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Article — Digitized Version

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Intereconomics

Suggested Citation: Jones, Colin (1970) : Keeping control of industrial mergers, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 05, Iss. 9, pp. 289-294, <https://doi.org/10.1007/BF02928915>

This Version is available at:

<https://hdl.handle.net/10419/138390>

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Keeping Control of Industrial Mergers

by Colin Jones, London

The necessity to arrive at a neutral system of government control of industrial mergers has long been discussed by the EEC-member-countries. But no agreement has been achieved up to now. The British system of control is presented for discussion as a model which has proved to be effective and could also be accepted by the EEC.

The scale of business operations has not yet outgrown the nation state and in many sectors of the modern economy it may never do so. But the increasing size of industrial corporations has begun to pose awkward problems of monopoly control for governments in the advanced industrial nations. Economies of scale appropriate—indeed essential—for international markets may lead to situations of excessive market power in the purely national home market.

Most countries have therefore passed some form of anti-trust legislation to deal with these situations. But, outside the USA, only Britain has developed a fully comprehensive nexus of controls, dealing not only with existing trusts and cartels but also with the creation of new trusts through mergers.

System of Control

Even in Britain, the system of control is of fairly recent origin. The first law dealing with monopoly—or trusts—was passed in 1948, the first anti-cartel law in 1956, and the first measure bringing mergers under public supervision was passed only in 1965.

To understand how the British anti-trust provisions operate, one must appreciate the policy background. As legislation now stands, anticompetitive practices can be dealt with either as a result of an investigation into monopoly power or under the 1956 cartel law which prescribes specific examples of collusive behaviour. Certain types of behaviour, such as collective discrimination, have been outlawed, while collective price agreements and related cartel behaviour have been made illegal, subject to the companies concerned making out a case for exemption in a court of law. The grounds laid down on which exemption may be sought are strictly and narrowly defined, the onus of proof is upon the

companies, and the assumption is that the practice is undesirable from the public policy point of view unless demonstrated otherwise.

In contrast, there is no preconceived presumption in the case of monopoly and other situations of dominant market power. Public policy is neutral. Monopoly is judged by the fruits, and the task of finding out the facts and weighing their implications is entrusted to an autonomous investigatory body, called the Monopolies Commission. The Government itself decides whether an industrial company should be referred to the Commission for investigation, and the Commission reports back to the Government with its findings.

If however the Commission has concluded that the company has abused its market power and the only effective remedy available is to break the company up into smaller independent units, this „divestiture“ is not always very easy to implement—although the Government has the statutory power to require this to be done. Because of this, and because also the early 1960s had seen a growing wave of industrial mergers in Britain resulting in a marked increase in the degree of concentration in several industries, it was decided to extend the Monopolies Commission's powers of investigation to mergers. Monopolies and situations of dominant market power could thus be investigated before they were created as well as afterwards.

Neutral Approach

The traditional neutral approach remained. Whether a proposed merger would be good or bad from the public interest point of view was for the Commission to decide in each case, taking into account all circumstances likely to be relevant—e.g. market strength and prospects for

greater efficiency. In one important sense however public policy was not neutral—or, to be more precise, it adopted an attitude of benevolent neutrality. For in the same year, 1965, the Government decided to establish another autonomous state agency, the Industrial Reorganisation Corporation, whose function was to assist industrial re-structuring and rationalisation such as through mergers. Thus with one arm the Government appeared to be promoting mergers, while with the other it was policing them.

This has not in practice led to any conflict in policy. Close liaison is maintained between the Government departments responsible for each policy so as to prevent any conflict arising. But the duality of approach has almost certainly had an influence upon the use made of the 1965 anti-merger law.

Up to the end of 1969 only 11 mergers were referred to the Monopolies Commission for investigation out of about 440 which had been considered by the Government under the 1965 law (these figures exclude newspaper mergers which are treated differently from other types of mergers). These 440 moreover were only about 10 p.c. of all the mergers that had taken place. On the other hand, of the 11 that have been referred for investigation, the Commission found only 4 likely to operate against the public interest. So, even if far more had been sent to the Commission, it is by no means certain that the number stopped would have been much higher. But, the effect of the 1965 law cannot be judged solely by the occasions when the Commission has been brought into action. One merger was abandoned after it had been referred, but before the Commission could begin its investigation. One was dropped when a reference to the Commission seemed likely. In at least 8 other mergers which were not referred to the Commission, the companies involved gave assurances to the Government on certain points. And the existence of the 1965 law and the powers it gives to the Government has undoubtedly entered into the calculations of industrial empire builders.

