

Efficiencies in vertical mergers: where are we and where do we go next?

Athens

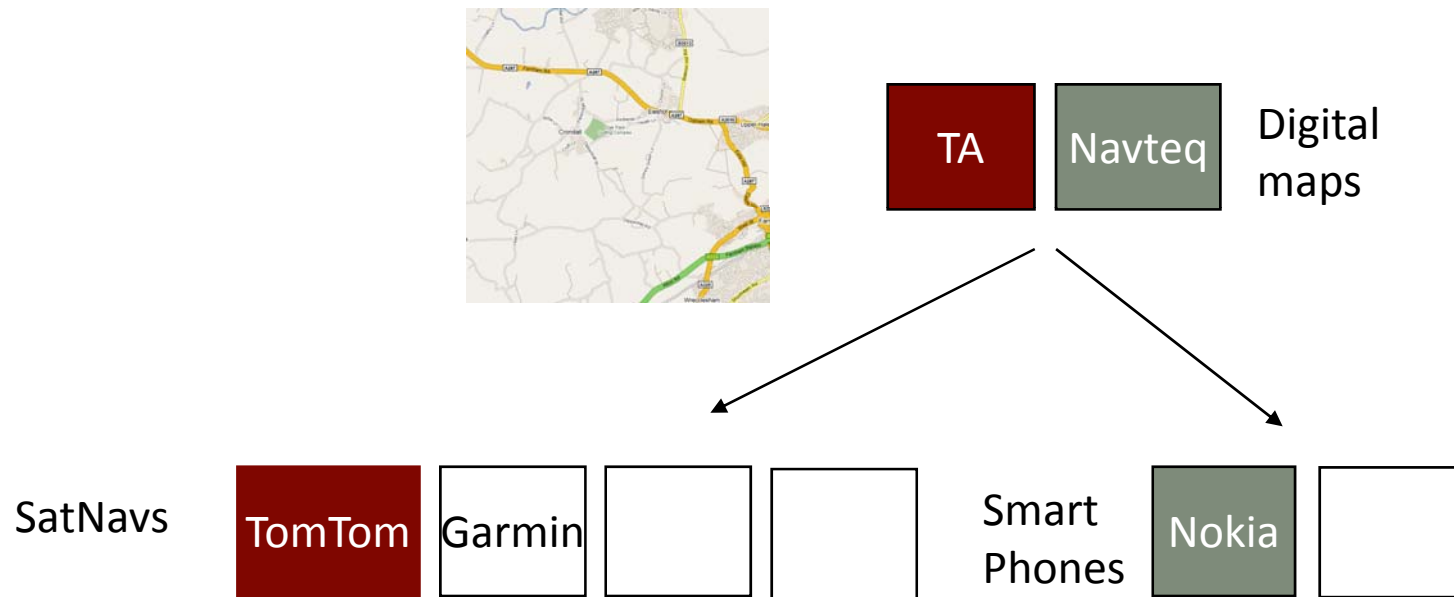
29th May 2009



Contents

1. There are potential benefits from vertical mergers
2. There are potential competition concerns
3. The net effect is often good for consumers; merger control should allow clearance based on efficiencies
4. The Commission's approach shows promise
5. Next steps

