New Trends in merger Analysis in Brazil and Abroad

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In recent years, merger analysis has been improved by a series of contributions from economic thinking and institutional collaboration. Among the results from these contributions, three trends are noticeable in the evolution of the merger analysis throughout the world and in Brazil:

1) The use of empirical and quantitative methods, mainly to deal with market definition and merger effects;

2) The revival of old concerns, especially with predatory practices, as unilateral effects of mergers and acquisitions; and

3) The growing collaboration of authorities in different jurisdictions to review mergers using similar patterns.

1) The use of empirical and quantitative methods in merger analysis

Beginning by the Brazilian experience, two recent and high profile cases leveraged discussions that indicated the need of quantitative research to enrich traditional qualitative investigation, based on the observation of market shares, replies of questionnaires to competitors and consumers, requests of several information from notifying parties, specialized press and so on. One of these cases was the merger between Antarctica and Brahma in 1999, which resulted in the creation of the company AmBev, and the other was the acquisition of Garoto, a national chocolate producer, with important expression in the market, by the Nestlé conglomerate, in 2001. The outcome of the merger between Antarctica and Brahma was the approval granted by Cade, subject to some structural and behavioral conditions, while the outcome of the purchase of Garoto by Nestlé was the simple and plain disapproval by Cade.

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\textsuperscript{2} Prepared to Antitrust Spring Conference, organized by the International Bar Association Antitrust Trade Law Section and Brazilian Institute of Studies on Competition, Consumer Affairs and International Trade, Copacabana Palace Hotel, Rio de Janeiro, 12-13 may 2005.
We have observed a clear evolution on the analysis between the two cases, as on the first one the quantitative methods were used to define relevant markets and consequently product substitutions – basically estimation of price elasticities – proper and crossed – and estimations of efficiencies that would result from the operation.

On the second case, the parties themselves, as well as the competitors that contested the case, presented the quantitative analysis from the beginning, even to define the relevant market – a tricky task in such a differentiated market as the chocolate one. Such analysis was used to discuss the patterns of the firms’ conduct in the competitive environment (so evolving to address demand-side and supply-side questions). Finally, there was a long debate of arguments brought to the process by parties and competitors on the degree of efficiency generation, the potential of sharing them with consumers, in the terms of the Law, and simulations on price conduct after the merger.

We could quote other cases recently decided by Cade\(^3\) and even mention the existence of new cases, those still in the pipeline of Cade’s decision, indicating the strength of this trend of relying on quantitative methods to complement qualitative analysis.

As may be well known, Brazilian legislation admits the possibility of authorization by Cade of operations that reduce competition provided that some conditions are imposed to neutralize the damage to the market and/or to share the benefits of efficiency generation with consumers. These conditions usually are written on a Performance Agreement (“Compromisso de Desempenho”), an instrument originally inspired by the European experience of discussing and negotiating with partners alterations on operations in order to make them compatible with the rules of free market. One of the main trends we could see ahead is the evolution of techniques to clarify, using quantitative methods, the appropriate scope of their generations and, especially, simulations of scenarios of sharing those benefits with consumers, result that is intrinsically linked with the competition environment, which means the degree of rivalry that will remain after the merger or acquisitions.

These tasks in Europe and the United States are already a sound reality. There, the use of empirical methods is considered to be one of the most important developments in the way merger and acquisition is evaluated.

\(^3\) Serrana/Manah (2004) among others.
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Still, the theme is not something of a novelty in the American antitrust environment. As stressed by Jonathan Baker and Daniel Rubinfeld in 1999⁴, empirical methods offer powerful tools for simulating the likely effects of alternative scenarios, particularly in respect of evaluating anticompetitive harms suffered by consumers and estimation of damages to the marketplace.

The use of empirical methods is considered to be one of the most important developments in merger and acquisitions evaluation in the United States. In Europe, as Lawrence Wu, Paul Hofer and Mark William point out⁵,

“If the statistical and econometric methods that have been applied recently by the European Commission continue, it is likely that the same will be said for European merger enforcement” (p. 73)

The full consequences of the incorporation of these new tools of investigation are not clear, so far, although observing recent EC merger investigations we could predict that assessing and quantifying unilateral competitive effects or non-coordinate effects, i.e., the potential for competitive harm caused by the enlarged entity, will be of particular concern. The focus is on whether the merging parties are close competitors and whether the combination will have significant effects on price.

It is worth mentioning that Nestlé-Garoto case has, in Brazil, raised this discussion on the potential for a merger to lead to higher prices once the merger is approved, following in the same pace of foreign authorities the international trend⁶.

Further information regarding this rich discussion that is gaining space in Brazilian antitrust analysis may be found in the following address http://www.ipea.gov.br/defconc/seminario/rel200501.htmlm, where can be found papers presented on a recent conference sponsored by IPEA (“Instituto de Pesquisa Econômica

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⁴ American Law and Economic Association Meeting.
⁶ In Europe we could mention cases like Volvo/Scania, in 2000, when the Commission focused its attention on two markets – trucks and buses. In this case the Commission had the collaboration of an outside econometric study; the Philips/Agilent HSG (a medical imaging company), in 2001, the GE/Instrumentarium case, in 2003, where GE intended to acquire control over the company that produces anesthesia and critical care equipment.
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Aplicada”), an economic research center, and SDE (“Secretaria de Direito Econômico”), the secretary of Ministry of Justice in charge of merger and practice investigation, with ANPEC (Associação Nacional de Pós-Graduação em Economia), the graduation economic courses association. There one can have a clear idea of the state of the art of Brazilian discussion on the theme, as well as some contributions from guests from the United States – precisely, from the FTC – and from the European Commission.

