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Generalized linear competition: From pass-through to policy

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Abstract Economic policy and shifts in input market prices often have significant effects on the marginal costs of firms and can prompt strategic responses that make their impact hard to predict. We introduce "generalized linear competition " (GLC), a new model that nests many existing theories of imperfect competition. We show how firm-level cost pass-through is a sufficient statistic to calculate the impact of a cost shift on an individual firm's profits. GLC sidesteps estimation of a demand system and requires no assumptions about the mode of competition, rivals' technologies and strategies, or "equilibrium" . In an empirical application to the US airline market, we demonstrate GLC's usefulness for *ex ante* policy evaluation and identify the winners and losers of climate-change policy. We also show how GLC's structure, under additional assumptions, can be used for welfare analysis and to endogenize the extent of regulation.

Keywords D43, H23, L51, L93

JEL Classification Pass-through, imperfect competition, regulation, carbon pricing, airlines, political economy.

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