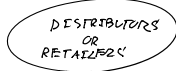


VERTICAL RESTRICTIONS : CONTRACTUAL RESTRICTIONS ON NON-PRICE TERMS

- EXAMPLE
- SALES QUOTA (= QUANTITY FORCED)
 - FRANCHISE (RIGHTS TO SELL THE PRODUCT)



- EX: CONSUMER GOODS
- CARS
 - ETC.



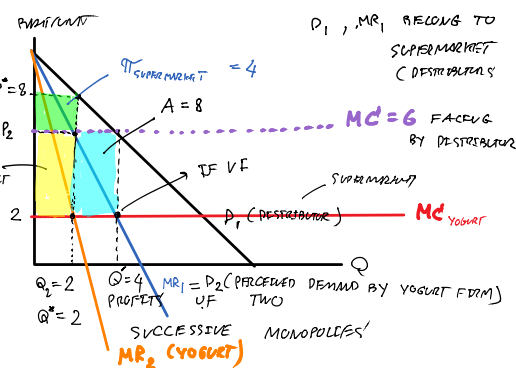
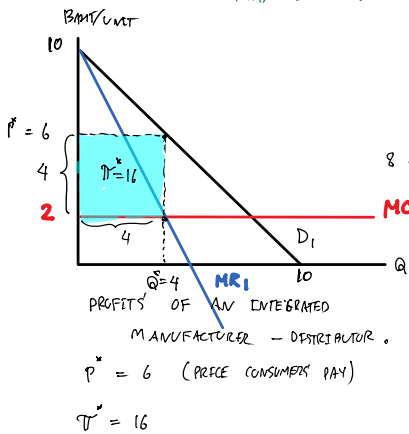
- EX: SUPERMARKETS
- BOOKSHOPS
 - CAR SHOWROOMS

Q: HOW COULD VR WORKS?

LEFT SIDE MONOPOLISTIC DOWNSTREAM FIRM (MANUFACTURER)
 MONOPOLISTIC UPSTREAM FIRM (DISTRIBUTOR)
 MORE, WE HAVE DOUBLE MARKUP FROM BOTH FIRMS IF THEY DO NOT VERTICALLY INTEGRATED.

- YOGURT FIRM CHARGES PRICE ABOVE MC WHEN IT SELLS YOGURT TO THE SUPERMARKET (FIRST MARKUP)
- SUPERMARKET CHARGES 'SELLING' PRICE ABOVE MC WHEN IT SELLS YOGURTS TO CONSUMERS.
- SO, CONSUMERS FACE W/ DOUBLE MARKUP NOW.

HERE WE WILL SHOW THAT "DOUBLE MARKUP WILL GIVE INCENTIVE FOR THE TWO FIRM TO DO VI OR VR IN ORDER TO PROMOTE EFFICIENCY AND THE TOTAL PROFITS."



- YOGURT FIRM PRODUCES $Q_2 = 2$ AND CHARGES $P_2 = 6$ TO DISTRIBUTOR (= SUPERMARKET). THIS IS THE 1ST MARKUP
- SUPERMARKET SELLS $Q^* = 2$ (AS WELL) AND CHARGES $P = 8$ TO CONSUMERS, THIS IS THE SECOND MARKUP
- CONSUMERS PAY $P^* = 8$ INSTEAD OF $P_2 = 6$ (ABOUT 30% HIGHER)

• JOINT PROFITS = $\pi_y + \pi_d = 8 + 4 = 12$ WHICH IS LOWER THAN π OF THE INTEGRATED CASE (THE LOSS OF PROFIT = $-8 + 4 = -4$)
 NOTICE THAT π IS NOW 25% LOWER.

INCENTIVE TO MERGE ARISES THEN.

TO SUMMARISE, FIRMS AND CONSUMERS ARE WORSE OFF W/ DOUBLE MARKUPS.

THIS PROVIDES INCENTIVE TO INTEGRATE OR DO VR,

AS YOGURT FIRM PREFERENCES SUPERMARKET TO CHARGE PRICE TO CONSUMERS

AS LOWEST AS POSSIBLE, WHAT YOGURT FIRM CAN DO IS TO
WRITE A CONTRACT TO REQUIRE MINIMUM SALES THAT
SUPERMARKET MUST COMPLY. OR THE CONTRACT CAN BE ABOUT
PRICE SETTING IN BETWEEN $P_2 = 6$ AND $P^s = 8$.