2) The renewed interest on predatory and exclusionary practices

The second trend in merger analysis is the renewed interest in predation and exclusionary practices, as a possible result of mergers and acquisitions that concern authorities, mainly the European Commission. As noted by Massimo Motta, the identification of exclusionary behavior is one of the most difficult topics in competition policy, and one could add, one of the most fascinating, due to the challenge of discriminating exclusionary practices from competitive behavior that ultimately benefits consumers.

The monopolization case, as the result of predatory pricing, is present in antitrust history since its beginning. Years of Chicago School learning helped to convince academics and practitioners that predatory practice, in general, would be irrational, while incompatible with profit maximizing rule. Recent developments in theory have brought new insight over this old theme.

For example, Aaron Edlin and Joseph Farrell, in a very recent paper state that

“Predation occurs when a firm offers consumers favorable deals, usually in the short run, that get rid of competition and thereby harm consumers in the long run.” p. 502

From this new point of view, the verification of prices below costs is no longer required to characterize a situation of predatory price, mainly if the firm is a huge conglomerate, active

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7 Seminar “Estudos em Métodos Quantitativos Aplicados à Defesa da Concorrência e à Regulação Econômica”, that took place in Brasilia, April 25 to 28, 2005.


9 The leading cases were Standard Oil and American Tobacco, both of 1911, condemned by Supreme Court, simultaneously inaugurating the Rule of Reason in antitrust decisions. Frederich Sherer and David Ross describe with erudition this initial phasis of antitrust in America. In Industrial Market Structure and Economic Performance, 3rd edition, Houghton Mifflin Co, Boston, 1990.

in many geographic and product relevant markets or if it has considerable cost advantages in relation to its competitors.

The major contribution to the renewed interest in developing economic models on predatory practices was given by the new theories on asymmetric information. In all cases, as Motta (op. cit.) stresses, the predator will try to use the entrant’s imperfect knowledge, as well as the potential investors or smaller competitors, and behave in such a way to convince the rival that it will not make profits and should give up its intent of entry or investing in the market dominated by the first. Reputation, Signalling and Deep Pocket models follow this logic.

Coming back from theory to practice, a number of recent cases decided by European Commission considered this kind of danger as a result of merger and acquisition. The concern with this kind of unilateral effect was decisive in cases involving conglomerate mergers, when there is no substantial overlap in specific relevant market but some conditions like large portfolios of brands, special advantages in complementary goods – that could be sold in packages – and asymmetric financial conditions (the so called deep pocket) raised a question that led to decisions made by the European Commission imposing conditions in order to neutralize potential use of dominant position in a predatory way or even blocking such operations.

One word about the Brazilian case law: so far, Cade has not dealt with this new trend, assuming that no case involving predatory and exclusionary practice adopted by dominant firms in order to exclude competition has been subject to the Council’s judging. Nevertheless, as soon as cases like that reach the final authority in antitrust in Brazil, we could expect a convergence with the treatment of these cases with the international tendencies, as we see in other fields.

3) The growing cooperation among merger control authorities

11 See, for example, Boeing/McDonnell Douglas (1996); Guinness/Grand Metropolitan (1997); GE/Honeywell (2001); and Tetra Laval/Sidel (2001). Although concerns with portfolio effects and its consequences to predatory practices are present mainly in European case law, there are some cases in United States where concerns with tying – in mergers involving complementary goods – led to consent decrees, as in the acquisition of Turner Broadcasting by Time Warner (1995); the acquisition of Alias and Wave Front by Silicon Graphics 91995 and the acquisition of McCaw by AT&T (1994).
Finally, one could state a third trend on antitrust enforcement worldwide. A remarkable fact was the reform of the European Commission merger control, which took place on January 2004 and led to strong convergence between the European method of analysis of horizontal mergers and the one described by the DOJ and FTC Guidelines in the United States.

For every observer or practitioner of antitrust, it is very exciting to witness the growing consensus in economic analysis, as well as the increasing number of cases that, for its impact in a considerable number of jurisdiction are being object of bi-lateral or multi-lateral cooperation. As stated by Mario Monti, in one of his last speeches as European Commissioner for Competition Policy\textsuperscript{12}, the reform provided a “one stop shop” for the scrutiny of large cross-border mergers, dispensing with the need for companies to file a multiplicity of national jurisdictions in the European Union. It has guaranteed that merger investigation will be completed within tight deadlines corresponding to the need of businesses

As we see, there are a lot of motives to be sanguine about the new trends in antitrust enforcement here and abroad. We hope that the unceasing efforts of Brazilian authorities towards the harmonization and rationalization of regulations will converge to this same target aimed by the European Union, of simplifying and speeding the merger control in benefit of the community of businesses and consumers.

\textsuperscript{12}“A reformed competition policy: achievements and challenges for the future” Center for European Reform, Brussels, 28 October 2004.