

Some Notes on Rebates

Roman Inderst

University of Frankfurt (IMFS)
& London School of Economics

For some of the material referred to on these slides see:

http://www.wiwi.uni-frankfurt.de/profs/inderst/Competition_Policy/competition_Policy.htm

(Loyalty) Rebates

- LRs take many forms
 - discounts/rebates may be incremental or non-incremental;
 - triggered by quantity threshold, share threshold, or both;
 - and may be triggered by purchase of multiple goods or confined to a single good
- Essential feature: Payment (on the margin) depends on overall level of activity of the buyer.
 - Link can be across (i) products, (ii) quantities, (iii) shares
 - E.g., (i) bundled disc., (ii) all-unit disc., (iii) market-share disc.

Focus

- No “unconditional rebates”
 - Means „constant unit price“ & price discrimination?
 - Extant literature largely useless (as counterfactual) (cf. Inderst/Valletti 2007; Inderst 07)
- Focus on Foreclosure
 - Large “anti-Chicago” literature → But of little use!
 - 100% exclusion is key! No distinction between contract types!
 - Main (perceived) message?
 - (Inefficient) foreclosure can arise “in certain game forms”?

(1) Contracts: „All-unit Discount“

- Price discrimination and efficient channel management as legitimate reasons?
 - In principle, yes (Kolay et al. 04).
 - But: Less convincing if much uncertainty and little control over final sales volume.
- Price discrimination: Analogy to tying?
 - There „lumpiness“ better justification for neg. incremental price?
 - (!) Why not first-degree PD?
- Drawback besides possible foreclosure → Dampens (long-term) competition (Endog. switching costs)

(2) Contracts: Market-Share Discounts

- Legitimate Business Rationale ?
 - „Rent Shifting“ (without DWL) (Marx/Shaffer 04)
 - Induces „non-contractible demand-enhancing services“. Less distortive than exclusive dealing. (Mills 04)
- But also further harm? (besides partial foreclosure)
 - As „facilitating practice“ to dampen downstream competition (Inderst/Shaffer 07)

Market Characteristics

- Starting point: Even a negative incremental price around the threshold should not put an equally efficient rival at a disadvantage
 - Obstacles of rival → Leading to (partial) exclusion
 - Capacity constraints → Negative incremental price „bites“
 - Analogous: Single vs. multiple markets
 - Financial constraints and costly customer acquisition („lock-in“)
(Shaffer/Ordover 06)
- Corollary: No (partial) exclusion if negative incremental prices forbidden

Summary (1): „On the *one* hand....“

- Effects-based vs. form-based?
 - LRs are neither „*the good*“ nor „*the bad*“, generally
- But possibly „*the ugly*“ (if used by dominant firm)?
 - All-unit discounts (“Discontinuity”).
 - In particular, spanning multiple markets/products
 - Market-share discounts
 - In particular, both as individualized discounts
 - No price-discrimination justification!

Summary (2): „On the *other* hand....“

- Chicago critique: „Nobody willing to pay for inefficient foreclosure“
- Has particular weight if
 - long-term co-existence of dominant firm and smaller rivals;
 - low fraction of long-term locked-in buyers;
 - no financial and capacity constraints.

Some Notes on Rebates

Roman Inderst

University of Frankfurt (IMFS)
& London School of Economics