



**Malaysian
Aviation Commission**
Suruhanjaya Penerbangan Malaysia

Guidelines On
**SUBSTANTIVE
ASSESSMENT OF MERGERS**

Published by



**Malaysian
Aviation Commission**
Suruhanjaya Penerbangan Malaysia

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Preface

These Guidelines sets out the substantive assessment of mergers by the Commission in determining whether an anticipated merger or a merger has anti-competitive effects. However, the Commission also recognizes that certain mergers may be completely neutral or have pro-competitive effects such as enhancing efficiencies in the industry or increasing consumer welfare.

The Commission welcomes and encourages mergers which have pro-competitive effect that benefit the growth and the sustainability of the civil aviation industry in Malaysia.

These Guidelines are published to facilitate mergers on a regulated basis taking into consideration the interests of the consumers and the industry.

1. Background

1.1 The application of the competition provisions under Part VII the Act will be based on the fair competition principle which is consistent with the functions of the Commission under section 17 of the Act and the general policy on economic regulation of the civil aviation industry of the International Civil Aviation Organisation. In applying the fair competition principle, the Commission will consider benefits to the public as one of the factors in its competition analysis.

1.2 These Guidelines are issued by the Commission in the exercise of its power pursuant to section 65 of the Act to provide explanation on the prohibition of mergers that have resulted or may be expected to result in an SLC in any aviation service market under section 54 of the Act.

1.3 The fair competition principle is applicable in assessing whether a merger that has resulted or may be expected to result in an SLC in any aviation service market could be allowed because there are economic efficiencies and social benefits directly arising from the merger that outweigh such SLC.

1.4 The types of conduct or factors as provided in these Guidelines which may be considered by the Commission in evaluating a merger are not exhaustive and the examples are for illustrative purposes only. The Commission will consider the specific facts and circumstances of each case and may take into account any other factor that the Commission deems relevant in the implementation of Division 4 of Part VII of the Act.

1.5 These Guidelines serve to supplement Part VII of the Act or any regulation relating to the same. These Guidelines should be read together with all other guidelines issued by the Commission pursuant to section 65 of the Act.

1.6 The concepts and principles in these Guidelines are based on domestic and international best practices relating to competition law.

1.7 The Commission may revise these Guidelines from time to time taking into account developments in competition law and the civil aviation industry.

1.8 Enterprises providing aviation services are advised to conduct self-assessment exercises of their businesses in respect of their conduct, procedures, management and control. Enterprises are also advised to have competition compliance procedures in place for their employees at all levels including the top management and the governing body, where applicable.

1.9 Any enterprise in doubt about how its commercial activities may be affected by Part VII of the Act may wish to seek independent legal advice.

2. The Prohibition under Section 54 of the Act

2.1 Subsection 54(1) of the Act prohibits mergers that have resulted or may be expected to result in an SLC in any aviation service market.

2.2 The prohibition in section 54 of the Act covers both mergers that have occurred and mergers that will occur which is termed as anticipated mergers. For the purpose of these Guidelines, reference to the term “merger” may apply to a merger that has occurred or an anticipated merger.

2.3 The assessment on whether a merger infringes the prohibition under section 54 of the Act involves the following two-step test:

- (a) whether a merger occurs within the meaning of subsection 54(2) of the Act; and
- (b) if a merger occurs, whether such merger has resulted or may be expected to result in an SLC in any aviation service market.

2.4 Further explanation regarding such assessment is provided in Parts 3 to 11 of these Guidelines.

3. Mergers

Situations Constituting Mergers under Division 4 of Part VII of the Act

3.1 Subsection 54(2) of the Act provides that a merger occurs in any of the following situations:

- (a) Two or more enterprises which were previously independent of each other, merge
 - This includes a situation where —
 - (i) two or more independent enterprises merge into a new enterprise; or
 - (ii) an enterprise is absorbed by and into another enterprise causing the former to cease to exist as a separate legal entity.
- (b) One or more persons or enterprises acquire direct or indirect control of the whole or part of one or more other enterprises¹
- (c) One enterprise acquires the assets including goodwill or a substantial part of the assets of another enterprise with the result that the acquiring enterprise is in a position to replace or substantially replace the acquired enterprise in the business or the part concerned of the business in which the acquired enterprise was engaged immediately before the acquisition
- (d) A joint venture is created to perform, on a lasting basis, all the functions of an autonomous economic entity

¹ This subparagraph should be read together with subsections 54(3), (4) and (5) of the Act relating to the element of “control”. This will be further elaborated in paragraphs 3.2 to 3.6 below.

- A joint venture performs all the functions of an autonomous economic entity when it operates in an aviation service market and performs the functions normally carried out by enterprises in that market. Such joint venture usually requires dedicated management and resources to support its daily operations and to carry out its commercial activities on a lasting basis. A joint venture that only takes over one specific function within the parent enterprises' commercial activities such as the research and development function without access to an aviation service market is unlikely to fulfil the element of performing the functions of an autonomous economic entity.

- The facts of each case would be considered to determine whether a joint venture is intended to operate on a lasting basis. The following are some of the examples where a joint venture is intended to operate on a lasting basis:
 - (i) The commitment of resources to the joint venture by the parent enterprises for the carrying out of the joint venture's functions as an autonomous economic entity

 - (ii) Where an agreement forming the joint venture provides that the joint venture is for a specific period
 - ❖ The period specified must be long enough to cause a lasting change in the structure of the enterprises concerned or the joint venture agreement provides that the joint venture may be continued beyond such specified period. However, provisions in an agreement forming the joint venture that provides for the possibilities of a dissolution of the joint venture by themselves do not prevent the joint venture from being considered as operating on a lasting basis.

