

Anti-Cartel Enforcement and Mergers with Coordinated Effects

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Día de la Competencia - Fiscalía Nacional Económica

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Introduction

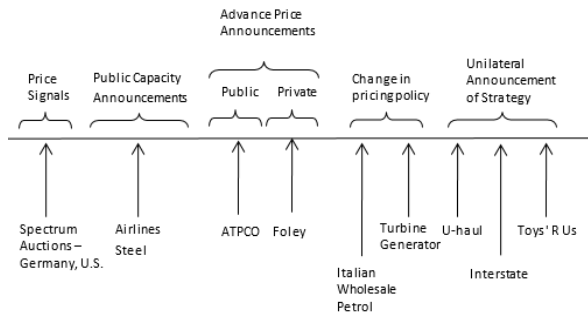
- Fiscalía Nacional Económica has had increasing success in discovering and prosecuting cartels.
 - Cases include retail pharmacies, asphalt, bus services, paper, shipping, refrigerator compressors, ...
- Growing activity in the leniency program
 - 2009-14: 22% (3 out of 14 convictions) had a leniency awardee.
 - 2015-16: 75% (3 out of 4 cases brought by the FNE) have a leniency applicant or awardee.
- Corporate fines have increased: Maximum of twice the profit gain or 30% of sales.

Introduction

How might firms respond to the increasing effectiveness of enforcement?

- In some markets, collusion is deterred.
- In some markets, firms collude by replacing direct and express communication ("explicit collusion") with indirect and non-express communication ("tacit collusion").
- Absence of express communication makes tacit collusion
 - more difficult to prosecute.
 - more immune to the leniency program.

Some Practices Supporting Tacit Collusion



Introduction

Some examples of tacit collusion

Advance price announcements: Container liner shipping (European Commission, 2016)

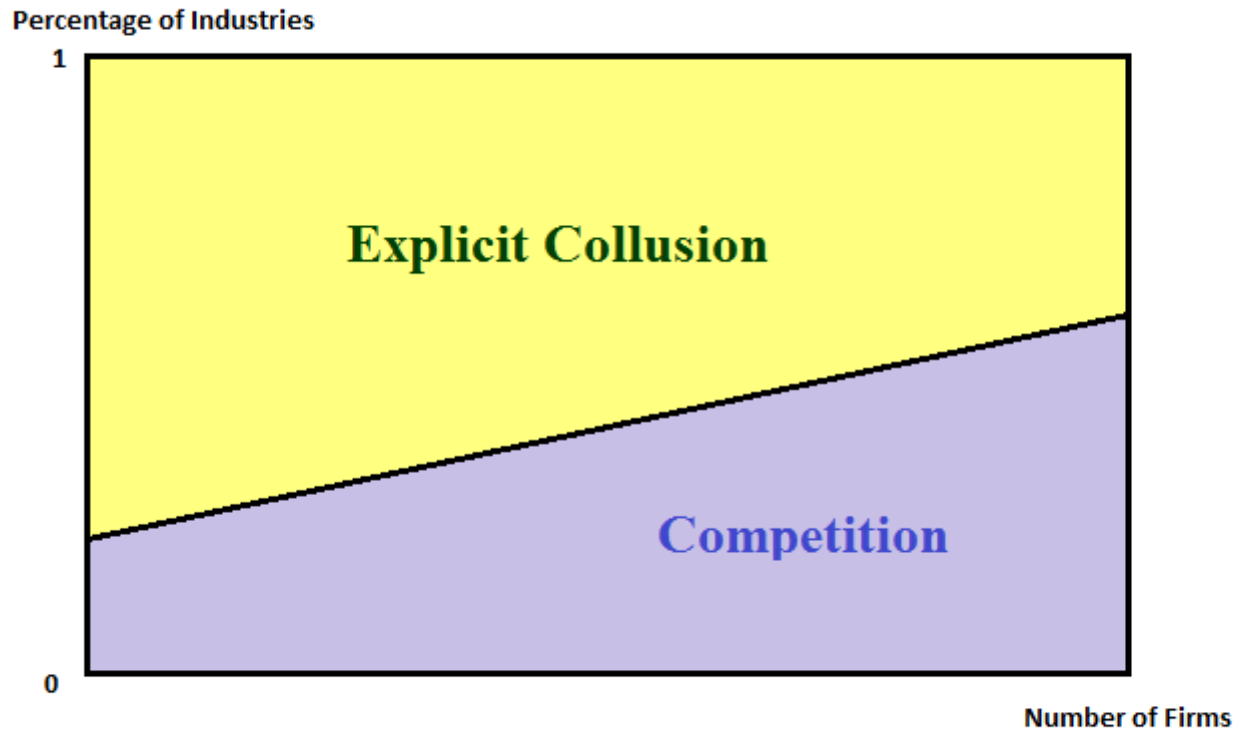
- 15 companies publicly announce future increases of freight prices.
- Announcements were made 3-5 weeks before their intended implementation date.
- Carriers typically responded by announcing similar intended rate increases.
- European Commission: "This practice may allow the companies to signal future price intentions to each other."

