Costless (or Near Costless) Predation through Predatory Bundling, Loyalty Rebates, and Price Squeeze

Assaf Eilat, David Gilo and Guy Sagi

Aim

- Clarify issues
- Assess antitrust approach

What is predatory bundling?

- Monopolist subject to competition:
  - Other products
  - Contestable quantities
- Raises price of monopoly product
- Price < MC for additional product

Example 1: tying 2 products

- Product M monopoly
- Product A in competition
- MC=c

- "Ordinary" pricing: Pm, c
  - →Bundle price= Pm + c
  - →Marginal price = c

- Predatory bundling:
  - – Pm + b, c, rebate of b
    - →Bundle price = Pm + c
    - →Marginal price = - b

Example 2: target discounts

- Firms A and B
- Buyers must buy 5 units from firm A
- Can buy additional 5 units from A or B

- “Ordinary” pricing:
  - 5 units at $2, 5 units at $1
  - Total price = 15
  - Marginal price = 1

Example 2: target discounts

- Predatory bundling:
  - 5 units at \$3, 5 units at \$1
  - 25% discount if buys for 20

→Total price = 15

→Marginal price = -4

→Marginal price of 5 units = 0

→Rival with above 0 MC not able to sell

Example 3: conglomerate selling a bundle

- Buyer requires 100 products
- Supplier A supplies all 100
- Other suppliers supply part of the products

- “Ordinary” pricing: Price = 1
  - Total price = 100, Marginal price = 1

- Predatory bundling:
  - Price = 1.20, $20 discount if buys for 120
  - Total price = 100
  - Marginal price = -18.80
  - Rival with MC=0: needs to offer 17 products

Example 3: conglomerate selling a bundle

- Supplier's market power:
  - – Efficiency of buying large portion
  - – Competing suppliers offer countervailing discount

Example 4: Price squeeze

- Infrastructure monopoly
- Must sell access to rival for P
- Downstream service competition

- Monopoly sells service for less than P

→ Marginal price of service is “negative”

- Resembles predatory bundling:
  - Buys from rival:
    - Indirectly “buys” access for P
  - Buys access + service from monopoly:
    - Pays less than P

Characteristics

- Marginal price < 0
- Can sell bundle for same price w/o predatory bundling
- No benefit to consumers in the short run
  - Unlike predatory pricing

- Could be costless for the monopoly
  - Stand alone "tying" product > Pm
  - Possible loss when rival's product superior
    - But similar loss when separate
    - Differentiation also cuts the other way
  - Some loss when some consumers need only M
    - But not when able to discriminate
      - When targets tailored-usually able

Efficiencies

- Tying efficiencies:
  - Cost savings in distribution
  - Metering
  - (But: safety, quality assurance, etc.)

- Predatory pricing "efficiencies":
  - Product promotion
  - learning by doing
  - network externalities

- Exclusive dealing efficiencies:
  - Possible
  - But unlike exclusivity for discount on all units

Presumption of harm

- Monopoly/substantial market power
- Marginal price < marginal costs
- Forecloses a sufficient portion

→ No burden to show substantial harm to consumers/that rivals lose competitive viability

Monopoly

- Single supplier

- Non-contestable quantity (brand loyalty, capacity constraints)
  - “must have” more important than size
    - “must have” + b + (c – b)
  - “must have” may be more likely when small:
    - E.g., computer retailer “must have” Macintosh

- Essential facility

Power in selling a bundle

- The only one with whole range

- Or, buyers could divide purchases
  - Substitute, but inferior

  → substantial market power
  - Often impossible to measure market share
  - Note that also restraint of trade

Marginal price < MC

- Allows mere “price tying”

  → Allows exploiting efficiencies

- More simple than “contestable share” < MC
  - Difficult to assess contestable share
  - Costless
  - No efficiencies

- Consistent with “downstream competition” scenario:
  - Bulk payment for exclusivity

    → marginal price < MC

Foreclose sufficient portion

- Large enough portion of buyers affected
  - Tailor individual targets?
  - Quantity discounts?
    - May affect a sufficient portion
      - When discounts are retroactive
- Should this be an element?
  - Analyze as predatory pricing
    - Costless
    - No short term benefit
    - Less efficiencies

Inference of rivals losing viability

- Presumption that rival not able to compete:
  - Loses viability over time:
    - Economies of scale
    - Incentives to invest
    - Learning curve
    - Reputation