



Monopolization Parts 1-3 (Monopoly Power in a Relevant Market) **ABRIDGED**

Antitrust
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Sherman Act § 2

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$100,000,000 if a corporation, or, if any other person, \$1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.

Mode of analysis

Monopolization claims proceed under a rule-of-reason sort of analysis, but courts tend not to use the label “rule of reason” for § 2 claims like they do for § 1 claims.

Monopolization elements

“The offense of monopol[ization] under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in [a] relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.”

United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966)

Monopolization elements

- (1) monopoly power in a relevant market
- (2) exclusionary conduct
 - a/k/a “anticompetitive conduct,”
“predatory conduct,” “monopoly
conduct”

Monopolization elements

- (1) monopoly power in a relevant market
 - 1. monopoly power
 - 2. a relevant market
 - a) product market
 - b) geographic market
- (2) exclusionary conduct

Monopoly power

Monopoly power is “the power to control prices or exclude competition.”

United States v. E. I. du Pont De Nemours & Co., 351 U.S. 377, 391 (“*The Cellophane Case*”) (1956)

IMPORTANT NOTE: What U.S. antitrust law means by “monopoly power” is different from what economists mean by that term (including as presented in our econ slides)!

Monopoly power

Monopoly power is “the power to control prices or exclude competition.”

- “Monopoly power” is more than “market power” under § 1.
 - But how much more, we can’t say.
- Theoretically, monopoly power can be proved by direct evidence.
 - But this is rarely available, so ...
- Generally, courts look to market share.

Monopoly-level market share

The law doesn't say exactly what market share constitutes monopoly power (MP), but some flags have been planted:

- 87% "leaves no doubt" that MP exists
- 80-95% is enough for Π to survive summary judgment on MP issue
- 75% means MP "may be assumed"
- >66% might be MP
- 50% is the bare minimum for MP for many lower courts
- 30% is insufficient even for \S 1 market power

(See p. 226 of Elhauge, 3d ed.)

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But if we are going to use market share to determine the existence of monopoly power, then we are going to need to know what the market is!

(See p. 226 of Elhauge, 3d ed.)

Monopolization elements

(1) monopoly power in a relevant market

1. monopoly power

2. a relevant market

a) product market

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Product market definition

“In considering what is the relevant market for determining the control of price and competition, no more definite rule can be declared than that commodities reasonably interchangeable by consumers for the same purposes make up that ‘part of the trade or commerce’, monopolization of which may be illegal.”

U.S. v. E. I. du Pont de Nemours & Co., 351 U.S. 377, 395 (“The Cellophane Case”) (1956)



The following are re-run slides ...

Elasticity

Re-run

- Elasticity can be read as “responsiveness” or “sensitivity” to change.
- If it’s “relatively elastic,” then it’s pretty responsive.
- If it’s “relatively inelastic,” then it’s pretty unresponsive.
- **Price elasticity of demand** is how responsive demand is to changes in price.

Substitution Effect

Re-run

- The more prices go up, the more consumers will tend to avoid those goods by purchasing substitutes.
- The closer the substitutes, the more likely it is that price hikes are going to make people jump ship and buy the substitutes instead.
- That means: Close substitutability tends toward more elasticity in demand.

Tending toward demand elasticity

- The goods are luxuries.
- Close substitutes exist.
- The time horizon is long.

Tending toward demand inelasticity

- The goods are necessities.
- Nothing's easily substitutable.
- The time horizon is short.

