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Applying the more economic approach in abuse of dominance cases

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Introduction

- Economics plays a central role in competition enforcement
- Economic analysis provides a framework to think about competitive interactions
- In EU merger control, economic analysis has long been a cornerstone to determine the competitive effects of concentrations
- Occasionally in the form of complex econometric studies to predict price effects



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Introduction

- More often simply through the use of basic economic concepts (elasticities, substitutability etc.) in the investigation
- Abuse of dominance cases, however, have traditionally been much more focussed on form-based assessment and per se rules
- Particularity in tying (e.g. *Hilti*), exclusive dealing (e.g. *Hoffmann-La Roche*) and rebates (e.g. *BA/Virgin*)



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Introduction

- Somewhat less in refusal to supply (e.g. *Bronner*), exploitative pricing (e.g. *Port of Helsingborg*) and predation (e.g. *AKZO*)
- Paradigm change visible with Guidance Paper
- This presentation will try to illustrate why and how economics can be usefully integrated in the analysis of abuse of dominance cases
- Examples from tying, exclusive dealing and rebates



The need for a theory of harm

- Traditionally the Court has considered tying, exclusive dealing and loyalty rebates as “*recourse to methods different from those governing normal competition*” (*Michelin*)
- The idea that these practices are “not normal”, derives from the German ordoliberal tradition
- Unfortunate influence on European competition law
- These practices are pervasive in competitive markets, where monopolization cannot be the aim



The need for a theory of harm

- E.g. Verboven (2008): There tends to be more price discrimination in competitive markets
- And very often they are also efficient: *“it appears that when manufacturers choose to impose such restraints, not only do they make themselves better off but they also typically allow consumers to benefit from higher quality products and better service provision”* (Lafontaine and Slade, 2008)
- So there is no presumption of harm



The need for a theory of harm

- Hence, one should investigate the effect of a practice compared to an appropriate counterfactual, rather than look at the form of conduct only
- Proof of anticompetitive foreclosure starts with developing a cogent theory of harm
- This is more than noting foreclosure (which is a defining characteristic of tying, exclusive dealing etc.)
- Rather: incentive, ability and consumer harm



Some examples from rebates

- Rebates allow aggressive pricing on marginal units while extracting rents on intramarginal units
- This generates pressure on all prices, so competition in rebates is typically fiercer (Marvel & Yang, 2008)
- Contrary to the ordoliberal belief, rebates are a natural element in the competitive process, even in the complete absence of cost justifications
- If a rebate has no anticompetitive object or effect, there is also no reason for assessing an “objective justification” (in fact there may be none)



Some examples from rebates

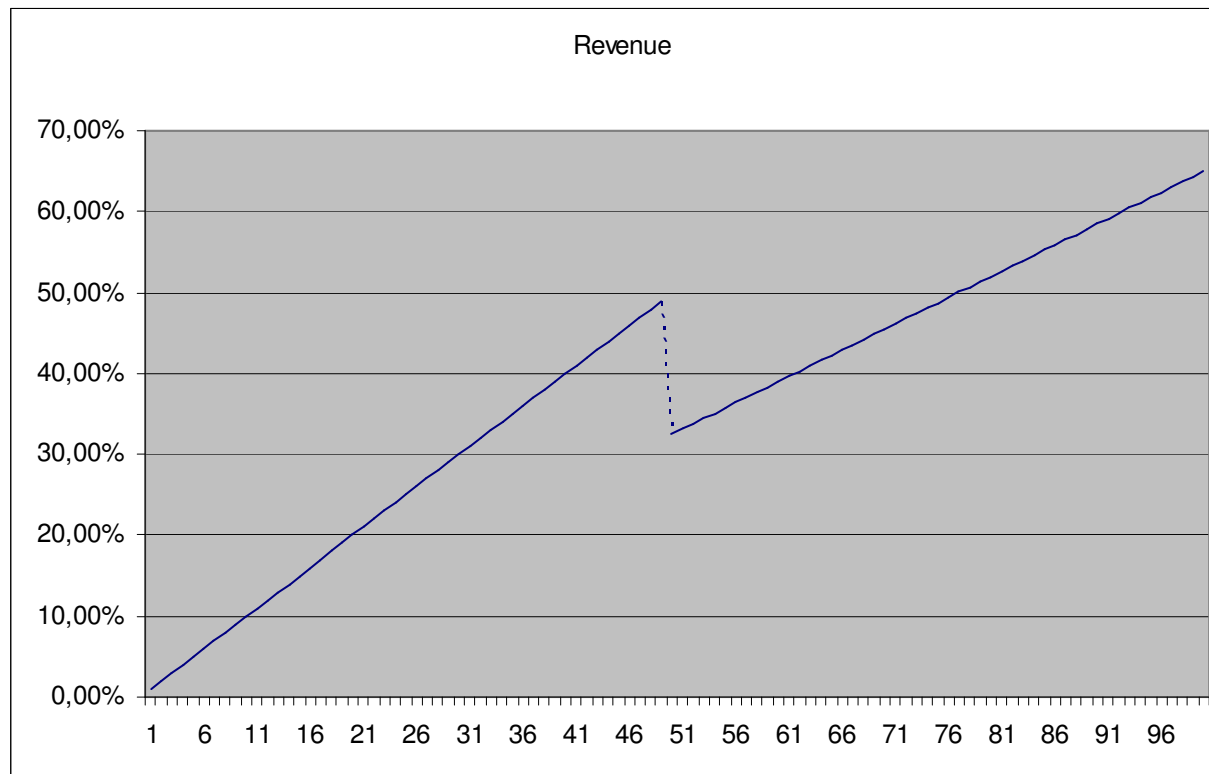
- How to go about an economic analysis here?
- Identify whether the rebate scheme could anticompetitively exclude efficient competitors
- Whether or not it does, depends on the characteristics of the market and on how the rebate is structured
- E.g., retroactive rebate *may* lead to foreclosure because for some range of quantities, prices can become negative



