



On-line Intermediation and Antitrust Economics

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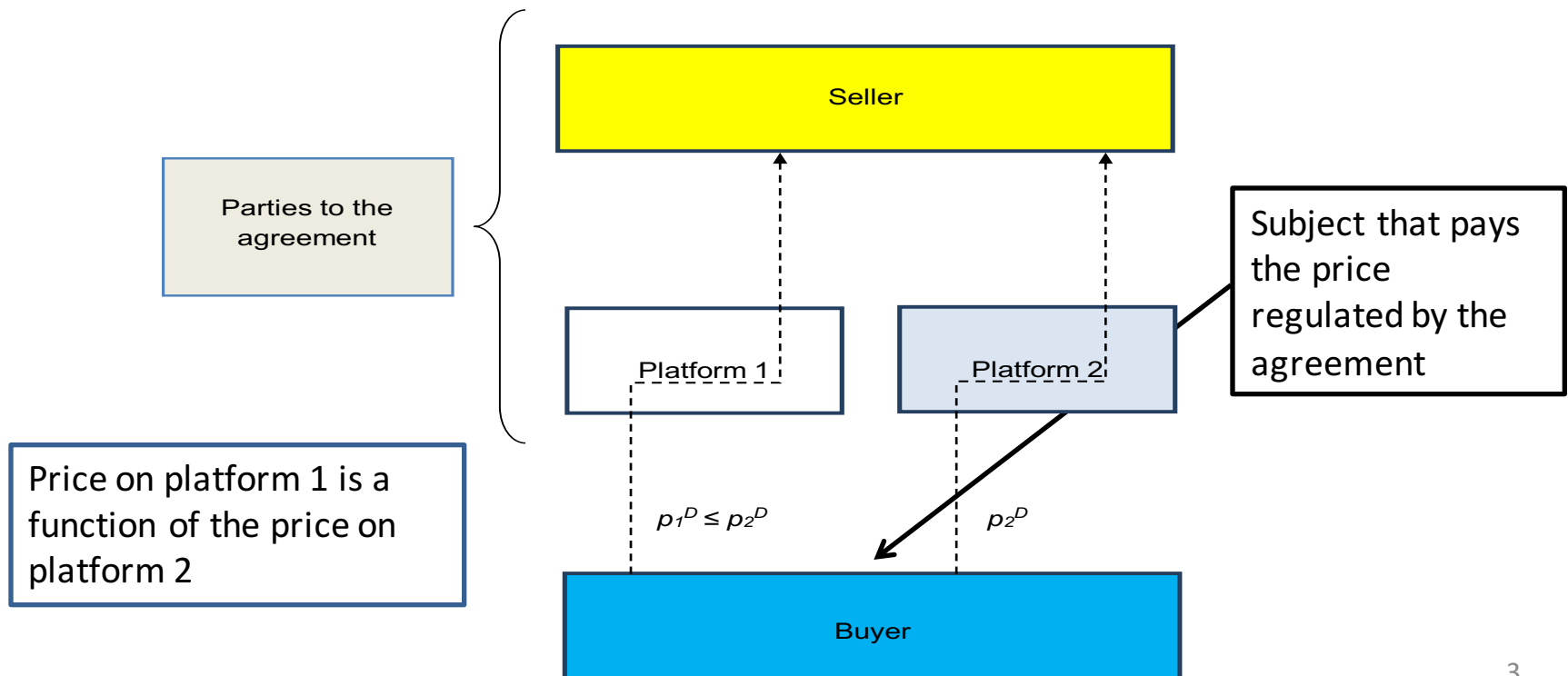
Outline

- Across-Platforms Parity Agreements (APPAs)
- Quick reference to the case law
- Theories of harm
- Efficiency justifications
- A simple framework to assess APPA's competitive effects
- Conclusions