Re-run

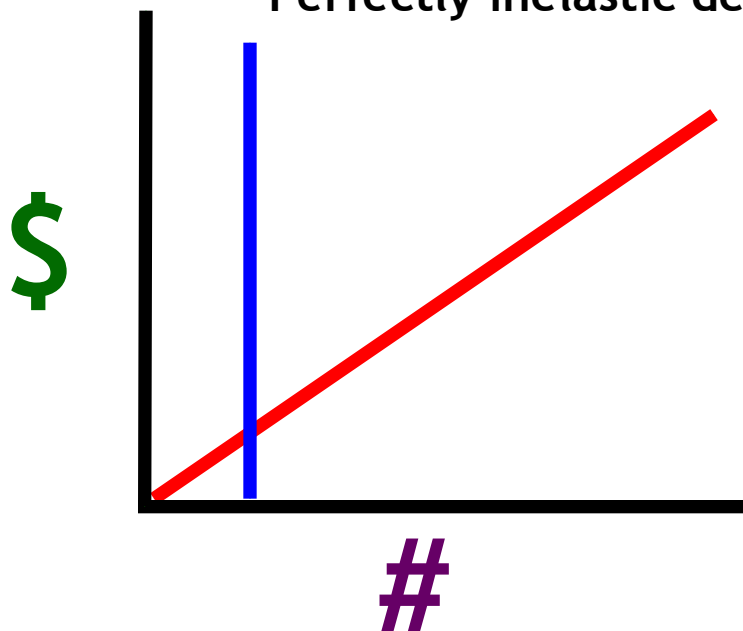
Price Elasticity of Demand

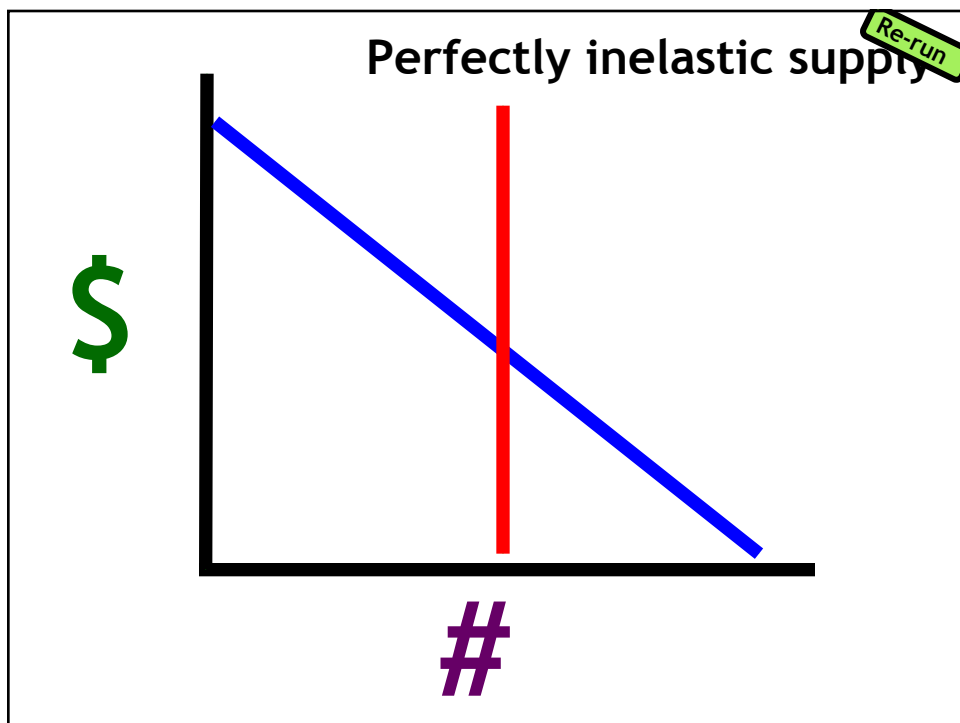
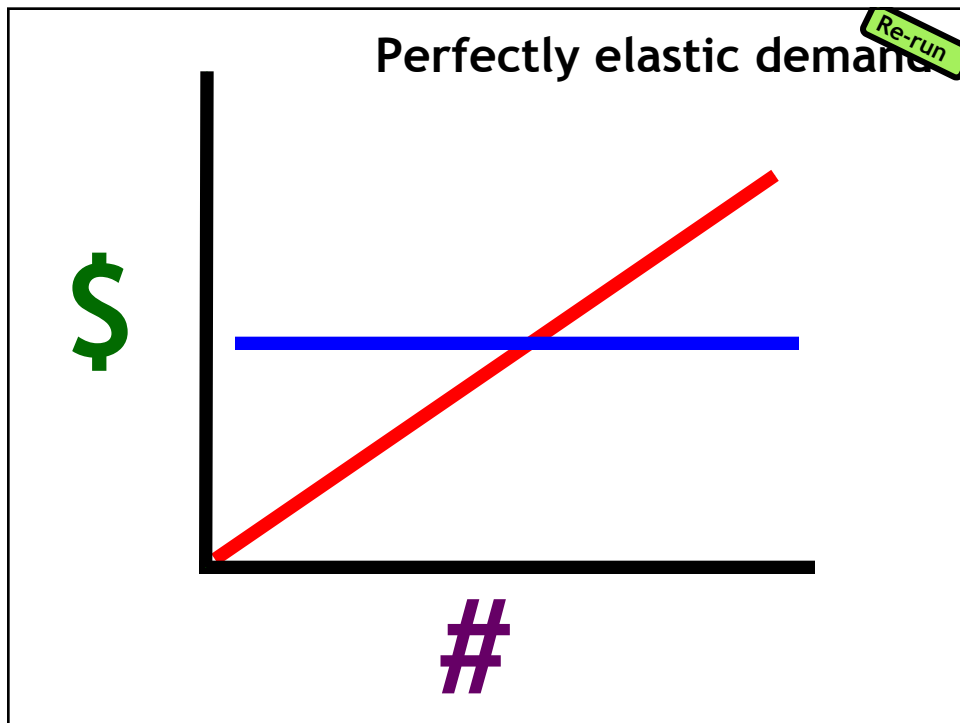
Re-run

