

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Non-price Effects of Mergers - Note by Consumers International

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This document reproduces a written contribution from Consumers International submitted for Item 4 of the 129th OECD Competition committee meeting on 6-8 June 2018.

More documents related to this discussion can be found at www.oecd.org/daf/competition/non-price-effects-of-mergers.htm.

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1. Introduction

1. Non-price effects in mergers are a regular part of standard analytical approaches. Their individual salience differs case by case and is largely driven by the claims made by merging parties, their customers/consumers and rivals. Competition authorities will occasionally identify other non-price factors in their analysis, though this is less usual.

2. The place and relevance of non-price factors rests in the area of consumer choice and price. If quality or innovation claims are to be accepted in a merger case, they must only be done so if in the post-merger market, the consumer or customer can decide whether the strategy succeeds or not. If the market is restricted such that a strategy of raising prices in return for claimed quality gains can succeed independent of consumers, then the merger will damage consumer welfare.

2. Summary

- Non-price effects are common and often analytically non-controversial for competition authorities
- For consumers the key test is whether a claimed strategy of ‘improving quality’ or ‘innovation’ can be advanced independent of the state of competition in the post-merger market
- Claims for ‘innovation’ or ‘quality’ should always be assessed relative to the ability of consumers, not merged firms, being able to choose winning strategies
- Competition authorities need to identify new metrics to assess the price consumers pay (in data transfer and access) in ‘free’ digital markets
- Only through quantifying the price consumers pay for ‘free’ goods will authorities be able to properly assess digital markets
- Competition authorities should apply existing approaches to digital markets by quantifying ‘price’ before considering different approaches to assessing mergers in these markets.

3. It can be challenging to identify markets in which non-price effects require substantial attention in merger review

3. Non-price factors in merger control usually focus on dimensions of a case that have been raised by parties, customers or rivals. It is less common for competition authorities to identify non-price factors in a merger case. Such factors tend to play the role of either (a) ancillary or contributory factors to price competition, or (b) efficiency style defence arguments to justify an otherwise difficult merger clearance.

4. Most non-price effects that require detailed analysis tend to be in the former camp, indicators that are linked in some way to pricing assessments, proxies for price

competition or ancillary measures. Many competition cases involve often-detailed assessments of these measures to the benefit of consumers. For example:

- Service Quality: e.g. Transport, many merger cases will analyse service frequency, product quality, consumer satisfaction and other indicia that often substitute or explain price competition
- Value for Money: e.g. Utilities, utility regulation involves a complex set of trade-offs between controlled or uncontrolled prices and essentially the ‘value for money’ that consumers receive for that price paid.
- Choice: egg Retail, mergers often focus on consumer ‘choice’ factors such a facia tests, where existing store provision is taken as the base case form which a merger is judged.
- Role of Mavericks: e.g. Financial services, performance issues often come into play in such mergers; do the merging parties play the role of ‘maverick’ in a market, such that their loss may have a disproportionately negative impact on the state of competition in the market.

5. Most of the existing analysis of non-price effects operates in the area where ‘choice’ and ‘price’ intersect. The working assumption of competition authorities is (rightly) the fact that where consumers have a good range of choices that encompass a range of quality and other non-price factors, then price as a factor in the market will largely take care of itself. This tends to be borne out in practice in a large number of normal retail markets.

6. The key problem with digital markets is the fact that choice and price have to some extent been delinked and competition authorities have lost the anchors and chain of causation that normally operates. If, one approach may deal with this problem, if it accepts that the price paid by consumers has not disappeared, but changed. If consumer information/data is the price paid by consumers for digital services, even in part, then any merger involving the joining of two datasets, even if they are datasets about the same individual, produces greater value for the merging parties. The consumer has thus created value for the merging party by giving them greater insight into that consumer, allowing them to target advertising, or other products at that consumer with greater chance of success. The consumer has thus created value. If a merger involves a greater intrusion into the dataset that is the consumer, then they could be argued to have paid an increased price for the products of that merged entity. For example, if the acquisition of What Sapp by Facebook involved Facebook having greater access to consumer data to allow them to sell more advertising then it could be argued that the consumer has paid a price for the merger through passing on more data that allows the merged entity to extract greater rent from them.

7. Such an approach to mergers will involve a reassessment of the ‘price’ that consumers pay to access the products of a merged entity. If the consumer transfers greater value or more data to the merged entity, then the price they have paid for the products or services has increased.

8. If we place the value and price paid in data and access provided, then assessing claims to innovate in consumer-focused markets becomes more possible. If, for example, a merger occurs between a social media company and a navigation software company, then the consumer has paid the price of their navigation data being acquired by a social media company. The benefit to the social media company is clear, in terms of ability to

sell advertising or location based ‘recommendations’. For the consumer the benefit can be arguable, but they may include access to more useful targeted information, if they opt in to receive it. Future innovation can also be judged in relationship to the value of the combined datasets held on consumers.

4. The precise interaction of price and non-price effects may be difficult to capture.

9. We have commented above on the relationship between choice and competition. Where the indicators move in opposite directions we would be cautious that the authorities involved are analysing the right indicators. A strategy to raise price, post-merger, is perfectly reasonable aim for a merging company. Indeed, many companies will justify a merger in documents to shareholders precisely on the grounds that margins will increase and price competition will lessen.

10. The test for competition authorities is not whether this is acceptable or not, as documents written for investors are very often very different to those submitted to competition authorities, but if there is sufficient competition in the remaining marketplace to undermine this strategy. If a firm wishes to move upmarket and produce better quality products for consumers, as long as it is the consumer deciding if that strategy works or not, then authorities should be more lenient in assessing the case. Providing the remaining choice, post-merger, in the marketplace is sufficient to provide consumers with a range of quality options at a range of prices, then indicia for a particular merger pointing in different directions is less important.

11. Competition authorities often deal with mergers where the rationale for the deal is to improve margins and returns for shareholders. This is often a proxy measure for raising prices post-merger, even if it is shrouded in the flag of efficiency arguments.

12. The strategy of a firm may be to achieve this through driving consumers to higher ‘quality’ products. The answer to whether this is a problem in a merger or not is the ability of the firm to sustain this strategy in the face of consumer objection. If the strategy is a poor one and consumers have choice, then the firm will fail. If the strategy is a poor one, but consumer choice is constrained in some way through market power, then the strategy will succeed, but through illegitimate means.

13. Competition authorities could gain by discussing such issues with utility regulators, who have developed detailed metrics to judge the quality strategies of regulated industries to justify price increases. The detailed assessment of the investment and innovation plans of regulated industries may provide some useful pointers.

5. When non-price effects are relevant, it may also be challenging to identify how they should be factored into the merger review process.

14. We consider that greater effort needs to be put into quantifying the price consumers actually pay for ‘free’ goods before focusing on where in the merger process discussions of non-price effects should take place. The role of data and consumer information in digital markets illustrates that competition authorities need to spend some time trying to develop new metrics to identify price and quality in digital markets. If an approximate, or proxy measure, for price in digital markets can be developed, then a good deal of the concern about how to evaluate such markets will decrease. It may thus make

more sense to try to bring digital market analysis more in line with established market analysis, rather than adapt existing analysis to digital markets. Even if authorities find that they have to adapt their procedures and calculations they should do so from the standpoint that digital markets still operate as markets rather than as some ephemeral processes that are incapable of sensible analysis.