Comments to “Anti-Competitive Effects of Common Ownership” by Azar, Schmalz, and Tecu

Mauricio Larrain
Columbia University
General impression

• Fascinating paper, relevant topic
Airlines Under Justice Dept. Investigation Over Possible Collusion

By CHRISTOPHER DREW  JULY 1, 2015

Federal prosecutors on Wednesday said they had begun an investigation into possible collusion among the airlines to limit seating, two years after the Justice Department approved the latest in a wave of airline mergers, saying the combination would benefit consumers.

In letters sent to airlines, prosecutors have asked for documents from the last two years related to statements and decisions they have made about limiting capacity on flight routes. By making it harder for passengers to find seats, airlines could restrain competition and increase fares.
General impression

- Fascinating paper, relevant topic
- Novel idea
QUANTIFYING THE COMPETITIVE EFFECTS
OF PRODUCTION JOINT VENTURES

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Final version received August 1985

A joint venture among competitors to produce output alters the parents’ competitive incentives. Any joint venture involves both joint financial interest and control over the production levels of the venture entity and the parent firms. The competitive incentives of the parents and rival firms depend on the exact financial interest and control arrangements made. This paper analyzes a number of alternative arrangements within the standard non-cooperative oligopoly model and devises a Modified Herfindahl–Hirshman Index (MHHI) to quantify their relative competitive incentives. Independent entry by a single parent and a full merger of the parents may be viewed as particular financial interest and control arrangements. The use of this methodology for policy analysis of proposed ventures is illustrated with the facts of the recent GM–Toyota joint venture.
Increase Importance Passive Investors

"% of equity mutual fund assets that are passively managed"

Figure from Appel, Gormley, Keim (forthcoming)
Investment management

The rise of BlackRock

In 25 years, BlackRock has become the world's biggest investor. Is its dominance a problem?

Dec 7th 2013 | From the print edition
General impression

- Fascinating paper, relevant topic
- Novel idea
- Policy “trilemma” interesting
- Holds in other industries
Ultimate Ownership and Bank Competition

José Azar, Sahil Raina, and Martin Schmalz*

PRELIMINARY. COMMENTS WELCOME.

Abstract

We document a secular increase of deposit account maintenance fees and fee thresholds with a new branch-level dataset, as well as substantial cross-sectional variation in these prices and in deposit rate spreads. We then examine whether variation in bank concentration helps explain the variation in prices. The standard measure of concentration, the HHI, is not correlated with any of the outcome variables. A generalized HHI (GHHI) that captures both common ownership (the degree to which banks are commonly owned by the same investors) and cross-ownership (the extent to which banks own shares in each other) is strongly correlated with higher maintenance fees, fee thresholds, and deposit rate spreads. We use the growth of index funds as a source of variation to suggest a causal link from GHIII to higher prices for banking products.
General impression

- Fascinating paper, relevant topic
- Novel idea
- Policy “trilemma” interesting
- Holds in other industries
- Important implications
High Exposure

Arizona State University, UC Berkeley (Econ), Boston College, Charles River Associates, University of Cologne, Columbia GSB, Düsseldorf Institute of Competition Economics, Federal Reserve Bank of New York, Federal Reserve Board of Governors, Goethe Universität Frankfurt, Harvard University (Economics / HBS Finance), Humboldt Universität Berlin, IESE, INSEAD, Lancaster University, McGill Desautels, Stockholm HHS, Toulouse School of Economics, Tilburg University, United States Department of Justice, UNC Chapel Hill, Universität Bonn, Universität Mannheim (finance), Universität Mannheim (economics), Universiteit van Amsterdam, University of Chicago (Booth applied economics), University of Michigan (finance; business economics/industrial organization; Center for Finance, Law, and Public Policy), Western University, Yale School of Management, EARIE 2015 (Munich), Econometric Society World Congress (Montreal), and conference audiences at European Finance Association Meetings (Vienna), FTC Microeconomics Conference, IFN Workshop on The Economics of Corporate Ownership (Stockholm), International Industrial Organization Conference (Boston), London Business School Summer Symposium on Corporate Finance and Corporate Governance, LSE Adam Smith Workshop, LSE Economic Networks and Finance Conference, 2015 NBER Corporate Finance (Chicago), 2015 NBER SI Law and Economics (Cambridge), Northwestern Law Searle Antitrust Conference, Tel Aviv University Finance Conference, Texas Finance Festival, and the Utah Winter Finance Conference
DuPont Defeats Peltz, Trian in Board Fight

