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Conclusions

In this paper, we introduced outside options in a setting in which, repeatedly, two agents take a joint action over time, cannot resort to side payments, and each period are privately informed about their favorite actions. The main results are as follows. Irrespective of how patient agents are, a mechanism that satisfies ex-post participation constraints can only attain outcomes that are bounded away from efficiency. In terms of current decisions, ex-post participation constraints introduces a new effect on the relative weights the agents have on them. Whenever a participation constraint binds, the player whose outside option became tempting is given, relatively to a forced participation setting, less weight on the current action.

Regarding the dynamics of bargain power, we proved that there will be a unique limiting distribution of power. This distribution is non-degenerate, memoryless and such that power continually changes of hands in the limit, meaning that the weight agents have on decisions varies from period to period. As a tractable way to analyze how differences in outside options shape the limiting distribution of power, we considered the extreme case in which only one of the players has an outside option. For that case, and in contrast to the case in which both players have outside options, the limiting distribution of power will be degenerate, and the player for which the mechanism has to satisfy participation constraints will eventually become a dictator.