

# Economic assessment of mergers: Transactions with vertical and horizontal elements



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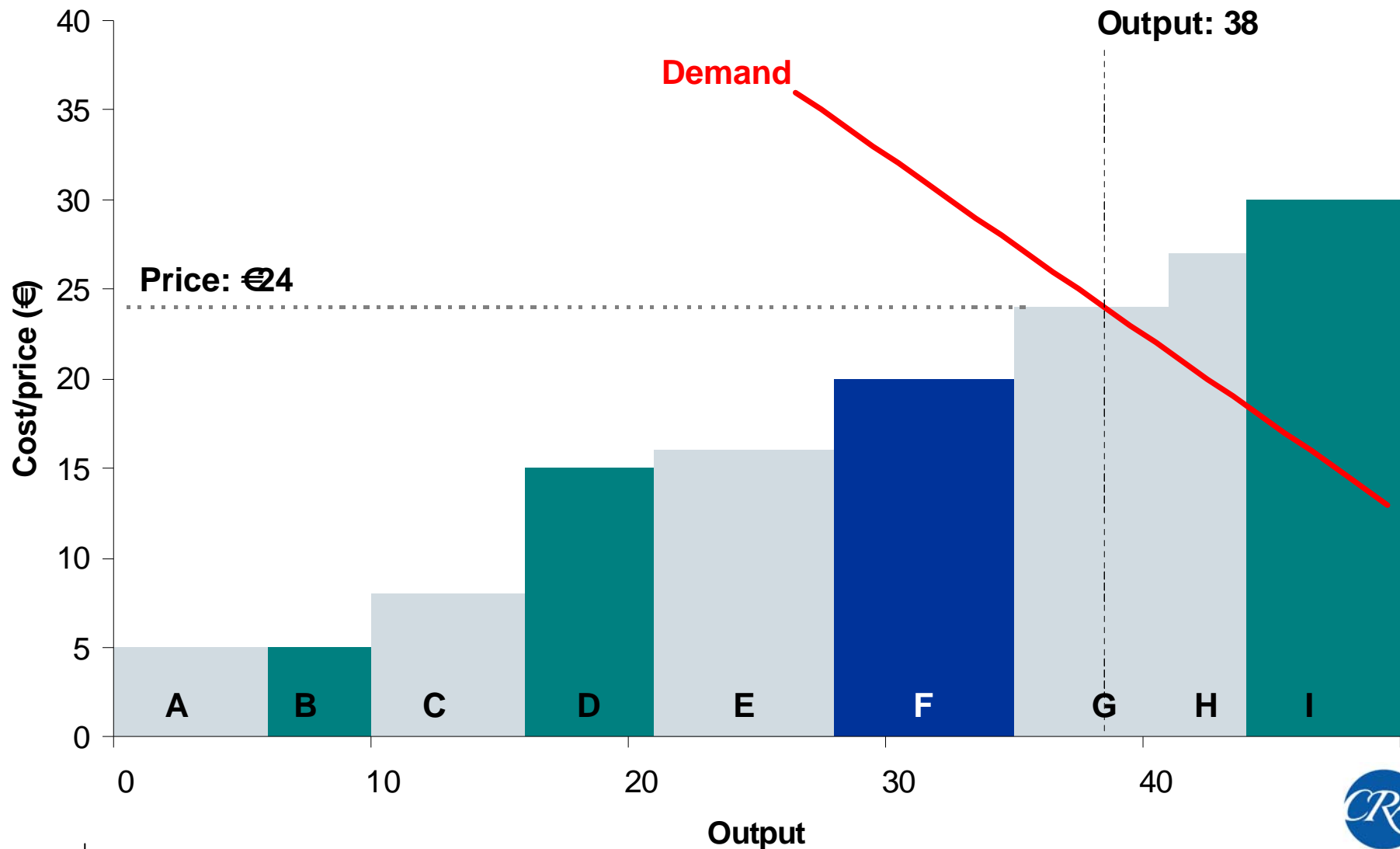
# Interaction of vertical and horizontal concerns

