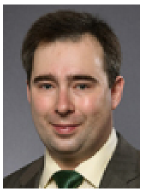
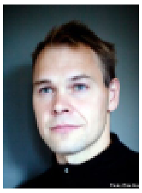
Boycotts are more likely to be effective in industries which are highly competitive

One of the most fundamental aspects of our market society is that consumers should have the ability to vote with their feet and to not buy certain products if they do not wish to. But when are these boycotts effective in causing corporations to change their ways? In new research, **Georgy Egorov** *and* **Bard Harstad** *find that boycotts should be more common and effective in competitive industries which have similar products, such as the oil industry, while in less competitive industries, government regulators may have to step in to settle issues and disputes.*

One of the most fundamental questions in economics is how we should determine which tasks should be done by the government, and what we can leave to the market. While traditional market failures are often used as an argument for involving the government, recent decades have seen an increased role for consumers and activist groups in pressuring firms to change their business practices. These groups have been successful in addressing a variety of concerns about business practices, ranging from environmental issues, such as water and air pollution, to those based on values, such as animal cruelty, child labor, or violations of privacy. To further their cause, activist groups, instead of lobbying legislators and influencing regulators ("public politics"), can run corporate campaigns that often involve boycotts to directly pressure one or several firms to change their business practices (this new phenomenon is often called "private politics").

Perhaps the most famous and vivid example of such a boycott is Greenpeace's actions against Royal Dutch Shell's attempts to sink Brent Spar, an obsolete offshore oil storage tank in the Atlantic Ocean in 1995 that caught attention throughout Europe and was particularly effective in Germany, where sales at Shell gas stations fell by 40 percent at one point. Remarkably, governments were fully on board with Shell's initial decision, and Greenpeace could only succeed by turning to consumers and organizing a boycott. Such success stories raise a natural question of whether activists and boycotts will replace government regulators as a primary way to deal with the negative effects of some commercial activities, because of their increased ability to reach consumers through new technologies.

Overall, however, boycotts are sufficiently rare (partly because many companies concede to minor demands before activists can begin one), and are not always effective at achieving their stated goals. For every Brent Spar story there is a Nestle one: for more than a decade various groups in different countries boycotted Nestle over its practices of marketing infant formula to mothers in the 1980s and 1990s, with little success, until in many jurisdictions regulators stepped in. A natural question is, which issues, for which firms and in which industries are likely to result in government regulation, in self-regulation under activist pressure, or no regulation at all?

In our work we model the interaction of a firm, an activist, and a regulator; the firm can impose permanent self-regulation at any moment; the government can impose regulation, and the activist can initiate a costly boycott and possibly call it off. We show that the likely scenario of these interactions critically depends on the competitiveness of the industry. If the industry is highly competitive, then a boycott is likely to be cheap for the activist (it is easy to persuade customers to boycott the firm as there are many close substitutes) and costly for the firm (it operates at thin margins, and consumers that switched to a competitor are unlikely to come back). Here, we would expect more boycotts and that they would be more likely to be successful. The firm is likely to give in with a high probability and without much delay during the boycott, and possibly will self-regulate even before the boycott materializes. Conversely, if the industry is not competitive, boycotts are costly for the activist and cheap for the firm to endure. In these cases, boycotts will be rare and rarely successful, and the issue is likely to be settled by the regulator.

We thus expect activists and boycotts to be common in competitive industries, whereas government regulators to be active in regulating relatively concentrated ones. The two examples above seem to fit the pattern: while the oil industry where Shell operated is highly competitive (similar product and similar production technologies), Nestle enjoyed a dominant position in food and beverages. The role of industry competitiveness, however, may explain more general phenomena, such as the relative prevalence of boycotts in the US (and to a lesser extent the UK), as opposed to continental Europe. More often than not, American firms operate in a more competitive environment, thanks to a large domestic market, whereas European firms often operate in much smaller markets. Obviously, in the recent decades the market has become much more competitive due to European integration; however, differences in local laws, languages, cultures and preferences still mean that competition between European firms is less fierce on average. This difference in competitiveness can explain why boycotts are an "American political tradition" and "American custom".

Some may argue that not all industries are more competitive in the US than in Europe; a notable example is the airline industry, which is dominated by four major airlines (American, Delta, Southwest, and United) in the US but is much more competitive, with many low cost airlines in Europe. This is a fair point, and consistently with the theory, we seldom, if ever, observe boycotts of airlines in the US. Even when some stories, such as dragging of a passenger from a flight, make some people announce their intention to boycott the company, e.g. on Twitter, such boycotts rarely take off. The airline industry is thus the exception that fits the rule.

- *This article is based on the paper, 'Private Politics and Public Regulation' in The Review of Economic Studies.*

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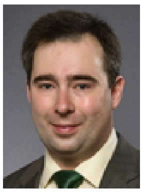

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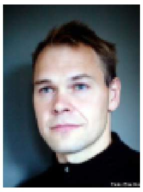
Georgy Egorov joined the faculty of the Kellogg School of Management in 2009 after receiving his PhD in Economics from Harvard University. His research interests include political economy and economic theory. He is currently working on questions related to weak institutions and their dynamics, interaction between market and non-market actors in business environments, and social image considerations in strategic decisions.



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