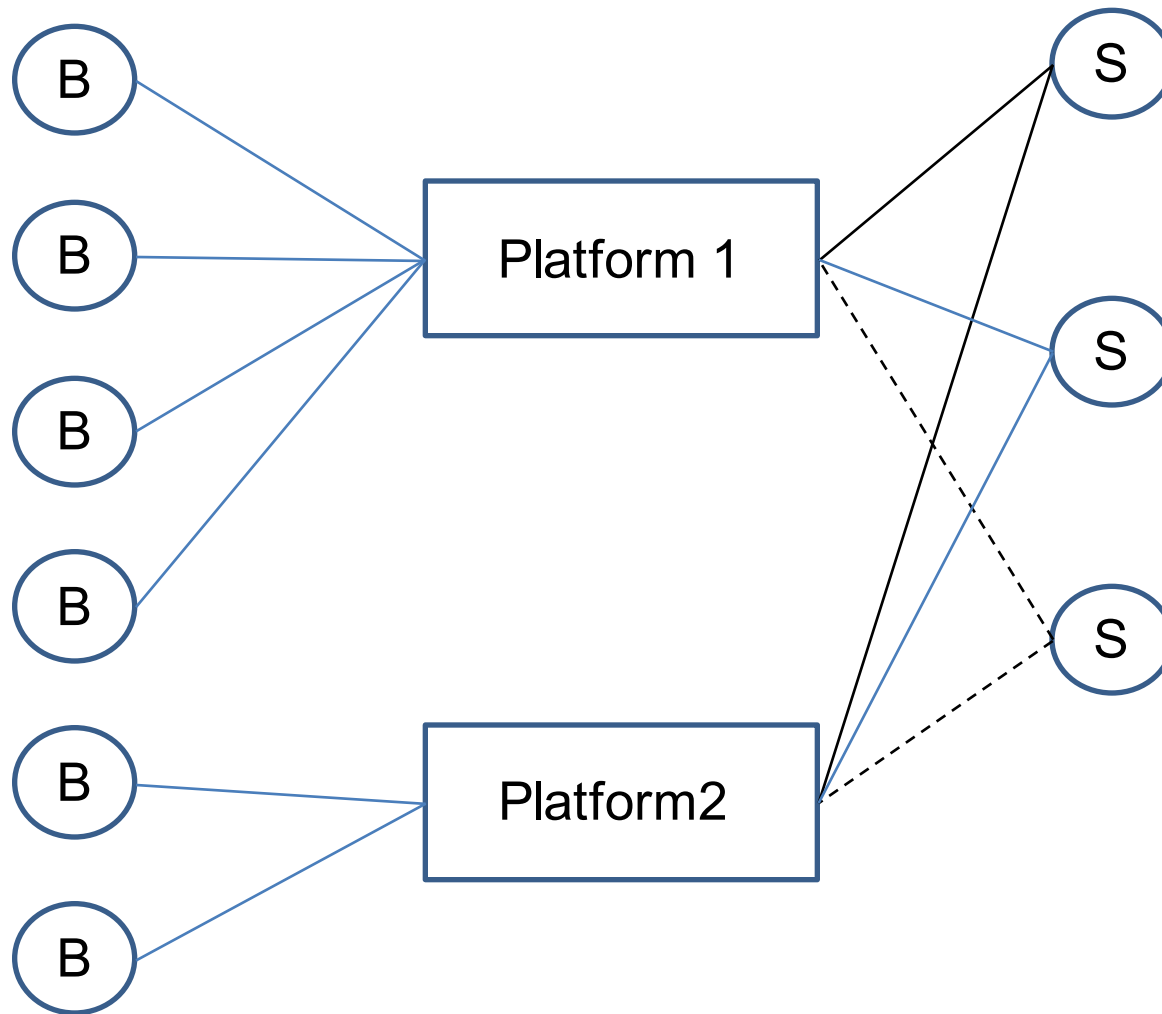
- Network effects can make recoupment possible.
 - Feedback effects prevent the prey's assets from being reused after the predation is over.
- Price *structure* can also be used in a predatory fashion.
 - Mobile services provider and choice of on-net and off-net prices.
 - Asymmetric media competition (*e.g.*, subscriber versus advertising-supported business models).
- Predation can be hard to detect.
 - Predation can be successful without triggering exit.
 - There are non-predatory reasons to price below cost and market may tip to monopoly even absent predation.
 - Above-cost predation is possible if predation means sacrificing short-run profits to weaken rival and doing so in a way that lowers welfare.

