What the current antitrust and merger rules and what they don’t

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Green innovation and mergers

It is a great pleasure to take part in this conference.

When I was preparing for this panel, I realized that I had almost forgotten that back in 1995 and 1996 I had worked on tradeable permits, including as an intern at DG3 (Industry). At the time this was ground-breaking work from an institution, and it was putting academic work into practice.

Twenty-five years later, European citizens continue to put the **environment** at the **top of their values**. And the European Commission continues to be an ambitious institution at the world’s scale. So congratulations for that.

It has been said earlier in the conference that competition law is not the primary instrument to achieve green objectives.

But not being the lead actor in the green script does not mean competition does not have a role to play.

The discussion must then seek to strike some balance between ensuring efficiency and fair deals for consumers in the future, while seeking to become a climate-neutral economy.

Such a balance is being devised taking into account three aspects discussed throughout the conference today: state aid, which is in my view the preferred vector for a strong contribution to the Green Deal objectives, horizontal agreements which we will tackle later, and merger review.

Our goal here today is of course to promote an open and constructive debate.

I would start by saying that we should **demystify** views that place competition policy as an obstacle - or as adversarial- to sustainability.

In many respects, this is **quite the opposite**.

Competition and innovation are generally **positively correlated**. They tend to go hand in hand. This is true also for competition and **green** innovation.

Competition is one of the key drivers of the **incentives** for firms to innovate.

It is contestability that induces innovation.

Historically, innovation has led to significant productivity and welfare increases. **And** to sustainability increases. Why?

Because firms want to develop **more efficient** production processes. This gives them competitive advantage over rivals.

More efficient production processes often mean that an important part of process innovation is **green innovation**. Think of the cases where firms focus on spending less energy, on reducing and reusing waste, on using renewable or more durable inputs.

So the **first point** is that strong competition creates incentives to reduce costs through innovation.

A **second point** I want to make is that strong **consumer demand** for green products is also a strong incentive for firms to be more sustainable in their production processes, and in the products and services they offer.

In fact, consumer demand is extremely powerful in driving change. And consumers are valuing sustainability more than ever. Either because they see sustainability as a good in itself or because they value sustainability features imbedded in products. Examples include fuel-efficiency in cars, energy efficiency in household appliances or the convenience of online services.

Consumers' **willingness to pay for green** is therefore an extremely powerful incentive for green innovation.

Keeping competition conditions strong is therefore a strong contribution of competition policy for the Green Deal.

So, how do enforcers do this in practice?

Let us look at **the role of innovation in competition assessments**.

As an example: innovation and R&D took centre stage in the Commission's assessment in the **Dow/DuPont merger**, in 2017. In this case, and in subsequent cases, most notably **Bayer/Monsanto**, the Commission found significant product and pipeline overlaps, as well as innovation capability overlaps.

In order to **preserve incentives for innovation**, the clearance of these mergers required significant divestiture commitments by the merging parties involving their R&D capabilities.

In the Bayer/Monsanto merger, the analysis of the Commission considered whether the merger would hamper *innovation competition* for crop protection and seed industries. This included the development of more environment-friendly products.

It was considered that consumers could be harmed:

(1) in the short run, by the loss of product quality and variety, and

(2) in the long run, by a significant loss of innovation, given the incentives of the merging parties to delay, redirect and discontinue innovation efforts after the merger.

This debate has prompted recent literature[1], highlighting **the role of competition in promoting innovation**.

These have been breakthroughs for competition enforcement that we should count as a very important **contribution** for sustainability and green innovation.

Another message drawn by competition authorities is that they need to be vigilant of attempts by incumbents to protect their market power through the acquisition of disruptive entrants.

[1] E.g., Federico, Giulio, Gregor Langus, and Tommaso Valletti (2018). "Horizontal mergers and product innovation." *International Journal of Industrial Organization* 61: 590-612 and Federico, Giulio, Fiona Scott Morton, and Carl Shapiro (2020). "Antitrust and innovation: Welcoming and protecting disruption." *Innovation Policy and the Economy* 20.1: 125-190.

If incumbents who are lagging in terms of green innovation adopt a killer strategy so as to prevent or delay the introduction of green innovation to the market, they may under certain circumstances[2] be halted by competition enforcers.

So, to finalize, this in my view is one of the best contributions of competition policy to the Green Deal. Because merger review can keep innovation alive.

Cooperation agreements and antitrust

The **first point** is that enforcers acknowledge that firms wish to operate in a predictable and certain environment from a legal standpoint. And in fact, enforcers strive to provide as much clarity as possible.

The **second** point is that the current debate on competition and sustainability has revived and acknowledged the flexibility provided by European law. The law indeed allows for some agreements to take place.

