

Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006

Question: bet 38 (ACCC)

Topic: Merger of the ASX and Sydney Futures Exchange

Hansard Page: Written

Senator CONROY asked:

- (1) Since taking over as Chairman can you indicate how many mergers the Commission has been responsible for stopping all together. In other words, have all mergers considered by the ACCC been allowed to proceed in one form or another?
- (2) In relation to the ASX and FSE merger you indicate in your media release that these are two separate monopolies, but that this doesn't present a problem under s 50. If this is the case then should we be concerned that one much bigger monopoly is being created and s 50 is powerless to stop it, particularly as your media release confirms that these separate monopolies now earn "earn very high returns on capital, well above what is generally found in competitive markets?
- (3) If s 50 is allowing one big monopoly to be created would it be fair to say that s 50 is weak and ineffective in dealing with such issues as creeping acquisitions?
- (4) If s 50 is unable to stop monopolies from being created, then how can s 50 or the Commission stop the growing concentration of Australian industry or the possible concentration of the media industry if the cross media rules were repealed?
- (5) Is the Commission concerned about the growing concentration of Australian industry or does the Commission feel that is sufficient from a competition point of view to simply have a duopoly in an industry?
- (6) While we can appreciate that the analysis of mergers may involve complex issues, would it be fair to say that the Commission's key question in a proposed merger is whether the merged entity can exert market power post merger, that is, the ability to raise prices without losing business?
- (7) Would it be fair to say that so long as there was some competition left in a market or there was possibility of some competition emerging in a market, the Commission would be powerless to stop the merger under s 50?
- (8) In considering the potential competitors to a merged entity does the Commission look at comparable competitors, that is, a competitor having

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006

comparable size and strength to the merged entity? For example, if the removal of the cross media rules led to a TV network and a major newspaper seeking to merge, then would a blog on the internet having very few daily hits be a comparable competitor

Answer:

- (1) **Since taking over as Chairman can you indicate how many mergers the Commission has been responsible for stopping all together. In other words, have all mergers considered by the ACCC been allowed to proceed in one form or another?**

Answer to Q.1

Since 1 July 2003, the ACCC has opposed 7 merger or acquisition proposals on a public basis.

In addition, the ACCC also considers requests for qualified clearance of mergers on a confidential basis. In some of these concerns/opposition has also been expressed (around 6 in the last two years).

- (2) **In relation to the ASX and SFE merger you indicate in your media release that these are two separate monopolies, but that this doesn't present a problem under s 50. If this is the case then should we be concerned that one much bigger monopoly is being created and s 50 is powerless to stop it, particularly as your media release confirms that these separate monopolies now earn "earn very high returns on capital, well above what is generally found in competitive markets?**

Answer to Q.2

Section 50 of the Trade Practices Act prevents mergers and acquisitions that are likely to substantially lessen competition in a substantial market. Since the ACCC found that the two exchanges were in separate markets, there was no lessening of competition in either market and therefore no breach of section 50. Effectively, the ACCC concluded that the merged exchange would have no more ability to exercise market power (and thereby maintain or increase its returns on equity) than the two separate exchanges.

- (3) **If s 50 is allowing one big monopoly to be created would it be fair to say that s 50 is weak and ineffective in dealing with such issues as creeping acquisitions?**

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006

Answer to Q.3

The ACCC found that a merger between the ASX and SFE was a merger between two separate monopolies in separate markets and, as such, did not contravene section 50. The ability of section 50 to deal with creeping acquisitions was not relevant to the ACCC's consideration of the proposed merger between ASX and SFE.

- (4) **If s 50 is unable to stop monopolies from being created, then how can s 50 or the Commission stop the growing concentration of Australian industry or the possible concentration of the media industry if the cross media rules were repealed?**

Answer to Q.4

It is important to note that a monopoly was not created in the ASX/SFE matter, as both existed as monopolies in their different markets prior to the merger. Section 50 prohibits all mergers and acquisitions (whether they would result in a monopoly or not) that would be likely to result in a substantial lessening of competition in a market. Section 50 applies to all Australian industries, including the media.

