Overview: Collusion and Competition in Oligopolistic Markets

- General Electric vs. Westinghouse
  - The competitive situation in 1963
  - Strategy consultant: recommendation
  - What GE did
  - Westinghouse consultant: recommendation
  - What Westinghouse did
  - Consent decree
- Cartels

The Turbine Generator Business

- The product?
- The players?
- The purchasing process?
- History of competition & pricing

Industry Attractiveness

Consultant's Recommendations

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GE Response: New Price Policy

- New GE price book with simplified formulas, standard features, and examples
- GE publishes the price book
- Lowered book prices significantly
- Prices calculated by multiplying book price by a standard multiplier, initially set at 0.76
- Announce: GE will sell to all customers at this published price *without exception*!

GE Response: Continued

- “Price protection clause” promising buyer that, if prices were lowered within 6-months of purchase, GE would give the price break
- Hired Peat, Marwick, Mitchell to audit compliance with the price protection policy
- Published list of all orders and quotations for several months prior to announcement.
- Announce policy with letters to clients, press releases

Why a Price Book?

- Facilitation of pricing for complex array of related products
- Steel and basing point pricing
- Airline attempts

Westinghouse Response

- Scrapped its own price book and began to use the GE book
- Adopted the 0.76 multiplier
- In June 1964, GE reduced its multiplier in response to suspected price cutting by W'hse
- In July 1964 Westinghouse
  - Announced a price increase
  - Published outstanding orders and quotations
  - Instituted a price protection clause

[*By September, both are back at pre-June level*]

Consent Decree

- Forbid price protection policy
- No distribution of price books
- No communication outside company of
  - Negotiation strategies
  - Formula or system for pricing
  - Percentage of book price
- No publication of outstanding bids
- What happened afterward?

A New Era for Anti-Trust

"The prototype price-fixing deal calls for competitors to gather in a smoke-filled room. But last week the Justice Department chalked up its first significant victory against a pricing arrangement so indirect that the supposed conspirators never even met."

-- Business Week, December 1976

Cartels

- What is a cartel?
- What's conducive to cartel formation?
  - Homogeneous products. Why?
    - Cartels often arise after "destructive competition."
  - Inelastic demand
  - High entry barriers
  - No Legal Impediments.
    - International business

Examples of Cartels

- Oil (OPEC)
- Uranium
- Diamonds (DeBeers)
- Government Supported Cartels

Understanding Cartels

Pinpoint the essentials:

- Agreement - How, where, etc.?
- Monitoring - How is it done?
- Enforcement - What is the threat to cheaters?

OPEC: Basic Analysis

- Agreement?
  - Open meetings among members
  - Production quotas set
- Monitoring?
  - OPEC monitors imports/exports, prices
- Enforcement
  - Threat to cheaters? Saudis will flood market.
- Ongoing Issues
  - External (non OPEC suppliers)
  - Internal - Domestic financing of OPEC members

What are the Most Visible Cartels in the United States?

Hints:

- Exempt from Antitrust

- There is a section of (almost) every daily newspaper devoted to them

Major League Team Sports

- MLB, NFL, NBA, NHL, etc.
- Monopolize output (games) and monopsonize key inputs (players, stadia, etc.)
- Relatively unencumbered before 1970's, now in bilateral monopoly situation with star players

Take Away Points

- Successful Collusion requires three elements: Agreement, Monitoring, Enforcement.
- Again: credibility, commitment, and the ability to understand your opponent are key aspects of strategic interaction.
- "Price protection/Most favored nation" clauses may actually limit competition.