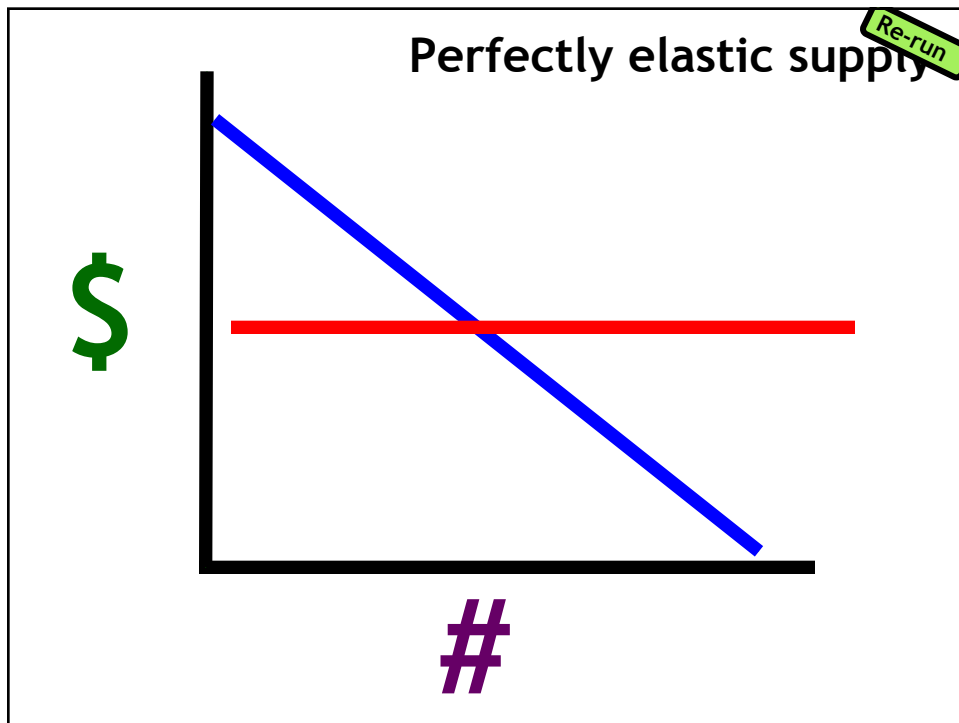
- **Price elasticity of demand** is how responsive demand is to changes in price, so ...
- If consumers will buy almost as much when the price goes up, that means demand doesn't change much with price, which is a situation where price elasticity of demand is relatively inelastic.
 - Examples: gasoline, insulin
- If consumers will rapidly cut how much they buy when the price goes up, that means demand changes a lot with price, which is a situation where price elasticity of demand is relatively elastic.
 - Examples: particular kinds of food

Perfectly inelastic demand

Re-run







Cross-Price Elasticity of Demand

- Cross-price elasticity of demand brings into consideration two different goods.
- Cross-price elasticity of demand is how responsive demand for one good is to changes in the price of another good.
- If the price of blueberries goes way up, then probably the demand for strawberries will increase.