**MARKET POWER:
ONE LUMP OR TWO?**

Market Definition: One market or two inter-related markets?

- Economic Perspective
 - Market definition should be a guiding framework *not* a set of blinders.
 - Trying to identify the sources of competition.
 - Both approaches can give rise to problems (e.g., missing linkages versus missing other forms of competitor).
- Legal Perspective
 - Potential issue of balancing consumer welfare effects *across* markets.
 - To what extent is concern ameliorated by finding that the two markets are inextricably linked?

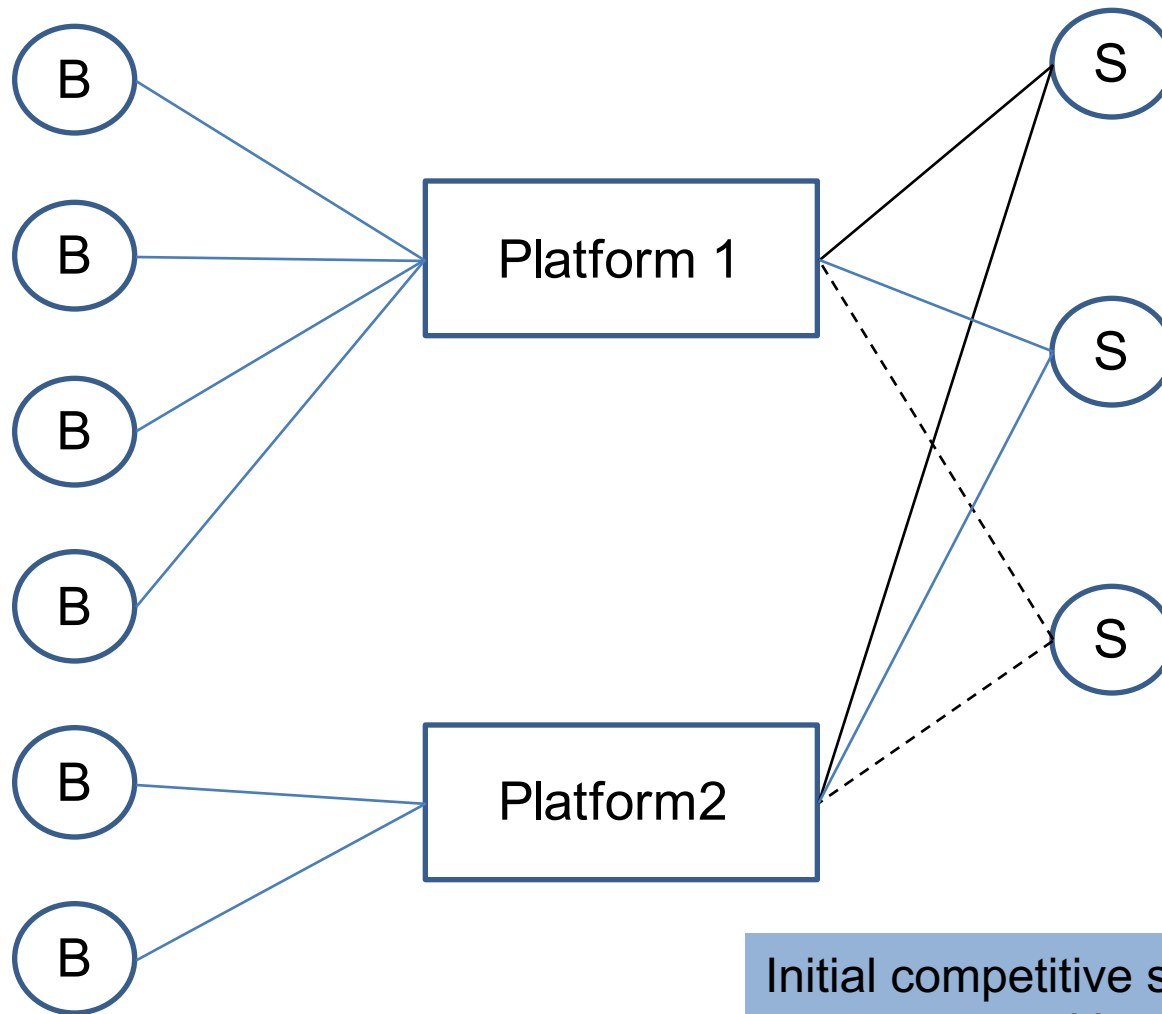
Single-homing, Multi-homing & Competition (or Not)