Across-Platform Parity Agreement

- Agreement between a seller and an (electronic) trade platform whereby the seller undertakes to charge on that platform a price that is not higher than the price charged on other platforms (including new entrants and the seller's own platform)





APPAs: Case Law

1. E-book (USA, EU)
2. Amazon (Germany, UK)
3. Motor Insurance (UK)
4. Online Travel Agents (UK)
5. Online Travel Agents – HRS (Germany)
6. Online Travel Agents – Booking, Expedia (Italy, France, Swede, Germany, and many others)



APPAs: Theories of harm

1. Softening competition/Collusion in the product market (e-book cases)
2. Softening Competition in the platform market (OTAs, Motor Insurance)
3. Foreclosure in the platform market (Amazon, OTAs)



APPAs: Efficiency justifications

1. Facilitating entry in the platform market (e-book)
2. Preventing free-riding on investments in ancillary services in the platform market (Amazon, OTAs)



A simple framework

- 2 Platforms: 1 and 2
- Platforms set a per-transaction fee: f_1 and f_2
- Sellers set their retail prices: p
- Consumers observe retail prices and choose how much to buy and where to buy it

Consider a reduced-form framework and let:

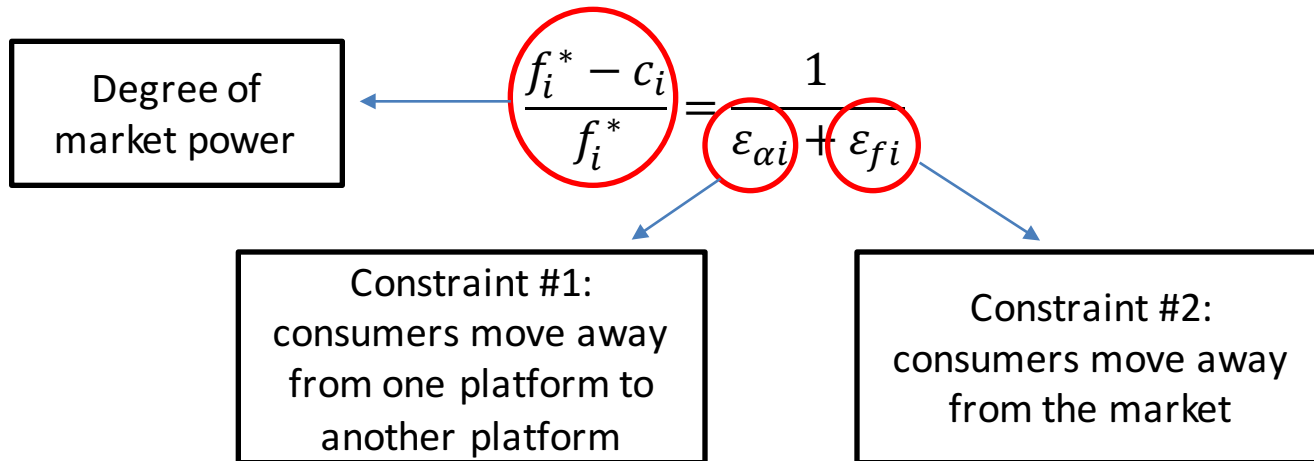
- $Q(f_1, f_2)$: total number of transactions in the product market (and as a consequence in the platform market)
- $\alpha_i(f_1, f_2)$: share of transaction that occurs on platform $i = 1, 2$
- Platform i demand function:

$$Q_i = \alpha_i(f_1, f_2) * Q(f_1, f_2):$$



The platform market equilibrium

- In equilibrium profit maximizer platforms set their fees so that



Where:

$\varepsilon_{\alpha i}$ is the “platform market share price elasticity”, and

$\varepsilon_{f i}$ is the “platform market size price elasticity”.



