European Commission

Competition *merger brief*

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Competition Merger Brief 4/2024 – Article 1

Competition *Merger Brief*

Celanese/Dupont (Mobility & Materials Business) – Engineering a crown jewel remedy

Amine Mansour, Constanza Marco Dufort, Jean-Christophe Mauger

In a nutshell

In specific high-performance thermoplastics areas, where industrial customers have strong quality requirements and need to re-qualify the products when there is a change of supplier, some additional safeguarding measures to a standard remedy may be needed to ensure restoration of competition following a merger.

This is why the Commission cleared the acquisition of DuPont M&M Business by Celanese only subject to a divestment Commitment of Celanese assets and a crown jewel commitment. The latter would have been triggered in case former customers of Celanese in TPC would not have qualified the buyer of the divestment business.

1. Introduction

On 11th October 2022, the European Commission ('EC') conditionally cleared the acquisition by Celanese Corporation ('Celanese') of the majority of DuPont's Mobility & Materials business ('M&M Business') ('the Transaction') in Phase I, subject to the divestment of Celanese's global thermoplastic copolyester ('TPC') business.

Celanese and the M&M Business are both active in the production and supply of engineering thermoplastics, which are high-performance plastics used for demanding applications. In particular, these performance requirements are related to mechanical strength and resistance to impact, heat and chemicals. These plastics are used in sectors such as automotive, electronics and other industrial sectors.

The Commission expressed serious doubts with regards to the production and supply of thermoplastic copolyester ('TPC') in the EEA, due to the Parties' high market shares, the low number of competitors and the lack of evidence of entry. In response to the Commission's serious doubts, Celanese offered to divest its activities in TPC in the EEA (the 'Divestment Business'). To mitigate risks associated with the transfer of the Divestment Business, and particularly of the compounding line coupled with the requirement to re-qualify products with customers, the Notifying Party identified a buyer before the Commission had to take a decision and further committed to divest additional assets ('crown jewel Commitment') to restore competition lost due to the Transaction in case the transfer of the Divestment Business and the requalification of a substantial share of existing customers could not be completed under a certain timeframe.

2. Horizontal overlaps in TPC

TPC is produced through several steps, typically involving polymerization and compounding.

<ins>Polymerization</ins>: The process begins with the synthesis of the base polymer, in which various monomers are reacted with one another to form into polymer chains.

<ins>Compounding</ins>: the base polymer is then compounded with additives to enhance its properties. These additives can include:

- Fillers: To improve strength and reduce costs (e.g., glass fibers).
- Stabilizers: To protect against degradation.
- Plasticizers: To improve flexibility.
- Colorants: For aesthetic purposes.

TPC is then sold for various end-uses, such as automotive or industrial & consumer goods. TPC is a high performance product that offers toughness, tear resistance, and unique chemical and temperature resistance.

Celanese acquired TPC production and compounding facilities in Ferrara, Italy, in 2016 as part of its purchase of the SO.F.TER Group. Until July 2021, TPC compounding occurred in Ferrara, but Celanese then sold that compounding site and moved all its engineering thermoplastics compounding operations to its Forli plant in Italy. The M&M business produced its own TPC, and also

manufactured and sold TPC via its joint-venture with Toray in Japan.

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The Commission found that the Transaction would raise serious doubts as to its compatibility with the internal market with regards to TPC, for the following reasons.

High combined market shares in an already concentrated market. At the EEA level, the Transaction would have led to a combined market share of [50-60]%, with a market share increment of [5-10]%. The number of competing alternatives would have been reduced from three to two following the Transaction, as only the Parties and DSM-Firmenich AG would have remained present. The post-Transaction HHI would have been [4500-5000], with an increment of [800-900]. The oligopolistic market structure of the TPC market in the EEA was confirmed by market participants.

The Parties were close competitors. Based on the high degree of substitutability between the Parties' products and the fact that rivalry between the Parties had been an important source of competition on the market, the Commission considered that the Parties were close competitors in the TPC market. Indeed, market participants explained that, with regards to TPC, Celanese and the M&M business had a similar geographic reach and a similar customer mix in terms of end-use.

Customers had limited possibilities to switch suppliers. In the TPC market, lengthy testing/qualification processes may have limited the ability and the incentives of the final or intermediate customer to switch to a new supplier. Indeed, the Parties' customers explained that, in order to qualify a new supplier or raw material, their automotive clients required a full homologation process, including approval at all levels of the supply chain. This procedure can be quite long, a TPC customer explaining that it could take at least 1.5 years.

Entry was unlikely. A majority of customers explained that there had been no entries in this market in the last five years. Notably, even assuming a global market for TPC, entry and expansion of Asian suppliers into Europe did not appear to be a constraint for EEA-based suppliers of TPC. One customer noted in that regard that alternative suppliers from the Asia-Pacific regions had a limited portfolio and were not viewed as competitively comparable in the market.

Customers expected price increases. Customers explained that, when Celanese acquired the SO.F.TER Group in 2016, prices for TPC in the EEA increased. Therefore, concentration in the industry had already led to price increases in the past, and customers considered that the Transaction would likely result in even higher prices for TPC.

3. Structural remedy for TPC

3.1 The Divestment Business

On 20 September 2022, the Notifying Party formally submitted a first set of commitments to eliminate competition concerns as regards TPC (the 'Initial Commitments').

The Initial Commitments consisted in the divestiture of the entire global TPC business of Celanese, and included, amongst others:

- Celanese's TPC manufacturing (polymerization) facility in Ferrara, Italy.
- a compounding line located at another Celanese production site in Forli, Italy to be dismantled by Celanese, transported and installed at the purchaser's compounding facility by the purchaser, as the Purchaser Taro Plast did not own a TPC compounding line.
- Trademarks under which Celanese sold TPC.
- At the option of the purchaser, all reasonable assistance by Celanese to obtain re-qualification / re-certification of the products currently supplied by the Divestment Business and a time-limited transitional toll-compounding agreement for an initial term of 6 months.

Beyond the standard purchaser requirements, the purchaser was also expected in the Initial Commitments to have the required capabilities in sales and R&D to integrate the assets of the Divestment Business and to be able to transfer the compounding line and qualify its output in accordance with customer requirements.

The Divestment Business included trademarks and production assets which had to be carved out from Celanese's activities in engineering thermoplastics. In August 2022, before the deadline for the Commission to adopt a decision, Celanese entered into an agreement to sell the Divestment Business to Taro Plast, an established competitor in the field of engineering plastics (although not producing TPC), with pre-existing functions such as sales, procurement and other corporate functions, as well as proven experience in compounding of other products, and based in Italy as well.

Respondents to the market test noted that the Divestment Business was viable and would allow the purchaser to compete effectively for the manufacture and supply of TPC at EEA-wide and global levels; Moreover, market feedback revealed that Taro Plast had the capacity to maintain and develop the Divestment Business as a viable and active competitive force, even though Taro Plast was not yet producing TPC and customers flagged the need for Taro Plast to quickly build up the necessary know-how and R&D capabilities in the area of TPC.

Based on feedback received from the market test, the Commission also identified some implementation risks associated with the transfer of the Divestment Business, and particularly in relation to the transfer of the compounding line from the Forli site to the premises of the purchaser. In particular, such transfer would require a re-qualification of the products manufactured on that compounding line with respect to their quality and suitability, which may take around 6 to 12 months. Despite the early identification of a buyer and its track record established in the market test, this qualification process introduced a risk that Taro Plast would not be able to produce TPC in the required quality in a sufficiently short period of time

after the transfer of the Divestment Business, thus jeopardising the competitiveness of the Divestment Business.

