

When Does Predatory Pricing Work?

$$\sum_{k=1}^P \frac{\text{(Monthly Sacrifice)}}{(1+i)^k} \quad \text{VS.} \quad \sum_{k=P+1}^{P+R} \frac{\text{(Monthly Return)}}{(1+i)^k}$$

Predator wants these to be *SMALL*:

- ❖ Monthly Sacrifice
- ❖ “P” — the number of months of predation
- ❖ “i” — the monthly hurdle rate

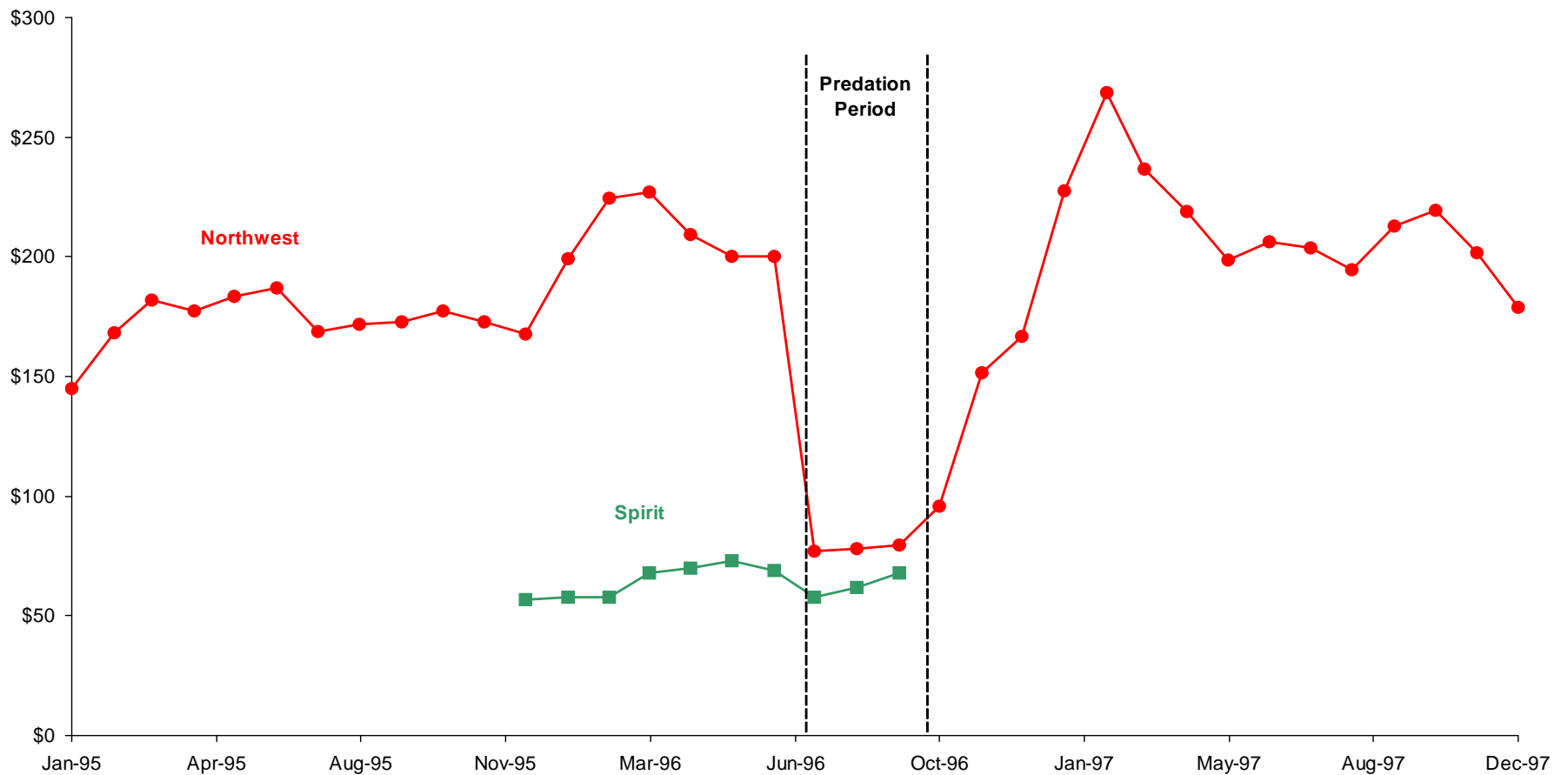
Predator wants these to be *LARGE*:

