

# A study of transatlantic conflicts economics essay

[Economics](#)



## A Study of Transatlantic Conflicts

### **European Business Management**

UB Number – 12022611 Course: MSc International Business & Management

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### **Number of words 3000**

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### **1. Introduction**

European Union and United States competition law appear to have a high degree of commonality between them. EU and US' antitrust organisations share a common objective. According to Fox (2009) both systems try to advance consumer's interest and protect free flow of goods in a competitive economy. " They both seek to protect competitors' access to markets and protect to some extent consumer freedom of choice and seller freedom from coercion"(Fox, 2009). Although they both seem to be developed, they haven't shared common grounds relating to mergers, whether it lead to vertical integration or horizontal over lapses. This paper stresses the analysis of anticompetitive effects, rules and principles and the linkages among competition regulation of US' antitrust authority and the European Community. To examine these affects two case studies have been taken into

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consideration. The first case study is of Boeing-McDonnell Douglas merger. This case will discuss how two major industrial giants in the field of civilian jets productions were repressed by the European Union. It would examine the increase in market share of Boeing, FTC's approval of the merger countered by the EU, differences between the judgement of both the nation's authority and the final settlement that they reached. The second case discussed will be of GE-Honeywell merger. Although this merger didn't go through, reasons for the failure of this deal are given ahead. It will discuss some of the major concerns of the European Union regarding it. In the end, conclusion will provide us with insightful idea and recommendations for both the nations to work on common grounds and build a better understanding amongst each other for future purposes.

## **2. Boeing-McDonnell Douglas Merger**

### **2.1 Introduction**

26th July 1997, could be landmarked as one of the major events in the history of aviations and aerospace. It was on this day that two major civilian jets producing companies, The Boeing Company (Boeing) and McDonnell Douglas Corporation (McDonnell Douglas) joined hands together to form a single entity (NYT1). This merger was resulting in an estimated annual revenues of \$48 billion, an increased market share from 60% to 70% and a combined backlog of \$120 billion (AMR1). This noticeable increase in the market share instigated Federal Trade Commission (FTC) to cross examine the facts and go over the details that might affect the market. However, the review favoured the merger and it was concluded by Robert Pitofsky and

other commissioners that this deal would not "substantially lessen competition" (FTC1).

## **2. 2 EU's Interference**

Although FTC reviewed the case and submitted their decision, European Commission (Commission) and European Union's (EU) Antitrust Authority weren't convinced with the outcome.(PRH1) They believed that the merger would substantially decrease the level of competition and significantly expand Boeing's market share. They were also concerned about the exclusive supply contracts between Boeing and three major airline companies (IDP1). EU's strength and authority to influence the merger was denied by concerned US congressman and other lawmakers. It was implied that such behaviour on EU's part was solely based to protect their home company i. e. Airbus (PRH2). EU clearly stated to the US authorities that investigation over their end was factually and rigidly based in accordance with the European Community (EC) law. If the proposed merger comes under criteria of a Community Law then the Commission has to take various factors into consideration before concluding a final statement. It will define the relevant product with its geographic market. It needs to establish if the company has a pioneering position in the market and how it can affect the competition via this dimension. Commission will evaluate company's profile by taking various economic dimensions into consideration like entry barriers, market share of its competitors, past trends in its supply and demand, etc (EC1). Any decision taken that might breach EC law will result in penalty. If the Commission feels that the merger doesn't aligns with EC law, it is authorised to fine a company upto 10% if it goes through with the merger

(IDP2). Or they can ask the company to consider certain modifications which might mould the merger in accordance with law (EC2). This constant argument between the Transatlantic nations escalated. Pearlstein and Swardson (1997) quoted US representatives and Commission members who stated that both the nations could be heading in a trade war. However, Boeing's chairman Philip Condit came to an agreement with EU and several key concessions were made to get EU's approval for the merger (BOG1).

## **2. 3 Opposing views of both nations**

In this section we will try and understand what resulted into such an opposing level of outcome by the antitrust authorities of the EU and the United States. Different legal philosophies will be outlined for both the committees on the basis of which review was conducted. According to FTC (1992) a merger regulation is constructed to prevent organisations to use this mode as means of enhancing their market power or facilitate their exercise (FTC2). Pitofsky (1992) stated that mergers might lead to a path which might enable an organisation to become a monopoly. As a result of this monopoly they can charge their customers with premium prices. This might also lead to lesser innovation and lack of motivation achieve efficiency in production (Pitofsky, 1992). Stock (1999) displayed in one of his studies that United States review for mergers is based more maintaining general structure of the market. It tries to prevent oligopolistic behaviour from firms and retain competition. On the other hand, sustaining or enhancing the power of dominant home organisations was the criteria for EU Merger Regulations. It is clear to say that EU law focuses more on the market leader while US law centers around market more generally. " A brief summary of U.

