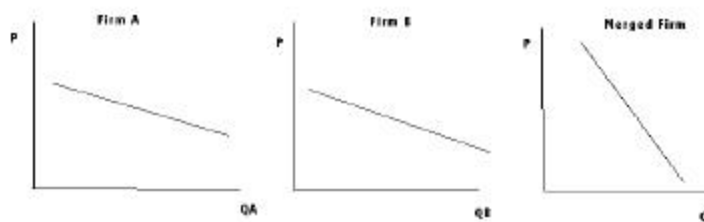


Antitrust

- Rules for limiting the use of market power
- Rules governing
 - Who can merge with whom
 - Competitive conduct
- First mergers, then conduct

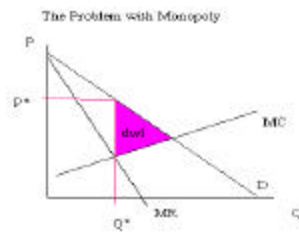
Why Merge?



- Megalomania
- To obtain market power
 - demand less elastic from broader groups (food vs. asparagus)
 - merged firm commands higher prices
- To achieve cost efficiencies
 - savings on fixed costs
 - “synergies”

Antitrust Rationale

- What market failure does antitrust seek to correct?
 - Monopoly:
 - prices too high (CS↓)
 - output too low
 - deadweight loss!



Antitrust Background

- US:
 - Origin in populist movement of 1870s
 - pressure from farmers concerned about railroads (*The Octopus*)
 - Sherman Act (1890) - about conduct
 - Clayton Act (1913) - mergers & conduct
- EU
 - “...place member states on an equal footing” --Van Miert
 - 1989 Merger Control law (also older member state laws)
- Japan
 - reaction to prewar Zaibatsu/cartel system
 - 1947 Antimonopoly Act

Enforcement

- US
 - Department of Justice, Federal Trade Commission, other agencies
 - separate from social planning
 - enforcement changes with administration
- Europe
 - DG IV of European Commission
 - “competition policy... is implemented with due regard for the present-day economic and social climate” -- Van Miert
- Japan
 - Fair Trade Commission
 - critics: it supports cartels
- Must pass muster in every jurisdiction where you operate
 - “positive comity” between US and EU

US Merger Guidelines

- Will the merger substantially lessen competition?
- First cut - HHI Analysis
 - market definition (what are the substitutes?)
 - product: Coke, Pepsi, Sprite, Snapple, Orange Juice, Vodka, Water
 - geographic
 - $HHI = \sum(\text{market share of product } i)^2$
 - intuition: $10,000/N$ for symmetric firms
 - look at ΔHHI :
 - $HHI_{POST} < 1000$, no problem
 - $1000 < HHI_{POST} < 1800$ and $\Delta HHI > 100$, problem
 - $1800 < HHI_{POST}$ and $\Delta HHI > 50$, problem

Why Do Regulators Worry about Δ HHI?

- Theory:
 - monopolists command higher prices than competitive firms
 - recall oligopoly models
- Evidence:
 - prices generally decline with the number of firms in market
 - e.g. bail bonds in CT
 - towns with 1 or 2 dealers, average rate = 9%
 - towns with 3 or more, average rate = 5%

US Merger Rules cont'd

- HHI alone can be misleading; also look at
 - Closest Substitutes
 - do customers view merging products as very similar?
 - Entry
 - how hard is it?
 - Failure, exiting assets
 - would purchased firm be a force?
 - Efficiencies
 - cost savings a plus (not as important as price increases, though)
- Bottom line: would prices be higher with the merger?

Some Proposed Radio Acquisitions

Jackson, MS				
call	AF	Market Share	pre-existing owner	proposed owner
WJMI	FM	20.4%	Holt	Capstar
WMSI	FM	17.2%	Capstar	Capstar
WKXI	FM	8.5%	WKXI	Capstar
WSTZ	FM	6.9%	Lewis	Capstar
WJDX	FM	6.1%	Spur	Capstar
WOAD	AM	5.9%	Holt	Capstar
WYOY	FM	5.5%	WLIN	New South
WVIV	FM	4.7%	WVIV	WVIV2
WTYX	FM	4.5%	Opus	WTYX2
WZRZ	AM	4.5%	WZRZ	Capstar
WMGO	AM	3.2%	WMGO	WMGO1
WJNT	AM	3.0%	WJNT	WJNT1
WKTF	FM	3.0%	Jenne	Capstar
WJKK	FM	2.6%	WJKK	New South
WKXI	AM	1.6%	Opus	WKXI1
WJDS	AM	1.4%	WJDS	Capstar
WJXN	FM	1.0%	WJXN	WJXN2

Can Capstar buy WJMI, WKXI, WSTZ, WJDX, and WOAD?