Such re-qualification would have required active support from Celanese given their experience in TPC production, their familiarity with customers, and their expertise as regards re-qualification in this field. In that context, the Commission considered that the Initial Commitments needed to be amended by additional safeguards that would further incentivise Celanese to assist the purchaser with the key re-qualification process to the best of its abilities and without delay. These additional safeguards should also be suitable to cater for any uncertainty stemming from the fact that a substantial share of TPC customers indicated that they were not very familiar with Taro Plast and that they expected Taro Plast to swiftly build capabilities in the area of TPC.

3.2 The crown jewel obligation

In order to address those concerns, on 30 September 2022, the Notifying Party formally submitted the Final Commitments.

To mitigate risks associated with the transfer of the Divestment Business, and particularly of the compounding line with the requirement to re-qualify products with customers, Celanese committed to divest additional assets to restore competition lost due to the Transaction in case the transfer of the Divestment Business and the requalification of a substantial share of existing customers could not be completed under a certain timeframe (the "Crown Jewel Obligation").

The Final Commitments also included the following amendments:

- Additional R&D capabilities through the transfer of appropriate key personnel and secondment arrangements; and
- The build-up of TPC inventory during the transition, and reservation of such inventory for the customers of the Divestment Business.

The Commission considered that the Final Commitments mitigated the risks associated with the transfer of the Divestment Business and the compounding line flagged by market participants in response to the market test. Indeed, a potential failure of the successful transfer of the Divestment Business and the compounding line was largely mitigated by the Crown Jewel obligation. The Final Commitments provide that the Notifying Party has only complied with the commitments if a substantial share of customers have migrated from the Notifying Party to the purchaser under a certain timeline, indicating that the purchaser indeed acts as a credible competitive force on the EEA and global market for TPC. On this basis, the Commission conditionally cleared the acquisition of the M&M business by Celanese. Taro Plast was approved in a separate buyer approval process.

4. Conclusion

The TPC remedy proposed by Celanese had some carve-out characteristics, taking from Celanese certain activities in engineering thermoplastics. Moreover, TPC customers have stringent requirements on quality, which forces them to requalify the product once divested. The TPC remedy therefore carried some implementation risks. Celanese sought to address these by proposing early on a purchaser with the required expertise to deliver a viable remedy.

Despite this, in view of potential implementation risks also with respect to the identified buyer, the Commission could accept this Commitment only with adequate safeguards. First, the Commission assessed that the purchaser possessed the necessary capabilities to successfully integrate the divested business and compete effectively in the market, along with the need for support from the seller to facilitate a smooth transition. The Commission's assessment of Taro Plast's capabilities and the inclusion of support mechanisms in the Final Commitments reflect this consideration. Second, the inclusion of the "Crown Jewel Obligation" in the Final Commitments provided further incentives for Celanese to support a smooth transfer of the production line and of the requalification process .

Ultimately, these measures were essential not only to replicate a competitive force in the TPC market but also to give the Commission the highest confidence that Celanese remains incentivised to ensure the success of the divestment process. The line transfer and requalification processes were ultimately successful.

European Commission

Competition Merger Brief 4/2024 – Article 2

Competition *Merger Brief*

Booking/eTraveli - A Booking that got cancelled

Marco Ramondino, Ana Lapiedra Carmona, Christian Grobecker, Itai Rabinovici, Jean-Michel Coumes, Valentine Genu

In a nutshell

In today's digital economy, fewer transactions are purely horizontal, vertical, or conglomerate in nature. This is also the case for the Booking/eTraveli transaction, where a dominant undertaking sought to acquire a complementary business that would strengthen its dominance on the core market.

There is consensus in the public debate that effective merger review of transactions in digital markets is required, in particular in view of the on-going tech revolution that will affect all sectors of the economy and society (AI, cloud computing, Internet of Things, etc).

The Commission's assessment in this case shows that the EU Merger Regulation can accommodate these new market realities in a credible theory of harm.

Introduction

On 25 September 2023, following an in-depth investigation, the Commission prohibited the acquisition of Flugo Group Holdings ('eTraveli') by Booking Holdings ('Booking') ('the Transaction').

Booking's main activity in the EEA is the provision of hotel online travel agency ('OTA') services under the Booking.com brand. In addition, it provides metasearch services for accommodation, car rental and flights via its KAYAK business. Finally, Booking provides access to its accommodation OTA services to other travel operators through commercial affiliated agreements. Prior to the Transaction, Booking already offered flights through a commercial affiliated agreement with eTraveli. eTraveli is primarily active as a flight OTA provider, operating via its brands Gotogate, My Trip, Seat24 and SuperSaver.

Merger review in digital markets: strengthening of the core market

This Transaction is an example of a business strategy frequently used in digital markets whereby a leading player seeks to acquire a complementary business with the aim of strengthening its position on its core market by developing or expanding an ecosystem of related services.

This type of business strategy does not fit neatly into the traditional framework for the assessment of mergers which makes a distinction between horizontal and non-horizontal mergers, including vertical and conglomerate transactions. Indeed, while the businesses being combined are complementary, the effects of their combination may be akin to those achieved by bringing together competing products and services without the need for specific exclusionary conducts.

The Special Advisers' report on Competition policy in the digital era (2019) observed that attention should be paid to the *"conduct of conglomerate firms that are dominant in a core market characterized by strong network effects and a large user base but, based on these particular strengths, including data, reach out to broader markets."* [1] It suggested potential theories of harm in cases where the acquirer operates an ecosystem that benefits from strong positive network effects which act as a significant barrier to entry.

A 2022 report to the Commission by Professor Viktoria Robertson which examines digital and tech merger cases from 19 EU Member States and the UK[2] observed that, despite the fact that mergers in digital markets may not fit neatly into the traditional categorisation of theories of harm, first, the Commission's decisional practice shows that the significant impediment of effective competition ('SIEC') test under Article 2(3) EUMR is starting to accommodate new market realities in complex digital markets that involve digital ecosystems, and second, the EUMR or national merger rules do not necessarily stand in the way for the review of cases involving

[1] Special Advisers Report to the European Commission, 'Competition policy for the digital era' (2019), p. 22.

[2] Viktoria H.S.E. Robertson, Merger Review in Digital and Technology Markets: Insights from National Case Law, Report to the European Commission' (July 2022).

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the strengthening of digital ecosystems. The report further confirms that the "*creation and strengthening of digital ecosystems are objectives that several digital platforms pursue, and* [that] *should therefore not be overlooked in the merger assessment*".[3] The main competition concern is not however the building or reinforcing of an ecosystem in itself according to the report, but rather its effects on the different markets: "*In fact, competition concerns in today's digital markets may arise not so much because of well-defined competition issues in specific relevant markets, and perhaps not even because of every single small merger that is completed. Instead, competition concerns related to digital platforms arise from the combined effects of these mergers in multi-sided markets with strong network effects, with a great many markets concerned*".[4]

The OECD issued a report in 2023 on theories of harm for digital mergers[5] in which it observed that, rather than a traditional focus on whether products or services are complements, substitutes or unrelated, "*at the core [of these theories of harm] is the notion that mergers involving ecosystems may have a broader impact in terms of entrenching the position and strength of the ecosystem as a whole*",[6] leading to negative effects on the markets concerned.