TomTom/Tele Atlas

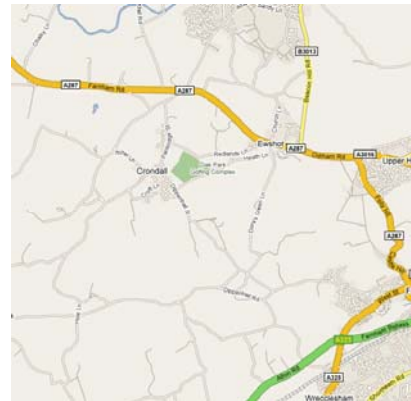


Investment efficiencies

Tele Atlas current technology



Tele Atlas digital map



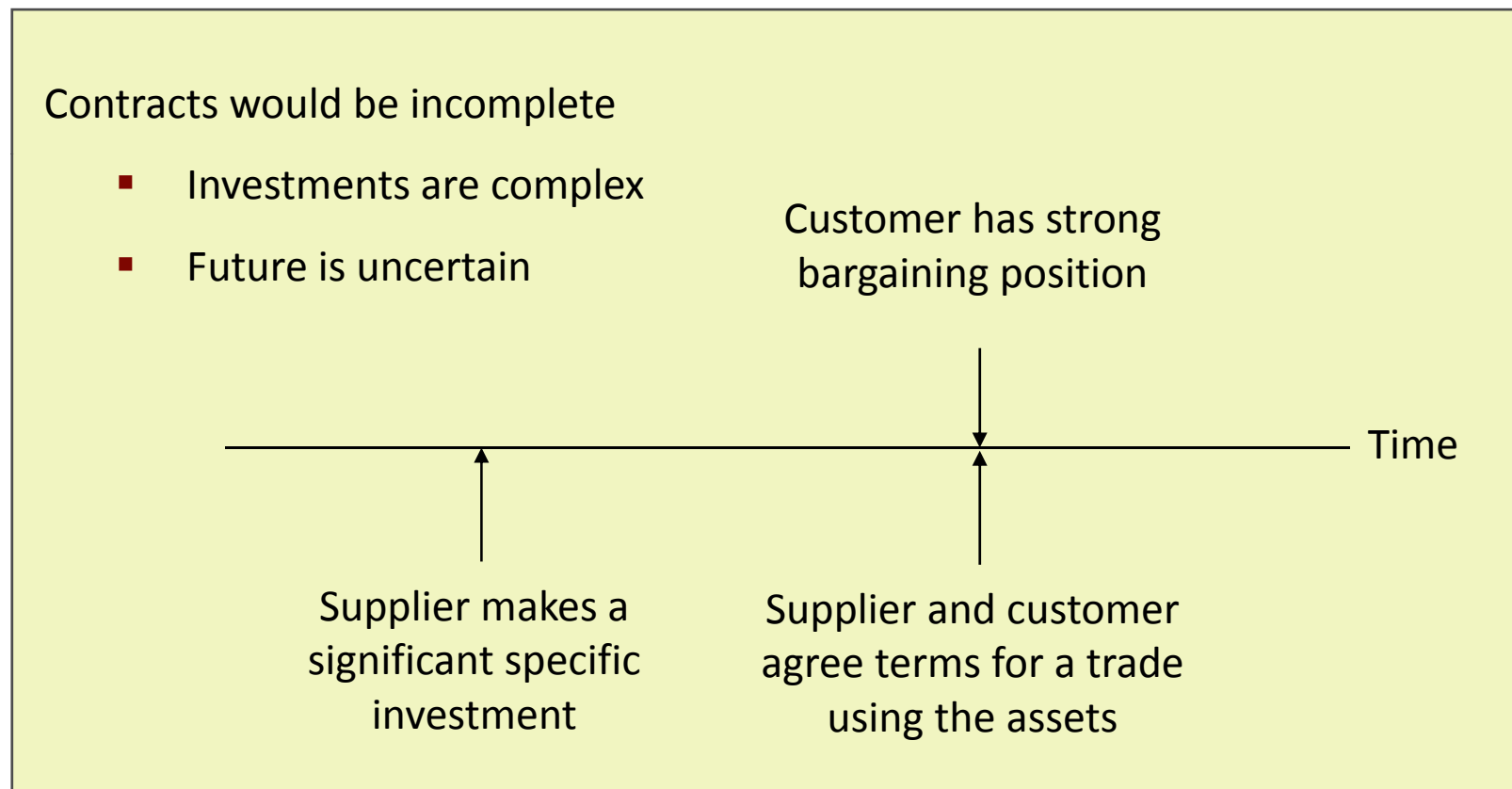
Data gathered by TomTom



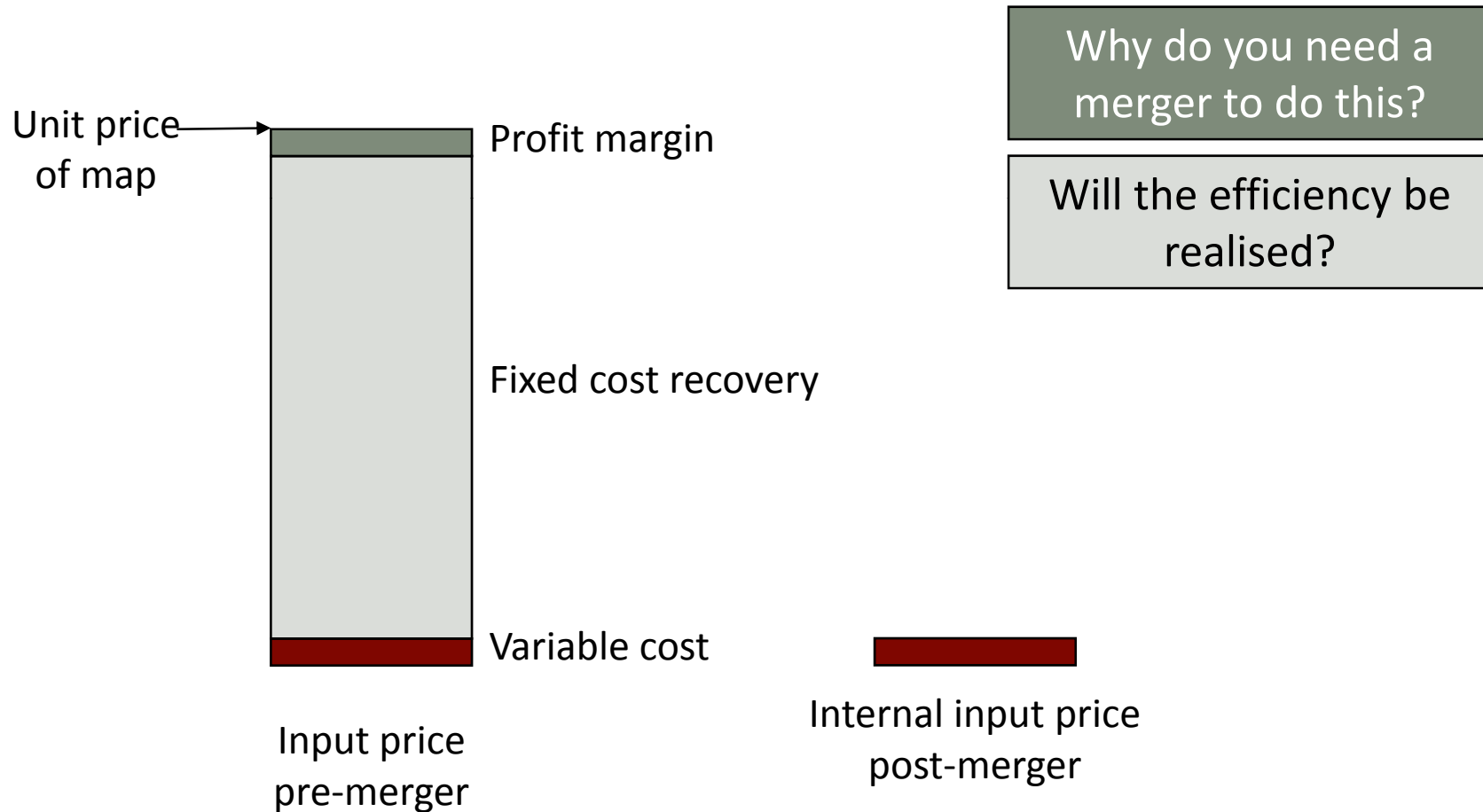
Probe data

26th March 2009

When does a merger create these efficiencies?