- However, a joint venture established for a short definite period for the mere purpose of carrying out a specific project may be considered as not having an operation on a lasting basis.
- A joint venture under paragraph 54(2)(d) of the Act would be jointly controlled by the enterprises that are parties to such joint venture where such enterprises are capable of exercising decisive influence with regard to the activities of the joint venture².
- A joint venture that does not constitute a merger under paragraph 54(2)(d) of the Act may be subject to section 49 of the Act.

3.2 Subsection 54(3) of the Act provides that control of an enterprise exists where a person or any other enterprise is capable of exercising decisive influence with regard to the activities of the former enterprise by reason of rights, contracts or any other means, or any combination of rights, contracts or other means. The existence of control in an enterprise depends on the capability of a person or any other enterprise to exercise such decisive influence regardless of whether the person or the other enterprise actually exercises such influence. Such control could exist by —

- (a) the ownership of the assets³ of the enterprise;
- (b) the right to use all or part of the assets of the enterprise; or
- (c) the rights or contracts which enable the exercise of decisive influence regarding the composition, voting or decisions of the enterprise.

3.3 In determining whether a person or an enterprise is capable of exercising decisive influence with regard to the activities of an acquired enterprise, a qualitative

² This subparagraph should be read together with subsections 54(3), (4) and (5) of the Act relating to the element of “control”. This will be further elaborated in paragraphs 3.2 to 3.6.

³ Assets of an enterprise may include brands, licences or intellectual property rights.

assessment would be carried out on a case by case basis taking into account all relevant circumstances including legal and factual considerations. Control may be found to exist in fact or in law.

3.4 Subsection 54(4) of the Act provides that control may be acquired by a person or an enterprise directly or indirectly. In the case of direct control, a person or enterprise becomes a holder of the rights or contracts, or entitled to use the other means provided in subsection 54(3) of the Act. However, a person or an enterprise may have indirect control over another enterprise if the person or the enterprise acquires the power to exercise the rights derived from the rights, contracts or any other means referred to in subsection 54(3), even though such person or enterprise is not the holder of the rights or contracts, or entitled to use the other means.

3.5 In determining the existence of indirect control, all relevant factors should be taken into consideration including the existence of links between an acquiring enterprise and an enterprise enjoying indirect control. Example of factors that may help to determine the existence of indirect control, amongst others, are –

- (a) the source of funding and family relations between the acquiring person or enterprise; and
- (b) the person or enterprise that allegedly has the actual power to exercise the control over the acquired enterprise.

3.6 An example of indirect control is where enterprise A is used by enterprise B to acquire the majority shares of enterprise C and exercises the rights conferred by such majority shareholding in accordance with enterprise B's instructions. In that situation, even though enterprise A is the majority shareholder of enterprise C, enterprise B acquires indirect control over enterprise C.

Types of Mergers

3.7 Division 4 of Part VII of the Act governs both horizontal mergers and non-horizontal mergers. Horizontal mergers refer to mergers between enterprises that operate at the same level of the supply chain in the same economic market. Non-horizontal mergers consist of vertical mergers⁴ and conglomerate mergers⁵.

Situations Not Constituting Mergers under Division 4 of Part VII of the Act

3.8 Subsection 54(6) of the Act provides that a merger shall not be deemed to occur in the following situations:

- (a) The person acquiring control is a receiver or liquidator acting as such or is an underwriter acting as such
- (b) All of the enterprises involved in the merger are under the direct or indirect control of the same enterprise
 - This may include a merger between a parent and a subsidiary enterprise or two enterprises which are under the control of another enterprise as well as an internal restructuring within a group of companies. Such mergers do not fall within the merger control regime under Division 4 of Part VII of the Act because they are unlikely to affect any aviation service market since these mergers are basically within a single economic unit where the enterprises involved do not enjoy real autonomy in determining their actions in any aviation service market even prior to the merger.
- (c) Control is acquired solely as a result of a testamentary disposition, intestacy or the right of survivorship under a joint tenancy

⁴ Mergers between enterprises that operate at different levels of the supply chain in the same economic market.

⁵ Mergers between enterprises that operate in different markets.

- (d) Control is acquired by an enterprise whose normal activities include the carrying out of transactions and dealings in securities for its own account or for the account of others under the circumstances stipulated in subsection 54(7) of the Act

3.9 The circumstances stipulated in subsection 54(7) are as follows:

- (a) the control is constituted by the enterprise's holding of securities in the acquired enterprise on a temporary basis; and
- (b) the acquiring enterprise's exercise of the voting rights in respect of those securities is —
 - (i) for the purpose of arranging the disposal of all or part of the acquired enterprise, its assets or securities within the specified period⁶; and
 - (ii) not for the purpose of determining the manner in which any activity of the acquired enterprise that could affect competition in an aviation service market is carried on.

⁶ "specified period" as provided in subsection 54(7) means –

- (a) the period of twelve months from the date on which control of the other enterprise was acquired; or
- (b) within a longer period as the Commission determines if it is not reasonably possible to effect the disposal within the period of twelve months from the date on which control of the other enterprise was acquired.