In the same vein, the 2023 Recommended Practices Chapter on non-horizontal merger analysis by the International Competition Network states that *"when a firm with a business ecosystem acquires a target that is active in (a) related market(s), it may raise potential competition concerns in the market of the acquirer or of the target; […]; it may increase barriers to entry and expansion; or it may block entry points into the core market from related markets […] If the acquirer has a business ecosystem, agencies should consider whether […] the transaction strengthens network effects […]. Such factors may protect, entrench or extend market power within an ecosystem through a dynamic combination of horizontal and non-horizontal effects".* The chapter explains more specifically that *"Acquisitions in related markets to a digital ecosystem may allow the merging firm to add a large amount of traffic and customer access to their ecosystem. This consolidation may reinforce network effects. In markets where consumer switching is low, this may work to the benefit of large digital ecosystems".*[7]

The Commission's decision in the Booking / eTraveli case (the 'Decision') focuses on the strengthening of Booking's existing dominant position in the hotel OTA market by raising barriers to entry or expansion that are already strong as a result of, among others, network effects and customer inertia. It is therefore an example of how the SIEC test under Article 2(3) EUMR can accommodate new market realities in digital markets.

An acquisition of a complementary product that strengthens Booking's core market

The acquisition of eTraveli by Booking was notified to the Commission on 10 October 2022. The activities of the Parties are largely complementary since Booking and eTraveli are mainly active on the hotel OTA market and the flight OTA market, respectively. The Commission found, however, that the Transaction was not so much aimed at expanding Booking's activities in a neighbouring market, but rather at finding new avenues of growth for its accommodation business.

The rationale behind the deal centres on Booking's vision for the 'Connected Trip,' which integrates various travel services offered by OTAs.[8] This concept is based on the strong overlap among customers using different travel products, such as flights, hotels, and car rentals. Booking views the expansion into flight offerings as a crucial step toward realizing the Connected Trip,[9] complementing its leading position in the accommodation market.

Flights are typically the first element travellers book when planning their trips, and as an 'entry point' of their booking journey, they present the opportunity to target potential customers for hotels.[10] Indeed, offering flights creates significant cross-selling opportunities for Booking's accommodation business — more so than other travel products which are typically purchased after accommodation.[11] This means that, through flights (and the Connected Trip), Booking can engage potential customers earlier in their travel planning journey, enhancing the chances of successfully cross-selling accommodation while achieving additional revenue from the sale of ancillary services (such as taxis, restaurants and activities).

Furthermore, developing the Connected Trip would likely increase customer loyalty and retention, making Booking's platform more attractive to existing users.[12]

Booking's dominant position on the hotel OTA market

Among all OTA services — such as hotels, flights, and car rentals — the hotel OTA market represents the largest sector in terms of total transaction value. Hotel OTA providers also earn the highest commissions, averaging between 10-20%, compared to less than

[3] *Ibid.*, paras. 231 and 233.
[4] *Ibid.*, para. 231.
[5] OECD, 'Theories of harm for digital mergers' (June 2023).
[6] *Ibid.*, p. 27.
[7] ICN Recommended Practices on Non-horizontal Merger Analysis, 2023. https://www.internationalcompetitionnetwork.org/wpcontent/uploads/2024/05/MWG-RPs-on-Non-Horizontal-Mergers-2024.pdf

[8] Decision. Section 6.5.2.1.
[9] See, for example, Booking's 2022 proxy statement, available at: available at https://s201.q4cdn.com/865305287/files/doc_financials/2022/ar/2002proxybookings.pdf. See further: Decision, Section 6.5.2.2.
[10] Decision, paras. 587-589.
[11] Decision, paras. 590-593.
[12] Decision, paras. 594-597.

5% for flight OTAs.[13] In the European Economic Area (EEA). Booking is by far the largest hotel OTA and has consistently captured a market share of 60-70% in both B2B (hotels)[14] and B2C (end customers)[15] segments, well above the level at which dominance can be presumed. Its main competitor, Expedia, is significantly smaller in the EEA and primarily focused on the US market.[16]

Booking's dominant position in the hotel OTA market is also confirmed by several factors. First, Booking anticipates continued growth in its sales.[17] Second, it has demonstrated the ability to operate independently from its customers and competitors; its commissions to hotels are consistently higher than those of its main competitors, and it can impose its terms and conditions on hotels.[18] The Commission's investigation also revealed that Booking outperforms its competitors in several areas, including having the largest hotel portfolio and the most loyal and broad customer base.[19] Moreover, the market investigation confirmed that Booking has the strongest brand recognition and the highest marketing expenditure in the EEA both of which help it attract customers and outpace competitors.[20] Finally, it is important to note that Booking has a material competitive advantage in that it has its own proprietary hotel inventory based on direct bilateral contracts with hotels. Many hotel OTA competitors rely on Booking to source hotel inventory and are therefore not fully independent competitors.[21]

As the dominant player in the hotel OTA market, Booking benefits from strong network effects that create significant barriers to entry and expansion. In essence, the greater the number of customers on a platform, the more attractive it is for hotels to be listed on that OTA and to provide better content.[22] Likewise, the greater the number of hotels on an OTA and the better the content, the more attractive the OTA is to customers. This self-reinforcing dynamic further raises entry barriers for competing OTAs. Compounding these effects are additional challenges for competitors, such as the difficulty in acquiring a broad portfolio of hotel properties, generating customer traffic through online advertising, and overcoming customer inertia.[23] Consequently, potential entrants face significant obstacles in achieving the scale necessary to compete effectively in the market.

[13] Decision, para. 213.
[14] Decision, para. 342 and Table 4.
[15] Decision, para. 349 and Table 5.
[16] Decision, Tables 4 and 5.
[17] Decision, Section 6.4.5.
[18] Decision, Section 6.4.6.
[19] Decision, Section 6.4.7. See in particular Section 6.4.7.4 and para. 527.
[20] Decision, Section 6.4.8.
[21] Decision, Section 6.2.4. and in particular para. 253.
[22] Decision, para. 218.
[23] Decision, Section 6.2.3 and paras. 227-229.

eTraveli: a strong flight OTA on a consistent growth path

The flight OTA market is much smaller in terms of total transactions value than the one for hotels, and commissions are lower. In effect, it is a 'volume' market where competitors try to capture as many transactions as possible and earn low fees on each. To a large extent, flight OTAs rely on meta-search services ('MSS'), where prices of flights can be compared, to attract customers to their platform.[24] Flight content can be sourced from global distribution systems but, to be competitive, significant investment in technology and time is required. eTraveli is an important player on the flight OTA market. The Commission's investigation revealed that it is considered as the strongest competitor on the most important competitive parameter: price.[25] While the market is fragmented, the Commission found that eTraveli is the second largest player on the market and it has been on a consistent growth path.[26] In fact, shortly after the prohibition decision, the CEO of eTraveli implied in an interview that they are the largest flight seller outside of China.[27]

Strengthening of Booking's dominant position

The Transaction did not fall neatly into one of the traditional categories of horizontal, vertical, and conglomerate mergers considered by the Commission's Horizontal Mergers Guidelines[28] ('HMG') and Non-Horizontal Mergers Guidelines[29] ('NHMG'). Nonetheless, in the face of a dynamic and rapidly changing economic reality, the fact that a situation is not expressly envisaged by the HMG or NHMG cannot relieve the Commission from its duty to examine whether a concentration may give rise to a significant impediment of effective competition.[30] On the contrary, the Commission is under a duty to prohibit any transaction that gives rise to a SIEC under Article 2 EUMR, even where, as in the present case, the impediment to effective competition resulting from the strengthening of Booking's dominant position on the hotel OTA market in the EEA is not a scenario fully covered by those guidelines.

