Trade-ins and Transaction Costs in the Market for Used Business Jets

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Manufacturers of durable goods can encourage consumers facing transaction costs to upgrade by accepting used units as trade-ins. These “buyback schemes” increase demand for new units, but increase the supply of used units if trade-ins are resold. In this paper, I investigate the equilibrium effects of buyback schemes in the market for business jets. I find that buyback increases demand for new units by 37% at fixed prices. However, in equilibrium this increase in sales is diminished by 38% due to substitution away from new jets among first time buyers. Because of this cannibalization, offering buyback is a dominant strategy for only 3 of the 6 major firms, with 3 firms offering buyback as a best response to other firms’ policies. I show that equilibrium buyback policies can change under counterfactual market structures: a simulated merger leads to a reduction in consumer welfare, 70% of which is due to a change in buyback policy.

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