

Supply-Side Factors Identify Market Participants, Not Markets: Global Antitrust Institute Comment on the EC’s Draft Notice on Defining Relevant Markets for EU Competition Law

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The Global Antitrust Institute (“GAI”) respectfully submits this comment to the European Commission (“Commission”) in connection with the Commission’s draft Notice on the Definition of the Relevant Market for the Purposes of Union Competition Law (“Notice”).¹ The GAI welcomes the opportunity to provide input on these draft provisions based on our extensive experience and expertise in competition law and economics.²

In this comment, we focus on the relationship between market definition and competitive effects analysis. In particular, we consider the Notice’s treatment of supply-side factors in defining relevant markets. Market definition is not an end in itself, but “a tool to structure and facilitate the competitive assessment,”³ being “only one step in the

¹ EUROPEAN COMMISSION NOTICE ON THE DEFINITION OF THE RELEVANT MARKET FOR THE PURPOSES OF UNION COMPETITION LAW (DRAFT FOR PUBLIC COMMENTS) (2022), https://ec.europa.eu/commission/presscorner/detail/en/ip_21_3585.

² The GAI is a division of George Mason University’s Antonin Scalia Law School and reports to the Dean of the Law School. In support of its mission, the GAI draws upon the independent expertise of the Law School faculty including Judge Douglas H. Ginsburg, Senior Judge of the U.S. Court of Appeals for the D.C. Circuit and former Assistant Attorney General in charge of the Antitrust Division of the U.S. Department of Justice; Joshua D. Wright, University Professor and former Commissioner of the U.S. Federal Trade Commission (FTC); John M. Yun, Associate Professor and former Acting Deputy Assistant Director, Bureau of Economics, FTC; Bruce H. Kobayashi, Paige V. & Henry N. Butler Chair in Law & Economics and former Director of the Bureau of Economics, FTC; Abbott B. Lipsky, Jr., Adjunct Professor, Director of Competition Advocacy for the GAI, former Acting Director of the Bureau of Competition, FTC, and former Deputy Assistant Attorney General for Antitrust, U.S. Department of Justice; and Dr. Alexander Raskovich, the GAI’s Director of Research. The GAI is grateful for the generous contributions from the individuals, foundations, and corporations who enable the GAI to carry out its mission. Its finances are managed through the George Mason University Foundation, Inc., established to support the activities of George Mason University. More information may be found at <https://gai.gmu.edu/>.

³ NOTICE, *supra* n. 1, at 4, ¶ 7.

Commission's assessment."⁴ Market definition sets the stage for an analysis of competitive effects, but the "Commission only decides on whether there are competitive concerns after having carried out a competitive assessment."⁵

Thus, defining a relevant market with its immediate consequences is not sufficient for a finding of competitive concern. But insofar as the Commission uses market definition as a prism through which to "structure and facilitate the competitive assessment," care must be taken in delineating the contours of the market, lest errors made at the market definition stage carry through to the competitive assessment itself.

For market definition to be a meaningful prelude to a competitive assessment, the market should delineate a set of goods and geographies within which significant market power could be wielded against consumers—if the market were controlled by a hypothetical monopolist.⁶ Given a proper focus on the potential for harm to consumers (not competitors), market definition should focus on demand-side substitution to capture the competitive options available to those consumers.

We commend the Notice's extensive consideration of supply-side substitution.⁷ The potential for firms to switch across production lines of non-substitutable goods can powerfully affect the post-merger equilibrium in a market defined on the demand side. But we respectfully urge the Commission to consider that supply-side substitution is better applied in the identification of market *participants*, not in defining the *market* itself. To conflate the two could obscure the ultimate concern of the competitive assessment: the potential for harm to *consumers*, not *competitors*.⁸

⁴ *Id.* at 6, ¶ 13.

⁵ *Id.*

⁶ Here and elsewhere, "consumer" should be understood symmetrically to encompass input sellers who may be vulnerable to an exercise of substantial market power by input buyers. See the discussion of "purchasing markets" in the NOTICE, *supra* n. 1, at 3-4, ¶ 6.