Consider a town with two gas stations:

- If the price of Shell gasoline goes way up, then the demand for Sinclair gasoline is going to go way up.



That's the end of the re-run slides.

Cross-Price Elasticity of Demand

- Cross-price elasticity of demand brings into consideration two different goods.
 - Cross-price elasticity of demand is how responsive demand for one good is to changes in the price of another good.
 - If the price of one good goes up, then the demand for the other good will increase if the goods are substitutes.
 - If the price of one good goes up, then the demand for the other good will decrease if the goods are complements.
- Consider the example of Sinclair gasoline and Shell gasoline.
- If the price of Shell gasoline goes way up, then the demand for Sinclair gasoline is going to go way up.

Note: “cross-price elasticity of demand” and “cross-elasticity of demand” are the same thing.

Cross-Price Elasticity of Demand

Formula:

$$\text{CPED} = (\% \Delta Q_d \text{ of B}) / (\% \Delta P \text{ of A})$$

CPED = cross-price elasticity of demand

%Δ = percent change

Qd = quantity demanded

B = product B

A = product A

P = price

Cross-Price Elasticity of Demand

$$\text{CPED} = (\% \Delta Q_d \text{ of B}) / (\% \Delta P \text{ of A})$$

If the price of 8-foot redwood 2x4 decking timbers goes up from \$10 to \$50, then the demand for boxes of decking screws goes down 75%. What is the CPED?

$$\text{CPED} = (-75\%) / (400\%) = -0.18$$

A negative CPED means the goods are complementary goods.

Cross-Price Elasticity of Demand

$$\text{CPED} = (\% \Delta Q_d \text{ of B}) / (\% \Delta P \text{ of A})$$

If the price of a jumbo roll of cellophane goes from \$100 to \$110, then the quantity demanded of glassine goes up 50%. What is the CPED?

$$\text{CPED} = (50\%) / (10\%) = 5$$

A positive CPED means the goods are substitute goods.

Cross-Price Elasticity of Demand

The Cellophane Case says high cross-elasticities of demand suggests the two goods are part of the same product market.

A positive CPED means the goods are substitute goods.

