Yale SCHOOL OF MANAGEMENT

Competition Enforcement and Digital Platforms

Fiona Scott Morton
Theodore Nierenberg Professor of Economics
Yale University School of Management

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Characteristics of Platforms

- Economies of Scale (low or zero MC)
- Economies of Scope (installed base)
- Increasing returns to data
- Network Externalities, so prone to “tipping”
- Often two-sided

⇒Large firms => concentrated market structure
⇒Competition *for* the market, rather than *in* the market

Consumer behavior shapes market structure

- Scale, scope, data and network externalities

And, biases demonstrated by behavioral economics

- Status quo or default bias
- Impatience or hyperbolic discounting

So, consumers do not

  - Scroll down to see more search results
  - Multi-home
  - Change default settings, remove default apps

=> Makes entry much harder; consumers don’t switch

=> Little entry, so high concentration persists

Entry is valuable

Entry increases competition

- whether the entrant is vertical or horizontal,
- successful, nascent, or potential,
- or another large platform in an adjacent space.
- Any kind of entrant provides choice, different features different quality; or the threat of those options spurs the incumbent

$\Rightarrow$ lower prices, higher quality and more innovation

$\Rightarrow$ Entry raises consumer welfare

A word on “free”

- “Free” is not a special zone where economics or antitrust do not apply
- “Free” means the money price is set to zero, rather than $2 or -$2, and other, non-monetary, conditions could be required
- Competitive prices could be negative: the consumer’s data is so valuable that the platform would pay money as well as free services to get it
- It could be that insufficient competition results in a platform marking up this negative competitive price to zero
- Today digital services are bartered by platforms in exchange for consumers’ privacy and data
- In principle, both services and data have market prices

Harms from market power

- Prices:
  - Advertisers may pay markups for online ads
  - Consumers may pay markups for services
- Quality:
  - Digital businesses learn by using high-dimensional, large datasets to explore every nook and cranny of consumers' behavioral biases
  - A platform uses this learning to respond to user's data in real time and offer targeted sales (e.g. makeup to depressed teenagers).
  - Framing, nudges, and defaults can direct a consumer to the choice that is most profitable for the platform but represents low quality content for the consumer

Harm to innovation

- Insufficient competition and entry result in harms to investment and innovation
- Economic research that concludes that anticompetitive creation or maintenance of market power will cause a reduction in the pace of innovation
- The lessening or blocking of innovative entry is of particular concern given its value to consumers

=> Critical harms learned from past tech antitrust cases, IBM and Microsoft, was the harm from control of the direction of innovation by a powerful company

Lack of Entry

- If market structure is concentrated, competition comes from entry and overthrow of incumbent
- But we just noted that entry is difficult:
  - Entry barriers like network effects, scale
  - Entry barriers like myopic and inertial consumers
  - Anticompetitive conduct like exclusive contracts, bundling, technical rules
  - Acquisition of small entrants by incumbent platform that represent nascent or potential competition
- One of the most helpful policies a government can adopt: find a way to lower entry barriers, protect entrants, induce more entry

Entrepreneurs and innovation

- A VC has little incentive to invest in an innovative startup that will implicitly or explicitly compete head-on with a tech giant
  - Will be excluded by platform (e.g. Vine)
  - Will be bought by platform (e.g. Instagram).
  - To the extent this is profitable, it also incentivizes duplication (e.g. pay for delay) which is inefficient
- Suppose exclusion by, and merger with, platform both become more difficult as competition enforcement improves
  - Harder to get bought by platform → less profit and innovation
  - Easier to take share from platform → more profit and innovation

Disintermediation by complement

- If a platform's partner is able to directly access and serve the platform's customers, it might disintermediate or replace platform
- Platform will therefore position itself as a mandatory bottleneck between partners and customers
  - Platforms can supply key complements themselves
  - Platforms can steer customers to complements of most benefit to them
  - Platforms typically maintain control over the user relationship to prevent disintermediation
- This concern must be taken into account in merger analysis. Is a current complement a future threat to an existing platform? And is this the reason for the acquisition or conduct?

Specific antitrust tools needed for improved enforcement

- Acknowledgement of the role of behavioral biases in a) the creation of market power and b) their effect on the quality of content
- The measurement of quality in light of zero money prices and implications for quality-adjusted prices
- The critical impact of potential competitors and nascent competition on consumer welfare
- Sophisticated market definition: what are consumers substituting between, whether there is competition on the platform between complements or competition between platforms
- Analysis of the specific exclusionary conduct in question and its anticompetitive effects

A regulator can establish general conditions conducive to competition

- Routinely collect data on digital transactions and interactions, and make public to the extent possible; policy makers and researchers can assess the performance of the sector.
- Create “light touch” behavioral nudges when they will make markets more competitive; make dimensions of competition more salient
- Facilitate open standards in such areas as micro-payments and digital identities
- Platform to Business regulation

Remedies

- When violation of competition law, antitrust authority devises a remedy
- Structural remedies most desirable: e.g. divestiture
  - Calls everywhere for FB to divest Instagram and WhatsApp
- But it is KEY to choose a remedy that restores the lost competition
  - Not a fine, which does nothing to help market structure
  - Zuck is ‘scrambling the eggs’ so divesture will not be effective
  - Better option: mandatory interoperability of FB

- When restoring the lost competition involves a behavioral remedy, better for a regulator to oversee because tech evolves. True also for:
  - Data sharing, full protocol interoperability, non-discrimination requirements, unbundling content from a platform, etc

Conclusion

- While there are downsides to both increased antitrust and new regulation (capture, pace of innovation), the costs of no oversight are higher than commonly thought even a few years ago: balance of harms has shifted significantly
- Antitrust works well when agencies are quick and courts enforce the law well, but not a complete solution even in that world
- Regulation needed for all the non-competition topics still to come, but also to design competitive markets, lower switching costs, and protect entrants
- Together, can create healthy competition in this sector