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CENTRO DE ECONOMÍA APLICADA

Abstract

We study trade intermediation in markets with an underlying network structure. A seller has a single unit of a good, which can be resold via successive bilateral bargaining between linked intermediaries until it reaches one of several buyers in the network. Intermediaries have heterogenous transaction costs. We analyze the outcomes of the unique stationary Markov perfect equilibrium in the limit as players become patient. The seller's profit depends not only on the number of middlemen along the path of trade, but on the complete collection of competing paths of access to buyers offered by each middleman. The seller prefers to trade along paths that entail many local monopolies, which do not necessarily minimize intermediation or maximize welfare. A decomposition of the network into layers of bargaining power characterizes the endogenous structure of intermediation. We provide comparative statics with respect to the network architecture and the cost distribution. Transferring costs to intermediaries closer to buyers increases the seller's profit, as does vertical integration; horizontal integration has an ambiguous effect. The results have implications for the prevention of corruption in hierarchical structures and efficient production in supply chains.