

Regulating platform competition in markets with network externalities: Will predatory pricing restrictions increase social welfare?

(by Ohad Atad and Yaron Yehezkel)

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## Synopsis

- The paper studies theoretically the effects of **prohibitions of predatory pricing** in markets with **network externalities**.
  - Interesting distinction between **symmetric and asymmetric regulation**.
- The paper models **competition** between **two platforms** in an **infinitely repeated game** with **uncertainty**.
- The paper adopts the concept of **focality** (past dominant platform is incumbent in current period).
- Demand and quality difference are **uncertain**.
- Outcome of **static** model: **inefficient incumbency**, but with dynamics ... and a warning ... **inefficient entry**.

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## Overview of the findings

- **No regulation**: inefficient incumbency.
- **Symmetric regulation**  $\downarrow$  CS but does not change welfare.
- **Asymmetric regulation**  $\uparrow$  CS and  $\uparrow$  welfare, and  $\downarrow$  **inefficient incumbency**, if market size is stable; **inefficient entry, if market size varies**.

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## Model setup

- $U_{it} = q_{it} + \beta N_t - p_{it} \quad i=\{A,B\}$ .
- $q_t = q_{Bt} - q_{At} \sim \text{iid } U[-\sigma, \sigma]$ .
- $N_t = n \geq 1$  with prob.  $\rho$ ;  $N_t = 1$  with prob  $1 - \rho$ .

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## Comments

- Fact: there is **limited** entry and exit in markets with networks but you give examples of the “good” (but with predatory pricing) **old days**.
- A theory that explains everything, explains nothing ... but a theory that explains something may not explain the real world. You are trying that.
  - Platforms innovate every period at **zero cost**.
  - Platforms have plenty of **liquidity** (deep pockets).
  - Marginal costs (**MC**) are **zero**; if  $MC > 0$ , predatory pricing is more difficult to be detected.
  - Condition  $\sigma > \beta N_t$  applies to markets with **breakthrough** innovations or weak network effects.
- Platforms are often **multisided** and there are various types of indirect network effects.

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## Questions

- In your examples of predatory pricing, were platforms **symmetric**?
- What changes if:
  - There were **deterministic cycles** in demand? Partial explanation in the paper.
  - Quality draws are **correlated** (and similarly for demand)?
  - Quality is **endogenous**?
  - Platforms are **differentiated**?
  - There is a **third platform** competing in the market?
  - The distribution of quality difference **highly concentrated**?
  - Quality **interacts** with network effects?
  - Predatory pricing has to be demonstrated in a **Court**? (Though this is a legal challenge.)
- How **practical** is it to implement an asymmetric regulation? Perhaps this is a concern for policymakers.

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THANKS FOR THE OPPORTUNITY TO DISCUSS THIS INTERESTING PAPER!

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