Unbureaucratic Commission

These results have been achieved without creating an excessively bureaucratic machine. The preliminary scrutiny of mergers is made by a panel of civil servants. Companies are not obliged by law to notify them of a proposed merger, although in practice most do so in order to get advance clearance of their intentions. Where no notice is given, the Government has up to six months after the merger has been completed or

after a merger first comes to its notice within which to decide whether to refer it to the Commission. If a reference is made, then the Commission is normally given a set period of up to six months within which to complete its report.

In practice neither stage takes anything like as long. The first or preliminary scrutiny is usually completed within two or three weeks at the most, and the Commission's investigations have lasted three to four months on average. Normally most mergers are referred before they are consummated and normally the companies concerned agree to suspend the merger until the Commission has reported without making it necessary for the Government to invoke its statutory power of ordering suspension.

Again, in the four cases where the Commission's judgement has been against a merger, the Government has usually been able to rely upon the voluntary consent of the companies concerned to abide by the Commission's findings. Only in one case has the Government had to resort to a statutory order prohibiting a merger. As satisfactory voluntary assurances have also been provided by companies in other mergers which were not referred to the Commission, the 1965 law has proved to be flexible and expeditious as well as a reasonably effective instrument.

Asset Value and Market Share as Criteria

Three further aspects of this law should be noted. The first is that it covers only mergers involving companies above a certain size. This is measured both by asset value and by market share. The assets test is that total assets valued in excess of £ 5 mn are being taken over, and it brings significant vertical and conglomerate mergers into the scrutiny net. The market power criterion is the same as that used in British monopoly law, namely one-third. This has applied ever since 1948 and so far Britain unlike other countries, has not chosen to vary its statutory definition of market dominance, although companies with more than a third of a market may not be in a dominant situation and companies with considerable market influence may have less than a third of their market.

For newspaper mergers rather different criteria apply. Because of public concern over the concentration of ownership in this industry and the disappearance of many titles in recent decades, no company owning newspapers with a combined daily circulation of 500,000 or more (including the circulation of a paper it proposes to acquire) may take over another newspaper or newspaper as-

sets without the written consent of the Government and, except in certain situations, the proposed merger must be referred for investigation by the Commission within a month of the consent being sought.

Undefined Public Interest

The second interesting point about the 1965 Monopolies and Mergers Act is that nowhere is the public interest defined. The legislators have left this entirely to be defined by the Commission. (In the 1948 Act on the other hand, under which monopolies in the supply of goods are scrutinised for their effect on the public interest, the latter is defined explicitly in the body of the legislation.) This perhaps is not so difficult to do in investigations of existing dominant market power. Past and present actions can be identified and appraised. But in the case of proposed mergers, the Commission has to arrive at a view based upon the balance of future probabilities, and its judgements here may not be so self-evi-

dent or widely accepted. In its first three adverse judgements, which involved horizontal mergers in deep-sea fishing and wholesale distribution, men's clothing, and banking, the Commission held that the detriment to the customers arising from the reduction in competitive pressure outweighed the likely gains in efficiency from the enhanced corporate scale.

In its fourth (and latest) adverse finding, a proposed conglomerate merger, the Commission took the view that the contested take-over of a group with banknote printing, plastics, and other interests by an erstwhile cinema film producer and exhibitor which had diversified into several new fields would lead to a loss of efficiency in the former group as many of its key executives had threatened to resign if the take-over went through. This decision naturally evoked a good deal of public discussion. It was also the only one that had to be enforced by statutory order instead of by a voluntary undertaking.

Continued on page 294

PUBLICATIONS OF THE HAMBURG INSTITUTE FOR INTERNATIONAL ECONOMICS

NEW PUBLICATION

STAATLICHE REGULIERUNG DER LINIENSCHIFFFAHRT IN DEN USA

(GOVERNMENT REGULATION OF LINER SHIPPING IN THE US)

by Wolfgang Reisener

In 1961 government regulation of liner shipping in the US was considerably tightened by the amendment of the Shipping Act of 1916. Since that time American shipping policy, carried out by the Federal Maritime Commission (FMC), is perpetually causing sharp discussions in international shipping quarters. The present publication examines these relations for the first time in a comprehensive and critical manner. It is of highest topicality in view of the governments' growing interference with shipping.