4. Substantial Lessening of Competition

4.1 Where it is established that there is a merger, the next step is to evaluate whether the merger would result or is expected to result in an SLC in any aviation service market. This is determined through the SLC test.

4.2 An effective competition, amongst others, may be characterised by a process of rivalry between enterprises where they compete to get a bigger market share, thus creating incentives for enterprises to reduce price, improve quality of services, enhance efficiency or introduce new and better services. An SLC may occur where a merger has a significant effect on rivalry between enterprises over time, reducing the competitive pressure on enterprises in any aviation service market to improve their services offered to buyers in terms of quality, efficiency or innovation. An SLC in an aviation service market would ultimately be detrimental to buyers either in terms of an increase in prices, lower quality of services or lesser choices made available to buyers.

4.3 Subsection 54(1) of the Act does not prohibit all mergers. Instead, only mergers that have resulted or may be expected to result in SLC are prohibited. Mergers that are found to be pro-competitive, neutral towards competition or having a trivial effect of lessening competition are not prohibited under subsection 54(1) of the Act. The effect of a merger on competition depends on the type of the merger, whether it is horizontal, vertical or conglomerate⁷.

The SLC Test

4.4 The determination of whether a merger has resulted or may be expected to result in an SLC would entail the following steps:

- (a) Define the relevant aviation service market

⁷ This is further explained in Parts 7 to 9 of these Guidelines.

(b) Develop a theory or theories of harm

- Developing a theory or theories of harm would help to identify the possible harm and effects on competition in a relevant aviation service market arising from a merger. Such possible harm and effects on competition will then be compared with the counterfactual i.e. the conditions and the degree of competition in the relevant aviation service market in the absence of such a merger.

(c) Develop a counterfactual scenario

- A counterfactual scenario refers to the conditions and the degree of competition in a relevant aviation service market in the absence of such a merger.
- In general, a counterfactual may be assessed based on prevailing conditions of competition in a relevant aviation service market which may be used as indicators of the future degree of competition in the aviation service market if the merger does not take place. However, the likelihood and imminence of changes to the prevailing market conditions that may affect the structure and degree of competition in a counterfactual may be considered. Examples of changes to the prevailing conditions of a relevant market include the entry of a new competitor, the expansion plans or exit of an existing competitor, the imminent failure of a merger party and regulatory changes.
- In the case of a merger involving a merger party that is failing, a merger party may invoke the “failing firm defence”. In the context of a counterfactual analysis, a merger party may claim that, without the merger, a merger party that is failing would exit the relevant aviation service market and competition provided by that merger party would be lost anyway. In such a case, the conditions and the degree of competition in a relevant aviation service market in the counterfactual

scenario may be no worse than those in a post-merger scenario. In other words, the loss of rivalry in the counterfactual of a failing firm may be similar to the loss of rivalry in the post-merger scenario.

- In assessing the failing firm defence, consideration would be given to all relevant facts including –
 - (i) whether a merger party is in such dire situation that it would exit the relevant aviation service market within the near future;
 - (ii) whether a merger party is unable to meet its financial obligations in the near future;
 - (iii) whether there is any serious prospect of reorganising the business; and
 - (iv) whether there is any less anti-competitive alternative to the merger.
- The failing firm defence must be substantiated with proof and evidence that a merger party is genuinely failing and that it would fail should the merger not occur.

- (d) Assess the competition in a relevant aviation service market and compare it with a counterfactual scenario

4.5 In carrying out the SLC test, the following factors may be considered, whichever is applicable:

- (a) aviation service market definition;
- (b) market power and market concentration;

- (c) competitive effects arising from horizontal mergers, vertical mergers or conglomerate mergers;
- (d) entry and expansion; or
- (e) countervailing buyer power.

5. Aviation Service Market Definition

5.1 The aviation service market definition analysis would assist in defining and identifying a relevant aviation service market within which the competitive effects of the merger would be assessed, focusing on the overlapping commercial activities of the enterprises involved in the merger. The Guidelines on Aviation Service Market Definition provide guidance pertaining to the definition and identification of a relevant aviation service market. Upon defining the relevant aviation service market, the effects of such merger to competition within that market and the counterfactual would then be assessed.

6. Market Power and Market Concentration

Market Power

6.1 Market power refers to the ability of an enterprise to adjust prices or outputs or trading terms without effective constraint from competing enterprises or potential competitors. A merger that eliminates effective competition between enterprises and provides market power to one or more enterprises may be considered as having the effect of an SLC in a relevant aviation service market. In this situation, such merger may allow the enterprise or enterprises with market power to raise prices, reduce quality and efficiency, restrict choices made available to buyers or restrain innovation.

Market Concentration

6.2 The degree of market concentration may be an indicator of the level of competitive pressure within a relevant aviation service market. Market concentration is a measure that generally depends on the number of enterprises in a relevant aviation service market and the size of the enterprises.

6.3 Market concentration may be measured by various ways including the following:

(a) Market shares

- Market shares may indicate the degree of market power held by an enterprise or enterprises.
- In general, the higher the combined market share of the merger in a relevant aviation service market, the more likely that such merger has resulted or be expected to result in an SLC. In assessing market concentration through market shares, it is necessary to identify the

market shares of other enterprises in the relevant market in order to compare with the combined market share of the merger parties. The differences in market shares between the merger parties and other enterprises in the relevant market would help to assess the level of competition in the relevant market.

- Market shares may be calculated based on sales revenue or value⁸, sales volume⁹ or capacity¹⁰, wherever appropriate.
- Historical data on market shares may also be considered as it could indicate the dynamics of a relevant aviation service market.

