

Theory of predation and recoupment essay

[Business](#), [Company](#)



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Introduction.

This essay looks at the theory of predation and recoupment in business and market analysis. The essay makes a preview of existing legislature on predation and recoupment practices and its efficiency. They also analyzes various cases of alleged predatory practices and the outcome of these cases, benefits accrued, damaged caused and the court ruling if any. (Bolton et. al. 2006)From the discussion, I drew findings, which try to identify and vindicate the type of market that the practice is common or is possibly practiced. I also give a critique on the matter and finally outlines the recommendation in the conclusion.

Methodology.

The theory of predation and recoupment test is jargon found in business industry and more specifically the market segment. It refers to the practice of a firm to cut prices to offer prices that are only profitable to that firm due

to added market power and control. This firm is the predator, the firm is supposed to gain by eliminating the smaller competitors or even frustrating the competitive ability of other firms in the industry. Recoupment refers to the impacts of predatory pricing in terms of the benefits accrued by the predator, which in most cases is used as a test to qualify a price move to be predatory. (Koller 1971)

The federal antitrust law on predatory pricing is very clear, though some analyst have termed it an ‘out of date policy’. The legislature defines the predatory pricing as follows: a price only qualifies to be predatory when it is determined that the alleged predator priced the service or the product using or below an appropriate level of cost for the particular item. A move must pass the recoupment test; the test requires a prove showing that in deed the predator will be able to recover the losses incurred during the below cost prices. The legislature also provide another condition; the plaintiff must demonstrate to the court beyond doubts that the deed will result to prices that are higher than the competitive prices that will enable the predator to recover the losses taking into consideration the time value of money. The legislature also provides the areas where the recoupments cannot be practical, areas of diffuse and competitive markets.

Predatory pricing is strategy that has been employed from ancient times in most oligopoly markets. Empirical studies by John McGee and Roland Koller, which were published in the years 1958 and 1969 respectively, give a clear evidence of some of these practices in the past. McGee details a case of an

early 20th century involving a company named Standard Oil owned by the Rockefeller family.

Goals.

The corporation was accused of cutting the prices below appropriate measure of cost in a bid to drive out competitors who were smaller companies. The plaintiff argued that the predator would later hike the prices after the exit and recoup the investment. The verdict stated that the move was irrational and the predator would make little gain if any. (DiLorenzo 1985)

Objectives.

The studies also explores the case of ‘fighting ships’, where a shipping company Mogul Shipping company was frustrating competition and investment by potential competitors. Fiona Scott Morton detailed of how the company would cut prices to eliminate new entrants to the Chinese trade. Lord Esher also confirmed reports of the company sending empty ship to outbid competitors. The Shipping Line even made greater losses, which it could not recoup, and the moves were termed as irrational. (Koller 1971)

Discussion (Findings).

The predatory pricing has continued to be utilized as a strategy in the market. The move has however mutated or upgraded to a more coherent and rational strategy in the 21st century. This has been illustrated by recent cases by Matsushita, Brooke Group, American Tobacco Corp, Canadian Air and Microsoft. The practice has also transformed to a more complex practice with inclusion of intellectual property rights and violations. Brooke Group Ltd

versus Brown Williamson Tobacco Corp case was one of the few that predatory pricing was confirmed. Brown Williamson Corp was able to prove to the case that the Brooke's pricing would lead to unjust and high prices that would enable it to recoup the losses incurred during the predatory pricing. Therefore, the ruling found Brooke Group guilty of predatory pricing. However, Supreme Court overturned the ruling of the smaller court for lack of prove of future hike in price. (Alison. &Sufrin 2007)

Another modern case involved Canadian flight industry, where the two largest companies Air Canada and Canadian Airlines merged and slashed the prices to below unavoidable costs. (DiLorenzo 1985)The new company Air, would price below unavoidable costs in routes that competitors operated. This move was to make competitors make losses, possibly eliminate them and prevent emergence and growth of new businesses. The government found the company to have violated the anti-competition act of Canada. American Tobacco was alleged to set stores in competitor's stronghold and sell cigarette in these store below the appropriate cost in a bid to eliminate the rivals. (Alison. &Sufrin 2007)

A complex scenario of the predatory pricing, involve the intellectual property in the technology industry. The best example in this case is the Microsoft versus Netscape Communication Corporation. In the case, Microsoft was alleged to have introduced the Internet Explorer in to the Windows operating software free in a bid to eliminate Netscape. Netscape Communication Corp designed, marketed and sold Netscape Navigator browser at the time, and it owned the patents to the product. Microsoft started offering a similar

product, free of charge, and in a more accessible form; preinstalled to the Windows Operating system unlike Netscape, which one had to buy from stores. The move forced the Netscape from the industry eventually. Since the case took to the court, there has been no significant verdict that has been delivered despite several rulings favoring Netscape. Microsoft has been frustrating the ruling using appeals and other legal bureaucracies. (Swartz 1997)

In my opinion, it is clear that the theory of predatory is very complex, it is quite practical and coherent especially in today's business setting. The theory is against the principles of a free market and should be checked. The case by Netscape was valid and Microsoft acts were unjust, Netscape ran out of business unfairly and so did many people lose their jobs and source of livelihood unfairly. The theory is a threat to emerging business and it is not constructive in any way since the predator rarely gains. On the contrary when not applied, the predator can gain in the long run from expanded market. This theory mostly thrives in the oligopoly market where there are several barriers to new entrant and there are few operators in a given industry. (Easterbrook 1981)

Recommendations.

The theory has really mutated in recent times to be more coherent and complex. (Easterbrook 1981)The legislature remains out of date and incapable of curbing the destructive practice. Amendments on the Federal antitrust law are recommended for proper regulations in the business industry. The law should restrain oligopoly market actors from this practice

that has led to closure of several bright ventures. (Bolton et. al. 2006) However, it is recommended that the new ventures should focus differentiate to reduce the impact of predatory pricing.

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