Competitive issues in two-sided markets

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Anne Perrot

Introduction

- Firms operating in the digital economy: more prone to become dominant
  - Direct and indirect network externalities
  - Efficiencies associated with the number of users: more users generate more interactions
- Emergence of big platforms, « internet giants », like the GAFA (Google Apple Facebook Amazon), are all two sided platforms
- Therefore more and more work and cases in the two sided context

Characteristics of a two sided market

- The platform facilitates or allows transactions between two sides of a market
- *Indirect* externalities between both sides of the market
- Not only the level but also the *structure* of prices matter
  - Absent one of these characteristics, vertical relationship or any other type of market
  - A super market is not a two sided platform
  - A payment system (cards) is a multi sided market

Economic mechanisms

- Virtuous circle of network externalities
  - Direct network externalities: social networks rely on their ability to attract users, users derive a higher utility, the larger the network
  - *Indirect* network effects at the core of two-sided platforms:
    - E-commerce: externalities between producers and consumers
    - Exchanges
    - Applications platforms (developers / users)…
    - Search engines : content providers/users of the engine/ advertisers

Economic mechanisms (2)

- Some usual mechanisms become false:
  - One side can subsidize the other one, the price may be 0 on one side without any predation
  - The level of prices is less important than the *structure* of prices to assess the existence of an anticompetitive behavior
  - Efficiency conditional upon the (large) size of the platform
  - Strong market forces toward monopoly
- Separation between pro and anti competitive mechanisms : tricky

Important features

- Multihoming/ single homing: can an agent on side A belong to several platforms without substantial costs or not?
- Single homing implies a restricted access agents of a given side, can derive from the intrinsic properties of the platform, or from exclusivity contracts

An example of a difficult case for competition policy and firms

- Exclusivity contracts: offer an example of a practice with ambiguous effects
  - Pro-competitive effect: allow price differentiation between platform and may prevent switch to monopoly
  - Anti-competitive effect: Can also prevent the development of alternative platforms if there are too many exclusivity contracts
  - A « small amount » of exclusivity can be profitable to competition
  - Problem: how « small » should be this amount?
- Exclusivity forces single homing where multi homing would be possible

The right timing of intervention in two-sided markets : too early/ too late

- However, once a platform has become dominant, it is very difficult to challenge its position
- For competition authorities, the right timing of their interventions may be difficult to determine
- Examples : Google as a search engine
  - classical example of a two-sided platform that relates audience to (on line) advertisers
  - Free for internet users while advertisers pay for space, keywords…
  - How to control Google's abuses now?

An example of a two-sided effect taken into account in a merger case

- The Conseil de la concurrence examined a merger between local newspapers (05-A-18) and stated that
  - The increase of the prices of the newspapers of the merged entity would lead to a loss of readers
  - This loss would affect the revenues on the advertisers' side (« two sided » effect)
  - Therefore there would be one positive effect (increase of the unit margin) and two negative effects (loss of sales, loss of advertising revenues)
  - Therefore unilateral effects would be less likely than in an usual market

Conclusion

- Due to the characteristics of the digital economy, more and more markets have two-sided aspects
- Efficiency is related to the size of the operations, so that dominant positions are the rule rather than the exception
- Many behaviors (exclusivity contracts, specific pricing schemes) can have pro or anti competitive consequences, depending on the context
- Adequate policy design for competition policy (timing, nature of the interventions) may be difficult to determine