

Sequential rationality

Sometimes the normal form doesn't tell the whole story...

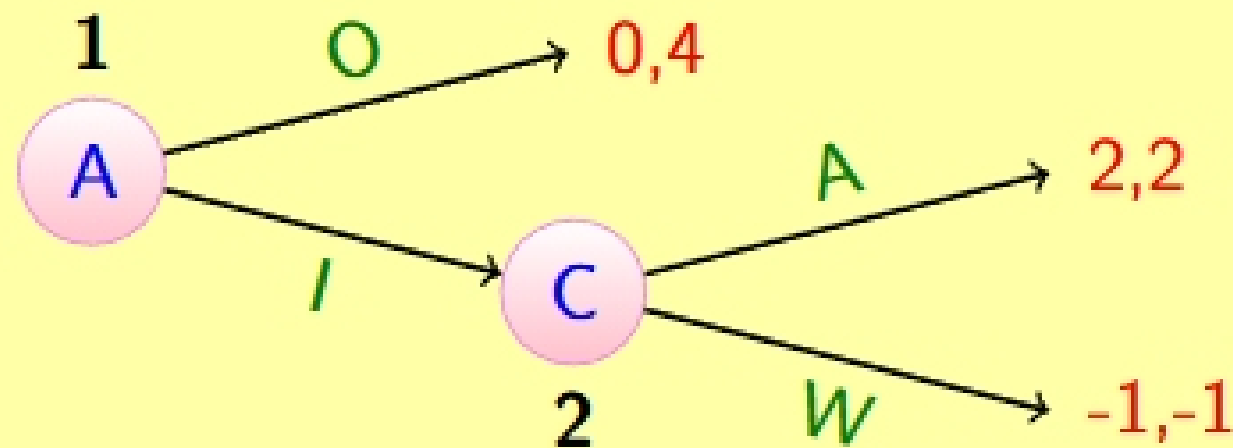
JW fig15.1

1 \ 2	A	W
I	2,2	-1,-1
O	0,4	0,4

- ▶ (I,A) and (O,W) are the (only) pure strategy Nash equilibria

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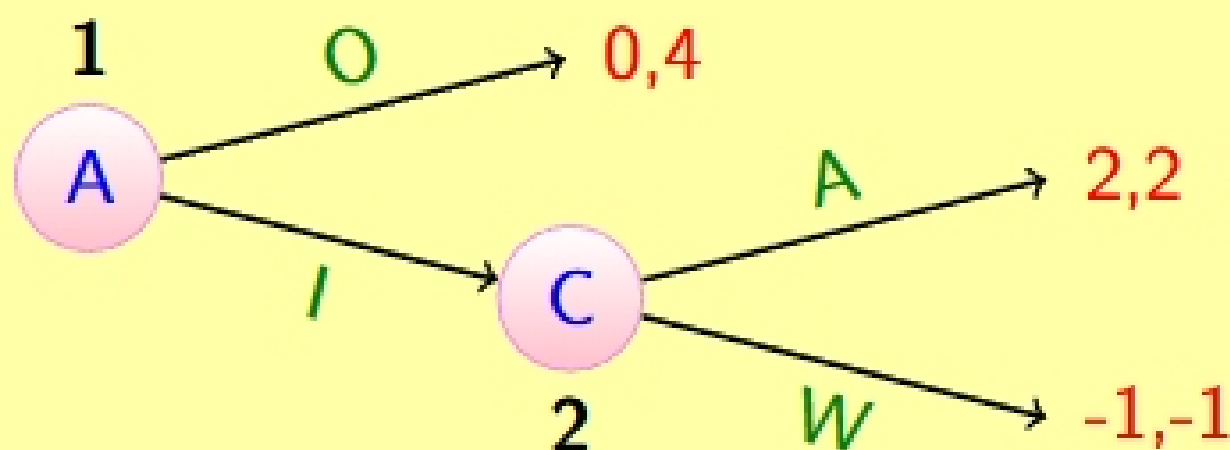
Sometimes the normal form doesn't tell the whole story...



- ▶ (I,A) and (O,W) are the (only) pure strategy Nash equilibria
- ▶ But not both N/E's are reasonable if P1=potential entrant, P2=incumbent; P1 decides whether or not to enter the market and P2 decides whether or not to engage in a price war (W) if P1 enters the market

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- ▶ (I,A) and (O,W) are the (only) pure strategy Nash equilibria
- ▶ But not both N/E's are reasonable
 - ▶ (I,A) makes sense
 - ▶ (O,W) says that P1 stays out but P2 would engage in a price war had P1 entered the market