The Degree of Competition

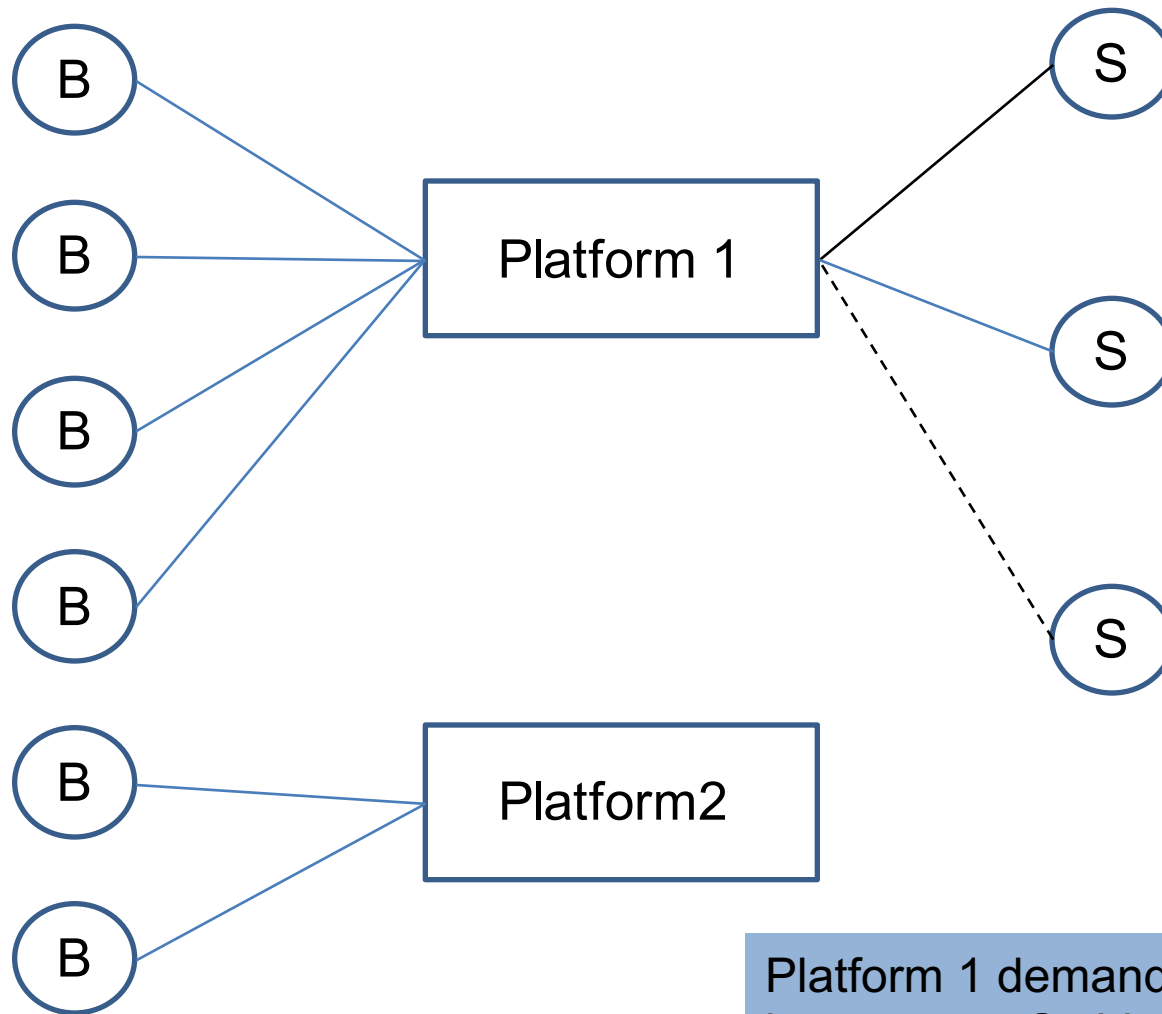
- Single-homing side faces competitive price, while multi-homing side faces monopoly price under certain assumptions.
 - A platform competes to attract single-homers and then sell “monopoly” access to them to multi-homers.
- Similar effect if both sides multi-home but one has platform decision rights.
- The nature of the demand by multi-homers is critical.