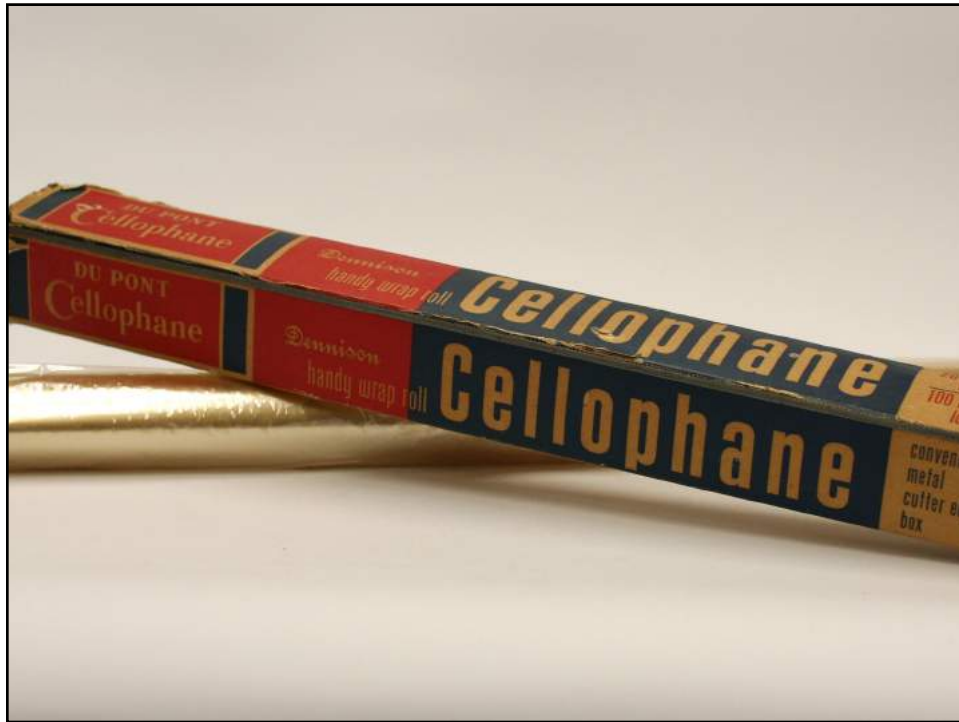
Cross-Price Elasticity of Demand

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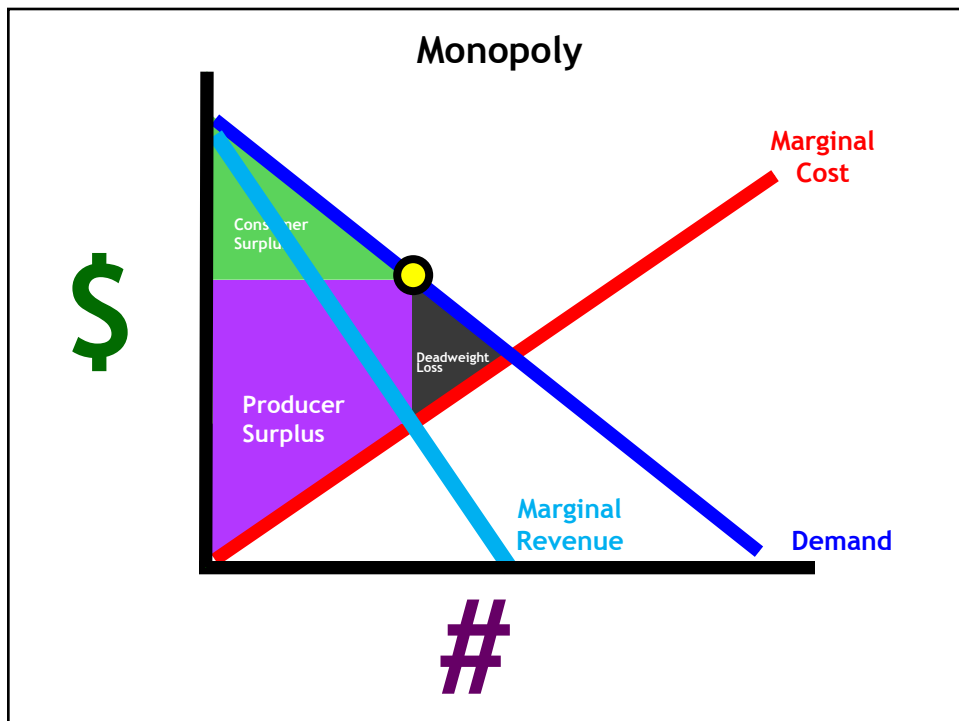
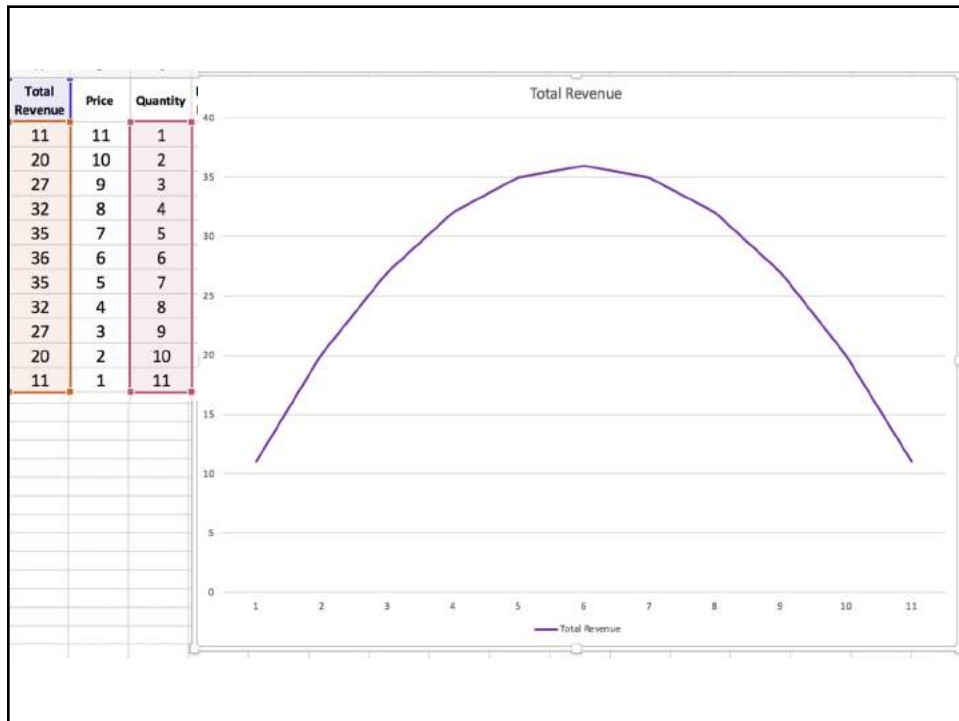
But we are given no indication in the materials for what magnitude of CPED is legally significant.





