More than Price Effects

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INTRODUCTION

• Competition authorities usually reluctant to accept “Failing firm defence”
• But recent cases more common (“Flailing firms” too?) – EC 2013: Aegean Airlines/Olympic Air; Shell/Nynas; UK Comp Commission: Optimax/Ultralase
• Shift in manufacturing to low cost areas of Asia means excess capacity & inevitable exit of assets
• Financial crisis gives rise to more distressed firms
• Both in mergers & state aid many calls by EU Policy Makers to be more lenient on allowing M&A as part of industrial strategy
CRITERIA FOR FAILING FIRM DEFENCE

- Idea: In world “but-for” the merger the outcome would be even less competitive. Three **necessary** conditions:

1. In absence of takeover, target would leave the market in near future. *If so:*

2. Without takeover, targets assets would leave the market; **and:**

3. There is no less anti-competitive purchase than the particular transaction under consideration
WHY ARE CRITERIA SO STRICT?

• Productivity growth the most important aspect of long-run economic performance (determines income growth)
• Economic research on “Big Data” using firm & plant level data on 100 millions of firms
• Traditional view: productivity all about firms adopting new technologies
• New view:
  – Huge dispersion of productivity between firms
  – About $\frac{1}{2}$ of economy wide productivity growth is due to industrial restructuring: inefficient low productivity firms & plant shrinking/exiting
• M&A shouldn’t prevent necessary reallocation of assets within a sector or necessary exit of inefficient firms
This is very much in the spirit of Schumpeter
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“The fundamental impulse that keeps the capital engine in motion comes from the new consumers’ goods, the new methods of production and transportation, the new markets... [The process] incessantly revolutionizes from within, incessantly destroying the old one, incessantly creating a new one. This process of Creative Destruction is the essential fact of capitalism.”
Schumpeter (p. 83, 1942)

Although probably his most famous quote was:
“Early in life I had three ambitions. I wanted to be the greatest economist in the world, the greatest horseman in Austria, and the best lover in Vienna. Well, I never became the greatest horseman in Austria“

Notes: Cumulative TFP growth index = 100 in 2008
Source: Conference Board Total Economy Dataset (2015)
MUCH OF THE EU-US DIFFERENCES DUE TO THE “LONG TAIL” OF LOW PRODUCTIVITY FIRMS. EXAMPLE:

% of firms with different levels of management quality

Source: Bloom, Sadun & Van Reenen (2015), WMS Survey
http://worldmanagementsurvey.org/ ~14,000 firms
ASSESSMENT

• Aegean Airlines/Olympic Air
  – Ongoing Greek crisis made it highly likely Olympic would exit & no credible alternative buyer (cf 2011 Decision)

• Shell/Nynas
  – Nynas buys Shell refinery at Harburg. Becomes only naphthenic base & process oil producer in EU
  – Shell showed refinery economically unsustainable in current form. No alternative buyers. Also some efficiency savings

• Optimax Clinics & Ultralase
  – 2 of 3 largest UK providers of laser eye surgery (Optical Express twice as big as combination)
  – CC considered Ultralase would’ve exited. Other bidders looked non-credible. Market share distributions similar (diersion ratios)

• Long Clawson/Millway (2009); Kingfisher/Focus (2011)
EXAMPLES (2013)

- Currently possible to run failing firm defence successfully
- Unclear that there is a case to weaken current framework
- Does show importance of carefully considering counterfactual evidence
FURTHER READING

- [http://blogs.lse.ac.uk/politicsandpolicy/archives/8131](http://blogs.lse.ac.uk/politicsandpolicy/archives/8131)
- [http://worldmanagementsurvey.org/](http://worldmanagementsurvey.org/)
EUROPEAN FALLING FURTHER BEHIND US PRODUCTIVITY SINCE MID 1990S

Notes: Cumulative TFP growth index=100 in 1996
Source: Conference Board Total Economy Dataset (2013)