Exercise of One-Sided Market Power



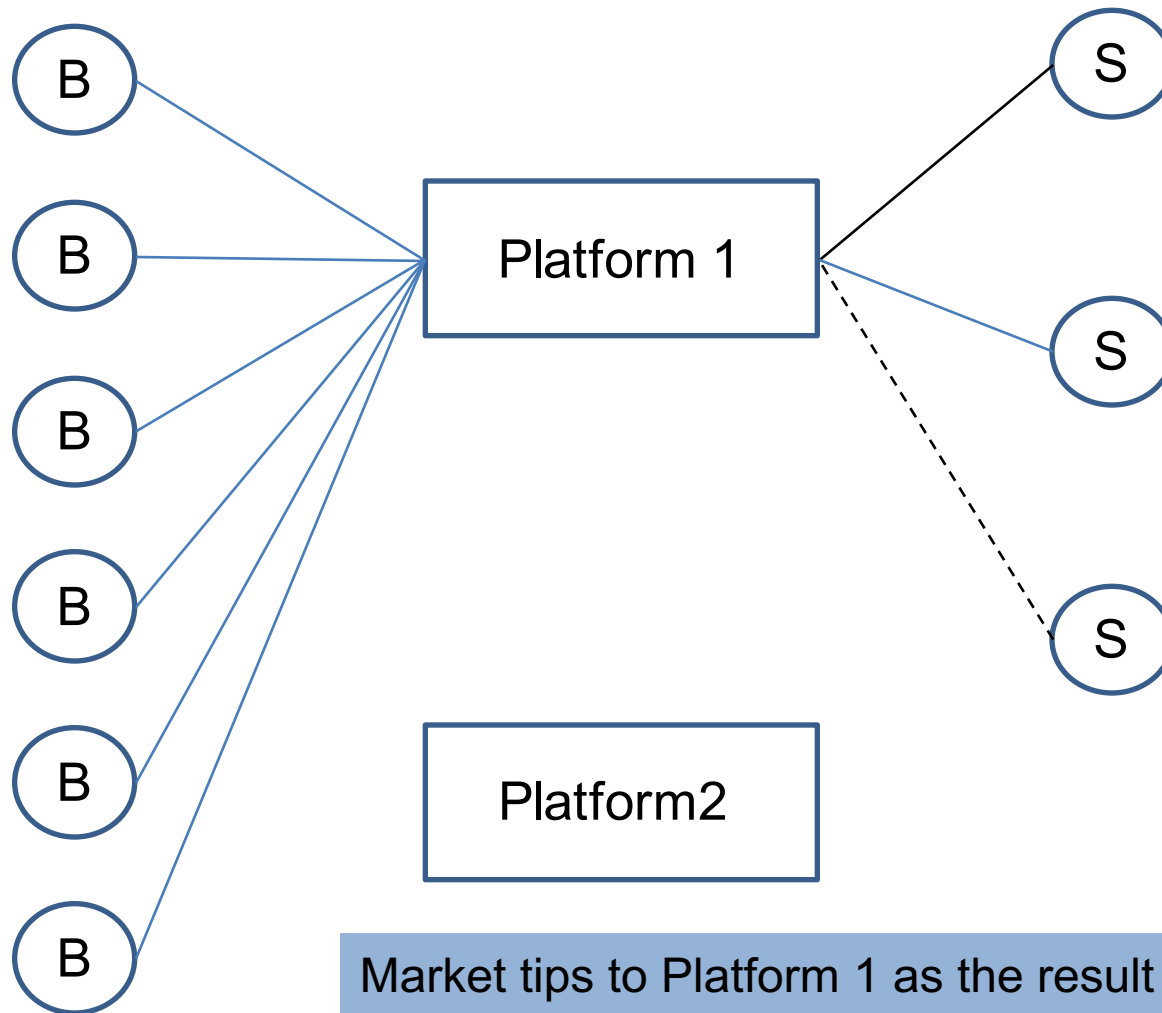
Initial competitive setting has strong competition to attract Bs.

