Market Definition and the Use of Upward Pricing Pressure

Submitted by: United Kingdom
Market definition and the use of upward pricing pressure

Paul Reeve
Head of Economics, Phase 1 Mergers
Competition and Markets Authority, UK

All views are my own
Market Definition

- Purpose and dangers
- Product market definition
- Geographic market definition

Upward Pricing Pressure (not covered in these slides)

- Basic concepts and different versions
- Measuring margins
- Measuring diversion
- Calibration: what level of UPP is a concern?
- Examples
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Why define markets?

1) It is part of the **legal framework**
   
   eg in the UK:
   
   …whether a merger “has resulted, or may be expected to result, in a **substantial lessening of competition** (SLC) **within any market or markets** in the UK for goods or services”

2) It helps to **frame the analysis**
   
   ▪ In horizontal mergers: helps us focus on main competitors
   ▪ In vertical mergers, dominance cases: we need to understand the market, not just changes in a market

3) Calculate market shares, HHIs etc

4) Consistency across cases; precedent value
Market definition is not a separate exercise

[Completed/Anticipated] acquisition by X of Y

Decision on relevant merger situation and substantial lessening of competition

Parties
Transaction
Jurisdiction
Counterfactual
Background

Market definition

Product scope
Geographic scope

Competitive assessment

Barriers to entry and expansion
Conclusion on substantial lessening of competition

Exceptions to the duty to refer
Take care when setting the scene

Ensco/Rowan (2019)
What is a market?

For competition law assessment, a ‘relevant economic market’ is defined as:

*a set of products or services that can be profitably monopolised*

Market definition uses the ‘hypothetical monopolist’ or ‘SSNIP’ test as its intellectual framework:

▪ “Given a particular set of goods or services, would a hypothetical monopolist of those goods or services be able to sustain profitably a Small but Significant and Non-transitory Increase in Prices above the competitive level?”
  ▪ If yes, this is a relevant economic market
  ▪ If no, widen the set of products and start again, until you can define a market that can profitably be monopolised
What is a market?

Supply-side factors

- Willing & able to supply; OR
- Conditions of competition similar

- Does this lead to a unique answer?
Consider a SSNIP on Fanta…
And it gets more complex…

And how useful are market shares?

- Differentiated products – closeness matters; beware chain of substitution
- Asymmetric competition
- Two-sided markets/network effects
- Potential competition/dynamic effects/killer acquisitions

As a result, merger analysis has moved away from a focus on market shares, and towards a more direct focus on competitive constraints.
Did market definition help these cases?

OFT (CMA’s predecessor):
“As no substantial competition concerns arise on any reasonable frame of reference affected or potentially affected by the Transaction, it was not necessary for the OFT to reach a conclusion on the exact scope of the frame of reference in this respect.”
So it assessed horizontal overlaps in “actual competition in the supply of photo apps and potential competition in the supply of social network services.”

DG Comp:
On consumer communications services:
“…the Commission will assess the effects of the Transaction in the narrowest relevant product market for consumer communications services, that is the market for consumer communications apps for smartphones.”
And on social networking services:
“there are important differences between WhatsApp and social network services”
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Product market – issues with price

- Different prices do not necessarily imply different markets
  - “Quality adjusted price”
  - Common price movements may be useful
  - But price movements are normally a firm, not all products
  - Or may be driven by common input cost changes

- Focus on marginal customers
  - How many need to switch? (eg United Brands – “toothless fallacy”)
  - Beware price discrimination

- Some products do not compete on price (eg online) – how to do a SSNIP?
Price correlation

- A and B closely correlated (0.8)
- C is not (0.1)

- eg Nestle/Perrier (EC case)
  - A = still water
  - B = carbonated water
  - C = other carbonated drinks

- How much correlation do you need for market to be A+B?
  - Benchmark against two products “known” to be in the same market
- But will we see common price movements across all products in A?
  - If so, is it common input costs changing?
Migration vs diversion

Future/Miura (2016)
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You can have more than one market

- National vs international
  - Pricing – national
  - Innovation – international

- National vs local/regional
  - Pricing – national
  - Service – local
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  - National vs international
  - Local/regional

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Current scale of imports

Don’t focus on where goods are produced – what do customers need?
- Sales, distribution, support

Is competition similar (e.g., same suppliers, shares of supply)?

Barriers: tariffs and regulation

What is important to competition?
Consider local factors, not where it’s made

Dover/Wayne (2016)
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  - National vs international
  - Local/regional

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In theory, use the HMT

- Figure shows store locations and households in Brixton
- Colours reflect 5/10/15 min etc. isochrones
- Make three assumptions:
  - Customers on average shop at their nearest store
  - Customers travel/distance trade-off equivalent to opportunity cost of leisure time (e.g. DfT transport modelling)
  - All stores have same VFM
- Start at 5 mins, increase prices at all 5 mins stores by a SSNIP, see if enough customers would switch outside market, if so expand
- Run until SSNIP test fails
- Results should vary across areas depending on locations of stores and customers
- Similar approach possible to explore e.g. rival ferry routes
The 80% ‘rule’
A catchment is not a market

Royal Bournemouth and Christchurch Hospitals NHS Foundation Trust / Poole Hospital NHS Foundation Trust (2013)
Willingness to travel?

So why not just look at competition directly?

Royal Bournemouth and Christchurch Hospitals NHS Foundation Trust / Poole Hospital NHS Foundation Trust (2013)
Catchments are endogenous to competition.
Uniform vs individual catchments

What catchment should we use?
- Average
- Maximum
- Individual
- More than 1 different catchment?

Do we know why it varies?
- Urban vs rural
- Demand is different
- Density of competitors

How far apart are company X’s stores?

Suggestion:
- Be cautious in identifying overlaps – large catchments
- Consider individual size in competitive assessment
Why define markets (2)?

1) It is part of the **legal framework**
   - OK – but at what stage?

2) It helps to **frame the analysis**
   - This is scoping the case, not market definition

3) Calculate market shares, HHIs etc
   - Less important/reliable than competitive effects analysis

4) Consistency across cases; precedent value
   - Each case is different. This is part of scoping
Questions?

paul.reeve@cma.gov.uk