Introduction

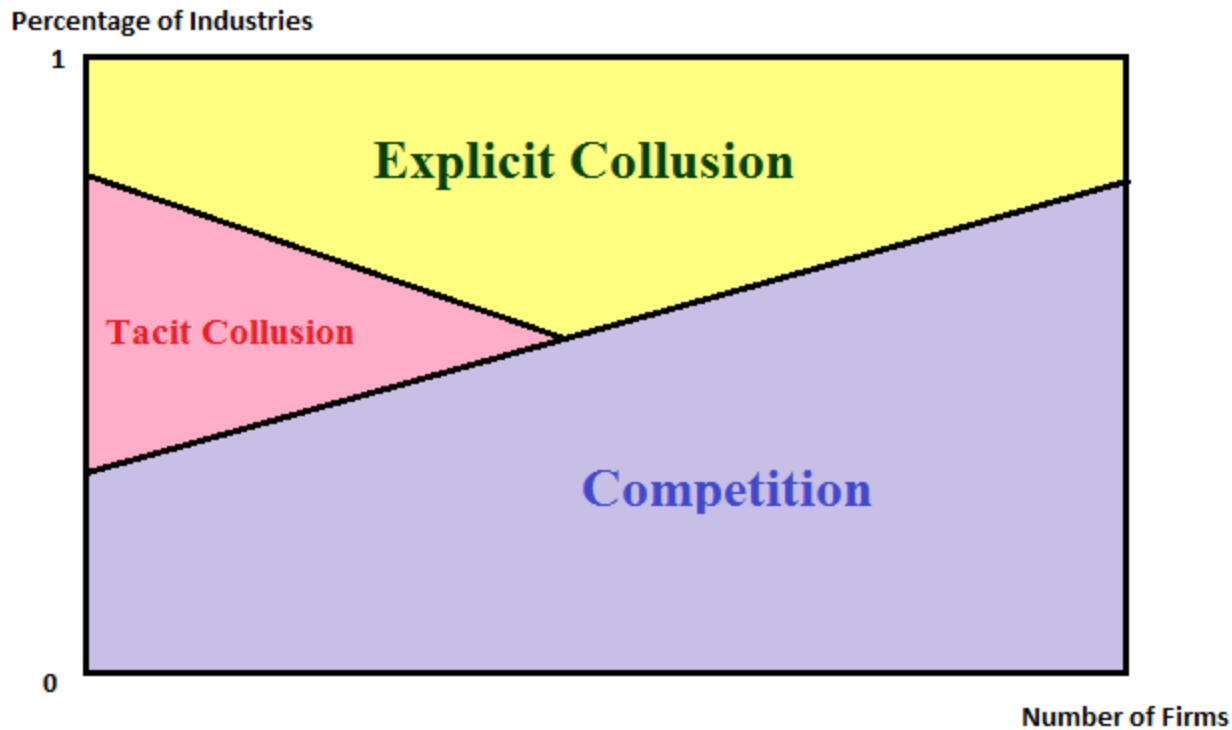
Some examples of tacit collusion

Public announcement of a strategy: Newspaper inserts (U.S. Federal Trade Commission, 2004)

