

# A framework for the economic analysis of exclusionary conduct

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## Disclaimer

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- Comments are based in part on “A Framework for the Economic Analysis of Exclusionary Conduct,” with B. Douglas Bernheim, forthcoming in the *Oxford Handbook of International Antitrust Economics*, Roger Blair and Daniel Sokol, editors.
- Views expressed should not be attributed to anyone other than the speaker, and may not represent the views of others at Bates White, including coauthors.

# Agenda

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- The most important mechanism of practical concern: Monopolist weakens rivals to protect its (usually future) market power
- Rule of reason approach to address this mechanism
- $P < C$  for price-only allegations; analysis of exclusionary conditions for rest
- Four necessary conditions to have anticompetitive effects
- Analysis and balancing of procompetitive justifications
- Diagnosing procompetitive and anticompetitive effects
  - Procompetitive and anticompetitive effects leave distinctive empirical traces in the record
- *ZF Meritor LLC v. Eaton Corp.*, 696 F.3d 254 (3d Cir. 2012) gets it right
- Implications for counseling clients

## Economic consensus over predation

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- Predatory pricing
  - Price < Appropriate measure of the monopolist's own cost
- Multi-product bundled discount
  - Attribution of discount to contestable product in predation framework
- First dollar discounts (a.k.a. quantity-forcing discounts)
  - Revisit multi-product attribution notion: “Single product bundling” (must carry brands; differentiated consumers)
  - Attribution of discounts to contestable portion of demand
- What is the appropriate measure of cost?

## Conduct involving exclusionary conditions is where the action is

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- Exclusive dealing
- Loyalty discounts (discounts depend on rivals' share of purchases)
- Partial exclusivity
- Restrictions on customers' dealings with rivals, such as:
  - Channel restrictions
  - Advertising restrictions
  - Restrictions on prices of rivals' products
- Negative tying
  
- Why would  $P < C$  be informative about these potentially exclusionary mechanisms?

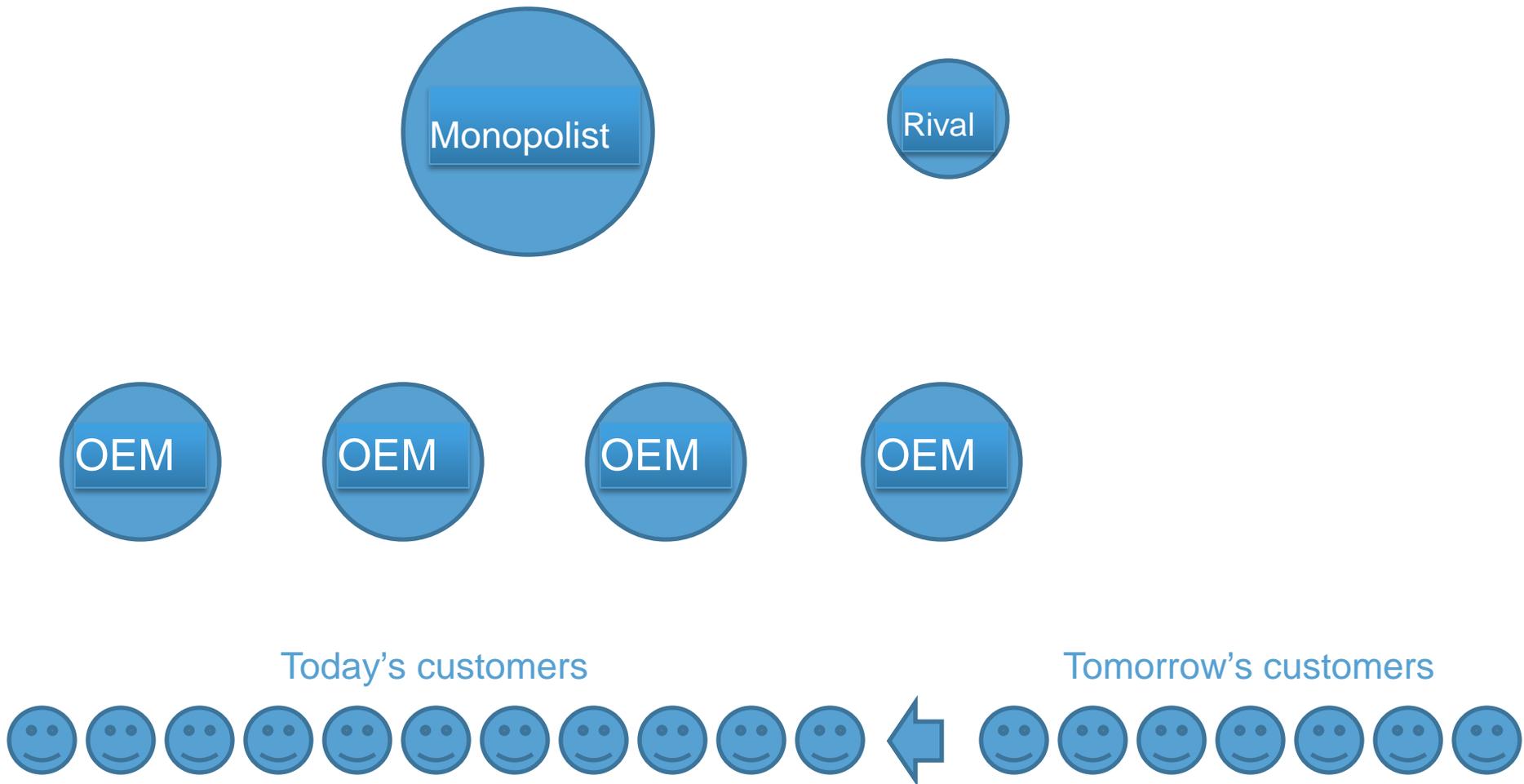
## Exclusionary conditions (or contracts referencing rivals)

