Predation

Econ 121

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Intuitive idea

- Out-compete rivals
- But don’t give consumers great deals (in long run)
- Instead, get and exploit a monopoly

Objections in Principle

- Isn't it good, not bad, if a firm out-competes rivals?
  - How is it possible to do so without giving benefit to consumers?
  - Even then, doesn't it prove that winner is more efficient?

Objections in Practice

- Price war more expensive for incumbent than for entrant
- Entrant can wait till incumbent is tired
- Assets still around even if entrant bankrupt
- Can customers contract with entrant?

American Airlines at Dallas

- DFW: major hub for American
- High fares, yet high percentage of traffic
  - Southwest at Love Field: Wright Amendment
- Several low-fare carriers entered at DFW
- American cut fares and added flights
- Low-fare carriers exited or retreated
- American raised fares again

DOJ sued American

- “Monopolization”
  - DOJ said it was not just “Predatory pricing”
  - Arguably different legal standard depending on what phrase one uses
  - Judge rejected DOJ claim, so predatory pricing rules would apply
  - How that played out

What are the rules?

- Supreme Court Brooke Group case
- Price below "some measure of cost"
- Realistic prospect of "recoupment"
  - Reality check?
  - Realistic prospect of harm to consumers?

What's cost got to do with it?

- Answer should help Supreme Court with its confusion about "measure"
- Areeda and Turner (1975): a firm won't price below cost unless it's up to something
  - Logic actually says look at whether IR<IC for all (or some?) increments
    - How does this differ?
  - But A&T flat-out wrong
    - Both "false positives" and "false negatives"

Various increments

- A little bit of output…
  - Look at MR versus MC
  - Do we insist a firm mustn't price even slightly below its profit maximum?
- All its output…
  - Look at "AVC" versus price
- Some other increment/alternative?

Above-cost Predation

- Incumbent has unit cost c
- Entrant would have unit cost e > c
- Can incumbent charge monopoly price > e?
- Argue that the "predation" problem is low prices as threat to entrant but not usually benefit to consumer
- How does this fit with