Double marginalisation efficiencies



Other possible efficiencies

Greater retailer effort

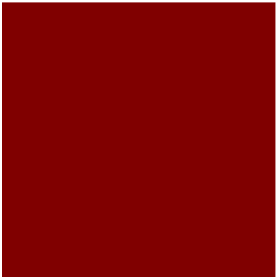
- (forwards integration into retailing)

Demand side efficiencies

- Airline mergers, Euronext / LSE proposed merger

Productive efficiency

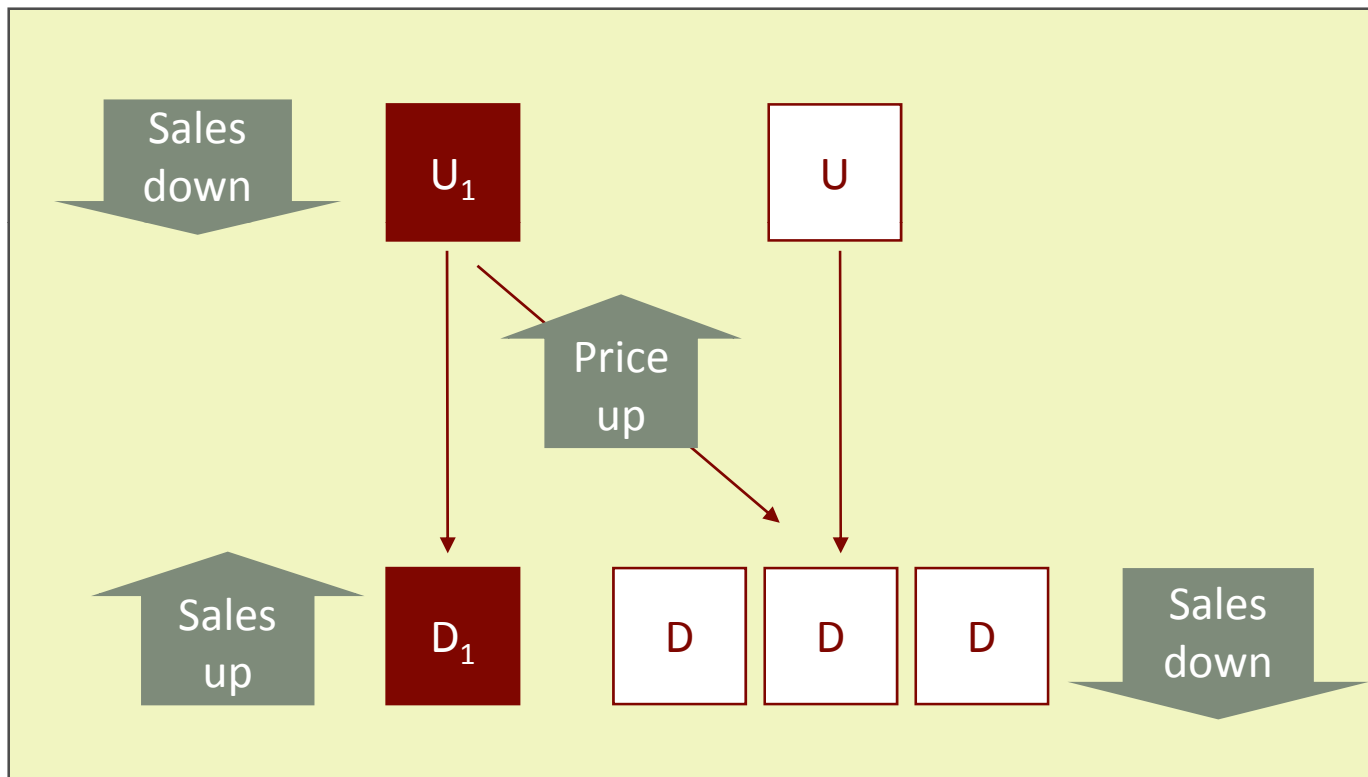
- Telecoms



Contents

1. There are potential benefits
2. There are potential competition concerns
3. The net effect is often good for consumers; merger control should allow clearance based on efficiencies
4. The Commission's approach shows promise
5. Next steps

