

Price Cycling in Retail Gasoline Markets: Theory and Evidence*

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Abstract

This paper documents new empirical evidence on equilibrium pricing in retail gasoline markets. Using daily data on retail gas prices for stations across 130 towns in Ontario for 2007-2008, we find that small and large markets (by population) exhibit pricing equilibria characterized by constant mark-ups over marginal costs, while intermediate sized markets have distinct price cycling behaviour, typically referred to as Edgeworth Cycles. We investigate how market structure affects the observed pricing behaviour, and we offer a simple theory of pricing, coordination and defection to explain the cross-sectional variation in pricing equilibria. Related anti-trust issues are also discussed.

JEL Classification: L11, L40, C21

Keywords: Edgeworth Cycles, Markov perfect equilibria, Coordination, Defection

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