

FTC official: Evidence, not theory, is key to analysing vertical deals

Pallavi Guniganti
4 June 2013

A senior economic policy adviser at the Federal Trade Commission said yesterday that evidence, not theories, is crucial to finding what he called the anti-competitive “outliers” among generally beneficial vertical deals between producers of complementary products. *Pallavi Guniganti* in Washington, DC

Speaking about the role of economic theory and modelling, FTC policy adviser Daniel O’Brien said that there were many “possibility theorems” as to the effects of vertical deals and collaborations, but those often hinge on details that are difficult to verify.

“If you have real evidence, that’s more compelling,” O’Brien said. “We need evidence of a net anti-competitive effect,” preferably with regard to output, because higher prices might be linked to better service and thus benefit consumers.

However, he added a company’s documents submitted during the review of a vertical deal may tell “a good story” about how a deal might affect output that is more compelling than theory.

“Documents tell stories about what the firms think about what they’re doing and why,” O’Brien said. Sometimes a company’s documents may show it is taking an action to prevent a potential rival from entering the market, which is distinct from typical business rhetoric about “killing the rival” by out-competing it.

Speaking at the Bates White annual conference yesterday, O’Brien also said that although companies’ market power is a necessary screen for enforcers to determine whether their behaviour can harm competition, it is “not a good test” because the efficiency benefits of a vertical deal tend to be greater the more market power the firms have.

While the US antitrust enforcers in 2010 revised their horizontal merger guidelines, there have been no official changes to Section 4, the agencies’ guidelines for vertical deals. The US Department of Justice’s 2010 “Antitrust Division Policy Guide to Merger Remedies” made some reference to vertical mergers, but enforcers have justified the lack of updates on the rationale that they bring relatively few such challenges. Case-by-case guidance makes more sense, they say.



Market power is not always a good economic test, said Daniel O’Brien

The lack of recent formal guidelines on vertical practices makes discussions by agencies on their current thinking especially meaningful, even when they do not claim to speak for the agency or its commissioners.

O'Brien began his remarks by contrasting what he called two parables, or paradigms of one company's effects on another, depending on whether their products are competing or complementary. Where the products are competing, Company A's increase in output is detrimental to Company B, he said, and if they conspire together horizontally, they would typically reduce their total output.

Where their products are complementary, however, Company A's increase in output benefits Company B, and their cooperation would increase total output.

This contrast in the results of vertical deals for competing and complementary goods was the core of O'Brien's discussion on how to evaluate vertical practices.

He acknowledged that a deal between complementary producers could harm competition if they had previously dealt with each other's rivals. Nonetheless, he deemed the benefits of complementary producers' cooperation to be "relatively unambiguous", whereas the potential harm from deals between rivals is ambiguous, and noted that empirical evidence supported this conclusion.

In addition to his current role as senior economic policy advisor at the FTC, O'Brien has served as deputy director of the FTC's bureau of economics, as well as chief of the economic regulatory section at the antitrust division of DoJ. O'Brien made these remarks in the course of a discussion about the economics of vertical foreclosure at the Hal White Antitrust Conference, sponsored by Bates White Economic Consulting. The conference honours the late Hal White, a leading economist and co-founder of the consultancy, who passed away in March 2012.