## How should analysis be carried out in mixed cases?

- **Many “vertical” cases raise horizontal issues**
  - Potential competition (entry based on adjoining market position)
  - Coordinated effects (e.g. information sharing, creation of a maverick)
  - Direct horizontal overlaps (change in both horizontal and vertical structure)
- **Vertical concerns are more likely to be raised by complainants?**
  - Can hurt rivals even where there is no harm to consumers
  - Application of guidelines in different settings is still being tested
- **For the cases with both horizontal and vertical effects, we face the challenge of how best to carry out these assessments:**
  - Assess both individually, and clear if neither raises problems (or fix problems associated with each theory of harm separately)?
  - Incorporate both into a single analysis/model of the market?
  - The following slides take one setting under specific assumptions on demand and costs, and look at the impact of a horizontal and vertical merger

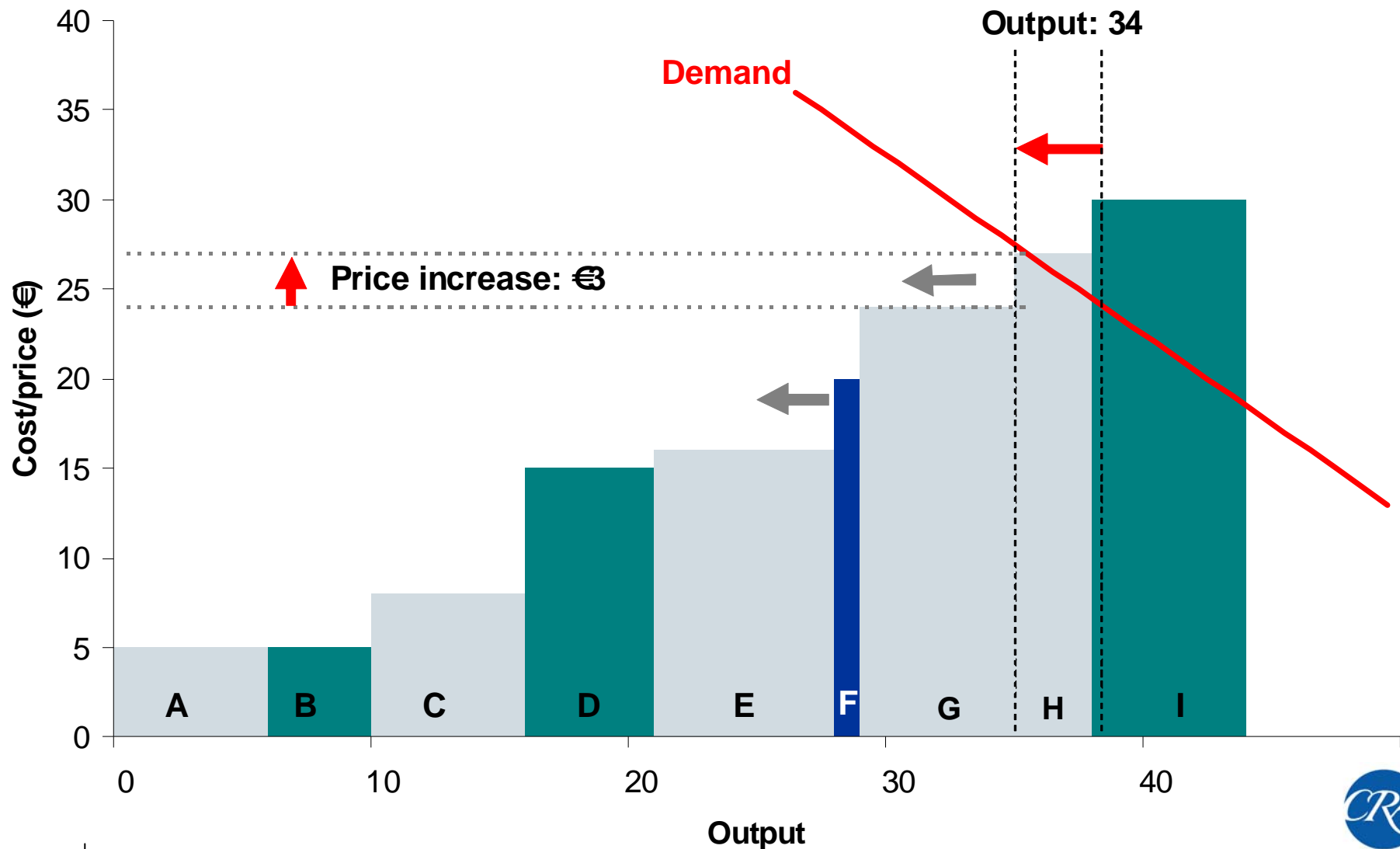
# Interaction of vertical and horizontal concerns

