Comments on

Certification and Exchange in Vertically Concentrated Markets

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Summary of the ideas and assumptions

- Model with asymmetric information on quality (seller is privately informed while buyer is not)

- Seller can pay a certifier to credibly signal product quality to the buyer

- Or the Buyer can ask the certifier to check (perfectly) the quality provided

- The certifier is a monopoly too -> second market failure in the model

- Certification is useful because of lemon's problem (without, hight quality would be driven out)

Main results : Buyer induced certification

- Buyer induced certification: it acts as an inspection device to detect low quality sellers

- The demand for certification is high when the cheating problem is large

- The certifier has incentives to manipulate its price in order to maximize the cheating problem, i.e.
  - high uncertainty for the buyer
  - intermediate prices for the good

- For a given certification price, signalling game where the product price posted may give incentives for the buyer to demand certification

Main results : Buyer induced certification

- PBE (in mixed strategy): buyer randomizes over certification and buying decisions (having observed prices) and seller randomizes over price

- Belief restriction: extension of Cho-Kreps intuitive criterion (with more pessimistic beliefs) to select equilibrium

- Full game: if prior belief of high quality is lower than 1/2 and high quality is not too costly, then the equilibrium induces

  - the belief $\mu = 1/2$ and price $p = \left(q_h + q_l\right)/2$

  - and buyer's willingness to pay for certification is maximized

Main results : Seller induced certification

- Simpler to analyze: signalling game occurs only if the buyer does not demand for certification

- Which happens only when the certification price exceeds the maximal surplus to be extracted from the high quality seller

- The low quality seller does not demand certification while the high quality always demands it

- The certifier can extract all the surplus from the high quality seller

- Hence the certifier prefers a situation where the privately informed party demands certification

Main results : Welfare

- Trade-of:
  - with Seller induced certification, the low quality good is always sold (not the case with Buyer induced certification)
  - But, certification may occur more often under Seller induced certification (socially wasteful)

- Nevertheless, SW is higher under seller induced certification

Comments

- Very interesting model where the task of signalling for the seller is influenced by a third player (certifier) who may also influence the decision of buying certification by the buyer

- Simple model but non trivial results

- With the proposed timing, the high quality seller would prefer the buyer induced certification situation (imperfect extraction of its surplus)?

- Impact of competition between certifiers?

- Imperfect quality of certification...does it depend on buyer or seller induced certification?