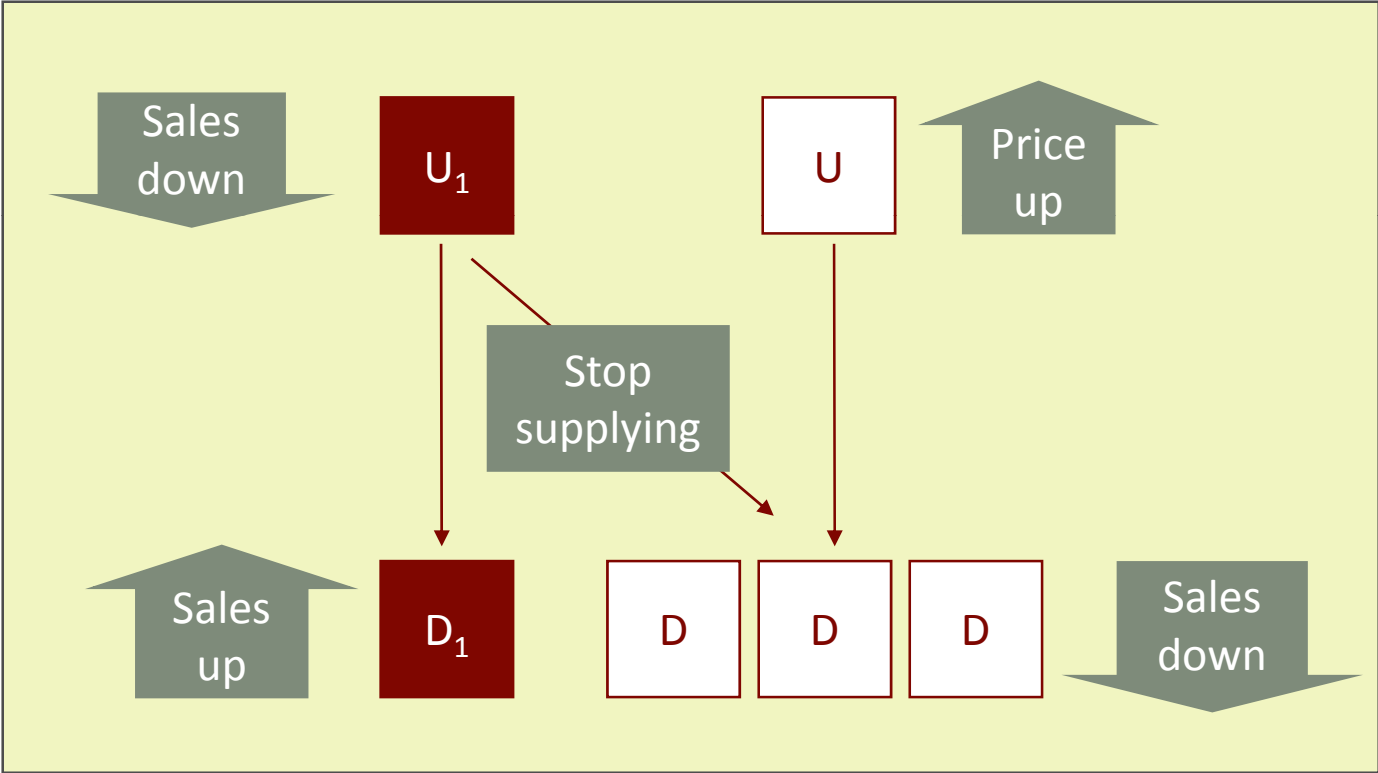
Partial foreclosure



TomTom / Tele Atlas, Nokia Navtek



Total foreclosure



TomTom / Tele Atlas, Nokia Navtek

Other possible harms

Confidentiality concerns

- TomTom / Tele Atlas, Nokia Navteq

Restoring monopoly power

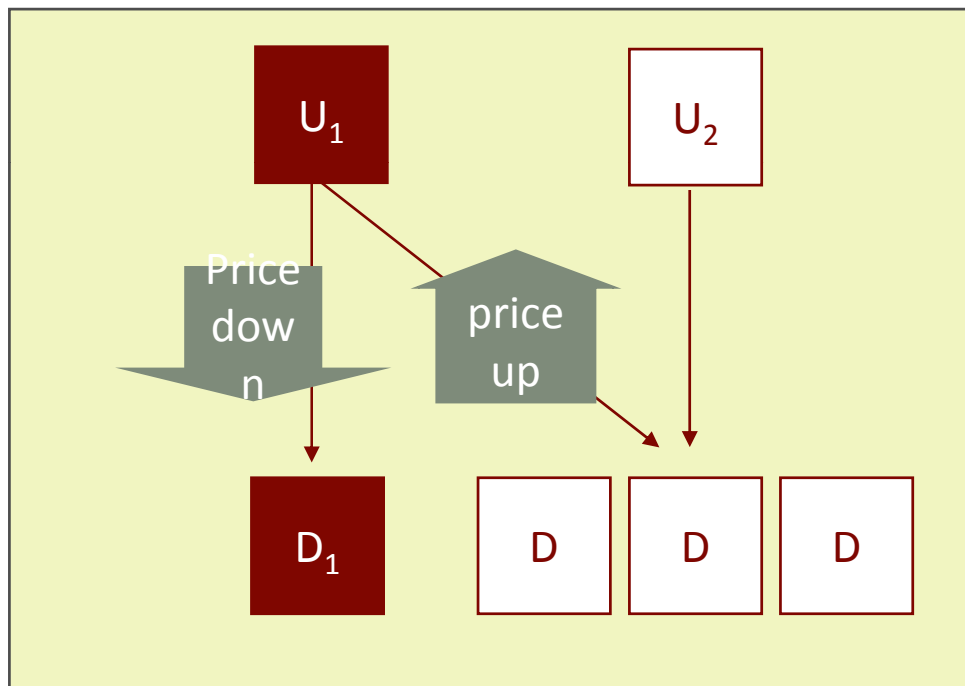
Greater coordination



Contents

1. There are potential benefits
2. There are potential competition concerns