(b) Concentration ratios

- Concentration ratios measure the aggregate market share of a small number of the leading enterprises in a relevant aviation service market.
- In this regard, concentration ratios of the biggest three enterprises (CR3), the biggest four enterprises (CR4) or the biggest five enterprises (CR5) may be considered, where appropriate.
- The concentration ratios do not take into account the differences in the size of each enterprise within the respective group of enterprises.

(c) Herfindahl-Hirschman Index

- HHI may be used as a measure of concentration in a relevant aviation service market by taking into account the number of enterprises in that market and the differences in the size of the enterprises.

⁸ In monetary units.

⁹ In number of units.

¹⁰ In number of units.

- The HHI is calculated by adding together the squared values of the percentage market shares of all enterprises in a relevant aviation service market.

6.4 The effect of a merger to the levels of competition within a relevant aviation service market may be measured by the difference between the HHI of the pre-merger market and the prospective post-merger market. Both the HHI of the post-merger market and the change in HHI due to the merger are indicative of the changes in the competitive structure in that market.

7. Competitive Effects Arising from Horizontal Mergers

7.1 As stated in paragraph 3.7, a horizontal merger refers to a merger between enterprises that operate at the same level of the supply chain in the same economic market.

7.2 A horizontal merger may result in an SLC in a relevant aviation service market by way of unilateral effects¹¹ or coordinated effects.

Unilateral Effects

7.3 Unilateral effects refer to the anti-competitive effects of a merger that can result from unilateral actions by a merger party or any other enterprise in a relevant aviation service market.

7.4 A merger may reduce competitive pressure on a merger party and enable it to exercise market power as a result of the elimination of competition between the merger parties. As a consequence of the merger, where a merger party is able to obtain market power, it may be able to unilaterally impose a price increase or behave anti-competitively in a sustainable and profitable manner. Since horizontal mergers involve mergers between enterprises that are providing the same or substitutable services, any loss of sales due to the price increase imposed by one merger party may be captured by the increase in sales by the other merger party.

7.5 In addition, a merger may also incentivise enterprises other than the merger parties in a relevant aviation service market to increase their prices due to the overall reduction of competitive pressure in that market resulting from the merger. The price increase by the other enterprises in a relevant aviation service market acting

¹¹ Also referred to as non-coordinated effects.

independently of each other without any coordination would also be regarded as a unilateral effect of the merger.

7.6 In assessing whether a merger may give rise to unilateral effects, consideration may be given to relevant factors such as —

- (a) the profitability of any price increase or reduction of supply;
- (b) whether other competing enterprises would increase their capacities or expand their commercial operations in response to any price increase or reduction of supply;
- (c) the existence of any close substitutes of the service provided by the merger parties;
- (d) the ease and likelihood of buyers switching to the services of other competing enterprises; and
- (e) the possibility of new competitors entering the relevant aviation service market.

7.7 Unilateral effects may occur in any aviation service market including aviation service markets with homogenous or differentiated aviation services.

7.8 The analysis of the unilateral effects of a horizontal merger would cover a wide range of considerations, primarily in relation to the change in the structure of a relevant aviation service market and the resulting impact of the merger on the behaviour of the merger parties as well as the other enterprises in a relevant aviation service market. Factors that may indicate unilateral effects arising from a horizontal merger include the following:

- (a) The number of enterprises in a relevant aviation service market is small

- (b) The merger parties have large market shares
- (c) The merger parties are close rivals in a relevant aviation service market where a substantial number of buyers would switch from the aviation services of one enterprise to another in the pre-merger period
- (d) The likelihood of timely and effective supply-side substitution for the aviation services by the other enterprises in a relevant aviation service market is low
- (e) A merger party is a strong new entrant to a relevant aviation service market that could have had been a strong rival to the other merger party since the former could be expected to grow in that market
 - In such a situation, a merger could eliminate such potential competitive pressure in that market.

The factors listed above are non-exhaustive. It is not necessary for all factors to be found cumulatively in order to conclude that there are unilateral effects arising from a merger.

Coordinated Effects

7.9 Coordinated effects refer to anti-competitive effects of a merger that can result from coordinated actions by the enterprises in a relevant aviation service market. Coordinated effects do not require the existence of an express collusion between the enterprises in a relevant aviation service market.

7.10 Coordinated effects may arise without any express agreement where there may just be tacit collusion between enterprises in a relevant aviation service market. Tacit collusion can arise from an understanding between enterprises as facilitated by certain

market conditions that it will be in their mutual interest to coordinate their commercial decisions.

7.11 A merger that reduces competitive pressure within a market may also give rise to coordinated effects by increasing the probability that competing enterprises will collude. A merger may also give rise to coordinated effects by increasing the probability of the merger parties to tacitly or explicitly coordinate their behaviour in other areas where they have not merged so as to reduce competition with each other.

7.12 Coordinated effects are more likely to occur from a merger where the following circumstances are present:

- (b) Enterprises are able to align their behaviour in a relevant aviation service market
 - The enterprises' ability to align their behaviour may arise from certain market conditions and characteristics such as market transparency, homogeneity or lower degree of differentiation of services and symmetry of size of and cost to the enterprises.

