

Strategic Yet Not Demanding: The Empirical Reach of Oligopoly with CES Preferences

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Abstract:

We consider the behavior of heterogeneous firms in oligopolistic markets when preferences are CES. We provide an explicit characterization of the implied passthrough-relevant demand manifold, a smooth curve representing the demand function in the space of the elasticity and curvature of demand. We show that Bertrand and Cournot competition with nested CES preferences imply the same passthrough-relevant demand manifold, but equilibrium location on the manifold depends on conduct. Through the demand manifold, we identify how Bertrand competition with CES is more restrictive in terms of predicted passthrough than Cournot competition with CES. The demand manifold also highlights testable predictions on the elasticity-curvature relationship which can be used to discriminate between monopolistic competition with variable elasticity demands and oligopoly with CES demands.