Outcome represents landmark setback to investment firm, activism movement

By JACOB BUNGE And DAVID BENOIT
May 13, 2015

DuPont Co. defeated the campaign by Nelson Peltz and his Trian Fund Management L.P. to land seats on the chemical giant’s board, dealing a landmark setback to one of the most influential activist investment firms.
DuPont and Monsanto

Highly concentrated seed market

Other companies 24.7
Monsanto 26
Pioneer 18.2
Syngenta 9.2
Vilmorin 4.8
WinField 3.9
KWS 3.6
Dow AgroSciences 3.1
Bayer 3.3
Sakata 1.6
Takii 1.6

Source: ETC Group (2013)
## Common Ownership

<table>
<thead>
<tr>
<th>Dupont (DD)</th>
<th>%</th>
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<tbody>
<tr>
<td>The Vanguard Group, Inc.</td>
<td>5.5</td>
</tr>
<tr>
<td>BlackRock Fund Advisors</td>
<td>5.0</td>
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<tr>
<td>State Street global Advisors</td>
<td>4.9</td>
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<tr>
<td>Capital Research &amp; Management Co.</td>
<td>4.0</td>
</tr>
<tr>
<td><strong>Trian Fund Management LP</strong></td>
<td><strong>2.7</strong></td>
</tr>
<tr>
<td>Fidelity Management &amp; Research Co.</td>
<td>2.5</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Monsanto (MON)</th>
<th>%</th>
</tr>
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<tbody>
<tr>
<td>The Vanguard Group, Inc.</td>
<td>6.4</td>
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<tr>
<td>BlackRock</td>
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<td>Fidelity Management &amp; Research Co.</td>
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<tr>
<td>State Street global Advisors</td>
<td>4.6</td>
</tr>
<tr>
<td>Capital Research &amp; Management Co.</td>
<td>3.3</td>
</tr>
<tr>
<td>Sands Capital Management LLC</td>
<td>2.7</td>
</tr>
</tbody>
</table>
Comment #1: Endogeneity

- Outcome variable is price:

$$\log(p_{ijt}) = \beta \cdot \text{MHHI delta}_it + \gamma \cdot HHI_{it} + \theta \cdot X_{ijt} + \alpha_t + \nu_{ij} + \varepsilon_{ijt}$$

- Explanatory variable also depends on price:

$$s = f(p)$$

$$\text{MHHI delta} = \sum_j \sum_{k \neq j} s_j s_k \frac{\sum_i \gamma_{ij} \beta_{ik}}{\sum_i \gamma_{ij} \beta_{ij}}$$

- Regressing prices over function of prices with over a million observations...
Comment #1: Endogeneity

- Instrument market shares with lagged shares?

- Use model-free specification (i.e., equal weights)

\[
\text{MHHI delta}' = \frac{\sum_i \gamma_{ij} \beta_{ik}}{\sum_i \gamma_{ij} \beta_{ij}}
\]

- Paper concerned with endogeneity ownership shares, not with endogeneity of market shares

\[
\text{MHHI delta} = \sum_j \sum_{k \neq j} s_j s_k \sum_i \gamma_{ij} \beta_{ik} \sum_i \gamma_{ij} \beta_{ij}
\]
Comment #2: Magnitude of Effects

- MHHI delta is > 2,000 points

- DOJ: if HHI +200 points after merger -> presumed likely to enhance market power

- MHHI delta is more than 10 times than threshold

- Framework interpret magnitude

- Compare with the banking industry paper
Comment #3: BlackRock-BGI Event

- BlackRock announces to acquire BGI on June 2009
- Consummation of acquisition in December 2009
- Other important things happening at that time
United Airlines and Continental Airlines agreed Sunday to a $3 billion merger that would create the world’s biggest airline, according to people briefed on the negotiations.