Two useful benchmarks

- Equilibrium:

$$\text{market power} = \frac{1}{\varepsilon_{\alpha i} + \varepsilon_{f i}}$$

- Perfect competition

$$\varepsilon_{\alpha i} = \infty \quad \text{--->} \quad f_i^* = c_i \text{ (no market power)}$$

- Monopoly

$$\varepsilon_{\alpha i} = 0 \text{ and } \text{--->} \quad \varepsilon_{f i} = \text{demand price elasticity} \quad \text{--->} \quad f_i = f^m$$



Case 1 (sellers only set prices): Equilibrium

- Effects on platform market equilibrium

$$\varepsilon_{\alpha i}^{APPA} = 0 \text{ (as in monopoly)}$$

and

$$\varepsilon_{f i}^{APPA} < \text{demand price elasticity}$$



$$f_i^{APPA} > f^m$$

- Platforms' fees become an ineffective means of competition as sellers cannot price discriminate across platforms
- Retail price will reflect an “average platform fee” so that platforms do not bear entirely the consequence on the market size of raising their fee
- Platform fees will be **above the monopoly level**



Case 1: Theories of harm explained

- Softening competition: self-evident (but... overshooting)
- Foreclosure
 - Platform 1: incumbent – Platform 2: entrant
 - Platform 2 cannot increase its market share through a low cost/low price strategy
 - Platform 2 market share may be insufficient to cover platform entry costs



Case 1: Efficiency justifications

- The same effects on $\varepsilon_{\alpha i}^{APPA}$ can support the efficiency claims
 - Free-riding: APPA prevents free-riding on platform 1 investments as its competitors cannot increase their market share by offering lower fees
 - Entry: If Platform 1 is the entrant, APPA prevents the incumbent from reacting aggressively to the new entry
- Efficiency justifications hinge on a less competitive platform market



Case 2 (sellers choose participation): Equilibrium

- If platforms are perfect substitutes $\varepsilon_{\alpha i}^{APPA} = \infty$ (perfect competition) as sellers decide to trade only through the least expensive platforms
- Implications:
 - More general parity requirements (e.g. OTAs require parity on room availability, booking and cancellation conditions)
 - APPA effective only if the platform has already some market power: “unavoidable commercial partner”
 - Captive consumers
 - Network effects
 - Superior ancillary services (reviews, payment system, return policy, etc.)



Case 2: Impact on theories of harm and efficiency justifications

- Softening competition (–)
- Foreclosure (+)
- Free riding (–)
- Entry (–)



A different efficiency justification: free-riding of direct sale channels

- Intermediaries improve buyers and sellers welfare by:
 - Reducing the uncertainty of making a satisfactory match
 - Reducing costs of (decentralized) search
- Platforms face a typical problem of intermediaries:
 - Once the platform has performed its matching function, sellers and buyers prefer trading directly, so as to save on intermediary fee



From “wide” to “narrow” APPA

- OTAs cases: Italy, France and Sweden closed the investigation against Booking with a “commitment decision”
- The narrow MFN clauses will only apply to prices and other conditions publicly offered by the hotels through their own direct online sales channels, leaving them free to set prices and conditions on other OTAs and on their direct offline channels, as well as in the context of their loyalty programs.
- Do narrow APPAs strike the right balance?
- Narrow APPAs do not eliminate all competitive distortions



Narrow APPA: Efficiency justifications

- Sellers Free-riding is an issue only if the platform adopts a transaction-based business model
- Other available business models
 - Advertising model ---> Pay per display or Pay per click
 - Membership fee model ---> Pay a fixed fee independent of search results and transactions
- Do the efficiencies brought about the intermediary depend on the business model? If so, which is the most (socially) efficient model?
- Is there too much intermediation in e-commerce (wasn't disintermediation one of the big promises of the web)?



Conclusions

- Foreclosure the most likely theory of harm
- Efficiency justifications not totally convincing
- Free-riding on the matching function of intermediaries is an issue
- Commitment decision likely to be inappropriate: a full-fledged investigation would have given the opportunity to further explore the pros and cons of various solutions



Thank You!