In order to assess whether the Transaction would lead to a material strengthening of Booking's dominant position on the hotel OTA market, the Commission first analysed to what extent flight OTA providers, and eTraveli in particular, could be an important customer acquisition channel for Booking and other hotel OTA providers. The investigation showed that the

[24] Decision, para. 269.
[25] Decision, para. 829.
[26] Decision, Table 13 and paras. 826-827.
[27] Skift, After Booking deal went bust, Etraveli CEO says price 'no longer in play', 3 October 2023, available at: https://skift.com/2023/10/03/after-booking-deal-went-bust-etraveli-ceo-says-price-no-longer-in-play/.
[28] Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, *OJ* C 31, 05.02.2004.
[29] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, *OJ* C 265, 18.10.2008
[30] Decision, Section 6.1.1.

Transaction would enable Booking to acquire a significant amount of additional customer traffic, which would provide Booking with new opportunities to cross-sell hotel rooms. Combined with information on Booking's evolution of so-called 'attach rates' (the percentage of customers who after booking a flight make a hotel reservation), the Commission established, on the basis of Booking's own projections, the number of additional website visits that it will generate as a result of the Transaction.[31] Going forward, Booking expected that the additional customer traffic would continue to grow as the merged entity would increase the number of flight OTA sales.[32]

The Commission further assessed the impact of the fact that the acquisition would allow Booking to further develop its travel ecosystem (it already offers car rental, taxi rides and attractions in addition to hotel OTA services). It found, based among others on Booking's internal documents, that this ecosystem would be able to leverage Booking's brand strength and existing customer inertia in the OTA sector.[33] The Commission's investigation showed that customers often directly visit the hotel OTA platform that they normally use and tend to make reservations only on that one hotel OTA.[34] Booking, as the dominant market player, would have profited even more from this inertia on its platform following the Transaction as it saw the development of the Connected Trip as another means to increase the stickiness of its customers.[35]

Similarly, the Commission's investigation revealed that the Transaction would likely have resulted in a further increase in barriers to entry and expansion and strengthened the existing network effects that favour the dominant player. As a result of this, Booking's dominant position on the hotel OTA market would have become even less contestable.[36] Both for current competitors and potential entrants, a path to developing a customer base in the hotel OTA market is through flights. Some rivals indeed currently leverage their flight OTA services to attract customers to whom they can sell the more profitable hotel OTA services. Competitors were thus likely to lose access to the significant additional traffic that Booking would have been able to generate as a result of the Transaction.[37] There were no sufficient alternatives to compensate for this loss of traffic. Other vertical travel OTA services (e.g. car rental, attractions) generate significantly less traffic than flights and hotels, while Booking already dominates other customer acquisition channels such as paid advertising. The investigation revealed that there were a series of players that would have the potential to expand their hotel OTA offering but that saw their chances reduced as a result of the Transaction, including: (i) hotel OTA providers which are (partially) dependent on others for their hotel inventory[38] but that have their own proprietary flight OTA business; and (ii) flight centric OTA providers that currently offer hotel OTA services provided by others but that in time may develop their own hotel OTA offering.[39]

The Commission's finding was confirmed by the fact that Booking's market position would have become less contestable as is illustrated by the expected stability or even growth in Booking's market share in the hotel OTA market resulting from the Transaction. The Commission found that the Transaction would likely have led to harm to hotels as it was likely that Booking's incentives to lower commissions and provide more beneficial terms and conditions to hotels would decrease. In addition, costs for hotels would have increased as the Transaction would have resulted in more sales of hotel rooms funnelled through Booking, which is one of the most expensive sales channels for hotels. Moreover, the Transaction may have resulted in higher prices for end-customers as Booking is an expensive channel from which to source hotel OTA services. The Commission also concluded that the likely negative effects arising from the Transaction would not be outbalanced by the limited economic efficiencies that were put forward by Booking.

Remedies

In order to alleviate the Commission's concerns, Booking proposed to show flight customers a choice screen on the flight check-out page, which is the page shown to travellers after they purchase their flight tickets. In such choice screen, Booking offered to display multiple hotel offers from competing hotel OTAs, allowing customers clicking on the displayed offer to be redirected to the hotel OTA's website. Following an extensive market test the Commission found that the proposed remedies were not sufficiently comprehensive and effective and did not eliminate entirely the identified competition concerns. The selection and ranking of offers by competing hotel OTAs were not sufficiently transparent and non-discriminatory, because KAYAK – a subsidiary of Booking – would have been in control of several aspects of their implementation. Furthermore, the commitments would have been difficult to monitor effectively, especially because of Kayak's algorithm working as a black box. Finally, the offers from competing hotel OTAs would have been displayed only on the flight check-out page and not in other important cross-sell opportunities that Booking would have enjoyed post-Transaction such as emails, notifications, or other pages of the website.

[31] Decision, Section 6.7.2.2.1.
[32] Decision, Section 6.7.2.2.3.
[33] Decision, Section 6.7.2.2.4.
[34] Decision, para. 949. See, more generally, Sections 6.7.2.3.1 and 6.7.2.3.2.
[35] Decision, para. 933 and further.
[36] Decision, Section 6.7.2.3.
[37] Decision, para. 972.
[38] It is a material competitive advantage for a hotel OTA provider to have proprietary hotel inventory through bilateral contacts with hotels. The main players profiting from this are Booking, Expedia and HRS. See Decision, para. 253.
[39] Decision, paras. 981-984.

Conclusion

The Commission's decision in the Booking/eTraveli case is an example of how the SIEC test under Article 2(3) EUMR can accommodate new market realities, even if the Commission's guidelines did not expressly envisage these at the time of their adoption. Moreover, it demonstrates the Commission's commitment to ensure effective merger review in new and complex situations, by identifying theories of harm that focus on market(s) where a transaction is meant to have an impact. Yet, this is nothing new. The Commission's decision comes in the context of a continuing debate on how to ensure effective merger review in digital markets, while considering potential efficiencies or remedies as long as they effectively address competition concerns.

European Commission

Competition *Merger Brief*

Korean Air/Asiana, Lufthansa/MEF/ITA, IAG/Air Europa - Soft landing or flying in the face of consolidation?

Linus Adelt, Borja Francisco Casado, Jean-Michel Coumes, Marine Dewaele, Valentine Genu, Susanna Kärkelä, Guoda Majauskaite, Jean-Christophe Mauger, and Tal Rothstein

In a nutshell

In its analysis of three recent aviation mergers, the Commission found that network carriers support their often more profitable long-haul flights by having a strong network of domestic and short-haul connections which generate feeder traffic and took this finding into account when analysing barriers to entry and remedy proposals, among other aspects.

The cases also illustrate that the Commission has moved beyond the previously used "slot remedy" approach, which in retrospect had often proved ineffective, towards solutions that provide sufficient assurance that entry and/or expansion by rivals will in fact materialise.