S. and EU practice in merger control illustrates that EU law is more concerned with monopoly creation and the complacency of a market-dominating firm, whereas U. S. merger review appears relatively more concerned with cartel facilitation and market-wide lethargy. Although U. S. law recognizes the danger that mergers can lead to anti-competitive unilateral conduct, agency practice tends to indicate that collusion and coordination between competitors persist as the stronger focus of merger regulation. EU law, on its face, appears to have a comparably greater focus on preventing anticompetitive conduct committed by the leading firm of an industry.(Stock, 1999) "

## **2. 4 FTC's Reasoning**

Although FTC was aware that this merger would have increased Boeing's market share up to 70%, they believed it wouldn't have affected the competition or any barriers to entry. They assured their investigation was highly efficient and no facts were overlooked. According to them McDonnell Douglas lacked the competitive edge and it couldn't have aided Boeing to gain any potential advantage in the market for civil aviation. On the other hand they expressed their concern about exclusive deals that Boeing made with three major airlines. They assured that anticompetitive effects of this deal will be monitored. But questions were raised with their decision. It was believed that FTC's investigation lacked an in depth analysis of facts and the sole purpose they approved the merger was to create a more dominant home player into the market. FTC clearly stated in a joint statement regarding the merger that accusations made towards them for developing a " national champion" were delusional. But they also added to this statement

that the only way to boost US' export, address concerns about balance of trade and create job employment is by enabling US' firms to compete vigorously domestically and internationally (FTC3).

## **2. 5 Conclusion**

In the end it can said that the Boeing-McDonnell Douglas merger case gives a deep insight to the functioning of both the US antitrust law and the EU competition law. Although Commission's investigation regarding the merger was officially justifiable and their decision was based lawfully on past instances, there is always a chance that such cases might be encountered by both the nations in the future. In a dynamic economy where Multinational Corporations are trying to grow and expand themselves through means of mergers and acquisitions such cohesive engagements will arise. EU and US should work together in the formation of better and faster communication channels which will aid them in organising and agreeing to cases this field. Only by working upon this can both these nations can promote transatlantic competition and safeguard the interest of consumers.

## **3. GE and Honeywell**

Although EU and US had to face a series of cohesive events in the Boeing-McDonnell Douglas merger case, one would assume that these two transatlantic nations must have worked on a better framework to establish better communication channels and meet with terms on a common ground relating to mergers and antitrust laws. Unfortunately that wasn't the case.

### **3. 1 Introduction**

On 19th October 2000, CEO of General Electric, Jack Welch proposed a merger of rival industrial conglomerate Honeywell. The deal would have been the biggest merger in industrial history resulting to a value of over \$40 billion. But things didn't turn the way it was expected by GE. EU's antitrust authorities solely prohibited the merger where as on the other side of the Atlantic it was approved by the US' Department of Justice and various other administrations (TIME1).

### **3. 2 Opposing Perspective**

Commission 's point of view towards the merger had two aspects. According to Article 82 of the Treaty of Rome, firms like GE which covered a major market share for Large Jet Aircraft engines were subjected to constant investigation. This article states that " Any abuse of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States" (EC3). Honeywell dominated the market for avionics and non-avionics aerospace components. Taking both the company's pioneering positions in the market at their own levels, EU's Merger Regulations didn't allow the merger to go through. Commission was certain that this deal will result into " conglomerate" effects which eventually will hamper effective competition. Merging parties can lead to practice restricted activities(EC4). There were three main arguments from Commission's perspective:

