ICLE International Center for Law & Economics

On the Antitrust Risks of Four to Three Mergers: A Case Study of a Potential ThyssenKrupp/Kone Merger
November 12, 2019
Eric Fruits and Geoffrey A. Manne

Today, Reuters reports that Germany-based ThyssenKrupp has received bids from three bidding groups for a majority stake in the firm's elevator business. Finland's Kone teamed with private equity firm CVC to bid on the company. Private equity firms Blackstone and Carlyle joined with the Canada Pension Plan Investment Board to submit a bid. A third bid came from Advent, Cinven, and the Abu Dhabi Investment Authority.

Also today — in anticipation of the long-rumored and much-discussed sale of ThyssenKrupp's elevator business — the International Center for Law & Economics released *The Antitrust Risks of Four To Three Mergers: Heightened Scrutiny of a Potential ThyssenKrupp/Kone Merger*, by Eric Fruits and Geoffrey A. Manne. This study examines the heightened scrutiny of four to three mergers by competition authorities in the current regulatory environment, using a potential ThyssenKrupp/Kone merger as a case study.

In recent years, regulators have become more aggressive in merger enforcement in response to populist criticisms that lax merger enforcement has led to the rise of anticompetitive "big business." In this environment, it is easy to imagine regulators intensely scrutinizing and challenging or conditioning nearly any merger that substantially increases concentration.

This potential deal provides an opportunity to highlight the likely challenges, complexity, and cost that regulatory scrutiny of such mergers actually entails — and it is likely to be a far cry from the lax review and permissive decisionmaking of antitrust critics' imagining.

In the case of a potential ThyssenKrupp/Kone merger, the combined entity would face lengthy, costly, and duplicative review in multiple jurisdictions, any one of which could effectively block the merger or impose onerous conditions. It would face the automatic assumption of excessive concentration in several of these, including the US, EU, and Canada. In the US, the deal would also face heightened scrutiny based on political considerations, including the perception that the deal would strengthen a foreign firm at the expense of a domestic supplier. It would also face the risk of politicized litigation from state attorneys general, and potentially the threat of extractive litigation by competitors and customers.

Whether the merger would *actually* entail anticompetitive risk may, unfortunately, be of only secondary importance in determining the likelihood and extent of a merger challenge or the imposition of onerous conditions.

A "highly concentrated" market

In many jurisdictions, the four to three merger would likely trigger a "highly concentrated" market designation. With the merging firms having a dominant share of the market for elevators, the deal would be viewed as problematic in several areas:

- The US (share > 35%, HHI > 3,000, HHI increase > 700),
- Canada (share of approximately 50%, HHI > 2,900, HHI increase of 1,000),
- Australia (share > 40%, HHI > 3,100, HHI increase > 500),
- Europe (shares of 33–65%, HHIs in excess of 2,700, and HHI increases of 270 or higher in Sweden, Finland, Netherlands, Austria, France, and Luxembourg).

As with most mergers, a potential ThyssenKrupp/Kone merger would likely generate "hot docs" that would be used to support the assumption of anticompetitive harm from the increase in concentration, especially in light of past allegations of price fixing in the industry and a decision by the European Commission in 2007 to fine certain companies in the industry for alleged anticompetitive conduct.

Political risks

The merger would also surely face substantial political risks in the US and elsewhere from the perception the deal would strengthen a foreign firm at the expense of a domestic supplier. President Trump’s administration has demonstrated a keen interest in protecting what it sees as US interests vis-à-vis foreign competition. As a high-rise and hotel developer who has shown a willingness to intervene in antitrust enforcement to protect his interests, President Trump may have a heightened personal interest in a ThyssenKrupp/Kone merger.

To the extent that US federal, state, and local governments purchase products from the merging parties, the deal would likely be subjected to increased attention from federal antitrust regulators as well as states’ attorneys general. Indeed, the US Department of Justice (DOJ) has created a “Procurement Collusion Strike Force” focused on “deterring, detecting, investigating and prosecuting antitrust crimes . . . which undermine competition in government procurement. . . .”

The deal may also face scrutiny from EC, UK, Canadian, and Australian competition authorities, each of which has exhibited increased willingness to thwart such mergers. For example, the EU recently blocked a proposed merger between the transport (rail) services of EU firms, Siemens and Alstom. The UK recently blocked a series of major deals that had only limited competitive effects on the UK. In one of these, Thermo Fisher Scientific’s proposed acquisition of Roper Technologies’ Gatan subsidiary was not challenged in the US, but the deal was abandoned after the UK CMA decided to block the deal despite its limited connections to the UK.

Economic risks

In addition to the structural and political factors that may lead to blocking a four to three merger, several economic factors may further exacerbate the problem. While these, too, may be wrongly deemed problematic in particular cases by reviewing authorities, they are — relatively at least — better-supported by economic theory in the abstract. Moreover, even where wrongly applied, they are often impossible to refute successfully given the relevant standards. And such alleged economic concerns can act as an effective smokescreen for blocking a merger based on the sorts of political and structural considerations discussed above. Some of these economic factors include:

- **Barriers to entry**. IBISWorld identifies barriers to entry to include economies of scale, long-standing relationships with existing buyers, as well as long records of safety and reliability. Strictly speaking, these are not costs borne only by a new entrant, and thus should not be deemed competitively-relevant entry barriers. Yet merger review authorities the world over fail to recognize this distinction, and routinely scuttle mergers based simply on the costs faced by additional competitors entering the market.
- **Potential unilateral effects**. The extent of direct competition between the products and services sold by the merging parties is a key part of the evaluation of unilateral price effects. Competition authorities would likely consider a significant range of information to evaluate the extent of direct competition between the products and services sold by ThyssenKrupp and its merger partner. In addition to “hot docs,” this information could include won/lost bid reports as well as evidence from discount

approval processes and customer switching patterns. Because the purchase of elevator and escalator products and services involves negotiation by sophisticated and experienced buyers, it is likely that this type of bid information would be readily available for review.

- **A history of coordinated conduct involving ThyssenKrupp and Kone**. Competition authorities will also consider the risk that a four to three merger will increase the ability and likelihood for the remaining, smaller number of firms to collude. In 2007 the European Commission imposed a €992 million cartel fine on five elevator firms: ThyssenKrupp, Kone, Schindler, United Technologies, and Mitsubishi. At the time, it was the largest-ever cartel fine. Several companies, including Kone and UTC, admitted wrongdoing.

Conclusion

As "populist" antitrust gains more traction among enforcers aiming to stave off criticisms of lax enforcement, superficial and non-economic concerns have increased salience. The simple benefit of a resounding headline — "The US DOJ challenges increased concentration that would stifle the global construction boom" — signaling enforcers' efforts to thwart further increases in concentration and save blue collar jobs is likely to be viewed by regulators as substantial.

Coupled with the arguably more robust, potential economic arguments involving unilateral and coordinated effects arising from such a merger, a four to three merger like a potential ThyssenKrupp/Kone transaction would be sure to attract significant scrutiny and delay. Any arguments that such a deal might actually decrease prices and increase efficiency are — even if valid — less likely to gain as much traction in today's regulatory environment.

View Article