- ❖ Monthly Return
- ❖ “R”— the number of months of recoupment

An important asymmetry:
Slow Entry, but Quick Exits by Target Firms

Detroit-Philadelphia

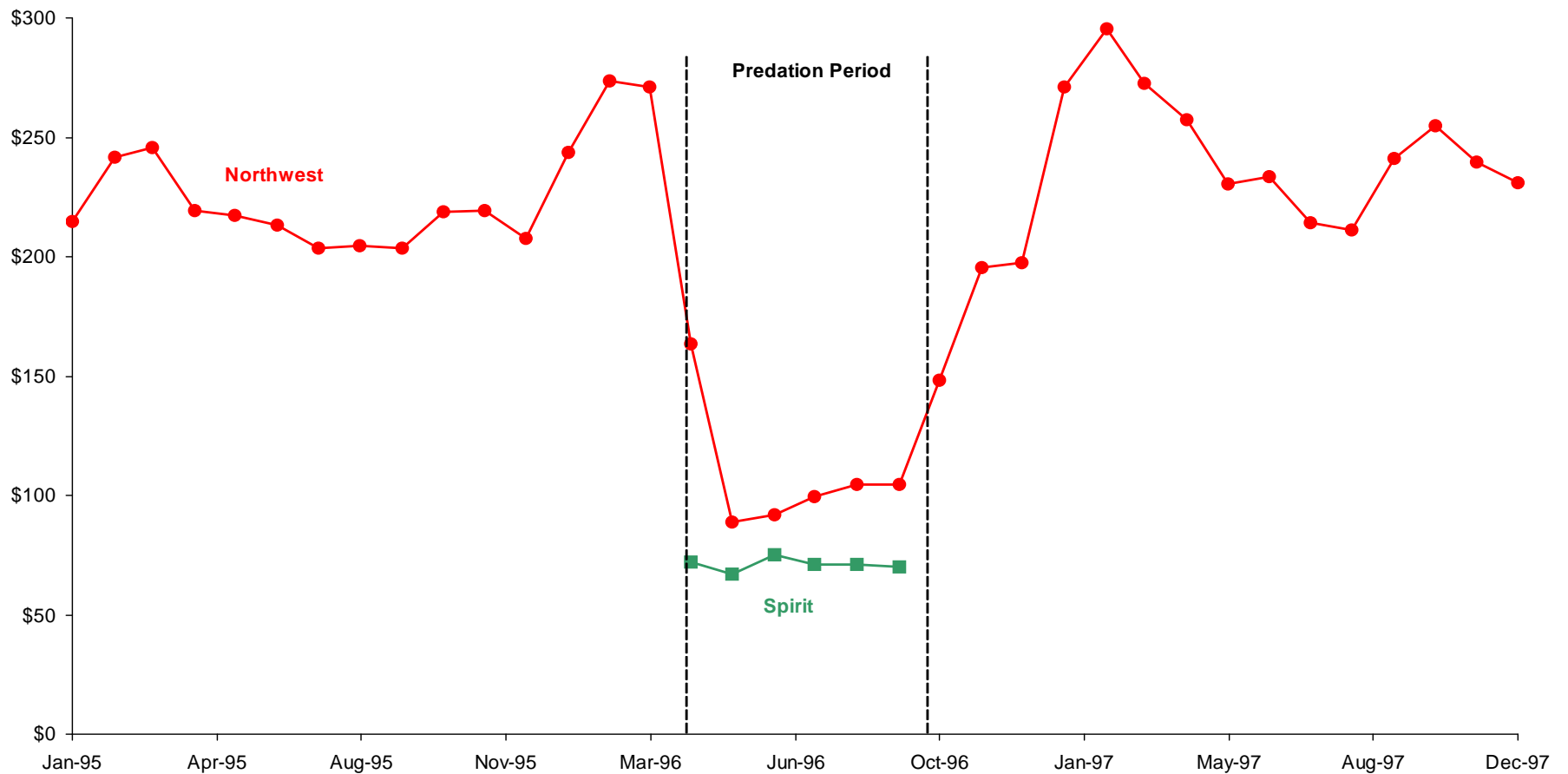
Northwest's and Spirit's Average One-Way Fares for "True Local" Passengers



*Northwest defines three types of local passengers: "true local", "connecting local", and "multi-destination local." "True local" passengers are nonstop local passengers.