- (c) Enterprises have the incentive to maintain coordinated behaviour
 - In order for coordination to be maintained, any deviation by an enterprise from the coordinated behaviour should be able to be detected and consequently "punished" by the other enterprises who participate in the coordination.
 - The detection of any behaviour that breaks away from the coordination may be possible in a more transparent market such as where there is price transparency.
 - To be able to maintain coordinated behaviour, other enterprises must be able to "punish" or react to any behaviour that is not in accordance

with the coordination by immediately cutting prices or increasing capacity. However, it is not necessary for any particular mechanism of punishment for coordination to exist. What is important is that there must be sufficient incentive for enterprises to accord to the coordination.

- (d) The coordinated behaviour could be sustained in light of other competitive constraints in a relevant aviation service market
- Coordination is more likely to be sustainable in a relevant aviation service market that is sufficiently mature and stable and faces limited potential competition that may disrupt such coordination.
 - A merger that removes an enterprise that was particularly aggressive in the pre-merger period may make coordinated behaviour more likely in the post-merger period.

7.13 In assessing the coordinated effects of a merger, the structure and characteristics of a relevant aviation service market and the existence of any history of coordination in the said market would also be considered.

7.14 Consideration would also be given to factors that would indicate the characteristics of a relevant aviation service market and how such factors would impact the coordinated effects of a merger. Such factors may include —

- (a) the level of concentration in that market;
- (b) the existence and degree of barriers to entry;
- (c) similarity between the enterprises in terms of size, market shares, cost structures, business strategies and risk taking behaviours;
- (d) the degree of market transparency;

- (e) the existence of institutions and practices that may aid coordination;
- (f) the stability of demand and costs in that market;
- (g) the historical stability of the enterprises' market shares;
- (h) the existence of competition between the enterprises in more than one aviation service market;
- (i) the existence of any short term financial pressure faced by any of the enterprises;
- (j) the possibility of expansion of operation by the smaller enterprises;
- (k) the degree of excess capacity in that market by coordinating enterprises and other enterprises in the said market; and
- (l) the degree of innovation in that market.

8. Competitive Effects Arising from Vertical Mergers

8.1 As stated in paragraph 3.7, a vertical merger refers to a merger between enterprises that operate at different levels of the supply chain in the same economic market. An example of a vertical merger is a merger between an airline and a ground handling company.

8.2 Vertical mergers may be pro-competitive and enhance efficiencies resulting from reduction of costs to provide better aviation services and to increase innovation. A vertical merger may also cause the decrease in prices due to the reduction of supply costs. Vertical mergers may also increase the incentive of a merger party to compete in a relevant aviation service market and thus increase the level of rivalry therein. These benefits of vertical mergers may ultimately enhance consumer welfare.

8.3 However, vertical mergers may in some circumstances reduce the competitive constraints faced by a merger party giving rise to unilateral effects¹² and coordinated effects¹³.

8.4 The competition concerns arising from vertical mergers are likely to be different from those of horizontal mergers. Vertical mergers do not involve a direct loss of competition between enterprises in the same relevant aviation service market and are unlikely to result in an SLC unless market power exists in the said market at any level of the supply chain.

Unilateral Effects

8.5 A vertical merger may give rise to unilateral effects by way of foreclosing competing enterprises in any aviation service market.

¹² Unilateral effects such as market foreclosure.

¹³ Coordinated effects such as increasing the ability and incentive of the merging enterprises to collude in a relevant aviation service market.

8.6 Such market foreclosure may occur in many ways including in the following situations:

- (a) If a merger party is an important buyer for an aviation service that it also provides, it may be able to dampen competition from competing providers of the latter aviation service in certain circumstances. For example, this could occur by sourcing its future needs entirely from its own upstream operation which may jeopardise the continued existence of alternative providers of that aviation service.
- (b) If a merger party provides a large proportion of an important aviation service to another aviation service market where it also competes, it may be able to dampen competition from its competitors in the latter market. This may occur by way of diverting its provision of the aviation services entirely to its own downstream operation.
- (c) If a merger party refuses to supply an aviation service to its competitors in another aviation service market or sells the aviation service to its competitors at a price that makes them uncompetitive, it may affect competition or foreclose that market to the competitors.
- (d) If a merger party controls an essential facility to an aviation service market, it might be able to reduce competition from its competitors by refusing to provide them with access to that essential facility. The merger party may also place competitors at a cost disadvantage by granting access only at discriminatory prices that favour the merger party's own business.

8.7 A merger is more likely to have the effect of market foreclosure if a merger party has market power in at least one of the relevant aviation service markets involved in that merger. If a merger party does not possess market power, its competitors could switch to other aviation service providers or buyers and hamper any market foreclosure effect arising from the merger.

8.8 Consideration may be given to whether a merger party has any incentive to foreclose competition and the likely effect of that foreclosure on competition i.e. whether the foreclosure would be profitable to the merger party. In certain cases where market foreclosure may not be profitable, a merger party may lack the incentive to foreclose the market to its competitors. For example, if a merger party refuses to supply an aviation service to its competitors in another aviation service market, the merger party's decrease in profits due to the loss of buyers may not be proportionate to the its increase in profits in the other aviation service market. In such a situation, it would be unlikely for the merger party to foreclose the market due to the lack of commercial incentives even if it is able to do so.

8.9 Consideration may also be given to the effect of a potential market foreclosure on competition in a relevant aviation service market. This includes the effect of the foreclosure to the ability of competing enterprises to enter the relevant aviation service market or expand their operations and the ability of competing enterprises to provide competitive constraints to the merger party. It is not necessary for the market foreclosure to force the competing enterprises to exit the relevant aviation service market in order for a merger to have the effect of an SLC in that market.