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Some examples from rebates



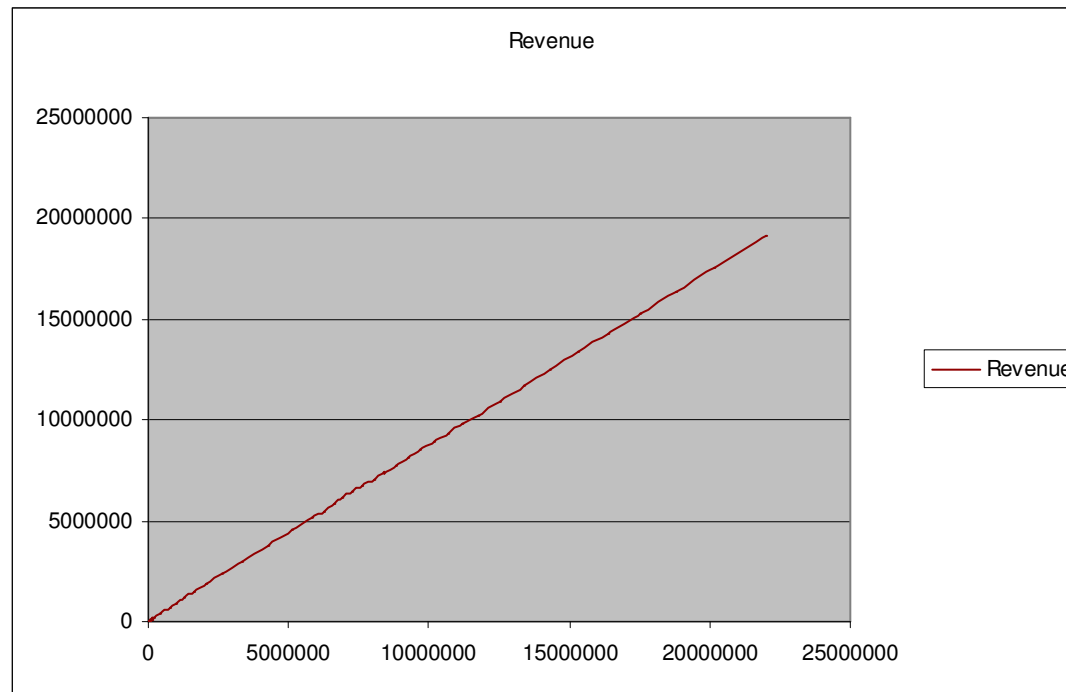


Some examples from rebates

- Guidance paper: conduct as-efficient-competitor test for contestable share
- *Velux*: rebate with many incremental steps
- Albaek & Claici (2009): retroactive rebates with many steps approximate incremental rebates
- Such retroactive rebates pass the AECT unless the incremental price as such is predatory



Some examples from rebates





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Some examples from rebates

- *CRV Holding B.V.* (Netherlands): firm with 80% market share gives 2% retroactive rebate in return for exclusivity
- In terms of product portfolio, capacity and diversification, other suppliers were in a similar position as CRV and could compete for the entire demand of a customer
- Case cleared on appeal as the Court saw no anti-competitive foreclosure



Anticompetitive effects in *Intel*

- Recent example where anticompetitive foreclosure was found: *Intel*
- Conditional rebates for (quasi-)exclusivity
- Much smaller part of the market contestable
- Intel's rebate schemes did not pass AECT (effective prices below AAC over the relevant range)
- Example: As AMD could not offer HP a compensating rebate, it offered one million x86 CPUs for free
- HP had to refuse (and took only small part)



Anticompetitive effects in *Intel*

- From a theory perspective, insights from literatures on no-cost predation and leverage (Simpson & Wickelgren, 2007, Abito & Wright, 2008, Shaffer & Inderst, 2009, and Greenlee & Reitman 2006)
- If purchasers compete downstream, they care less about the *absolute* level of input cost, but more about *relative* level
- Dominant firm can “play off” OEMs against each other and “pick winners” by levying market power from non-contestable share into contestable share



Anticompetitive effects in *Intel*

- E.g., to accept agreement with AMD, HP requested that *"AMD will establish a fund of \$25M per quarter [...] for potential 'retaliatory' acts from Intel. Such acts may include unusual discounts that Intel may provide to an HP competitor targeted at impacting HPQ's PC business or the unusual loss of discounts or market development funds from Intel as a result of the execution of this agreement."* (¶ 1393)
- This sort of playing off can allow exclusion or marginalization without sacrifice



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Anticompetitive effects in *Intel*

- Other factors:
 - Intel is a must stock item (indispensable for OEMs)
 - Important R&D and returns to scale, so foreclosure has strong effects and can raise rivals' cost
 - CPUs make up significant portion of downstream cost
 - Substantial part of market foreclosed
 - Loopholes closed even through exclusive dealing downstream (retailers)
 - “Naked” restraints (bribes to delay AMD innovations)



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Anticompetitive effects in *Intel*

- In sum:
 - As-efficient-competitor-test failed
 - Credible theory of harm
 - Consistent set of circumstantial factors suggesting anticompetitive foreclosure
- Likely short-run consequences: higher prices
- Likely long-run consequences: lower innovation