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Game theory and mediation

- ▣ **Game theory** deals with interactions where the actions of one 'agent' influence the outcome for the other, and vice versa.
- ▣ **Mediation:** An impartial third party helps two disputants/negotiating parties agree by meeting, holding discussions and transmitting information between the two.

Main points

1. Mediator can 'add value' even in negotiation between supremely rational, self-interested agents.
2. But rational agents might not want to mediate
3. Take this all with a pinch of salt – it's economic theory!

Situations I'm thinking of...

- Commercial dispute
- Buyer and seller haggling
- A new independent country negotiating a promise to be fiscally prudent in return for entry into a common currency...

Important characteristics:

- Each party receives a value if 'walk away' – 'BATNA'
- Mutually beneficial agreement may be possible at some 'price'
- Want to gain surplus for themselves

Why is there a role for mediation?

- In world where everyone knew each other's BATNA, less role for mediator
- But we have 'asymmetric information' and 'strategic behaviour'.

Might mean:

1. No agreement when mutually beneficial agreement possible
2. Expend resources negotiating when no mutually beneficial agreement is possible
3. Expend more resources than necessary reaching a mutually beneficial agreement

Why does mediation help?

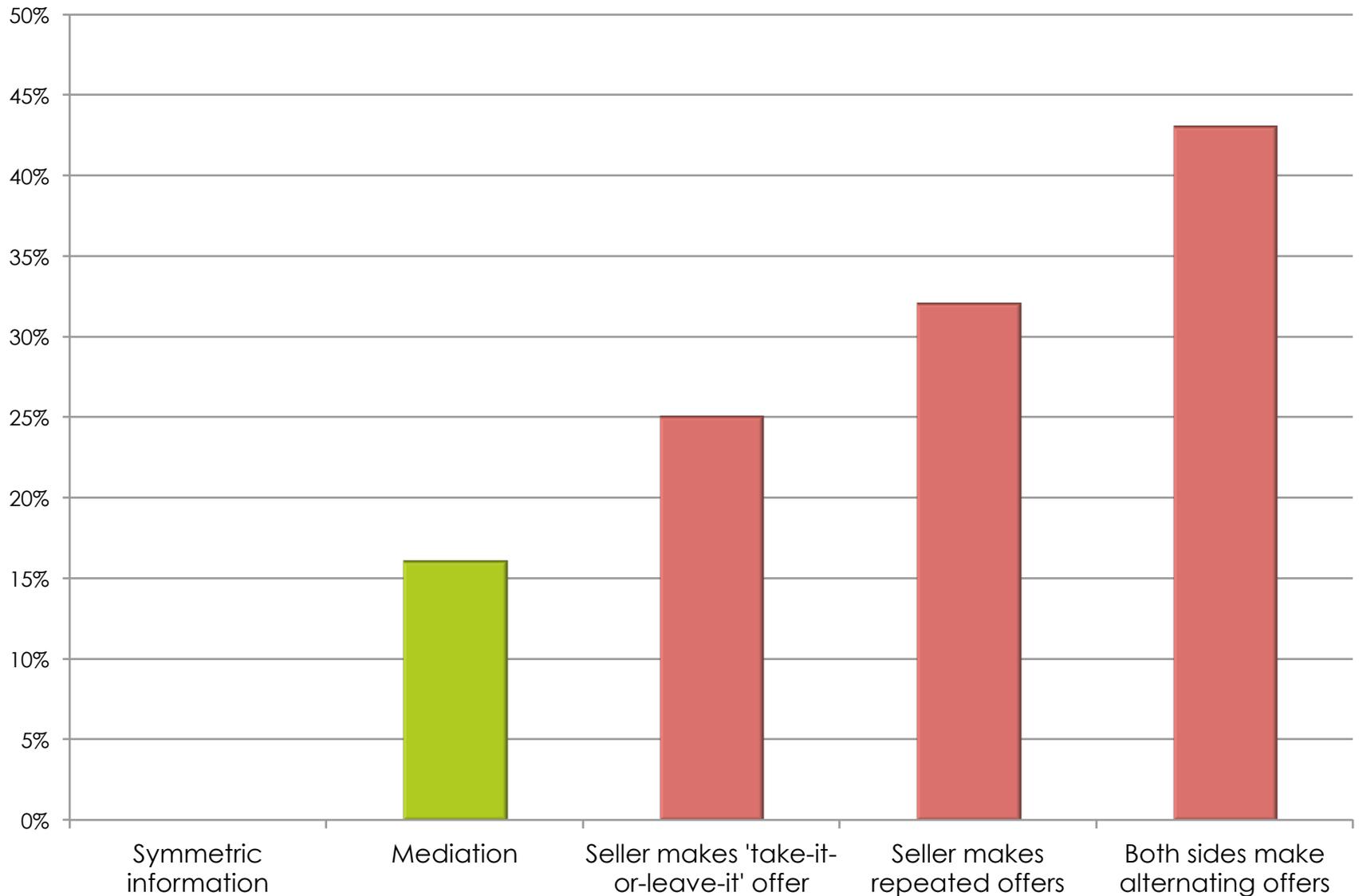
1. Can transmit partial information

- Incentive to tell the truth not be strategic
- Quickly identify if no mutually beneficial agreement possible

2. Can implement pre-agreed process

- Less incentive to be strategic
- More likely to reach agreement when this is possible
- Shorter, less costly negotiation

Average unexploited gains due to no (or delayed) agreement



Solicit offer mediation produces the highest expected ex-ante surplus of any interim efficient game.

- Myerson and Satterthwaite, 1983

In English:

If the parties knew that they were going to be entering some negotiation process the next day, but did not know their BATNAs in advance, they could choose no better negotiation process than mediation.

A twist...

- In the real world, people agree to mediate or not to mediate already knowing who they are.
- Some parties will have an incentive not to commit to mediate.
- They may succeed in claiming more of the pie for themselves, but the total lot of society will tend to be smaller.
- Could there ever be situations where we should legally mandate mediation?