Coordinated Effects

8.10 A vertical merger may have coordinated effects although such occurrence may be rare. Coordinated effects arising from a vertical merger may occur in many ways including the following:

- (a) A vertical merger may allow a merger party to gain access to commercially sensitive information about the activities of other enterprises in a relevant aviation service market which may facilitate coordinated behaviour by the merger parties.

- (b) A vertical merger that results in market foreclosure may reduce the number of enterprises in a relevant aviation service market to an extent that it is easier for the remaining enterprises to coordinate their behaviour in that market.
- (c) A vertical merger may increase the level of symmetry or transparency in a relevant aviation service market. For example, a merger party may acquire better knowledge of the selling prices in upstream or downstream aviation service markets resulting from a vertical merger which may facilitate coordination in either the upstream or downstream aviation service markets.
- (d) A vertical merger may facilitate coordination by increasing barriers to entry or reducing buyer power thus reducing the possibility of disruption of such coordination by a new entrant or a strong buyer in a relevant aviation service market.
- (e) A vertical merger may make it easier for enterprises to punish or incentivise coordination with the presence of a merger party that possesses market power in one or more aviation service markets.

8.11 In assessing the coordinated effects of a vertical merger, all relevant factors would be considered including —

- (a) the relationship between the merger parties before and after the merger;
- (b) the extent of vertical integration in a relevant aviation service market before and after the merger and whether the vertical integration involves competing enterprises;
- (c) the market shares of merger parties in the upstream and downstream aviation service markets;

- (d) the existence of any supply arrangements between the merger parties;
and

- (e) the characteristics of the aviation service markets such as the transparency of information.

9. Competitive Effects Arising from Conglomerate Mergers

9.1 As stated in paragraph 3.7, a conglomerate merger refers to a merger between enterprises that operate in different markets.

9.2 In general, a conglomerate merger is less likely to give rise to an SLC. However, a conglomerate merger may result in an SLC where the merger strengthens a merger party's portfolio power or market power derived from a portfolio of brands that it possesses and services that it provides. This often arises in mergers between enterprises that provide complementary services or services that are generally provided to the same set of buyers.

Unilateral Effects

9.3 A conglomerate merger may give rise to unilateral effects where the merger allows a merger party to strengthen its market positions or market power through tying¹⁴ or bundling¹⁵ practices. Such practices may result in the foreclosure of a relevant market to competing enterprises.

9.4 However, the unilateral effects arising from a conglomerate merger are only likely in situations where it is difficult for existing enterprises in the relevant aviation service market or new entrants to the said market to provide competing bundled or tied services or pose a competitive constraint upon a merger party. Similar to vertical mergers, the analysis of unilateral effects of a conglomerate merger would include the assessment of the merger party's ability and incentive to foreclose competition in a relevant aviation service market.

¹⁴ Tying occurs when an enterprise refuses to provide a service unless the buyer also acquires another service from it.

¹⁵ Bundling refers to the conduct of an enterprise that sells services that are bundled together at a price that is much lower compared to the total price of the services if they are acquired separately.

Coordinated Effects

9.5 A conglomerate merger may increase the potential for coordination especially where the merger party's competitors in one aviation service market are also its competitors in another market. The assessment of coordinated effects arising from a conglomerate merger is similar to that of a horizontal merger.

10. Entry and Expansion

10.1 Anti-competitive effects of a merger elaborated in Parts 7 to 9 of these Guidelines may be reduced by the entry of new competitors into a relevant market or by the expansion of operation by existing competitors.

Entry by a New Competitor

10.2 The entry or potential entry of a new competitor may pose competitive constraints on existing enterprises in a relevant aviation service market. In a relevant aviation service market where entry by a new competitor is likely and could occur easily and in a timely manner, it may be more difficult for a merger party to exercise market power and profitably increase prices, reduce capacity or adjust trading terms in a sustainable manner.

10.3 The entry of a new competitor into a relevant aviation service market or the threat thereof may impose sufficient competitive constraint where the entry is likely, sufficient in extent and timely.

10.4 The likelihood of a new competitor to enter a relevant aviation service market may be assessed by the existence or degree of barriers to entry to the said market including sunk costs, economies of scale or scope, regulated entry or access to essential facilities. Consideration may also be given to the experience of other enterprises that have entered or exited from the relevant aviation service market in the recent years and any planned entry by a new competitor.

10.5 Any entry by a new competitor must be of sufficient scope to pose competitive constraints upon a merger party and prevent such merger from resulting in an SLC.

10.6 The timeliness of the entry of a new competitor is vital in order to pose competitive constraint upon a merger party in response to any attempt by the merger

party to exercise its market power. The new entrant should also have a staying power to provide effective post-merger competition in a relevant aviation service market.

10.7 In addition, consideration may also be given to the effect of a merger on the likelihood of a new competitor to enter a relevant aviation service market. A merger may increase barriers to entry. A merger may also reduce or eliminate the competitive constraint represented by new entry especially if the merger involves the acquisition of an enterprise that was perceived as a potential new entrant or competitor.

10.8 In addition, a vertical merger may create barriers to entry in situations where —

- (a) the degree of vertical integration between the two aviation service markets is so extensive that an enterprise that enters into one aviation service market would also have to enter into the other aviation service market simultaneously in order to compete effectively in the former market;
- (b) the requirement of entry into the latter aviation service market makes entry at the former aviation service market significantly more difficult and less likely to occur; or
- (c) the structure and characteristics of the former aviation service market is so conducive to anti-competitive behaviour such as collusion that the increased difficulty of entry is likely to affect the aviation service market's performance.