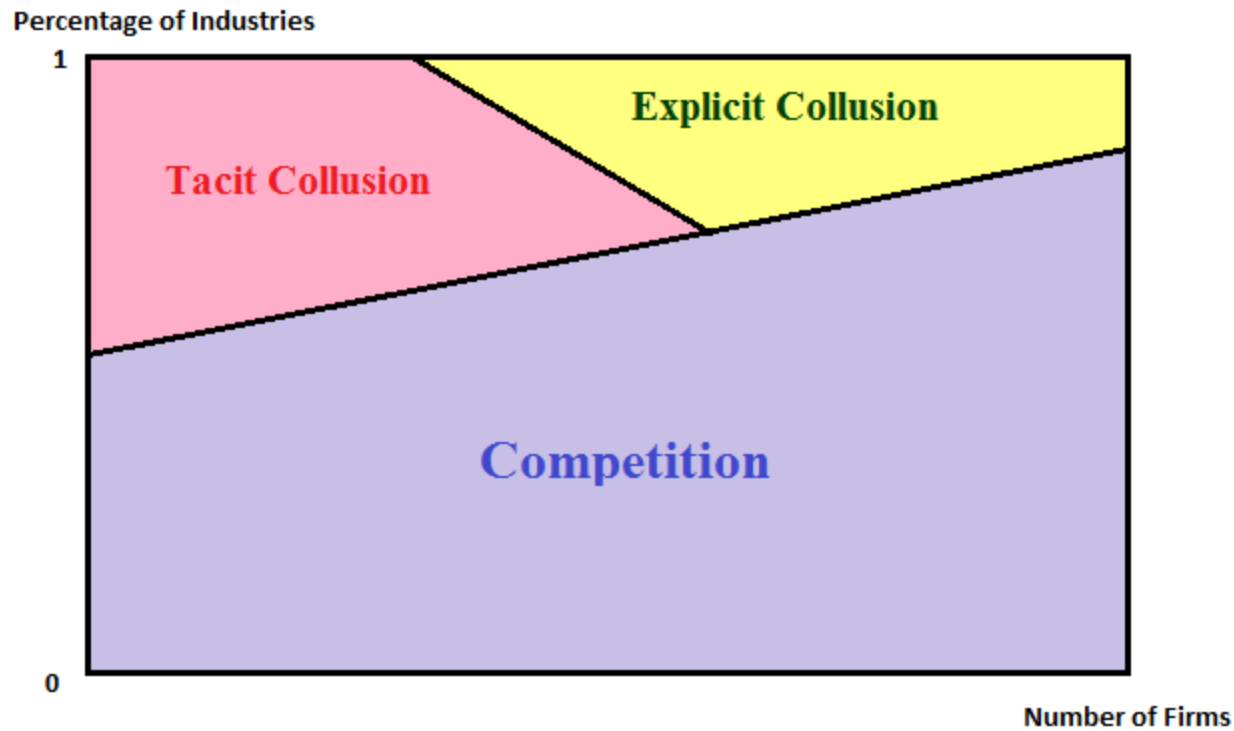
- Two suppliers: Valassis Communications and News America Marketing.
- 2002-04: Valassis engaged in a price war in an announced attempt to achieve a 50% market share.
- July 2004 - Valassis' CEO publicly announced a new business strategy:
 - Abandon its 50 percent market share goal
 - Restore the pre-price war price level.
 - Threaten to resume the price war if News America continued to compete aggressively.



No enforcement of competition law



Some enforcement of competition law



More enforcement of competition law

Introduction

- Tacit collusion typically requires
 - price transparency
 - small number of firms
- Price transparency is needed because firms coordinate through their price announcements or prices.
- Small number of firms is needed because coordination is difficult without express communication.
- A more concentrated market is conducive to all forms of collusion but is especially critical for tacit collusion.