Detroit-Boston

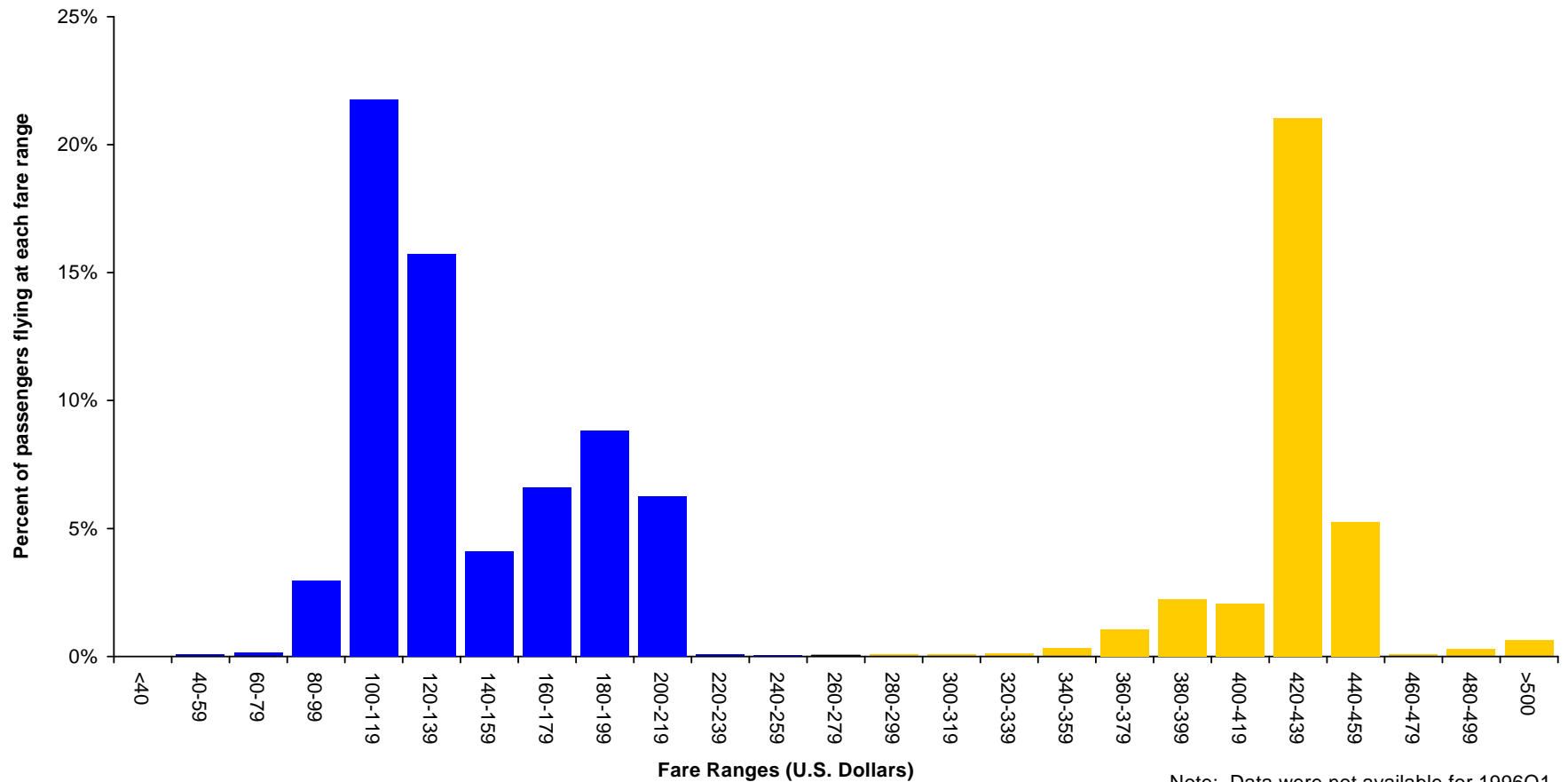
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Detroit-Boston

Northwest's Fare Distribution for Local Passengers Before the Alleged Predation 1995 Q2 – 1995 Q4



Note: Data were not available for 1996Q1.