10.9 With regards to a conglomerate merger, the possibility of any entry constraining a merger party may be assessed by considering whether another enterprise could replicate the portfolio of services offered by the merger party. Consideration may also be given to whether the creation of the portfolio of services itself represents a strategic barrier to entry and could limit the ability of competitors to either extend their portfolios or to enter new aviation service markets.

Expansion of Operation by an Existing Competitor

10.10 Another important competitive constraint on the post-merger behaviour of a merger party is the ability of the competing enterprises in a relevant aviation service market to expand their capacity quickly. The factors influencing the ability of an existing competitor to expand its capacity are similar to those influencing the ability of a new competitor to enter a relevant aviation service market in particular whether expansion by an existing competitor is likely, sufficient in extent and timely.

11. Countervailing Buyer Power

11.1 Countervailing buyer power refers to the bargaining strength of the buyer relative to a merger party due to the size and commercial significance of the buyer and the ability of the buyer to switch to other competing enterprises that compete with the merging enterprise. Countervailing buyer power may be possessed by one or more buyers.

11.2 Countervailing buyer power could constrain or considerably diminish the ability of a merger party to charge high prices, lower supply or set trading terms. For example, if a merger party increases its prices, a powerful buyer of the merger party's aviation services may switch or threaten to switch to those of a competing enterprise.

11.3 Even where buyers have no choice but to purchase the aviation services from a merger party, the buyers may still be able to constrain prices if they are able to impose substantial costs on the merger party such as by —

- (a) refusing to buy other services or products provided by the merger party;
- (b) delaying purchases or payments;
- (c) threatening to enter the relevant aviation service market themselves or sponsor market entry by offering a new entrant a long-term contract to cover the entry costs; or
- (d) increasing competition amongst the competing enterprises by establishing a competitive tender for purchases of aviation services.

11.4 The evaluation of countervailing buyer power as part of a merger assessment may include the following considerations:

- (a) whether there is sufficiently strong bargaining position held by a buyer or buyers in a relevant aviation service market;
- (b) the extent to which the countervailing buyer power may change post-merger; and
- (c) whether the countervailing buyer power is sufficient to prevent an SLC in that post-merger aviation service market.

11.5 Amongst factors that may be considered in assessing the considerations stated in paragraph 11.4 are —

- (a) the existence and degree of buyers switching between the merger parties during the pre-merger period;
- (b) the existence and degree of buyers switching to other enterprises that provide similar or substitutable services during the pre-merger period;
- (c) the proportion of revenue attributed to large buyers of a merger party;
- (d) past negotiations between buyers and a merger party including in terms of price or quality of service;
- (e) whether a buyer has a large volume order such that it could or has sponsored entry for a potential competitor that is not currently in the relevant aviation service market;
- (f) consideration by and commercial viability of buyers executing vertical integration or sponsoring any new entry; and
- (g) history of buyers successfully hampering attempts by an enterprise in a relevant aviation service market to raise prices or exercise market power and whether such buyer power would be changed by a merger.

11.6 With regard to countervailing buyer power in relation to a conglomerate merger, consideration may also be given to the incentives of buyers to acquire the portfolio services from a single enterprise. In a situation where buyers can and do source the portfolio services from multiple enterprises and are likely to continue to do so after a merger, it is unlikely that the merger would substantially lessen competition.

12. Economic Efficiencies and Social Benefits

12.1 Parts 7 to 11 of these Guidelines elaborate on possible anti-competitive effects of a merger and factors that may lessen or enhance those effects. However, while a merger may harm competition, it may also give rise to economic efficiencies or social benefits.

12.2 With regard to a notification of a merger, subparagraphs 55(2)(b)(i) and 56(2)(b)(i) of the Act provide that the Commission may make a decision that the prohibition in section 54 of the Act has not or will not be infringed because of the effect of an exclusion. A merger that has resulted or may be expected to result in an SLC in any aviation service market may be allowed by way of an exclusion if there are significant economic efficiencies or social benefits arising directly from the merger that outweigh such SLC.

Economic Efficiencies

12.3 A merger party may claim that there are significant economic efficiencies arising directly from the merger including supply-side or demand-side efficiencies that outweigh the merger's SLC in an aviation service market.

12.4 Supply-side efficiencies arise if a merger party could supply its services at lower cost as a result of the merger compared to the merger parties operating separately prior to the merger.

12.5 Examples of supply-side efficiencies include the following:

(a) Cost reduction

- Cost reduction may arise from horizontal, vertical or conglomerate mergers resulting from economies of scale or economies of scope.

- Cost reduction may also result from more efficient processes or working methods across a portfolio of services.
- The claims of efficiencies by way of cost reduction and the extent to which it would stimulate competition or lower prices made available to buyers may be considered. For example, a merger between two of the smaller enterprises in a relevant aviation service market could gain such efficiencies through merger and thus exert greater competitive pressure on larger competitors in that market.
- Cost savings that are only likely to translate into increased profits for the merger parties may not be given much consideration as efficiencies.

(b) Removal of double marginalisation in vertical mergers

- A vertical merger may enable and incentivise a merger party to eliminate double marginalisation of profits in different levels of a supply chain that would be present during pre-merger period.