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- Four necessary conditions to have anticompetitive effects:
  - Diminished ability of rival to compete
  - Enhanced market power of monopolist
  - Harm to consumers
  - Negative contracting externality
- Analysis and balancing of procompetitive justifications
  - Requires existence of (different) contracting externality to rationalize unusual contracting forms or pricing mechanisms
- Procompetitive and anticompetitive externalities leave a distinctive empirical trace in the record
  - Negative contracting externality must exist for exclusionary conditions to defeat Bork Critique
  - Different contracting externality must exist to rationalize procompetitive justifications

## A simple visual aid: primary mechanism of antitrust harm in both predation and exclusion cases

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# A simple visual aid: ZF Meritor v. Eaton



- Databook restrictions
- Databook removal
- Pricing penalties
- ?? Other threats ?? (e.g. supply reliability)



LTAs: 78%

92%

95%

97.5%

Today's customers

Tomorrow's customers



## Key take aways

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- $P < C$  is useful to diagnose predation; not useful for exclusionary conditions
- The most important and common mechanism of harm is to prevent the rival from becoming a competitive threat in the future by depriving the rival of sales today
  - Sales by rival today typically lead to a more competitive rivalry in the future for there to be AT harm
- AT harm requires a negative contracting externality (NCE)
  - The AT harm is generally not to current purchasers
  - Simple stories that rely on single period intuition will lead you astray
- NCE can be exploited by carrots or sticks (or both)
- Pro-competitive justifications involve an externality or other market failure for which the exclusionary conditions are the solution
- Examination of the NCE and the pro-competitive rationale (market failure) will typically distinguish anti- versus pro-competitive situations

## Counseling clients

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- Market power screen - only monopolists need be careful with exclusionary conditions
- Restrictions on dealings with rivals often have procompetitive justifications
  - These always involve contracting externalities
  - Explore least objectionable alternatives to overcome contracting problems
  - Document those contracting problems
  - Document alternatives explored
- Don't confuse desire to sell more or sell more profitably with being procompetitive
  - If selling more occurs because rival is weakened, it is anticompetitive
- Price above cost in the competitive increment
- If objective is to weaken rival, consider clearly procompetitive alternative strategies

## What did the dissent in *ZF Meritor v. Eaton* get wrong from an economic perspective?

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- Coercion (both majority and dissent got this wrong)
  - Carrots or sticks, or both, can be used for exclusion
- Exclusivity mean 100% exclusive
  - Judge Greenberg rails against “de facto partial exclusivity”
- Looks at the pro- v. anti-competitive balance as a static question:
  - Dissent balanced Eaton’s motives to “win the business” against current impact on ZF
  - Real AT harm is in the future
  - Current impacts on the rival are source of future AT harm
- Saw no actual foreclosure (!)
- Commodity versus differentiated products
  - Cites A&H and HH, who also get this wrong
- Worried more about clever lawyers’ craftily worded complaints than about clever monopolist’s craftily structured exclusion

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