Introduction

In 2023, the Commission received notification of three proposed transactions between airlines with operations in Europe, *Korean Air/Asiana*, *Lufthansa/MEF/ITA* and *IAG/Air Europa*.

Each of these cases involved the merger of two network carriers.[1] Moreover, *Lufthansa/MEF/ITA* involved the combination of complementary Lufthansa hubs in Austria, Belgium, Germany and Switzerland and ITA hubs in Milan and Rome, while *Korean Air/Asiana* and *IAG/Air Europa* involved the combination of two carriers with overlapping hubs, Incheon in Seoul in South Korea and Madrid in Spain, respectively. While the *Korean Air/Asiana* and *Lufthansa/MEF/ITA* mergers were cleared with remedies, the parties abandoned the *IAG/Air Europa* merger due to the competition concerns identified by the Commission.

This article presents four aspects that were particularly relevant in these cases: the network dimension of competition, the regression analyses, the counterfactual analysis and the remedy assessment.

The Commission's assessment of these three proposed transactions came in the context of a debate on whether increased consolidation in the European airline industry would improve long-term competitiveness of the industry and overall connectivity in Europe or whether it would unduly harm passengers. In this context, recent reports[2] published by the European Commission show the significant negative effects that increased market concentration can have on market outcomes for passengers. These reports highlight the already concentrated nature of the European aviation market, particularly when looking at airline routes, with most routes in the EU being served by only one or, at most, two carriers. They also show that several large mergers have increased overall concentration in the United States above the levels seen in Europe and find that US passengers are paying significantly higher prices per mile flown than European passengers.

Assessing airline networks

The Commission's standard framework to assess airline competition is based on the so-called 'Origin & Destination' (O&D) approach. Under that approach, each distinct city-pair route that passengers can travel on (directly or via connecting stops) is considered a separate product market. A route that is operated by both merging parties is considered a horizontal overlap.

In addition, market shares played an important role in the competitive assessment, particularly as an initial screen to identify those markets where competition concerns were most likely to arise. Market shares were assessed separately for each relevant O&D overlap, based on both the total number of tickets

[1] Network carriers are airlines that operate a hub-and-spoke business model.

[2] European Commission, *Protecting Competition in a Changing World – Evidence on the evolution of competition in the EU during the past 25 years*, 2024, and Lear et al, *Exploring Aspects of the State of Competition in the EU*, 2024.

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sold to passengers flying on the relevant O&D as well as based on the overall capacity and flight frequency on the route.

The Commission's investigations showed, however, that the O&D approach on its own does not always capture the full impact of airline mergers. Where airlines operate integrated networks of flights, those networks shape competitive dynamics, influence airline competitiveness and can create or reinforce dominant positions in the market.

The Commission's assessment in *Korean Air/Asiana*, *Lufthansa/MEF/ITA* and *IAG/Air Europa* therefore focused not only on the O&D dimension, but also on the network dimension of airline competition. This was particularly relevant because each case involved the proposed merger between two network carriers. Network carriers operate a hub-and-spoke business model from their main airport hubs which takes advantage of the strong synergies between long-haul routes, on the one hand, and domestic as well as short-haul routes, on the other hand.

Why networks matter in airline markets

The Commission's investigations found that a significant proportion of passengers on domestic, short-haul and long-haul flights are connecting passengers, with many long-haul passengers connecting to a domestic or short-haul flight at either or both ends of the route. For example, on a long-haul flight between Rome and Washington, a significant proportion of passengers will have an onward connection in either Rome or Washington (e.g., to connect to other cities in Italy, Europe, or the US). The Commission found that for network carriers, long-haul flights tend to be more profitable than domestic or short-haul flights. Additionally, many long-haul routes cannot be operated profitably without access to a wide range of domestic and short-haul destinations that attract connecting passengers onto these long-haul flights.

Network carriers therefore have an incentive to "feed" long-haul routes with connecting passengers and offer extensive networks of domestic and short-haul flights that serve as strategic feeder traffic for their often more profitable long-haul operations. The Commission found that the domestic and short-haul operations of a network carrier, including the times of arrival and departure as well as the frequency of flights, are carefully planned to support the network carrier's long-haul operations in the most efficient and profitable way.

Importantly, network carriers are distinct from point-to-point carriers, including low-cost carriers such as Ryanair and EasyJet. Unlike network carriers, most point-to-point carriers operate only domestic and short-haul or only long-haul flights and often do not offer passengers the option to connect to another flight at either end of the route. As a result, point-to-point carriers typically operate from a wider range of airports compared to network carriers, who usually only operate from a few strategically selected airport hubs where they hold a large slot portfolio. Those large slot portfolios at their main hub(s) allow network carriers to maintain and adapt a dense and wide network of routes and can act as a barrier to entry and expansion for competitors.

Since point-to-point carriers operate more independent flights without a need for each flight to feed passengers onto other (long-haul) flights, point-to-point carriers are less dependent on peak time slots and rather focus on ensuring a seamless rotation of aircraft throughout the day. They enter and exit new routes more opportunistically depending on their recent profitability rather than taking into account the connectivity and contribution of that route to their overall network – resulting in different choices of routes and often fewer frequencies flown compared to network carriers.

Relevance of networks for recent cases

In the three recently investigated airline mergers, the Commission's understanding of the network dimension of airline markets helped to inform its assessment of i) barriers to entry and expansion, ii) the strength of the constraint imposed by point-to-point rivals, iii) overlaps with and between one-stop connections, and iv) the remedy design.

Barriers to entry and expansion

Having a hub at both ends of a route (or having a hub at one end while a close partner operates a hub at the other end of a route) can allow a network carrier to gain a significant competitive advantage over rivals that do not benefit from such a strong presence and to make market entry more difficult for rivals.

In the *Lufthansa/MEF/ITA* investigation, many of the short-haul routes for which the Commission identified competition concerns involved routes that connect an airport hub operated by Lufthansa with an airport hub operated by ITA. The Commission considered that the parties' high historical market shares on these routes could at least partially be explained by the high barriers to entry and expansion that rivals face on such hub-to-hub routes. First, it is highly unattractive for other network carriers to enter routes without the ability to connect passengers at either end of the route. Indeed, network carriers tend not to fly routes that do not involve one of their hubs or that are outside of the countries in which they have their main base(s). Second, rival airlines may be dissuaded from entering new routes if there is already a dominant, high-frequency offer by a rival on the route. Third, rival airlines may take into account the reaction to market entry by the strong carrier(s) already active on the route. Using their large slot portfolios, incumbent network carriers can expand their own services on the routes, for instance at the exact same flight times as those of the market entrants, and thereby make market entry unprofitable. Fourth, the large slot portfolio held by the network carriers can lead to airport congestion, in particular at peak times of the day, making market entry more difficult.

The Commission also found that the parties enjoyed particularly high market shares on several long-haul routes that connect ITA's long-haul airport hub in Rome-Fiumicino with an airport hub of

one of Lufthansa's North American joint venture partners United Airlines and Air Canada (e.g., Rome-Washington and Rome-Toronto). Given that it is often difficult to profitably operate long-haul routes without having access to a dense network of short-haul and domestic flights at either end of the route, the Commission considered that airlines without an airport hub at either end of a long-haul route faced additional significant barriers to entry and expansion on these routes.