- (5) **Is the Commission concerned about the growing concentration of Australian industry or does the Commission feel that is sufficient from a competition point of view to simply have a duopoly in an industry?**
- (6) **While we can appreciate that the analysis of mergers may involve complex issues, would it be fair to say that the Commission's key question in a proposed merger is whether the merged entity can exert market power post merger, that is, the ability to raise prices without losing business?**
- (7) **Would it be fair to say that so long as there was some competition left in a market or there was possibility of some competition emerging in a market, the Commission would be powerless to stop the merger under s 50?**
- (8) **In considering the potential competitors to a merged entity does the Commission look at comparable competitors, that is, a competitor having comparable size and strength to the merged entity? For example, if the removal of the cross media rules led to a TV network and a major newspaper seeking to merge, then would a blog on the internet having very few daily hits be a comparable competitor**

Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006

Answer to Questions 5, 6, 7 and 8

The Commission's role is to administer the Trade Practices Act 1974, including section 50, which prohibits mergers and acquisitions which would be likely to substantially lessen competition in a substantial market. Section 50 requires the following matters to be taken into account when determining whether a merger or acquisition would be likely to substantially lessen competition:

- the actual and potential level of import competition in the market;
- the height of barriers to entry to the market;
- the level of concentration in the market;
- the degree of countervailing power in the market;
- the likelihood that the acquisition would result in the acquirer being able to significantly and sustainably increase prices or profit margins;
- the extent to which substitutes are available in the market or are likely to be available in the market;
- the dynamic characteristics of the market, including growth, innovation and product differentiation;
- the likelihood that the acquisition would result in the removal from the market of a vigorous and effective competitor; and
- the nature and extent of vertical integration in the market.

The key focus of the assessment of any merger is whether the merged business would be likely to possess greater market power than the individual merger parties would possess if the merger did not proceed. In particular, the ACCC compares the level of market power that the merged business would be likely to possess if the merger proceeds with the level of market power each merger party would be likely to possess if the merger did not proceed. If the merged business would have significantly more market power than the merger parties if the merger did not proceed, then the merger would be likely to raise competition concerns.

Generally, market power exists where a merged business would be able to impose a sustained small but significant price rise on its customers (or an equivalent lowering of quality).

A merged business may have significantly more market power than the individual merger parties if these parties are significant competitive constraints on each other, and if no other significant constraints existed (for example, other significant competitors, imports or likely new entrants to the market).

Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006

Whether a merger or acquisition would leave only two players in a market would clearly be relevant to the assessment of a proposed merger. Even if more competitors remained, an analysis of the market share of these competitors would be relevant to the assessment of the proposed merger. In particular, both issues relate to the level of market concentration post-merger. However, all the merger factors listed above need to be considered before a conclusion can be formed on whether a merger or acquisition would be likely to breach section 50. Market concentration is only one of the factors the ACCC has regard to in a merger review.

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates 30 May – 1 June 2006



Australian
Competition &
Consumer
Commission

NewsRelease

ACCC not to oppose merger between Australian Stock Exchange and Sydney Futures Exchange

The Australian Competition and Consumer Commission will not oppose the merger between the Australian Stock Exchange and the Sydney Futures Exchange, ACCC Chairman, Mr Graeme Samuel, said today.

"The ACCC considers the proposed acquisition is unlikely to substantially lessen competition given the strong evidence that the ASX and SFE are separate monopolies, and to a large extent do not compete already, nor are they likely to substantially compete in the future", Mr Samuel said.

"The ACCC received no persuasive evidence that the current lack of competition between the ASX and SFE was likely to change in the foreseeable future", Mr Samuel said. "Further, both local and overseas experience suggests that it is very difficult for exchanges to attract trade in financial products away from other exchanges".

The ACCC noted both parties earn very high returns on capital, well above what is generally found in competitive markets.

Market inquiries raised some concerns about access to the ASX's clearing and settlement facility, CHES, for clearing equities. However, given that the SFE's clearing and settlement system is unable to clear equities, it was apparent that the merger is not the cause of the concerns about access.

"For us to oppose the merger, we are required to substantiate a lessening of competition that results from the merger itself", Mr Samuel said. "Concerns about access to CHES are more appropriately addressed in other ways".

Similarly, market inquiries raised some concerns about recent increases in ASX and SFE fees. These increases were unrelated to the merger and further illustrate the lack of competitive constraint between the ASX and SFE.

Market inquiries also raised some concerns that the merger will reduce product innovation. However, the ACCC concluded that product innovation is driven primarily by market participants devising products to meet client needs. These products are not necessarily traded on exchanges, nor is there any significant evidence of innovation being driven from competition between the ASX and SFE.

"The ACCC opposed a merger between ASX and SFE in 1999. At that time, it believed that the ASX and SFE were likely to compete in the future, particularly given proposed legislative changes that were expected to facilitate competition. However, there is no evidence that these changes, which commenced in 2002, have actually had this effect", Mr Samuel said.

The Australian Stock Exchange operates a national stock exchange for equities, derivatives and fixed interest securities. Sydney Futures Exchange provides futures and options on interest rates, equities, currencies and commodities.

The ACCC will issue a Public Competition Assessment on its website explaining in detail the reasons for its decision in relation to this matter shortly.