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ECONOMIC ANALYSIS IN MERGER INVESTIGATIONS – Contribution from Ukraine

- Session III -

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More documentation related to this discussion can be found at: oe.cd/eami.

Please contact Mr James Mancini if you have questions about this document [James.Mancini@oecd.org].

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Economic Analysis in Merger Investigations

- Contribution from Ukraine –

1. The bodies of the Antimonopoly Committee of Ukraine (hereinafter – AMCU) exercise merger control to prevent:
 - monopolization of the markets,
 - abuse of monopoly (dominant) position,
 - restriction or distortion of competition.
2. Despite the fact that AMCU was launched in 1992, the economic analysis unit was established in December 2015 within the Department of Competition Policy, which dealt with strategic analysis, economic issues related to specific situations, economic impact assessment, and actual reporting of the AMCU's activities.
3. In July 2017, the Chief Economist unit became an autonomous Economic Analysis Department responsible for economic analysis, planning and reporting on the activities of the AMCU with its eleven employees according to the staff schedule.
4. When considering merger and acquisition cases in accordance with the Rules of Procedure of the Antimonopoly Committee of Ukraine, the State Commissioners may involve the Department of Economic Analysis to provide professional opinions as a part of a case team together with legal and investigation or market department. The team of economic analyses is headed by a Chief Economist who can involve employees in working with the structural unit investigating the M&A case.
5. Economic analysis is an important component of the study of the impact of actions and consequences that may occur in the M&A on the general market situation and the level of its monopolization.
6. To carry out economic analysis, economic experts use analytical tools and other sources of information, in particular, financial statements of enterprises, strategic documents, questionnaires, other open data, etc.
7. An example of involving economists in the investigation of mergers and acquisitions can be illustrated through the following decision.
8. In 2019, the AMCU approved its Decision № 263-r¹ on the acquisition by Private Limited Liability Company “Metinvest B.V.” (The Hague, The Netherlands) (hereinafter – Metinvest Group) shares of the private joint-stock company “Dniprovskiy Coke Plant” (Kamyanske, Dnipropetrovsk Region, Ukraine) (hereinafter – DKHZ).
9. DKHZ and Metinvest Group are competitors in the markets of blast furnace coke and by-products of its production, such as coke nut, coke breeze, crude benzene, ammonium sulfate, raw materials for the production of carbon black, as well as products of processing coal tar, namely: pitch, phenolates, benzene compartment polymers, coal oil.

¹ <https://amcu.gov.ua/npas/rishennya-263-r-vid-18042019>.

10. The economic analysis of the mentioned acquisition case was carried out in two stages:

- assessment of the case itself;
- analysis of the behavioral remedies assumed by the companies in order to avoid the negative consequences on competition from the acquisition.

11. The Department of Research and Investigation of Manufacturing, Pharmaceuticals and Retail Markets and the Department of Economic Analysis in the processing of case materials investigated the relevant groups of factors, among which the following should be singled out:

1. Market shares of the parties to the merger in the by-products markets involved

12. The analysis of the data showed that the combined shares of the Metinvest Group and DKHZ after the merger in the markets of coke and coke products, including coal, pitch, coke nut and coke breeze are significant.

2. Analysis of possible anticompetitive effects of vertical merger

13. After analyzing the unilateral effects of the merger, it was determined that the potential anticompetitive effects in the markets of such by-products as coal-absorbing and pitch oil could be:

- increase in price or restriction of access to products used by other economic entities in production, respectively, the impact on prices of other producers, and hence on competition in markets;
- impact on the above-mentioned markets by ousting of competitors if DKHZ restricts the purchase of raw materials from other producers and switches exclusively to the processing of raw materials of the Metinvest Group.

3. The probability that the market power of the buyer will act as a balancing factor in the anti-competitive effects of the merger

14. According to the case file, there is a market power of the buyer in the pitch market, because there is no alternative to its implementation. The Metinvest Group's need for pitch is insignificant, and sales of pitch to unrelated third parties are a forced measure that the Metinvest Group cannot and will not be able to influence.

4. The probability that the entry of new competitors will act as a countervailing factor in the anti-competitive effects of the merger

15. The analysis of the case materials showed that the ability of competitors to switch to alternative sources is quite problematic and associated with risks due to time constraints, as well as increases the costs, especially logistics. The number of competitors is small, and the entry of new competitors into the market of coke and coke products is limited by significant barriers (including financial, etc.).

5. Falling firm defence

16. The Department of Economic Analysis analyzed the financial condition of DKHZ and assessed the probability of the risk of bankruptcy of the business entity. Bankruptcy risk was assessed using:

5.1. The Beaver ratio

17. According to the value of the Beaver ratio, there was a risk of bankruptcy. The value of the coefficients did not exceed the minimum value, which reflects the undesirable reduction in the share of profits directed to the development of production.

5.2. The Altman multifactor model

18. In accordance with international practice, the multi-factor Altman model was used to predict the bankruptcy of the enterprise, which also confirmed the high and, in a certain period, very high risk of bankruptcy of DKHZ.

19. As a result, granting permission for this acquisition provides an opportunity to improve the financial condition of DKHZ and prevent bankruptcy, and, consequently, the probable exit of the company from the market.

20. Taking into account the analysis, this acquisition may lead to restrictions of competition in certain markets for coke by-products, namely the coal oil market and the pitch market. However, it is possible to permit the transaction if the negative consequences are averted by the parties fulfilling certain requirements and obligations in accordance with the Law of Ukraine "On Protection of Economic Competition".

21. The Department of Economic Analysis also analyzed the commitments proposed by the Metinvest Group, which are ready to assume the participants of the declared merger in order to eliminate the corresponding negative impact on competition. This analysis was based on data on actual market demand of these by-side products.

22. Pursuant to the AMCU's decision on the merger permit with remedies, the Metinvest Group was obliged to sell outside the Metinvest Group at market prices:

- 70% of the total sales of coal pitch,
- 50% of the total sales of coke nuts, coke breeze and coal-absorbing oil production of DKHZ.

23. These commitments eliminate the potential adverse effects of the merger on competition.

24. As a result, economic analysis is a necessary and important component in merger investigations. It helps to establish the factors and consequences of the financial condition of economic entities and the impact of its activities on the general market situation. Accordingly, it plays an important role in building market relations and effective competition policy.