Tacit collusion with price matching punishments

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Abstract

We re-examine tacit collusion under a simple punishment rule, in which firms match any price decrease by their rivals, but otherwise leave their prices unchanged. We provide conditions under which this simple rule is an equilibrium strategy, and sustains collusion. Interestingly, the standard ambiguous relationship between product substitutability and tacit collusion is unambiguous under this new setting. We also explain the relationship with the theories of price matching guarantees, kinked demand curves, and continuous reaction-function equilibria.