122 pages, 1969, paperbound, price DM 34.—

V E R L A G W E L T A R C H I V G M B H - H A M B U R G

GERMAN PRISM

Growth Rate of GNP Below OECD-Average

According to a forecast of OECD the GNP of seven major industrial member states of OECD calculated in prices of 1968, in 1980 will surpass that of 1970 by 96 p.c. Japan will be at the top with a growth of 160 p.c. Far behind follow France with 79 p.c., Italy with 72 p.c. and Canada with 69 p.c. The anticipated growth rates of the US (58 p.c.), the Federal Republic of Germany (57 p.c.) and Britain (37 p.c.) will remain below average. In the case of Germany and Britain the lowest increase by 2 p.c. of the number of persons employed is being expected as compared with an average of 11 p.c. for the seven countries.

New World Bank Loan of DM 200 mn Signed

Between the World Bank and a syndicate of German banks headed by Deutsche Bank AG, with the cooperation of Dresdner Bank, an agreement on the floatation of a new DM-loan has been signed on July 22, 1970. The nominal value of the loan, which will be offered for sale to the public, amounts to DM 200 mn. The rate of interest is 8.5 p.c. (six months coupon), the selling rate is 99.25 p.c. Thus the rate of return will be 8.8 p.c.

The loan is non-redeemable and will be repaid at its nominal value on August 1, 1980. It will be quoted at all German stock exchanges. The proceeds will be spent within the scope of the World Bank's general activities.

20 Million Motor Vehicles Need High- ways up to 1985

Today 14 mn passenger cars are driven on Germany's highways and streets. Up to 1985 there will be 20 mn of them. Therefore a comprehensive expansion of the highway system has top priority among the Federal Government's long-term plans.

Today's super-highway net of 4,500 kilometers (km) is to be enlarged to 10,000 km. The present 800 km of double-track Federal highways are to be extended to 3,000 km, so that a total of 13,000 km of double-track Federal highways will

be available. By that time a total number of 20 mn cars—i.e. one car for three persons—will be on the roads, and the demand for cars will be about satisfied in the Federal Republic. The extension of highways planned for this final stage should also meet long-term requirements. Even if one does not believe that this year's price boom will continue for the next 15 years, DM 125 bn will be required for this plan, of which DM 93 bn will be provided for by the mineral oil tax earmarked to 50 p.c. for road building. The hitherto lacking billions must be found yet.

DM 9 bn Earmarked for Educational Reform

At a press conference on July 30, the Federal Minister for Education and Science, Professor Hans Leussink, explained his Ministry's financial planning for the next years: As a start the Ministry's expenditure on education and science is to grow from DM 2.8 bn in 1970 to DM 9 bn in 1974, i.e. by at least DM 6.2 bn. This is an increase by more than 200 p.c. The share of expenditure on education, science and research in the total budget will nearly double from 5.3 p.c. to almost 10 p.c. within a period of 5 years.

In the past years Federal expenditure on education and universities has been relatively small and will therefore grow faster than expenditure on science and research. But also the latter will grow considerably more than the Federal Republic's total budget. Expenditure on education and universities in 1971 will nearly reach 40 p.c. of the Ministry's total expenditure and in 1974 will surpass 50 p.c.

Guidelines for German Development Aid

The Federal Minister for Economic Cooperation, Dr Erhard Eppler, in July explained the Federal Government's development policy. Among other things he said that the medium and smaller nations' responsibility for development policy is growing steadily. Regarding its total performance in absolute terms the Federal Republic is second after the USA, and relative to its GNP it is at the top of all donor countries. This, however, does not apply to public aid. According to a report to DAC there has been an increase of total contributions by approx.

30 p.c. from DM 6,654 mn (1968) to DM 8,646 mn (1969). The share in the GNP was 1.44 p.c. More than two thirds of all performances are private capital transfer, hardly one third public development aid.

A public hearing of the Bundestag Committee for Economic Cooperation showed a far-reaching agreement between experts and the Federal Ministry for Economic Cooperation as regards tasks and points of emphasis. The target of giving 0.7 p.c. of the GNP as public aid before the end of the decade is acknowledged by a majority. Tied-up deliveries are to be further reduced. Softer credits are to counteract increasing indebtedness. Technical aid, above all training aid, is to enjoy priority. A.o. the following measures are to realise these guidelines: Development aid is to get priority in the budget. The total increase of authorisations establishing an obligation is to amount to 11 p.c. In the multilateral field the following measures are provided for from 1971 on: increased contribution to the development programmes of the UN, population control, World Food Programme, expansion of the EEC-fund through the new association agreement, capital increases for World Bank and IDA, and a German monetary contribution to the special fund of the Asian Development Bank.