Introduction

- Success against explicit collusion can result in more tacit collusion.
- The best strategy for fighting tacit collusion is to create an inhospitable environment by
 - restricting information exchanges.
 - avoiding highly concentrated market structures.
- Prohibit mergers with coordinated effects (that is, which would result in a market structure conducive to tacit collusion).

Avoid Market Structures Conducive to Tacit Collusion

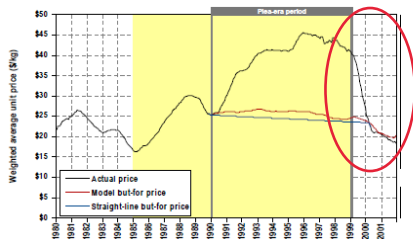
- A merger that results in a market structure for which it is profitable for two firms to collude has a high risk of coordinated effects.
- Tacit collusion is significantly more likely between two firms than between three or more firms.
 - Experimental evidence
 - Market evidence

Avoid Market Structures Conducive to Tacit Collusion

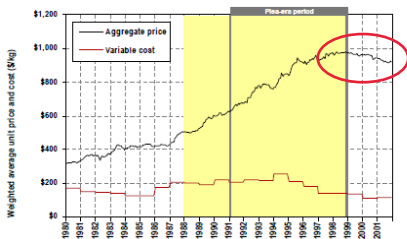
Vitamins Cartel (16 markets)

Post-Cartel Change in Price (16 markets)				
Number of Suppliers	Number of Markets	Did Prices Fall?		
		Yes	No	Unclear
2	5	1	4	0
3	4	3	0	1
4	5	4	0	1
5	1	1	0	0
6	1	1	0	0

Avoid Market Structures Conducive to Tacit Collusion



Vitamin A (3 suppliers)



Beta Carotene (2 suppliers)

Avoid Market Structures Conducive to Tacit Collusion

- A merger has a high risk of coordinated effects if it results in a market structure such that it is profitable for two firms to tacitly collude.
- High-risk mergers are when the pre-merger market has
 - 3 firms so the merger results in 2 firms.
 - 3 large firms and a competitive fringe so the merger results in 2 large firms and a fringe.
 - more than 3 firms but only 3 firms are close competitors and 2 of them merge.

Avoid Market Structures Conducive to Tacit Collusion

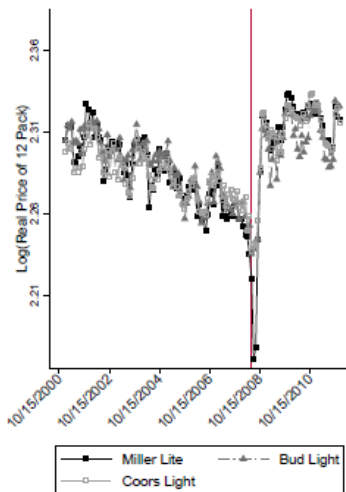
Case: Beer (United States) - Miller and Weinberg (2016)

- Merger (joint venture) of SABMiller and Molson Coors Brewing Company.
- ABI, SABMiller, and Molson Coors competed in the same sub-market.

	Market Shares					
	ABI	SABMiller	Molson Coors	Modelo	Heinken	Total
Pre-Merger	36%	18%	11%	10%	6%	80%
Post-Merger	36%	29%		10%	6%	80%

Avoid Market Structures Conducive to Tacit Collusion

- Declining trend of retail prices since 2001 sharply changed after the merger.
- Competition between SABMiller, Molson Coors, and ABI was replaced with tacit collusion between Miller-Coors and ABI.



Avoid Market Structures Conducive to Tacit Collusion

- Many markets in Chile are suitable or close to being suitable for tacit collusion.
- Mergers are likely to have a high risk of coordinated effects.

Market	Market Share			C3
	Largest firm	2nd largest firm	3rd largest firm	
Mobile phones	37%	35%	23%	95%
Retail pharmacies	43%	29%	27%	99%
Supermarkets	36%	28%	28%	92%
Beverages	38%	35%	26%	99%
Dairy products	54%	26%	11%	91%

Avoid Merger Remedies

- In some jurisdictions - such as the United States - it is common to approve anticompetitive mergers with a "merger remedy."
- A merger remedy most commonly has the merged firm sell some assets (such as capacity) to another firm.
- Case: American Airlines and U.S. Airways (United States, 2015)
 - These two airlines dominated some route markets where entry was difficult.
 - Remedy: Airlines were required to sell off takeoff and landing slots in select airports to low-cost carriers.

