Resale Bargaining, Upfront Payments and the Countervailing Power Hypothesis

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We assess the competitive effect of upfront payments such as slotting allowances in a situation where a manufacturer faces a polarized retail sector which consists of a dominant retailer and a competitive fringe of retailers such as Chen (2003). We show that the vertically integrated profits can realize in equilibrium where upfront payments play a crucial commitment role in eliminating the vertical and horizontal externalities. Exclusion of fringe retailers may occur if slotting allowances are prohibited. But the gains are neither profits extracted from the manufacturer nor passed onto the consumers. The paper offers a theoretical basis for Stigler's criticism (Stigler, 1954) on the concept of “Countervailing Power” proposed by Galbraith (1952).