## A standard unilateral effect – pre-merger



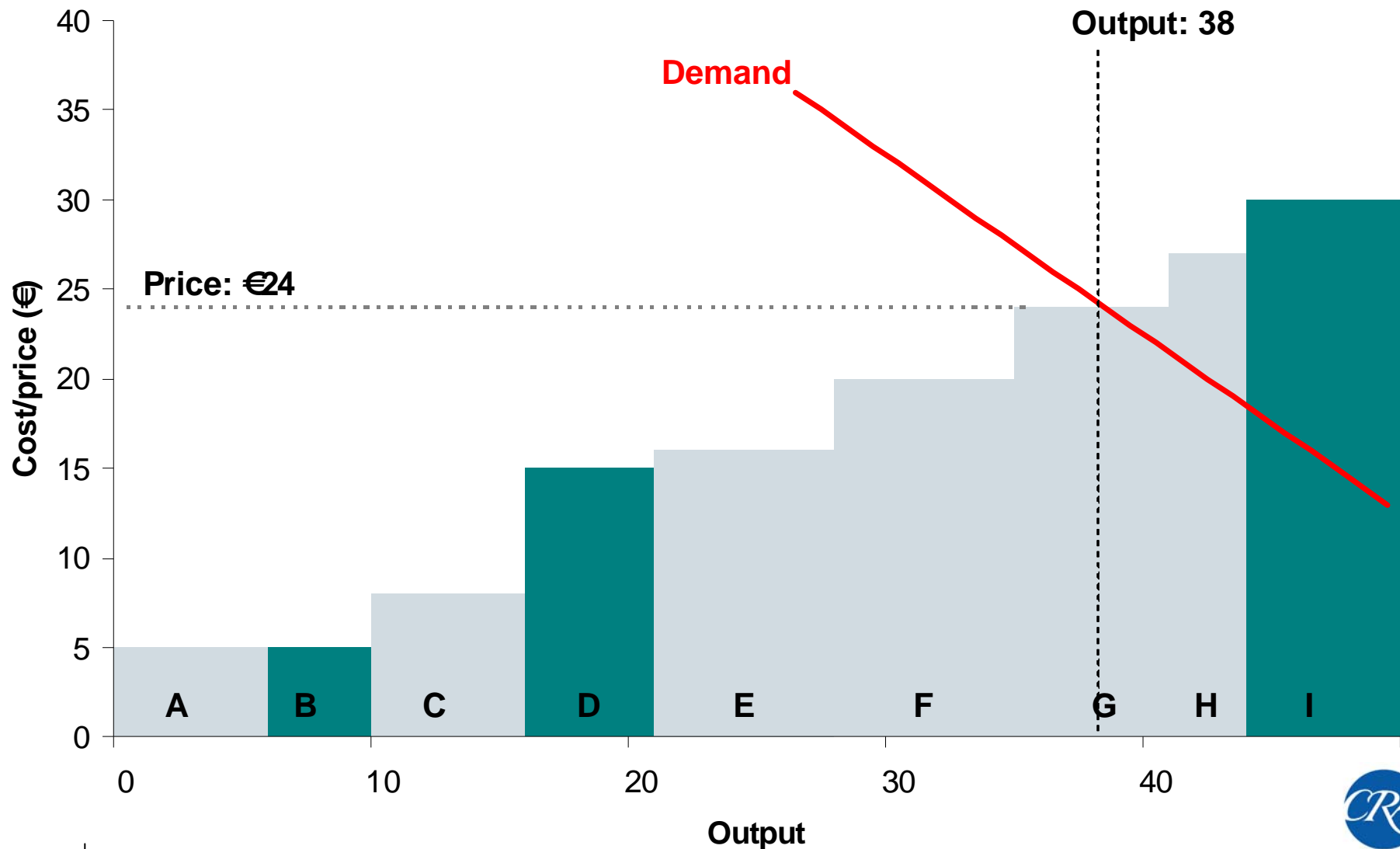
# Interaction of vertical and horizontal concerns

