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Monopoly Power with a Short Selling Constraint

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Abstract

We show if a speculator can benefit from reducing a monopoly's rents through short selling, then a speculator may take a short position in a monopoly, overcome the barriers to entry, and compete with the monopoly. The competition drives down the monopoly's rents, and as a result, the short position becomes profitable and covers the cost of entry. If entry is impossible, then the speculator may coordinate and pay the firm's counter-parties to stop trading with the monopoly rather than entering. In either case, increasing a speculator's ability to short a firm's rents results in a constraint on the monopoly and forces it to act more like a price taker. Although we are unaware of such a mechanism being attempted in practice, it does provide a potential market based approach to antitrust regulation.

Keywords: antitrust, monopoly, short selling

JEL Codes: G18, K21, L12

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