# Bargaining, Mergers, and Investment in Incomplete Information IO*

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**Abstract**

Bargaining has come to the forefront in many applied areas in economics. The typical approaches to modelling it, based on variants of Nash bargaining, cannot be reconciled with the assumption that agents are privately informed about their values and costs, nor with the empirical observation that negotiations frequently break down. In this paper, we analyze bargaining, mergers, and investment in the incomplete information IO paradigm, and we show that vertical integration can harm social and consumer surplus, horizontal mergers make bargaining less efficient, and investment incentives align with efficiency if and only if bargaining is efficient. This allows us to analyze ways in which mergers and vertical integration affect the efficiency of investment. We provide an illustration of the straightforward application of the model to market data.

**Keywords**: second-best mechanism, (generalized) Nash bargaining, bargaining externalities, bargaining power, Nash-in-Nash, incomplete information, countervailing power
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