3. The net effect is often good for consumers; merger control should allow clearance based on efficiencies
4. The Commission's approach shows promise
5. Next steps

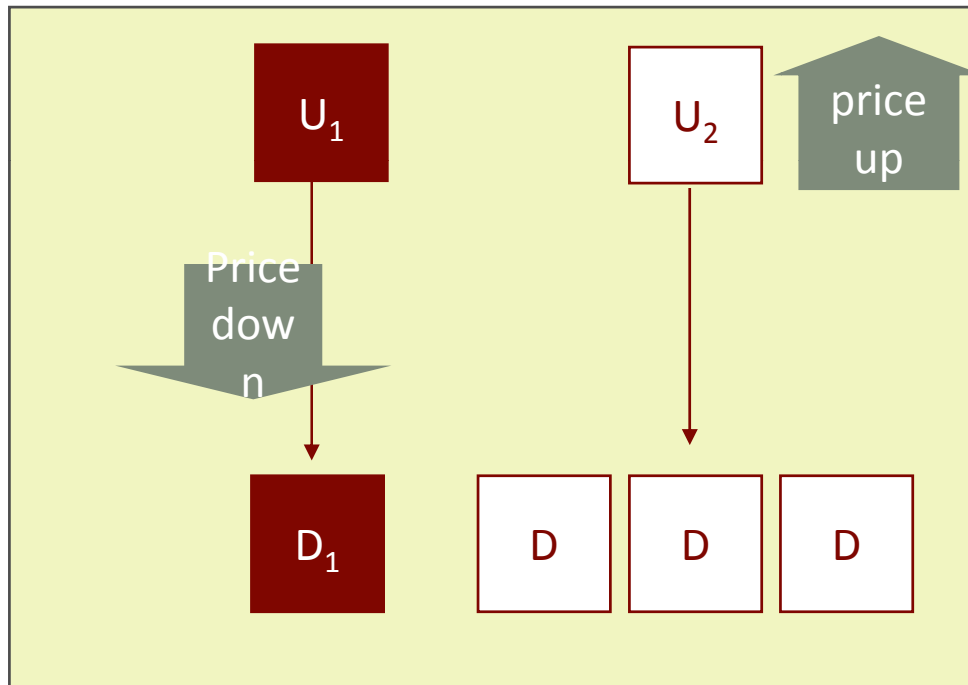
Balance of pricing effects: partial foreclosure



Cost from higher input price is more than offset by double margin efficiencies

(Church report)

Balance of pricing effects: total foreclosure



Final prices could go up

What do we know about the net effect?

