Product distribution restraints are not equal, research shows

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Heski Bar-Isaac is a Professor of Economic Analysis and Policy at the University of Toronto's Rotman School of Management. He is a CEPR Research Fellow and Associate at CRESSE. He is Editor of the Journal of Industrial Economics and member of the AER's Board of Editors. Credit: Rotman School

Sometimes, there's the "price" and then there's the price.

Online shoppers may be pleasantly surprised to find the price of their chosen item has dropped once they've moved to the checkout phase of their purchase.

It could be because they are the beneficiary of something called a Minimum Advertised Price restraint, or MAP. That's where a manufacturer limits a seller from advertising a product below a certain price threshold. Consumers, however, may still be able to buy the product for less in store or at the moment of online checkout.

Regulatory authorities and critics concerned with anti-competitive practices have frequently considered this form of "vertical restraint" as having the same marketplace impact as a restriction that prevents a seller from selling a product below a certain price, called Resale Price Maintenance (RPM). That's a mistake, say researchers.

Using three different scenarios, Heski Bar-Isaac and John Asker illustrate that MAP has different impacts on competition and consumers than RPM, depending on market conditions. Because of MAP's greater flexibility, there are circumstances where MAP can be more beneficial than either RPM or no restrictions, and other circumstances where it is detrimental in comparison to both

"MAP allows for different prices to be out there whereas RPM doesn't," said Prof. Bar-Isaac, who is a professor of economic analysis and policy at the University of Toronto's Rotman School of Management. Prof. Asker is a professor of economics at UCLA.

The research is particularly timely given that the use of vertical restraints in e-commerce "really seems to have blossomed," said Prof. Bar-Isaac.

MAP provides more benefit to consumers who are motivated to look around for the lowest price while still allowing manufacturers to get more money out of less price-discriminating shoppers.

Its greatest benefits are seen when retailers provide an additional service to the manufacturer as part of their agreement, such as targeted product education to customers. In this scenario, everyone wins, because manufacturers and consumers benefit from the additional education, while retailers may have the opportunity to obtain higher profit margins.

However, MAP can make it easier for manufacturers to collude on wholesale prices, when retailers might add variable markups, by including a MAP agreement as part of the collusive agreement and facilitating mutual monitoring.

The differing economic impacts illustrated by the three scenarios show that it's misguided to treat MAP as carrying the same anti-competitive risks as RPM and applying a blanket policy to it, the research points out.

"There is no one-size-fits-all scenario here, so it's important to look at things on a case-by-case basis," said Prof. Bar-Isaac.

More information: Heski Bar-Isaac et al, Blockholder voting, *Journal of Financial Economics* (2019). DOI: 10.1016/j.jfineco.2019.11.005

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