The Cellophane Fallacy

- a/k/a “the Cellophane Trap”
- If raising prices by the would-be monopolist causes buyers to flee to substitutes, that doesn’t mean the would-be monopolist isn’t a monopolist. It may just mean that the monopolist is already at the profit-maximizing output level.



Using cross-price elasticities of demand

- You can't take anything from high CPED at current price levels, since the defendant may already be at the profit-maximizing monopoly price.
- You can conclude from a high CPED at competitive price levels that there's a single market.
 - But buyer-substitution rates in a competitive market aren't observable in a non-competitive market, where market power is already being brought to bear.
- You can conclude from low cross-price elasticities of demand that there are separate markets - whether at current prices (whether competitive or not).

Cross-Price Elasticity of Demand

$$\text{CPED} = (\% \Delta Q_d \text{ of B}) / (\% \Delta P \text{ of A})$$

If the price of light bulbs goes from \$1 to \$2, then the quantity demanded of candles goes up 0.000000001%. What is the CPED?

Let's just agree that
the CPED is "very low."

This does not suggest light bulbs and candles are substitute goods and therefore should be in the same market.

Determining a relevant product market

There is widespread agreement that whether a given market counts as a relevant market ultimately depends on

whether the rate of buyer substitution to other items would constrain a monopolist in the posited market from significantly raising prices above competitive levels

(Elhague 3d ed, p. 240)

FTC/DOJ merger guidelines' Hypothetical Monopolist Test

A “relevant product market” is one where, if one firm was the only seller of that product, they would be able to impose a small but significant and non-transitory increase in price (SSNIP). “Small but significant” is quantified at at least 5%.

Consider:

- All paper manufactured from trees felled on a Tuesday in Klamath County, Oregon.
- All wine manufactured from grapes grown in Napa County, California.
- All blueberries never exposed to chemical herbicides and insecticides and therefore certifiable as “organic.”

Monopolization elements

(1) monopoly power in a relevant market

1. monopoly power

2. a relevant market

a) product market

b) geographic market

(2) exclusionary conduct

Geographic market

A geographical market is the geographical area in which customers are willing to go to find substitutes in response to an increase in price and where suppliers are willing to come in response to an increase in price.

Geographic market

Consider:

- Every gas station within a three block radius of the law school raises prices by 5% over rivals outside that zone.
- Every gas station in Norman raises prices by 5% over rivals outside the city.
- Every gas station in Oklahoma raises prices by 5% over rivals outside the state.

Geographic market

Consider:

- All carpet cleaning services in Norman raise their prices by 5% over rivals outside the city.
- All carpet cleaning services in the Oklahoma City metro area raise their prices by 5% over rivals outside the metro.
- All carpet cleaning services in Oklahoma raise their prices by 5% over rivals outside the state.