⁷ NOTICE, *supra* n. 1, at 15-17, ¶¶ 34-39.

⁸ "Market definition leads to the identification of the relevant competitors of the undertakings involved when offering products as well as the relevant customers." NOTICE, *supra* n. 1, at 3, ¶ 5. The identification of relevant competitors should be informed by but distinct from market definition, as we discuss below.

A firm that does not currently provide a relevant product but could profitably do so quickly and without significant sunk costs in response to, say, an increase in the price of relevant products, should properly be designated a participant in the relevant market. The Notice takes an entirely different tack, however, analyzing whether the scope for supply-side substitution is sufficiently large, involving a sufficiently broad set of producers, to allow for an expansion in the defined market to include goods that are not substitutes for a given set of consumers.⁹

The Notice's approach is problematic, or at best unclear. Expanding the market to encompass goods not substitutable on the demand side necessarily expands the set of relevant consumers to include groups with heterogeneous demands, potentially with different purchasing options and vulnerability to harm. Although the Commission's aim is to undertake such an expansion in the defined market *only* when the competitive conditions facing the consumer groups are homogeneous,¹⁰ those conditions are quite restrictive. The consequence of this approach is that supply-side factors will commonly be excluded from the identification of market participants. This potentially yields a biased competitive assessment that materially understates the breadth of options available to consumers and the competitive impact of such options.

The Notice states that the Commission will nonetheless take account of a solitary or small number of swing producers in its competitive assessment.¹¹ But insofar as that competitive assessment has been "structure[d] and facilitate[d]" by the market definition analysis, failure to account for any swing producer as a market participant is problematic.

Traditionally, one of the primary functions of market definition is to identify participants in the market, assign market shares to those participants, and compute concentration levels and changes. As the Notice states: "Market definition makes it possible to calculate market shares, which the Commission may use to assess an undertaking's competitive strength for the purposes of the competitive assessment."¹²

⁹ NOTICE, *supra* n. 1, at 3-4, ¶ 6.

¹⁰ NOTICE, *supra* n. 1, at 15, ¶ 35.

¹¹ NOTICE, *supra* n. 1, at 15, ¶ 38.

¹² NOTICE, *supra* n. 1, at 5, ¶ 9.

Thus, failing to account for supply-side substitution in the identification of market participants incorrectly sets to zero the competitive strengths of swing producers, while unjustifiably inflating the competitive strengths of the undertaking and other competitors operating in the defined market.

A more realistic and accurate depiction of competitive conditions in a relevant market (properly defined on demand-side factors alone) would be, first, to recognize as a market participant *any* firm that could profitably swing production into the relevant products quickly and without significant sunk cost. Second, a “market share” could be imputed to such a swing producer, even though the producer currently has no sales in the relevant market, calculated to best assess the producer’s competitive strength in the relevant market through swing production. The imputation of a market share to a swing producer would require a competitive assessment of the swing producer’s incentive and ability to swing into the market, based on such factors as relative margins earned on different products and capacities on different production lines.¹³

As a matter of economics, there is no bright line dividing market definition and the identification of market participants and their competitive strengths from the competitive assessment. We recommend that the Commission apply an assessment of the competitive strengths of swing producers to the identification of participants in the relevant market.

¹³ Another important function of modern market definition, beyond the calculation of market shares, is to determine whether firms in the relevant market would have an incentive to raise price. See Daniel P. O’Brien & Abraham L. Wickelgren, *A Critical Analysis of Critical Loss Analysis*, 71 ANTITRUST L.J. 161 (2003); Michael L. Katz & Carl Shapiro, *Critical Loss: Let’s Tell the Whole Story*, 17 ANTITRUST 49 (2003). These types of competitive assessments, consistent with this comment, also require that relevant antitrust markets correctly identify both the potential harm to consumers and the relevant set of market participants.