Similarly, in *Korean Air/Asiana*, the Commission found that the ability to offer connecting flights, as well as having access to feeder traffic, are important to route profitability and can therefore constitute a barrier to entry on the overlap routes. If demand on the route is insufficient, an air carrier that is unable to offer connecting flights or otherwise rely on feeder traffic will have difficulties to fill its aircraft and operate the route profitably.

Strength of the constraint from point-to-point rivals

On many of the domestic and short-haul routes investigated in *IAG/Air Europa* and *Lufthansa/MEF/ITA*, the only airlines competing with a direct connection with the parties are point-to-point carriers, such as Ryanair and EasyJet. Other network carriers would generally not be present unless their own airport hub is at one end of the relevant route.

Besides the fact that these point-to-point carriers often operate from more remote airports than the parties (e.g., Hahn Airport rather than Frankfurt Airport and Beauvais Airport rather than Orly or Charles de Gaulle Airport in Paris), which limits how closely point-to-point carriers compete for customers with a preference for flying from a main airport, the Commission found that the competitive constraint from these point-to-point carriers was limited on certain domestic and short-haul routes due to the network dimension of airline competition.

In particular, the parties themselves fly domestic and short-haul routes to/from their own airport hubs with higher frequencies than point-to-point rivals (often multiple times a day) as their operations are not only supported by point-to-point passengers flying directly on these routes themselves, but also by the significant share of connecting passengers, particularly those connecting to a long-haul flight at the parties' airport hub. Point-to-point carriers, on the other hand and by definition, rely entirely on passengers seeking to fly directly (without connecting to additional destinations) and therefore often cannot profitably match the parties' frequencies. The Commission therefore considered that the competitive constraint from point-to-point carriers on network carriers was limited on certain domestic and short-haul routes of the parties, particularly those that serve as important feeder routes for the parties' long-haul operations.

Assessing overlaps with one-stop connections

Operating a network of flights that interconnect at hubs means that network carriers can offer many connecting flights[3] in addition to direct flights. A significant proportion of long-haul passengers travel to their final destination via at least one connecting stop, for instance because prices are lower on the indirect connection[4] or because there is no direct flight available. Similarly, passengers on short-haul routes may decide to take an indirect connection, for instance due to more convenient flight times.

Therefore, the Commission assessed the effects of the transactions on competition not only on routes where both parties have a direct connection, but also on routes where only one of the parties has a direct connection whereas the other party has indirect connections only, as well as on routes where both parties have indirect connections only. The Commission's assessment of indirect connections focused on routes where the parties' hubs were located conveniently to offer an indirect flight with limited increases in flight times – such as on connections between the Iberian Peninsula and South America through Madrid in the *IAG/Air* Europa case or connections between Central Europe and Italy in the *Lufthansa/MEF/ITA* case.

In the *Lufthansa/MEF/ITA* investigation, the Commission identified competition concerns on several short-haul routes connecting small and medium-sized cities in Italy with cities in some of Lufthansa's core countries, specifically in Germany and Switzerland. The Commission found that these short-haul routes are primarily served by the Parties' own direct and convenient indirect connections whereas point-to-point carriers, such as Ryanair and EasyJet, do not serve them.

The Commission also assessed whether there could be competition concerns on indirect routes in the *IAG/Air Europa* investigation in light of the parties' overlapping airport hubs, and dense and wide networks allowing for convenient connecting flights, in Madrid.

Remedy design

The Commission also considered the network dimension of airline competition when assessing potential remedy options. In its assessment, the Commission had to take into consideration how carving out routes that are part of a network would affect the overall competitiveness, profitability, and viability of the divested business. For example, by separating short-haul and domestic routes from the long-haul routes which were operated in an integrated way, potential remedy takers would not benefit from the network effects resulting from the connections between the routes. This may mean that such a remedy would not represent a

[3] Passengers travelling via at least one connecting stop are also called 'indirect passengers'.

[4] In the recent airline investigations, the Commission found that passengers travelling on long-haul routes generally prefer direct over indirect connections. Therefore, airlines are often able to price direct connections at a premium compared to indirect connections.

viable divestment business or, in any event, one that is less competitive than it was in the hands of a network carrier.

In *Korean Air/Asiana*, pursuant to the commitments, only an airline with an existing hub-and-spoke network at Incheon Airport could have been approved as a potentially suitable remedy taker for the passenger remedies by the Commission. This criterion was meant to strengthen the remedies by ensuring that the remedy taker would be able to compete effectively with the merged entity on the remedy routes, considering the importance of having access to feeder traffic for the successful operation of long-haul routes.

In *IAG/Air Europa*, the Commission took into account the network dimension in its remedies assessment as both parties were network carriers operating a large number of overlapping routes from the same hub in Madrid. These considerations led the Commission to preliminarily conclude, including on the basis of a market test, that a combination of two remedy takers, one for the long-haul routes and one for the domestic and short-haul routes[5], would not be a sufficient solution.

Estimating the impact of lost competition

To evaluate the potential effects of the proposed transactions in *Korean Air/Asiana*, *IAG/Air Europa* and *Lufthansa/MEF/ITA*, the Commission conducted regression analyses examining the relationship between the number of competitors and price levels per route. This statistical approach provided valuable insights into how reduced competition might impact consumer prices. By quantifying the association between these two variables, the Commission was able to identify a clear general link between increased market concentration and higher prices, supporting the broader evidence gathered during the investigations.

For instance, that analysis carried out in *Lufthansa/MEF/ITA* supported empirically that ITA's presence on a route was associated with lower average Lufthansa prices. This provided additional support to the Commission's findings based on qualitative evidence that ITA and Lufthansa were close competitors on several routes. Interestingly, the Commission also discovered several internal documents from Lufthansa which showed that Lufthansa itself had estimated the impact of an increase in market concentration as a result of the transaction on prices and market participants' profit margins (including those of Lufthansa and ITA). These internal analyses by Lufthansa provided further confirmation for the results of the Commission's regression analysis by showing that Lufthansa itself was expecting price increases on several overlapping routes due to the increase in concentration resulting from the transaction.

[5] https://www.volotea.com/en/press-room/news/volotea-and-abra-group-avianca-and-gol-announce-joint-venture-agreement-to-strengthen-connectivity-between-europe-and-the-americas/.

Counterfactual assessment

Counterfactual assessments[6] can play an important role in the competitive assessment of aviation mergers. In order to assess the counterfactual arguments put forward by the parties in the recent aviation cases, the Commission relied on various evidence, including the results of its market investigation, IATA and EUROCONTROL reports, numerous economic submissions prepared by the external economic advisors of the parties, as well as the parties' internal documents. In this regard, internal documents proved to be a particularly useful source of evidence allowing the Commission to verify claims made by the parties in relation to their business strategies absent the merger. In line with its practice,[7] the Commission considered that internal documents prepared in the ordinary course of business (for example, before the proposed merger was agreed upon or without the knowledge of the preliminary competition concerns), would generally have higher probative value than the internal documents that could have been influenced by the Commission's review of the proposed merger.

The counterfactual plays a particularly important role in those cases where one of the merging companies is in a poor financial state.[8] This was a particularly relevant aspect of the Commission's investigation in *Korean Air/Asiana* due to the severe impact of the Covid19 pandemic on the parties' passenger operations, Russia's war of aggression on Ukraine as well as Asiana's ongoing financial difficulties.