Monopolization elements

(1) monopoly power in a relevant market

1. monopoly power

Now we're coming back to this.

2. a relevant market

a) product market

b) geographic market

(2) exclusionary conduct

Monopoly power

It's mostly about market share ...

But also relevant are:

- barriers to entry
- capacity constraints
- changing consumer demand
- demand elasticity

Monopoly power

It's mostly about market share ...

But also relevant are:

- barriers to entry
- future capacity constraints
- changing consumer demand
- demand elasticity

Barriers to entry

Key point: Even if a firm has 100% market share, there will be no monopoly power if there are no barriers to entry - meaning it is very easy for competitors to jump into the market.

Barriers to entry

Barriers to entry are things that stop market entrants. If there are no barriers to entry, then it is easy for competitors to spring up.

Examples of barriers to entry:

- huge fixed costs, start-up costs
- government regulations
- patents, other IP rights
- lack of access to needed inputs or essential resources
- network effects

Barriers to entry

Barriers to entry are things that stop market entrants to entry, then it spring up.

Examples of barriers to entry:

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- government regulations
- patents, other IP rights
- lack of access to needed inputs or essential resources
- network effects

But note: The Chicago School, which is very influential in the courts, says huge fixed costs / start-up costs don't count if the alleged monopolist has the same costs.

Monopoly power

It's mostly about market share ...

But also relevant are:

- barriers to entry
- future capacity constraints
- changing consumer demand
- demand elasticity

Monopoly power: future capacity constraints, changing consumer demand, demand elasticity

future capacity constraints

- If an alleged monopolist won't be able to produce in the future, then it may have no monopoly power, such as a coal company that is out of coal reserves.

changing consumer demand

- If consumers no longer want the alleged monopolist's product going forward, than past dominant market share may not be probative.

demand elasticity

- Even with overwhelming market share, if consumers can very easily do without the product, then an alleged monopolist may not have monopoly power.

Monopolization analysis to-do list

- (1) monopoly power in a relevant market
 - 1. figure out the relevant product market
 - 2. figure out the relevant geographical market
 - 3. look at the market share
 - 4. consider barriers to entry
 - 5. consider whether future capacity constraints, changing consumer demand, or demand elasticity might let an alleged monopolist off the hook
- (2) exclusionary conduct
 - [for this analysis, you'll use what we cover next ...]*

Hypotheticals ...

Hypo: Landers Lawn Care

Hypo: In Verdant Valley, a town of 50,000 people that is a three-hour drive from any other town, there is only one provider of lawn mowing services: Landers, which has 238 customers. The closest there is to other firms providing such a service are arborists that trim trees. *Does Landers have monopoly power?*

Hypo: Landers Lawn Care

Does Landers have monopoly power?

Almost certainly not. The relevant product market appears to be lawn mowing services. Arborists are a separate market, because tree trimming is not reasonably substitutable for lawn mowing. The relevant geographical market appears to be Verdant Valley, because you can't take your lawn out of town to be mowed, and probably no one is going to drive six hours round-trip to mow your lawn. The market share in this market is 100%. That's more than sufficient for monopoly power just in terms of market share, but there are essentially zero barriers to entry. Anyone can get a lawn mower and start mowing people's lawns.

Hypo: Facebook

Hypo: Let's stipulate that the relevant product market is social-networking services that allow friends to post, view others' posts, make comments and register likes - with integrated messenger functions, and that the relevant geographic market is the world. Let's suppose Facebook's share of this market is 93%.
Does Facebook have monopoly power?

(This is for discussion in class ... There's no pre-prepared answer slide.)

Hypo: Vayatom

Hypo: Suppose Vayatom builds nuclear power plants for electric utilities, and suppose it costs \$4 billion to build a staff of engineers and to design and test a new nuclear reactor and plant facility that can be marketed. Vayatom has:

- 85% of the new nuclear plant market worldwide
- 100% of the new nuclear plant market in the USA
- 7% of the new power plant market in the world
- 1% of the new power plant market in the USA

Does Vayatom have monopoly power?

(This is for discussion in class ... There's no pre-prepared answer slide.)