(c) Increase in investment

- For example, a vertical merger may incentivise a merger party to make investments in new products, processes or commercial strategies.

(d) Differentiation of aviation services

- A horizontal merger may result in merger parties increasing the level of differentiation of aviation services they provide. This may be done in order to reduce cannibalisation between the aviation services of the merger parties and to penetrate into different segments of a relevant aviation service market. The other competing enterprises

may also respond by further differentiating the aviation services that they offer in order to effectively compete with the merger parties. As a result, the number of variety and choices of aviation services made available to buyers would increase.

- However, differentiation of aviation services may also have negative effects on a relevant aviation service market by reducing substitutability between aviation services offered by the merger parties and reducing price competition between the aviation services. This is due to the fact that it is harder to compare prices between differentiated services as compared to homogenous services. The merger may allow a merger party to profitably increase price in one aviation service since any loss of sales due to the price increase in one aviation service may be captured by the increase in sales of the other competing aviation service provided by a merger party.
- The effect of differentiation of aviation services and the extent to which it would increase efficiencies would be determined on a case by case basis.

(e) Increase in capacity and network of aviation services

- A merger may increase economies of scale or economies of scope which allows the merging enterprise to expand the capacity and network of aviation services made available to buyers.
- For example, a merger between two airlines may allow a merger party to commence scheduled air transport services on a route that would be too thin to be viable for an individual airline. The merger party could also expand the network of flights offered or increase capacity at a lower cost.

12.6 Demand-side efficiencies arise if a merger party's aviation services become more attractive to buyers as a result of the merger.

12.7 Examples of demand-side efficiencies include the following:

(a) Increased network of aviation services available to buyers

- A merger may result in better and more expansive aviation services made available to buyers. For example, a merger between airlines may open up new routes to passengers allowing a new seamless network of flights. However, in such a situation, the merger parties would need to prove that the efficiencies are merger-specific and could not have been achieved through other means.

(b) Price effects of complementary aviation services

- A merger may result in merging enterprises offering lower prices for complementary aviation services as compared to the prices previously charged by different enterprises.

(c) Benefits of "one-stop shopping"

- Demand-side efficiencies may arise when a merger party's aviation services are not substitutes for each other and buyers may have a stronger incentive to buy a range of services from the merger party due to reduction of transaction costs or increased quality assurance.

Social Benefits

12.8 A merger party may claim that there are significant social benefits arising directly from the merger that may offset the merger's SLC effect. This is consistent

with the fair competition principle that guides the Commission's application of the competition provisions under Part VII of the Act.

12.9 However, it is emphasised that any claim of significant social benefits arising directly from a merger should be examined strictly. The term "social benefits" would be interpreted based on —

- (a) the relevant policy objectives of the Act such as improvement of connectivity as provided in subparagraph 17(1)(a)(i) of the Act; or
- (b) any other relevant public policy objectives such as environmental protection, health, safety and employment.

Substantiating Claims of Economic Efficiencies or Social Benefits

12.10 A merger party claiming significant economic efficiencies or social benefits arising from a merger shall identify and provide evidence on the nature of the economic efficiencies or social benefits such as —

- (a) the type of economic efficiencies or social benefits;
- (b) how the economic efficiencies or social benefits would be achieved;
- (c) whether the economic efficiencies or social benefits are timely or would occur within a reasonable period of time;
- (d) whether the economic efficiencies or social benefits are likely and sufficient to prevent or remedy an SLC;
- (e) whether the economic efficiencies or social benefits would only occur as a result of the merger and could not have been attained by any other feasible means that would pose less competitive concerns; and

- (f) the magnitude of the economic efficiencies or social benefits.

12.11 Any claim of economic efficiencies or social benefits that are vague, speculative or unsubstantiated would be rejected.

12.12 The determination of whether a merger that has resulted or may be expected to result in an SLC should be allowed by way of an exclusion requires the weighing of claims of efficiencies or social benefits arising from a merger against the merger's SLC effect. In this regard, to the extent possible, merger parties should provide data to support any monetary or numerical estimates of the value of the economic efficiencies or social benefits and the merger's effects on competition together with the assumptions and reasoning upon which the data relies. Without the detail and transparency behind the modelling used in the calculations, little weight will be placed on the claims of economic efficiencies or social benefits.

12.13 In cases where it is not possible to credibly quantify the economic efficiencies or social benefits and the effect of a merger on competition, a qualitative assessment will be carried out. A sufficient basis must be provided by a merger party to support any claim for the existence and size of the economic efficiencies or social benefits and the SLC effect of the merger.

13. Glossary

1. Act Malaysian Aviation Commission Act 2015 [Act 771].
2. buyer A consumer, or an enterprise that acquires or uses any aviation service primarily for the purpose of resupplying the service or providing any aviation service.
3. Commission Malaysian Aviation Commission.
4. Guidelines Guidelines on Substantive Assessment of Mergers.
5. HHI Herfindahl-Hirschman Index.
6. market power The ability of an enterprise to adjust prices or outputs or trading terms without effective constraint from competitors or potential competitors in a relevant aviation service market.
7. merger party An enterprise that is a party to an anticipated merger or a party involved in a merger. This may refer to an enterprise that merges with another enterprise, an enterprise that acquires another enterprise, an enterprise that is acquired by another enterprise or the merged entity, whichever is applicable.
8. merger parties All enterprises that are parties to an anticipated merger or parties involved in a merger.