Exercise of One-Sided Market Power



Platform 1 demands exclusivity by users on S side.

Exercise of One-Sided Market Power



Market tips to Platform 1 as the result of exclusivity despite strong initial competition for Bs.

A one-sided focus on harm can be appropriate.

- It is meaningful to talk about one-sided harm to competition or an increase in market power with respect to one side of the market.
- For example, platforms can affect the degree of multi-homing or steering.
 - Debit card exclusive bugging or platforms that charge membership fees v. transaction fees.
 - Credit card networks' steering limits.
- One-sided price fixing could harm that side.
- But the analysis should account for larger picture...

SEE-SAW AND OTHER FEEDBACK EFFECTS

Seesaw Effect



- Factors driving prices upward on one side might drive prices downward on the other.

Problems on the Playground

- Weyl (2010): be careful about assuming a seesaw effect— need to understand source of change look at full equilibrium.
- Rate *structure* can affect both total and division of surplus.
- Two-sided price *level* generally will be affected (cross-platform pass through 100%.)
- Are there actual cases in which the feedback effects are large and make a difference?



THE WELFARE STANDARD

(aka: Is it time to Give Up on Competition?)

Two-sided pricing is a complicated mess.

- It can be very difficult to assess what prices are optimal, what the competitive level is, and how various welfare measures will change.
- In 2003, MasterCard and Visa paid merchants over \$3 billion to settle a case related to the platforms' policies of tying credit and debit card acceptance.
 - Rochet & Tirole showed that tying might offset distortions in the debit and credit pricing structures and lead to higher total surplus.
- How should the courts take this possibility into account?

Role of Process in Assessing Liability

- Economists often focus on uni-dimensional welfare measures, such as consumer or total surplus.
- EU and US competition policy is concerned with protecting the competitive process.
 - In other words, it matters how a given end-state was achieved.
 - U.S. Supreme Court has blessed monopoly pricing as long as the monopoly was obtained on the merits.
- This distinction matters.
 - *U.S. v. Visa et al.*

CONCLUDING REMARKS

It's déjà vu all over again, again.

4. CONCLUSION: ANTI-TRUST ASPECTS

Need to renew anti-trust analysis for two-sided markets:

- It can be useful to think in terms of one-sided market power and/or competitive harm.
- Predatory pricing was not a big source of confusion.
- The see-saw effect does not justify anticompetitive behavior.
- It's not time to abandon competition, yet.