Market Structure and Price Dispersion: Asymmetric Oligopoly with Sequential Consumer Search

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Abstract

This paper presents a new theory of price dispersion based on firm size. We build a model of oligopolistic price competition among n large firms with sequential consumer search in which search is with replacement and without recall. Since search is random, consumers are more likely to meet sellers from a larger firm. This reduces the consumer's outside option of rejecting a trade with a seller from a larger firm, generating a greater market power for a larger firm. For a given distribution of firm size, there is a unique stationary equilibrium, and price dispersion arises as a pure-strategy equilibrium. We show that price dispersion disappears as search frictions disappear. Interestingly, there is a non-monotonic relationship between the degree of search frictions and the degree of price dispersion.

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