

STOCKHOLM UNIVERSITY
Department of Economics

Course name: Antitrust and Regulation
Course code: EC7114
Examiner: Astri Muren and Sten Nyberg
Number of credits: 7,5 credits
Date of exam: Tuesday, February 17, 2015
Examination time: 3 hours

Write your identification number on each paper and cover sheet (the number stated in the upper right hand corner on your exam cover). Do not write answers to more than one question in the same cover sheet. Explain notions/concepts and symbols. Only legible exams will be marked. No aids are allowed. If you think that a question is vaguely formulated: specify the conditions used for solving it.

The exam consists of 4 questions. Each question is worth 25 points, 100 points in total. For the grade E 45 points are required, for D 50 points, C 60 points, B 75 points and A 90 points. The assignment replaces question 4. If you have completed the assignment but choose to answer question 4 the best score counts.

Question 1

(i) Suppose a merger between two firms will lead to a price increase and a reduction in MC that are equally large. Illustrate the welfare effects of this in a graph and discuss how the comparison depends on the level of competition at the outset. (ii) Farrell and Shapiro examine the effects of mergers in a Cournot model. Explain when and why a merger will tend to expand output and lower price in their model. (iii) Explain the UPP test. How does it work, what does it say and what data are needed to implement it?

Question 2

Suppose an input monopolist (upstream) delivers to a firm having monopoly on the downstream market. (i) Explain what double marginalization means and its effect on economic efficiency. Illustrate this in a graph (ii) Suppose another input supplier with lower marginal cost can enter, and will find it profitable to do so unless the buyer has signed an exclusive contract with the incumbent monopolist. Explain the "Chicago" argument for why an exclusive contract is unlikely to be signed. (Hint: A graph can make it easier to explain).

Question 3

A regulated firm has accounting cost $c = \theta - e$, where θ takes values between 6 and 12. The firm's effort, e , implies a cost of $e^2/4$. The regulator can observe c but not θ or e and considers a price regulation $p(c) = a + bc$. Demand is inelastic and equal to 1 unit, and the regulator values consumer surplus more highly than profit.

(i) Determine optimal a for three cases, $b=0$, $b=0.5$ and $b=1$.

(ii) Assume that the regulator could hire an inspector who could determine the true θ . How much would a firm with $\theta = 6$ be willing to pay to have information about its θ suppressed in the three cases determined under (i)?

(iii) Discuss with reference to these results how the possibility of regulatory capture could affect regulatory policy.

Question 4 (Essay question)

Many regulated industries are characterized by the fact that a network is crucial at some stage in the production process. Describe briefly the different functions that networks can have in production and explain why networks are important in regulated industries. Describe the different ways of structuring such industries and discuss the implications of these for regulatory challenges and practices.

Results will be posted on March 10 the latest. **Good luck!**