In most cases the competitive conditions existing at the time of the merger constitute the relevant comparison for evaluating the effects of a merger. However, some cases may require a different benchmark. At the time of the *Korean Air/Asiana* investigation, the parties had not yet fully resumed their pre-Covid19 level of operations, including certain flights between Seoul and the EEA. In its assessment, the Commission disregarded the short-term effects of the Covid19 pandemic, and focused on possible structural changes in the market, such as, for example, a lasting entry or exit of competitors or structural shifts in competitiveness.[9] As the most recent IATA seasons of operation were heavily impacted by Covid19, the Commission assessed the market situation pre-Covid19 and used it as a proxy for the likely market positions of the parties and their competitors after the effects of the Covid19 pandemic would have subsided.

[6] A counterfactual assessment is a comparison of the competitive conditions that would result from the transaction with the conditions that would prevail absent the transaction. See Horizontal Merger Guidelines, paragraph 9.

[7] See Case M.7932 – Dow/DuPont, paragraph 46.

[8] See, for instance, M.9287 – Connect Airways/Flybe, paragraphs 242 et seq.

[9] The Commission adopted a similar approach in other aviation cases that were notified during the Covid19 pandemic. See, for example, M.9489 – Air Canada/Transat (abandoned), Commission's press releases of 25 May 2020 and 2 April 2021, and M.9637 – IAG/Air Europa (abandoned), Commission's press release of 29 June 2021.

Russia's war of aggression against Ukraine was another important element of the counterfactual in *Korean Air/Asiana* due to the closure of the trans-Siberian overflight space, which meant that flight times between Seoul and the EEA had increased. The Commission considered that the increased flight time for carriers that cannot or would not want to fly over Russia as well as the exit of Russian carriers from the relevant market were structural effects on the passenger market.

Finally, the Commission's market investigation did not show that Asiana was a failing firm or that, absent the transaction, Asiana would become significantly less competitive due to its financial state.

Remedies

The challenges of slot remedies

The fact that there is no obvious pre-existing business to divest presents a challenge for the design of effective remedies in airline cases. In addition, the ease of exit from specific routes increases the risk that even if entry is achieved, it might be short-lived and insufficient to address the competitive concerns on a lasting basis.

In past airline cases, the Commission accepted so-called 'slot remedies', in which the merged entity would make available to potential entrants – after closing of the merger and only upon request – take-off and landing slots at airports on routes where competitive concerns were identified. These remedies are meant to facilitate entry on the problematic routes. Slot remedies were accepted in a long list of cases.[10] However, slot remedies did not always prove successful. In some cases, slots were not taken and hence did not lead to entry on the routes. In some other cases, where entry did take place, the entrant was active only for a short period of time, either due to bankruptcy of the remedy taker or due to exit from the route.

This experience shows that often slots are not the only (or the main) barrier to entry and expansion.[11] Other barriers, such as the need for network and scale, lack of crews and aircraft, and the position of the merged entity on the route are sometimes more difficult to address through remedies. Building on this experience, the Commission sought to increase the likelihood that sustainable entry would occur when accepting remedies in aviation cases.

Increasing certainty of entry and shifting the risk

In *Korean Air/Asiana,* the Commission concluded that the commitments proposed by Korean Air remedied the competitive concerns arising from the transaction as they went beyond traditional slot remedies. The remedy taker is South Korean carrier T'way, an established airline with a hub in Seoul and a network of operations out of South Korea in East Asia and beyond. Korean Air committed to make available to T'way the necessary assets to start operating on the four problematic long-haul routes between South Korea (Seoul) and the EEA (Barcelona, Frankfurt, Paris and Rome). The assets made available by Korean Air include slots at Incheon Airport and at Barcelona, Frankfurt, Charles de Gaulle, and Rome Fiumicino airports, as well as traffic rights required to operate on these routes and trans-Siberian overflight rights.[12] Korean Air also committed to provide lease agreements for certain aircraft, access to crews and support for maintenance and overhaul services, for a transitional period.[13] T'way committed in an agreement with Korean Air to operate on the remedy routes for a certain minimum time. Korean Air undertook to enforce T'way's commitment.

Furthermore, Korean Air committed not to complete the merger until T'way has started operating on the four overlap routes. In this respect, these remedies go beyond traditional fix-it-first or upfront-buyer remedies, as Korean Air had to divest part of the remedy assets prior to implementing the merger. By doing so, the risk of no entry, which materialised in some past cases, was shifted from the public interest to the parties.

Unlike traditional slot remedies, which are open ended, the remedies in this case were structured around a remedy taker which had been identified by Korean Air upfront. This allowed the Commission, assisted by an independent advisor, to assess, prior to the clearance decision, the viability and suitability of the remedy taker and its business plan, as well as the sufficiency of the assets proposed by Korean Air to enable entry on the routes and thus increase the certainty that entry would be sufficient to address the competitive concerns identified.

In *Lufthansa/MEF/ITA*, the Commission was satisfied by the parties' proposal to provide slots and any other support necessary as required by the remedy taker (such as aircraft, crew, ground handling services, etc.) to ensure the entry of one or more remedy takers on the short-haul routes of concern, combined with the obligation for the parties to enter in some form of connectivity agreement with the remedy taker to address concerns on direct/indirect overlaps. Furthermore, the parties proposed to improve indirect connections on the problematic long-haul routes. For both sets of remedies, the parties undertook to ensure that the remedy taker operates for at least a certain minimum time on the routes of concern, and the closing of the transaction was made conditional on suitable remedy takers being found and approved by the Commission.

Conclusion

The three recent in-depth investigations in the airline sector demonstrate that the traditional O&D approach to assessing

[10] For example: M.3280 – Air France/KLM, M.3770 – Lufthansa/Swiss, M.5364 – Iberia/Vueling/Clickair, M.5440 – Lufthansa/Austrian Airlines, M.6447 IAG/bmi, M.6607 – US Airways/American Airlines, and M.7333 – Alitalia/Etihad.

[11] In some cases, where the relevant airport is not congested at any time of the day, slots may not be a barrier to entry and expansion at all.

[12] These rights could be used should flying over Russia become possible again.

[13] Additional commitments were offered to address the competitive concerns identified in relation to air transport of cargo, which is not covered in this brief.

horizontal overlaps does not always suffice to fully capture the competitive dynamics of this industry, particularly where the two merging parties are network carriers. Therefore, in these three recent investigations, the Commission has also considered the network dimension of airline competition which arises from the synergies between the domestic and short-haul operations, on the one hand, and the long-haul operations, on the other hand. The Commission used these insights to inform its assessment of barriers to entry and expansion, the strength of the constraint imposed by point-to-point rivals, overlaps with and between one-stop connections, and the remedy design.

The Commission's competitive assessment in these cases was supported by regression analyses which identified a clear general link between increased market concentration and higher prices, supporting the broader evidence gathered during the investigations.

Furthermore, the assessment of the appropriate counterfactual to the merger played an important role in the assessments. In *Korean Air/Asiana* in particular, the Commission undertook a detailed assessment illustrating how the Commission distinguishes between structural changes and temporary changes and how the Commission assesses situations where a merging company is in financial difficulties.

Finally, the Commission fed its experience with pure 'slot remedies' in airline mergers into the assessments and accepted commitments in both *Korean Air/Asiana* and *Lufthansa/MEF/ITA* that increase the certainty of entry on the routes of concern and shift the risk of non-entry from the public interest to the merging parties.