Vertical mergers are good for consumers

Lafontaine and Slade
2007 review of
empirical literature

- 16 Studies of consequences of VI
- 13 Consumer welfare rose
- 3 Result is ambiguous
- 0 Welfare fell

Investment
efficiency theories
predict vertical
structure

Implications for merger control

- The framework should allow deals to be cleared on efficiency grounds.
- It should be able to include non-price efficiencies in the assessment.
- The standard of evidence required for showing efficiencies should be at least as easy as for showing harms.



Contents

1. There are potential benefits
2. There are potential competition concerns
3. The net effect is often good for consumers; merger control should allow clearance based on efficiencies
4. The Commission's approach shows promise
5. Next steps

Who does what

Commission identifies the impediments to competition

And does the balancing

- “In its assessment, the Commission will consider both the possible anti-competitive effects arising from the merger and the possible pro-competitive effects stemming from substantiated efficiencies benefitting consumers.” (Para 21)

Parties have to substantiate efficiencies

- “The effect on competition needs to be assessed in light of efficiencies substantiated by the merging parties.” (para 52)
 - Benefit consumers;
 - Be merger-specific and;
 - Be verifiable. (from para 53)

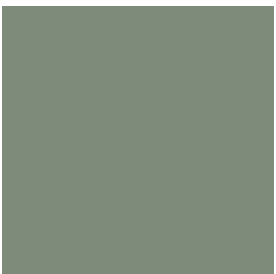
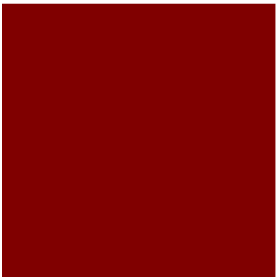
Where do we stand?

Good

- Lots in the Guidelines about how important efficiencies are.
- Accepts that double margin efficiencies are a benefit.
- Accepts that investment efficiencies can drive vertical integration, and has a framework for analysing whether this is relevant in a particular case.
- The Commission did balancing in TomTom / Tele Atlas. But
 - It cleared the deal on other grounds
 - Both benefit and harm could be quantified (relatively) easily

Bad

- No acceptance of automatic balancing for partial foreclosure.
- No clearances relying on efficiencies.
- No standard for quantifying or otherwise balancing non-price efficiencies.



Contents

1. There are potential benefits
2. There are potential competition concerns
3. The net effect is often good for consumers; merger control should allow clearance based on efficiencies
4. The Commission's approach shows promise
5. Next steps

Next steps for the Commission

In general

- Continue to use cases to comment on efficiency analysis from the parties.

Provide guidance on

- What frameworks can be used to establish efficiencies of different sorts?
- Is a rough estimate of the size of an efficiency better than nothing?
- Is the standard for demonstrating an efficiency tougher than the standard on the Commission for showing an impediment to competition?
- What is the basic framework?
 - Full quantitative balancing
 - Focus on the most likely outcomes

Options for the basic approach

Option 1: Full quantitative balancing

Option 2: Consider only the most likely effects

- “The commission examines the various chains of cause and effect with a view to ascertaining which of them is the most likely.” (NHM Para 21)

Pros and cons of Option 1

- Pros: Gives an answer that takes everything into account
- But: Costly and time consuming. And either too hard or too easy to appeal

Pros and cons of Option 2

- Pros: Quicker and easier, and allows better judicial oversight
- Cons: But involves simplifications

Next steps for the parties

Provide detailed analysis of efficiencies

- Explain the theoretical basis of the efficiency.
- Provide convincing evidence that the theory applies, to show:
 - Consumers benefit
 - The efficiency is merger specific
 - And it is likely to materialise and be significant
- Provide a quantification if at all possible.

Examples of quantified non-price efficiencies

- TomTom / Tele Atlas (rejected)
- Airline mergers
- Euronext / LSE