Conglomerate Effects: One of the commission's arguments was that GE could force aircraft builders to take a bundle of products including Honeywell's avionics equipment, which would give Honeywell an unfair advantage over



its direct competitors - a theory known as "conglomerate effects (NYT2)." According to Commission this could result in activities which might affect Honeywell's competitors resulting in exit from the market. They also argued that such activities will diminish the scope of investment and block all entrants for potential competitors. According to Choi(2007), "the merged firm will reduce the price of its bundled system and expand market share relative to the situation prior to the merger. Prior to the merger, any price cut by one of the merging firms will tend to benefit the other's sales. In the absence of the merger, neither party will take account of this benefit of a price cut on the other's sales. Following the merger, however, the merged entity can "internalize" these "pricing externalities" arising from the complementarity of their components by reducing the price of the bundle to below the level the two players would choose if acting independently. This will expand the merged firm's sales and market share." Horizontal and Vertical Effects: According to an article from the New York Times(2001), Commission another argument was that this merger would create or strengthen dominant positions on several markets and that the remedies proposed by G. E. were insufficient to resolve the competition concerns resulting from the proposed acquisition of Honeywell. Excerpts from this article also highlighted that Commission feared that the combined power of both these companies would have resulted dominant positions in the markets for the supply of avionics, non-avionics and corporate jet engines, as well as to the strengthening of G. E.'s existing dominant positions in jet engines for large commercial and large regional jets. Thus, a horizontal overlap along with vertical integration into Honeywell activities combined with GE's financial power would have created or strengthened their positions

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in some markets. Merger Efficiencies: Patterson and Shapiro (2001) outlined the different views of what constitute " efficiencies" in the case of Honeywell and GE. According to them U. S.' approach and reasoning regarding efficiencies was straightforward and had excellent economic stance. They believed mergers that lead to lower prices are procompetitive. They based the effects of mergers on the economic incentives that the merger entity will face." Therefore, if combining the assets of the merging firms gives the merged entity an economic incentive to reduce prices that would not otherwise arise, the combination involves merger-specific efficiencies that count in favour of a proposed merger." On the contrary they gave quite a different approach to efficiencies for EU in GE and Honeywell merger. According to " Genuine" efficiencies, such as cost savings were welcomed and count in favour of the merging parties." However, lower prices that result from " strategic behaviour" do not count as " efficiencies" and may be regarded as anticompetitive. " EU's approach lacked in economic merit.

### **3. 3 Conclusion**

Although both the antitrust authorities were subjected to the same set of facts, the resulting decision was entirely different. This might be a result of different legal standards. Such conflicts might also arise due to difference of judgment on alike facts. Based on GE/Honeywell, we must conclude that mergers in the EU may be subject to an efficiency offense whereby they are blocked precisely because they provide incentives for the merged entity to set lower prices. Under these circumstances, convergence would seem to require either a wholesale rewriting of the efficiencies portion of the Guidelines or a reversal of course by the EU After the deal resulted in a

complete failure, Mr. Mario Monti, the European commissioner in charge of competition faced a lot of criticism. Some analysts stated in an article in the New York Times that Mr. Monti has introduced a new dimension of unpredictability and uncertainty by invoking novel theories that have rarely been used elsewhere. Some believed that the DOJ didnt take a proper investigation while others said that " Mr. Monti has not been motivated by a desire to protect European companies from American rivals." . Many analysts assert that it would be a mistake to infer that European and American antitrust enforcement practices are headed in opposite directions. Both sides, they say, remain anchored to similar goals of enhancing competition and keeping markets open. Some say there is a difference in emphasis, with European regulators concentrating first on whether a merger will hurt business competition, while those in the United States focus initially on whether it will hurt consumers. But others say the distinction is diminishing.

#### **4. Recommendations**

In light of both the cases given above, following recommendations are suggested: Although both the nations share the same interest, they should devise a standard procedure to accomodate based upon internationally trusted antitrust standards. For the Boeing-McDonnell Douglas case, a more simpler recommendation is that Boeing could have reached with terms eventually with the Commission. There was no need to include antitrust authorities from both the nations breathing upon each other neck. As written above in the case, such activities give rise to trade wars which should always be averted. Therefore, as long as negotiations are justifiable and in accordance to the law, a mutually accepted solution could always be

reached. Commission can set up a Peer Review Panel. This method can provide them fresh mindset and might also give them an alternative view point. It is also advised that the level of transparency is increased. Merging parties should have better access to files regarding the investigation. This allow them to defend themselves against false acquisitions. Merging organisations should provide better efficiencies to justify their proposed merger. Efficiencies is an economic theory that states that the greatest benefit to society of any action is achieved when the marginal benefits from the allocation of resources are equivalent to the marginal social costs of the allocation. This allow the commission to study whether the strengthened position via this proposed merger will aid in customer welfare or will it to lead anti-competitive practices.