The deal, to be announced officially on Monday, would form a coast-to-coast behemoth with a leading presence in the top domestic markets, including New York, Chicago and Los Angeles, along with an extended network to Asia, Latin America and Europe. The deal was completed in a remarkably swift three weeks, and would give the airlines the muscle to fend off low-cost rivals at home and to take on foreign carriers abroad.
Comment #3: BlackRock-BGI Event

- BGI had a large stake in United relative to other airlines

- Could United-Continental merger be driving some of the results?
Comment #4: Markups

• Theory of MHHI is about markups:

\[
\sum_j s_j \left( \frac{P - C'_j(x_j)}{P} \right) = \frac{1}{\eta} \left[ \sum_j \sum_k s_j s_k \frac{\sum_i \gamma_{ij} \beta_{ik}}{\sum_i \gamma_{ij} \beta_{ij}} \right]
\]

• Paper looks at prices

• What about markups?
Oil dives below $35, lowest in 11 years, as U.S. supply swells

NEW YORK | BY CATHERINE NGAI

Crude oil prices plunged 6 percent on Wednesday, diving below $35 per barrel for the first time since 2004 as data showing a shockingly large build-up of U.S. gasoline supplies fed fears that a global surplus was still growing.
Fury of travellers as oil price plunges but cost of flights stays sky-high

The global cost of fuel has dropped to a 12-year low, but the savings being made by airlines isn’t being passed on to passengers.

Greedy airlines are charging passengers hundreds of pounds in fuel surcharges even though oil prices have plunged to a 12-year low.

A barrel of Brent crude oil – which dictates the cost of aviation fuel – has fallen from almost $100 to below $30 in the past year.

Yet airlines have not passed on the savings by lowering fares, sparking claims they are misusing surcharges to inflate ticket prices.
Comment #5: Mechanism

- Paper shows incentives and outcomes

- From legal view, mechanism might not matter much. In economics, we care about mechanism

- Do more to disentangle mechanisms
  1. Funds tell portfolio firms not to compete
  2. CEOs are paid not to compete
  3. Funds vote against pro-competition measures
Comment #6: Implications

1. Enforcing existing antitrust law

2. Optimal corporate governance

3. Macro consequences
Raising Corporate Profits
I caught a bit of CNBC in the locker room this morning, and they were talking about stock buybacks. Oddly — or maybe not that oddly, given my own experiences with the show — nobody brought up what I would have thought was the obvious question. Profits are very high, so why are companies concluding that they should return cash to stockholders rather than use it to expand their businesses?

After all, we normally think of high profits as a signal: a profitable business is one people should be trying to get into. But right now we see a combination of high profits and sluggish investment:
Labor Share of Income

Labor Share in the Nonfarm Business Sector

1947-2000 average

2014:Q1
Larrain and Mian (2016)

\[ \Delta \text{Concentration top4} \]
\[ p_{gap} = -0.01 - 0.05 \text{ top4} \quad R^2 = 8.6\% \]
\[ n = 151 \quad \text{RMSE} = 3.015713 \]

\[ \Delta \text{Concentration top8} \]
\[ p_{gap} = 0.10 - 0.06 \text{ top8} \quad R^2 = 9.9\% \]
\[ n = 151 \quad \text{RMSE} = 2.994144 \]

\[ \Delta \text{Concentration top20} \]
\[ p_{gap} = 0.23 - 0.07 \text{ top20} \quad R^2 = 12.2\% \]
\[ n = 151 \quad \text{RMSE} = 2.955394 \]

\[ \Delta \text{Concentration top50} \]
\[ p_{gap} = 0.32 - 0.07 \text{ top50} \quad R^2 = 13.6\% \]
\[ n = 151 \quad \text{RMSE} = 2.93288 \]
Conclusions

- Fantastic paper
- New view competition/governance/efficiency
- Definitely recommend to read!
Thanks!