## A standard unilateral effect – post-merger



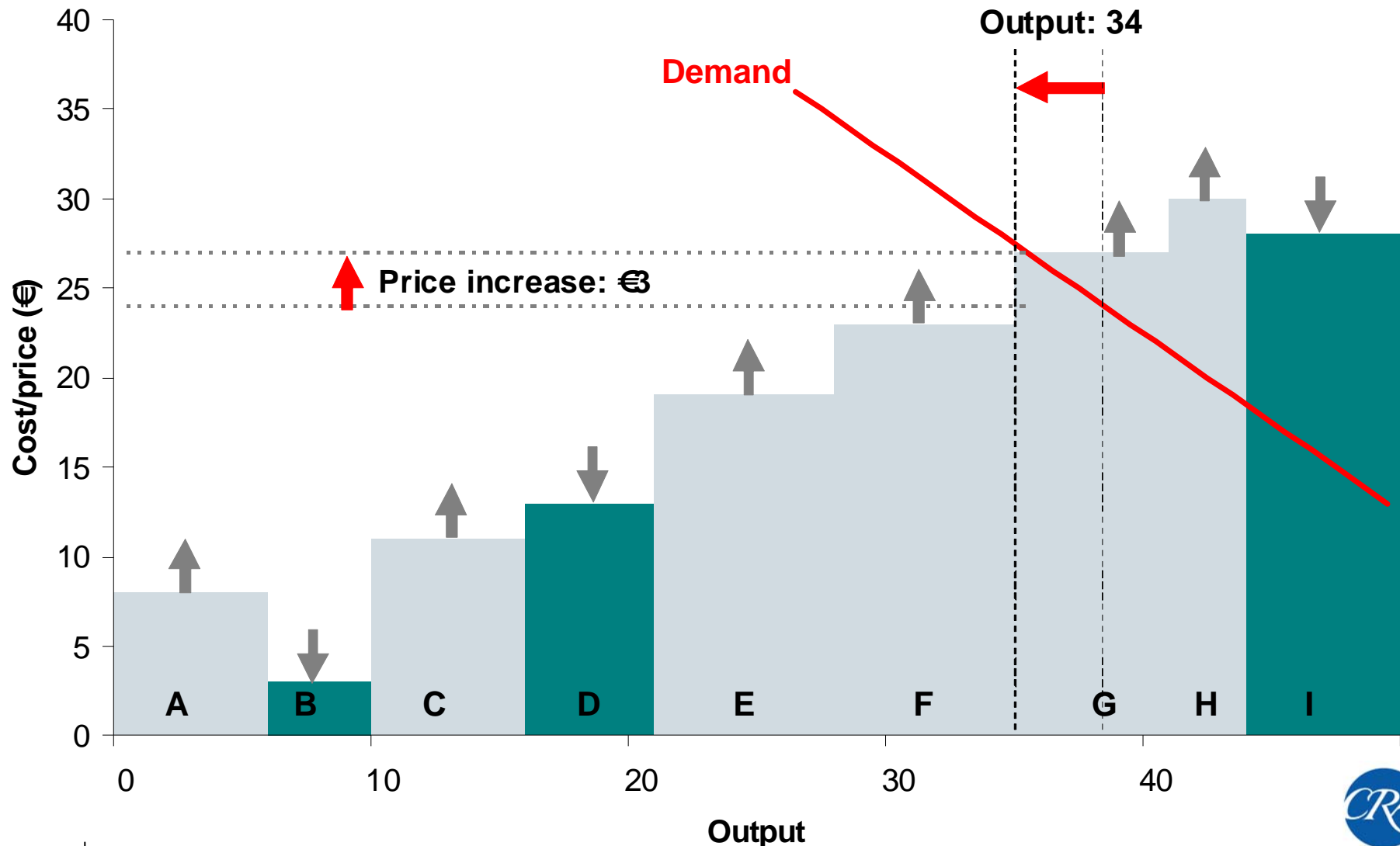
# Interaction of vertical and horizontal concerns

