Negotiations and Exclusivity Contracts for Advertising

Anthony Dukes • Esther Gal-Or

Graduate School of Industrial Administration, Carnegie Mellon University,
5000 Forbes Avenue, Pittsburgh, Pennsylvania 15213
Katz Graduate School of Business, University of Pittsburgh, 210 Mervis Hall,
Pittsburgh, Pennsylvania 15260
ajdukes@andrew.cmu.edu • esther@katz.pitt.edu

Exclusive advertising on a given media outlet is usually profitable for an advertiser because consumers are less aware of competing products. However, for such arrangements to exist, media must benefit as well. We examine conditions under which such exclusive advertising contracts benefit both advertisers and media outlets (referred to as stations) by illustrating that exclusive equilibria arise in a theoretical model of the media, advertisers, and consumers who participate in both the product and media markets. In the model, stations sell advertising space to advertisers and broadcast advertising messages to consumers.

Conditions leading to higher equilibrium levels of advertising can be unprofitable for advertisers because high levels of advertising make consumers better informed and thus lead to fiercer product price competition. As a result, media stations may be less profitable as well because their payoff is determined as a fraction of the advertiser surplus generated in the product market.

Stations mitigate this effect by offering advertisers exclusive advertising contracts. With such contracts, consumers are less informed about competing products, yielding higher producer surplus. It is profitable for stations to offer exclusivity when commercial advertising is an important means for advertisers to inform consumers about their products.

(Advertising; Market Structure; Media)