European Commission

Competition Merger Brief 4/2024 – Article 4

Competition *Merger Brief*

Oiling the Wheels of Competition: The Multi-Faceted Assessment of the Bunge-Viterra Deal

Marianne Auffret, Otmane Sbitri, Roxane Tonnelier

Introduction

On 1 August 2024, following a Phase I investigation, the Commission conditionally approved Bunge's USD 8.2 billion acquisition of Viterra (the 'Transaction').

Both Bunge and Viterra (the 'Parties') are global agribusinesses which activities relate to every step of the agricultural value chain, from the upstream growing of crops to the downstream supply of food products and other consumer goods to end-customers. This Transaction may be a first serious attempt at consolidating the agribusiness sector, impacting in particular the **oilseed markets in Europe**.

Oilseeds are crops with high fat content and are essentially of three species: rapeseed, soybean, and sunflower seed. These crops are processed to extract crude oil from the seed, while the residual meal is used to produce livestock feed. Crude oil is subsequently refined into edible oil for human consumption or biodiesel to fuel engines. Edible oil can be processed further into solid fats, such as margarine.

An hourglass-shaped market

Upstream farmers and downstream consumers are counted in the thousands. However, a very concentrated group of traders and processors operate between those two fragmented levels. This tight group is led by the so-called 'ABCDs' (for ADM, Bunge, Cargill, and Dreyfus), but also includes other large international players such as Glencore, the mother company of Viterra Pre-Transaction.

The Parties and their competitors generate profits by buying agricultural products - such as oilseeds - and reselling them, as such or in a processed format, at a higher price. They rely on a variety of assets on a global basis for transport, storage, and processing to take advantage of price differentials between (i) geographic areas, (ii) seasons, and (iii) between crops and processed products.

The Commission had serious doubts that the Transaction would have reduced competition in the rapeseed and sunflower seed value chains in Central Europe.

In this brief, we focus on some of the salient features of this case, notably the Commission's assessment of the Parties' buyer power vis-à-vis farmers and its approach to quantifying market power and remedying competition concerns in value chain markets.

In a nutshell

The Commission conditionally approved Bunge's acquisition of Viterra. The merger posed competition concerns in the oilseed value chains in Central and Eastern Europe. A holistic approach was used to assess the Parties' market power in this hourglass-shaped industry, including capacity shares, trading shares, supply shares, and qualitative data.

A remedy was accepted, involving the divestment of Viterra's businesses across the value chain in Hungary and Poland. This highlights the importance of protecting the value chain in critical industries, such as agriculture, where market power concentration can have significant impacts on consumers and producers alike.

Farmers vs. Traders: how the ABCDs influence European agriculture

Global agricultural trading – and the resulting pricing of crops – directly affects the livelihood of European farmers.

Farmers typically focus on growing crops and have very limited ability to store and distribute their production after harvest. To reach the market, they typically hand over their production to *originators* that are third parties – such as the ABCDs and other smaller intermediaries – collecting crops from individual farmers and preparing them for marketing (i.e., ensuring crops cleaning, quality checks, subdivision in uniform batches, etc) and further processing.

The Commission's investigation showed that - whether buying directly from farmers or other intermediaries - Bunge and Viterra typically exert **market power on the purchasing side** of the

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oilseed markets towards farmers. This is because they have the scale to purchase high volumes and have access to wide infrastructure networks which allow them to transport these volumes from the warehouse to a faraway destination on railways and waterways. In such a setting, even if farmers do not directly sell their crops to the Parties, they are still affected by their commercial strategies and pricing policies.

Market power: Seen Through a Multi-Proxy Lens

The Commission's investigation underscored the challenges of quantifying market power in the oilseed industry. The merger of Bunge and Viterra, two vertically integrated companies operating throughout the oilseed value chain, posed specific challenges due to the fact that the Parties' market shares, based solely on their sales to third parties, did not account for their internal consumption for further processing. Thereby such market shares did not present a reliable picture of the merged entity's market power in an industry where value is extracted at the end of the chain.

To gain a comprehensive understanding of the market structure and competitive dynamics, the Commission employed a multi-faceted approach combining different metrics and proxies. This involved assessing the Parties' market power through capacity shares, which capture the market structure at a level of production where barriers to entry are the highest, providing valuable insights into the Parties' and competitors' production capabilities and influence on market outcomes.

In addition to capacity shares, the Commission used a trading share proxy to measure the Parties' trading power, which reflected their ability to control volumes (whether sold to third parties or controlled internally) in the market. A supply share proxy was additionally relied on to measure the volumes the Parties bring into (i.e., produce or import) a market. To assess their market power on the demand side, the Commission also used a different metric based on the total volume purchased. The latter offered, for instance, a more comprehensive understanding of their market power towards farmers upstream.

The use of alternative methods and data sources, such as capacity shares, market power proxies, and qualitative data, highlights the complexity of measuring market power in the oilseed markets. The Commission's approach demonstrates the importance of considering various metrics and data sources to gain a deeper understanding of market dynamics and assess market power accurately. By employing a comprehensive and nuanced methodology, the Commission was able to gain a more accurate understanding of the market structure and competitive dynamics in the oilseed industry.

Defying (Market) Gravity: Balancing Market Power with a Value Chain Remedy

Increased gravitational pull in key oilseed regions

In the case of vertically integrated players, market power is often exerted throughout the value chain, but most of the value is extracted at the end of the chain, typically at the refining or processing stage. In such cases, market power must be assessed holistically throughout the value chain, taking into account the interdependence between the different levels of the production process.

This is particularly true in the oilseed industry, where the value of the final product is significantly higher than the value of the intermediate products. Vertically integrated players like the Parties, which are active at multiple stages of the production process and are among the few big processors, exert a "gravitational pull" affecting the entire value chain: their market power at the key value-adding stage of the process both feeds into and derives from their market and buyer power upstream.

As a result, the Commission's investigation revealed that the acquisition of Viterra by Bunge would have increased market power both vis-à-vis farmers upstream and customers downstream throughout the entire rapeseed and sunflower seed value chains where they were both already strong players, i.e., in Poland and Hungary. The Transaction as notified would therefore have negatively impacted competition throughout the value chain in those areas, which are key regions for growing oilseeds and therefore the manufacturing of oilseed-based products in Europe.

A full spectrum fix to remedy full chain issues

To address issues arising in such markets, the Commission typically only accepts remedies which allow for the reproduction of a similar integration level across the value chain. This approach is also necessary to maintain the viability of the remedy in markets where capabilities at all levels of the chain are key to be competitive.

In this case, the Commission's clearance was conditional upon the divestment of Viterra's entire businesses across the value chain in the problematic areas. This includes Viterra's origination, processing and refining assets and personnel in Hungary and Poland. The remedy removed the entire horizontal and vertical overlap between the Parties in key geographic areas for the EU oilseed industries and ensured that the remedy taker would be able to efficiently compete with the merged entity at all levels of the value chain.

Conclusion

In many basic industries, market power analysis must consider the entire value chain, taking into account the interdependence of the different stages of the production process and the asset-based "gravitational pull" of vertically integrated players. The Bunge-Viterra merger highlights the importance of protecting the value chain in critical industries, such as agriculture, where market power concentration can have significant impacts on consumers and producers alike.