German Federal Postal Administration Becomes an Enterprise

On July 30, 1970, the Federal Minister of Transport and for Posts and Telecommunications, Georg Leber, announced at the Federal Press Conference his Ministry's plans for a reform of the German Federal Postal Administration. This Administration will be reorganised as an enterprise. In future it will not be led by a minister but will be run by a managing board and a board of directors.

Regarding the economic and financial structure the draft contains a new formulation of the principles of economic operation and of the financial relations with the Federal Republic as the owner. The Federal Postal Administration is to be operated in such a way that earnings cover expenses and profits adequate to the demand for capital resources will be achieved as a contribution to the self-financing of the enormous investments above all in the telecommunications sector.

True, the Federal Government keeps the right to give directions concerning the Postal Administration's objectives and business policy. But

it is obliged to pay the balance if the carrying out of such a direction causes additional expenses or lower receipts for the Postal Administration.

Klöckner-Werke Registering a Vigorous Stimulation of Turnover

During the past three months Klöckner-Werke AG, Duisburg, registered an extraordinary stimulation of turnover. Total turnover in the first nine months of the business year 1969/70 rose by 20.1 p.c. as compared with the previous year's corresponding period—i.e. by 18.9 p.c. with steel production and by 21.9 p.c. with processing. The monthly average of sales to outside parties with DM 188.5 mn is higher by more than 22 p.c. than a year ago. Reasons mentioned for this year's vigorous turnover increase are, apart from the rise in production, the further shifting to better qualities of rolled steel production that has risen by 4.6 p.c. to 232,000 tons and the above average growth rate of higher quality processed products.

Promotion of Direct Investments in LDC's

The business report of Deutsche Gesellschaft für wirtschaftliche Zusammenarbeit GmbH (DEG: German Company for Economic Cooperation, Ltd.) can show a balance sheet to be proud of. With own resources of DM 100 mn it promotes direct investments in developing countries to the tune of DM 800 mn. For 1969 this is more than one quarter of all direct investments in less developed countries. Africa is the focal point of the Company's activities, closely followed by Latin America and Asia. In the last business year there have been no problems in developing countries, no participation of the Company has been expropriated. Above all the projects of the Company's affiliate, Deutsche Hotelgesellschaft für Entwicklungsländer (German Hotel Company for Developing Countries), has opened up new foreign exchange resources for LDC's, whose importance is obviously underestimated in the Federal Republic. At any rate the image of DEG still requires intensive promotion in Germany. The line between political and economic tasks must be drawn more clearly. Moreover, the DEG should be allowed to make more propaganda than hitherto for investments in the Third World. For this would help to increase private aid for LDC's considerably.

Continued from page 291

Emphasis on Efficiency

This emphasis upon efficiency, which featured in all four judgements although as a decisive factor only in the last one, leads on to the third and last point about British merger law. This is the scope allowed by the mergers legislation for full account to be taken of the benefits of greater efficiency brought about by increased size. Merger policy does not seek to preserve external competitive pressure at all costs, as in the USA. Some reduction in this external spur to efficiency might be accepted on the grounds, presumably, that this loss would be outweighed by the gain in efficiency resulting from the larger scale of operation.

The prospects of greater international competitiveness resulting from a take-over, in other

words, might be held to outweigh the likelihood of a merger reducing competition in the home market—although the steady removal of tariffs helps to counteract this reduction in many industries. Lately, scepticism has grown in Britain about the weight of arguments based upon economies of scale—not only whether they exist in marketing, finance, management services, and research as well as in plant size but also whether they are actually fully exploited after a merger. The first result of this scepticism is the Government's proposal to seek powers to refer mergers for investigation by the Commission some time after they have taken place to see whether the alleged advantages actually out-balanced the possible disadvantages. This will be done later this year when the Monopolies Commission is itself merged with the National Board for Prices and Incomes, another investigatory agency, to form the Commission for Industry and Manpower.

PUBLICATIONS OF THE HAMBURG INSTITUTE FOR INTERNATIONAL ECONOMICS

BESTIMMUNGSGRÜNDE DER PREISENTWICKLUNG AUF DEM WELTZINNMARKT 1950—1967

(Determinants for the Price Development in the World Tin Market 1950—1967)

by Helmut Stodieck

In the world tin market the frequently abrupt price fluctuations typical of raw materials are particularly conspicuous. The present study analyses the chances for a stabilisation of this special market. Among other things the depiction of price influences on production, consumption, fluctuations of stocks and East-West trade are taken into consideration. From this and from the characterisation of the stabilising effects of international tin agreements promising starting points for a slowing down of world wide price fluctuations are resulting.

Octavo, 186 pages, DM 34.—

V E R L A G W E L T A R C H I V G M B H - H A M B U R G