U.S. Department of Justice Antitrust Division

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INTRODUCTION

These comments address two of the primary competition issues identified by the organizers of this workshop and the authors of papers on competition in NAFTA markets:

- whether the elimination of trade barriers reduces market concentration; and
- whether special competition rules are or should be applied to the agriculture or agribusiness industries.

These issues are addressed from the perspective of U.S. antitrust law enforcement. The comments reflect my personal views, and not necessarily those of the U.S. Justice Department.

NAFTA'S EFFECT ON MARKET CONCENTRATION

When U.S. antitrust authorities analyze the competitive effects of horizontal mergers, they attempt to determine whether the transaction is likely to create or enhance market power or to facilitate its exercise in the product and geographic markets in which the merging firms compete. Guidelines for this analysis are found in: U.S. Department of Justice/Federal Trade Commission, *Horizontal Merger Guidelines* (*the "Guidelines"*), § *1.0*.[1] The relevant geographic market is defined as a geographic region in which a hypothetical monopolist could profitably impose a small but significant, non-transitory price increase. In most cases, a 5 percent price increase will be considered small but significant. (*Id.*, §§ 1.11, 1.21).

[1] The *Guidelines* are available on the Antitrust Division's website ("usdoj.gov").

When a Free Trade Agreement (FTA) eliminates customs duties, quotas or other trade barriers, it often expands the relevant geographic market. To illustrate this point, assume that: (a) U.S. and Mexican firms sell a particular product in their domestic markets for approximately the same price; (b) the United States imposed a 10 percent duty on imports of that product before NAFTA: and (c) the United States eliminated duties on imports from Mexico upon NAFTA's implementation. Before NAFTA, the relevant geographic market might encompass all of the United States (with say six firms in that market). Even though there were, say, four Mexican producers located just south of the U.S. border in this hypothetical example, the relevant market would exclude Mexico if the addition of a 10 percent duty to the cost of imports from Mexico would make it impractical for consumers to switch to any of the four Mexican producers in order to avoid the U.S. producer's 5 percent price increase. *(Guidelines*, § 1.2).

Continuing with this example, if NAFTA eliminated the U.S. 10 percent customs duty, it might become feasible for U.S. consumers to switch to the Mexican producers in order to avoid the U.S. producer's 5 percent increase. If enough consumers were likely to switch to the Mexican producers to make the 5 percent price increase unprofitable, the relevant geographic market would be expanded to include the region in Mexico where the four Mexican producers were located.

The expansion of geographic markets, however, does not always result in market de-concentration. To illustrate this point, again assume that NAFTA eliminated the 10 percent customs duty. If all of the Mexican firms were independently owned, the number of firms in the relevant geographic market would increase from six to ten, and the relevant geographic market would be less concentrated after NAFTA. But, if some of the U.S. producers owned or controlled some of the Mexican producers, the larger post-NAFTA U.S./Mexican geographic market could be more concentrated than the smaller pre-NAFTA U.S. geographic market.

As a note of caution, governments that have the power to expand relevant geographic markets by adopting FTA's usually retain the power to subsequently contract those geographic markets. For example, NAFTA authorizes member countries to exclude or limit imports by imposing antidumping duties, countervailing duties and other forms of import trade relief. NAFTA also includes "snap back" provisions that reimpose duties or quotas if there is a sudden surge of imports. And, currency fluctuations that occur after the adoption of an FTA can offset the elimination of customs duties.

RULES FOR ANALYZING COMPETITIVE EFFECTS OF AGRIBUSINESS MERGERS

The *Guidelines* apply a common framework for analyzing the competitive effects of mergers in all industries. In one sense, however, there are special rules for agriculture and agribusiness, because the application of this analytical framework requires an investigation into the specific competitive conditions in the industry in which the merging firms compete. Despite the specific nature of each merger investigation, it is possible to sketch some broad generalizations about merger investigations in the agriculture and agribusiness industry. First, although concentration at the farm level continues to increase as the number of U.S. farms decreases, farming tends to be an unconcentrated industry. It is unlikely that the U.S. competition authorities will challenge one farmer's purchase of acreage from his neighbor.

Second, the Department of Justice is concerned about mergers among firms that sell inputs to farmers that may create, enhance or facilitate the exercise of monopoly or oligopoly market power. Recent investigations under Section 7 of the Clayton Act include:

- Monsanto's acquisition of DeKalb Genetics corporation (which resulted in Monsanto's agreement to spin off important rights to agrobacterium-mediated transformation technology and to license its Holden's corn germplasm rights, as the price for avoiding a challenge in court);
- the New Holland/Case merger (which resulted in divestitures of New Holland's four-wheel drive and two-wheel drive tractor business and Case's hay tool business); and
- Monsanto's proposed acquisition of Delta & Pine Land's cottonseed business (which resulted in the parties' abandonment of the transaction).

The Department of Justice is also concerned about mergers among firms that buy products from farmers. Under the *Guidelines*, market power includes monopsony or oligopsony power- - the power to depress the price paid for a product below the competitive price. (*Id.*, § 0.1). Farmers, in particular, may be vulnerable to the exercise of monopsony power, because the relatively high cost of trucking their crops to distributors or processors in comparison to the value of crops often means that it will not be feasible to ship them very far past the closest buyer's facilities in order to get a better price. As noted in the MacDonald paper, the Department's actions in the Cargill/Continental transaction provide a useful insight into our analysis of concentration in the grain distribution business. After evaluating numerous local geographic markets in which the transaction might have created, enhanced or facilitated the exercise of monopsony power, we required divestitures of Cargill or Continental facilities in all of the approximately twelve local markets in which we concluded that the transaction might create this type of market power.[2]

The adoption of an FTA can affect our monopsony analysis in some cases. For example, if NAFTA made it feasible for farmers in northern Montana to sell their crops to nearby Canadian grain distribution companies, as well as nearby U.S. firms, the relevant geographic market would be expanded to include those Canadian buyers. As with the previous monopoly power example, the adoption of NAFTA could, but would not necessarily, ameliorate monopsony concerns by reducing concentration in the relevant geographic market. On the other hand, if NAFTA eliminated all Canadian duties and quotas, but its sanitary regulations precluded U.S. farmers from selling their crops to Canadian grain distributors, we would exclude those firms from the relevant geographic market, no matter how close they might be to the U.S. farmer.

[2]The Antitrust Division's website (http://www.usdoj.gov) includes pleadings, briefs, press releases and other public documents for recent merger investigations and court cases. Documents such as Competitive Impact Statements and Responses to Public Comments often provide useful summaries of our legal and economic analysis.