Avoid Merger Remedies

John Kwoka (*Mergers, Merger Control, and Remedies*, 2014)

- 53 studies of approved and consummated mergers in the United States ("merger retrospectives")
 - Price *increased* in 87% of mergers.
 - Average price increase = 7.39%
 - Average price increase for mergers with "remedy" = 7.68%
- Conclusion: There is no evidence that remedies work (that is, eliminate the anticompetitive effects of a merger).

Avoid Merger Remedies

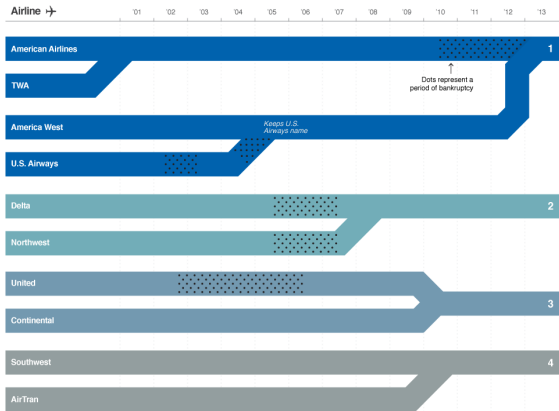
- Recommendation: Be wary of merger remedies as a policy response.
- Misuse of merger remedies in the U.S.
 - Merger remedy should be used only when a merger is overall not harmful with the exception of some markets and the remedy can carve out those harmful exceptions.
 - Merger remedies have been used when a merger is overall harmful and the remedy carves out the most harmful parts. Evidence shows that what remains is harmful.
- Better to prohibit a harmful merger than approve it with an ineffective "remedy".

Concluding Remarks

- Tacit collusion exists and is appearing in many markets in all sorts of forms.
- **Chilean markets are ripe for tacit collusion** because of high concentration and increasing enforcement against explicit collusion.
- The most effective way to stop tacit collusion is to avoid market structures conducive to it, which means prohibiting mergers with coordinated effects.
 - A merger has a high risk of coordinated effects if it results in a market structure such that it is profitable for two firms to tacitly collude.
 - As a general rule, those mergers should be prohibited.
- There is no evidence that merger remedies work.
 - As a general rule, anticompetitive mergers should be prohibited, not "fixed" by a remedy.

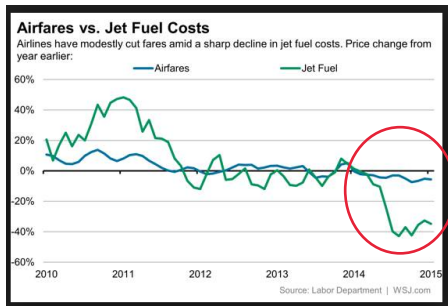
Concluding Remarks

Cautionary Tale: U.S. Airlines Industry



Concluding Remarks

Cautionary Tale: U.S. Airlines Industry



Inflation-Adjusted Air Fares

- 2009-2011: Fares rose 10.2%.
- 2011-2014: Fares rose 2.4% in spite of a steep drop in fuel prices.

Concluding Remarks

Cautionary Tale: U.S. Airlines Industry

- 2002-2014: Capacity utilization (load factor) rose from 72% to 83%.
Why has capacity not increased?
- July 2015 - U.S. Dept of Justice opens investigation.
 - Airlines constrained capacity at roughly the same time.
 - Airline executives expressed in public statements their commitment to a new business model of "capacity discipline".
 - CEO of United: "We are very focused on capacity discipline, but we're not going to do it at the expense of United and to the benefit of others. The whole industry needs to have that level of discipline."
- Hypothesis: Mergers created a market suitable for tacit collusion \Rightarrow agreement to limit capacities \Rightarrow higher prices.