What Triggers Investigation? EU

- Similar to US, but...
- Abuse of market dominance (single firm or oligopoly) important
 - less focus on consumer prices, collusion than US
- Higher threshold of size/share than US
- Authority vested in Competition Committee, but part of Commission which has other policy objectives.
 - Industrial policy
 - keeping peace among EU members

Antitrust - Conduct

- Some basic business decisions:
 - Pricing, capacity, marketing
 - Can you do whatever you want?
 - No. Must not run afoul of antitrust regulation
- Relatively Clear Violations
 - Cartel behavior - price fixing, output agreements
 - *per se* illegal in US
 - discouraged in EU, Japan
 - DeBeers (NYT 1/12/98)
 - “...cannot visit the United States, by far the company's biggest market, because of a legacy of unresolved antitrust cases stretching back decades”, “fear of being subpoenaed”
 - Oppenheimer does not “mind calling a cartel a cartel, though he prefers to refer to it as ‘**single-channel marketing**’.”

Antitrust - Fuzzier Areas

- “Exclusionary Acts”
 - actions by a single firm that may help it maintain its monopoly or facilitate its acquisition of monopoly
- Hard to distinguish “bad acts” from competitive behavior
 - Judge Easterbrook: “Aggressive competitive conduct by a monopolist is highly beneficial to consumers. Courts should prize and encourage it under the antitrust laws. Aggressive exclusionary conduct by a monopolist is deleterious to consumers. Courts should condemn it under the antitrust laws. There is only one problem. Competitive and exclusionary conduct look alike. The dominant firm is an aggressor and expands its market share at the expense of its smaller rival. The rival yelps and sues.”

Acts Judged under “Rule of Reason”

- Predatory pricing
 - drive out competitor by pricing below cost, then raising price
 - logically requires
 - inability to merge
 - market power
 - subsequent gains > price war losses
 - barriers to (re) entry

Predatory Pricing in Airlines?

- Question: When is a competitive response predatory?
- Reno Air (small carrier): It's a free-for-all out there. [When Reno enters, the incumbents] trash the market with low fares. The majors are engaged in blatant predatory activity, and the government is doing nothing about it.
 - complaints to DOJ
- Lawyer Kenneth Quinn: 'Drawing the line between tough competition that is beneficial to consumers, and predatory tactics that are harmful to competition, often is difficult.'
 - fuzzy area
- DOJ view:
 - fare discounting in response to an upstart is OK ('the essence of the competitive process')
 - network changes plus fare cuts spell trouble
 - problem: added flights to bracket the new entrant's flights or more new capacity than traffic projections reasonably justify
- Example: Northwest Airlines restarted its Minneapolis-Reno service, overlaying much of Reno Air's network, after Reno Air decided to launch Reno-Minneapolis in 1993.
 - Northwest backed down under DOT pressure

- Tying
 - selling two products together
 - ok to "tie" pencils and erasers, baloney and bread, but...
 - illegal if
 - market power in one of two products
 - "forcing" - products not otherwise sold together
 - clear?

Microsoft

- What did Microsoft do?
 - (according to DOJ)
 - leveraged its monopoly power in OS
 - Viewing Navigator as a threat to OS monopoly, M used exclusionary contracts
 - Tied IE to Windows
 - Attempted to divide the market with Netscape

Discussion Questions

- What strategies are available to radio station owners after the Telecommunications Act of 1996 that were unavailable before?
- Why might firms wish to purchase additional radio stations?
- If you operated in this market, what strategies would you pursue, and why?
- What types of regulatory concerns would you expect firms to confront?