It occurs to me that we may need to **effectively communicate the leeway** that already exists in our competition framework regarding sustainability initiatives. Not just to firms, but to other stakeholders, including consumers and society at large. So that the debate is not skewed against competition law.

So, **openness and guidance to stakeholders** may be key to avoid businesses shying away from sustainability initiatives. But also to avoid giving the wrong impression to consumers, that competition law is not open to agreements between firms. It is open, under certain circumstances. Accepted agreements may include standardised packaging, waste production and waste management; or standardised certification and labelling.

When some of the conditions in agreements are not in line with the principles set in the regulations and in the guidelines, then these are cases that likely deserve further scrutiny.

Let us not forget that the primary responsibility, as competition enforcers, is to ensure that sustainability agreements are not used to hurt competition dynamics nor consumers. Applying article 101 is a mission that needs to be carried out and we only have enforcers to do that.

And the risk of cartels hidden behind sustainability claims is real. It happened before with detergents, in a parallel agreement among some players; or more recently, there is a statement of objections on car makers because of possible restrictions to competition on emission cleaning technology. Furthermore, through such agreements, we risk having firms disclosing a significant volume of **strategic information** to each other. And commitments for sustainability may be used as focal points for coordination. We also know empirically that cartels are more likely to be formed when economic conditions vary in a way such that markets become more predictable.

A final point from me, and because we need to take all circumstances into consideration: our economic recovery will need competition rules to remain strong, not to be mild and lenient, in the coming times. The internal market needs to remain open and innovative, particularly under current circumstances.

Given the need to maximize the potential of what could be a difficult recovery, this is not the time to weaken competition policy. The European competition framework has an in-built flexibility that allows for certain horizontal agreements, the "right ones", to take place.

Efficiencies

[2] This is reviewed under merger analysis: by protecting their business through **green killer acquisitions**, incumbents are seeking to eliminate competition, at the cost of less quality, lower variety and higher prices.

My general view is that **existing** tools **provide the opportunity to bring sustainability concerns** into the competition analysis.

Sustainability may be, in itself, valuable to both consumers and to society in general. In that case, it is **a dimension of competition** and, as such, environmental positive effects may be treated as efficiencies and environmental negative effects treated as harmful.

This applies equally to mergers and to agreements between firms that may be restrictive of competition, but be offset by net benefits.

A couple of examples include:

(1) The two-decade old **CECED[3] case**, which involved an agreement on phasing out inefficient washing machines, is a paradigmatic example. At a first stage, the horizontal agreement was exempted under what is now Article 101(3) because the washing machines were more energy-efficient. Even though the cost of production and the price of washing machines would have increased, consumers could expect to recoup the additional cost in their electricity bill.
(2) Likewise, in the Aurubis/Metallo merger last year, there were important sustainability considerations. The Commission was concerned whether competition in the copper recycling sector would be reduced and, after an in-depth assessment, found that harm was unlikely to occur. When the merger was cleared, this concern was framed in the context of the European Green Deal, given the role of copper in the circular economy.

So, we must not underestimate the strength of the tools we already have. Such tools can accommodate sustainability concerns.

However, environmental concerns may involve significant negative externalities. This means **green efficiencies typically occur out of the market**. And competition assessments usually narrow down efficiencies to relevant markets and related markets.

This raises **questions** for competition authorities.

Should we allow restrictions to competition that harm consumers, but are offset by social gains out of the market?

In other words, where consumers lose, but society is still better off?

And what is the scope of the "society"? Its national borders? The EU? The world?

We would all want the first-best solution, where someone would ponder all benefits and harm, with perfect information, and then optimize the trade- offs. But a first-best world is a theoretical construction.

A proxy for this may be what exists in several member states: governments have the possibility to weigh all the positives and negatives and allow some mergers in the public interest. In doing this, they are nevertheless required to minimize negative effects for competition and consumers.

But let's go back to our discussion. What happens if we, enforcers, are required to push the boundaries of what is currently state-of-the-art in terms of markets and efficiencies?

Then, we would no longer be dealing with market definition as per the established practice. And evaluating out-of-market efficiencies would raise significant methodological issues.

Such new concepts would, at least for a while, create significant legal **uncertainty** for firms.

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[3] CECED - *Conseil Européen de la Construction d'Appareils Domestiques.*

At the same time, competition authorities would be faced with so-called **"administrability" challenges in enforcement**. Enforcers, like firms, act best when a clear set of rules and guidelines exist. By "act best" I mean with accuracy and predictability. This, in turn, translates into more certainty for firms.

So to sum up, such a methodological revolution on competition policy enforcement could risk backfiring, and promote neither sustainability nor competition. This may well be a case where **out of market efficiencies are better addressed by regulation**, rather than by competition policy.