## A standard vertical effect – pre-merger



# Interaction of vertical and horizontal concerns

## A standard vertical effect – post-merger



## Key drivers of profitability of the strategies

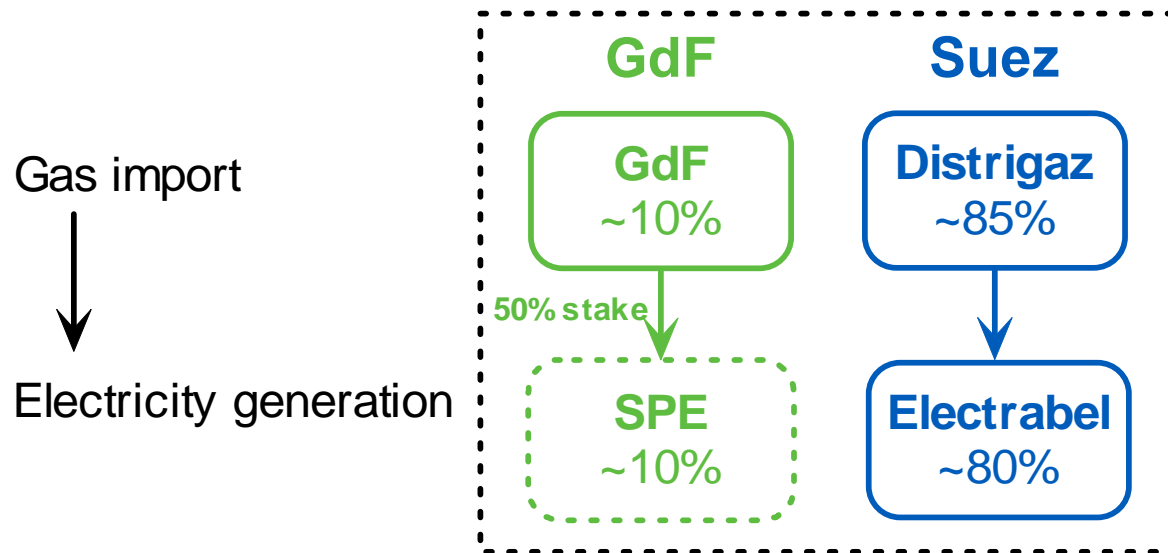
What if we implement a mixed merger (both horizontal and vertical)?

- **How is the analysis of these merger effects changed if we pursue both mergers in parallel?**
  - Possible trade-off between horizontal and vertical effects:
    - **Horizontal arithmetic when RRC has been implemented:** F is now a lower cost plant and enjoys higher prices – is it still worth sacrificing profits on it in order to get a price increase on B and D?
    - **Vertical arithmetic when unilateral output restriction has been implemented:** The more downstream output is reduced, the less downstream volume remains on which to benefit from a yet higher downstream price due to raising rivals' costs
  - Merger effects are therefore not necessarily a straight “sum” of individual vertical and unilateral effects
  - Whether the merger is pro- or anti-competitive could depend on this trade-off (e.g. if vertical effect was expansionary, but the horizontal effect contractionary: what is the overall impact?)
- **Many single cases combine horizontal concentration with a change in vertical balance**

## Case study: GDF/Suez

Divestment to deal with horizontal problem also has vertical results

- Remedies offered included sale of 50% stake in SPE, and divestment of Distrigaz (s.t. contracts with the merged firm)
- Removes horizontal overlap and rival vertical integration
- Can the upstream divestment compensate for the loss of vertical pricing efficiency downstream (e.g. by encouraging more downstream entry)?



# Conclusions

## Mixed horizontal and vertical mergers

- **Many cases change both vertical and horizontal market structure**
- **Separate isolated analyses of each may be misleading**
  - Divestments to solve a horizontal problem may have vertical costs
  - In other cases apparent vertical issues may be resolved if horizontal concerns are fixed
  - In some cases vertical efficiencies could compensate for small horizontal effects
- **We can incorporate both effects into a single merger model**
  - Such models will need rely on a particularly large number of assumptions if they are to incorporate two markets and their interactions;
  - However, this is one method to at least identify which assumptions matter, and attempt to assess effects in a systematic, internally consistent way
- **Potential interactions should be taken into account:**
  - In a more or less formal way, to reflect the focus of the merger and availability of data
  - May have an impact on the likely merger impact and the effectiveness of any remedies

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