Merger assessment guidelines

Draft for public consultation

20 March 2025

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Australian Competition and Consumer Commission
Land of the Ngunnawal people
23 Marcus Clarke Street, Canberra, Australian Capital Territory, 2601

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Foreword

On 10 December 2024, the Australian Parliament passed significant reforms to the *Competition and Consumer Act 2010 (Cth)* (the Act) in relation to merger control.[1]

The key objective of merger control is to enable the Australian Competition and Consumer Commission (ACCC) to prevent anti-competitive mergers and acquisitions from proceeding.[2] Under the merger control regime, merger parties must notify the ACCC of certain acquisitions that meet applicable notification thresholds or fall into specified classes. The ACCC retains the ability to investigate and take enforcement action against any merger that is not notified if it is likely to substantially lessen competition.

The merger reforms represent a major change to the process that the ACCC uses for assessing mergers affecting Australia.

The ACCC's substantive approach continues to involve testing whether the merger, if put into effect, would have the effect, or be likely to have the effect, of substantially lessening competition in any market. The merger reforms clarify that a substantial lessening of competition can include creating, strengthening or entrenching a substantial degree of power in a market.

If the ACCC determines that a merger may not be put into effect because it is likely to substantially lessen competition, or may be put into effect only with conditions, a merger party may apply for a determination that the merger should be allowed to proceed on the basis of a net public benefit.

The purpose of these guidelines is to explain our approach to analysing the potential effects of mergers on competition. This should provide predictability to businesses, their advisers, and the community as to how the ACCC will apply the substantial lessening of competition test and the net public benefit test in different merger situations.

In preparing these guidelines, we've drawn on our experience analysing the competitive effects of mergers, the latest economic literature, decisions of Australian courts and tribunals and the work done by relevant international bodies, such as the Organisation for Economic Co-operation and Development Competition Committee.

The general principles set out in these guidelines provide the analytical framework for assessing whether a merger is likely to substantially lessen competition or result in a net public benefit. Each assessment will, however, depend on the application of the analytical framework to the relevant facts.

It isn't possible for these guidelines to cover every issue or circumstance that may arise. In practice, individual mergers involve a variety of facts and situations, and our analysis will be tailored to the specific circumstances of the merger under assessment. We will apply these guidelines in a way that is consistent with our statutory role and provides flexibility for individual circumstances.

These guidelines replace the merger guidelines (2008) and merger authorisation guidelines (2018), and should be read together with the merger process guidelines (2025). They reflect the ACCC's analytical approach at the time of publication and may be revised periodically,

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1 *Treasury Laws Amendment (Mergers and Acquisitions Reform) Act 2024*, 10 December 2024.

2 In these guidelines, the term 'acquisitions' includes mergers, and we refer to mergers and acquisitions interchangeably.

based on new legal precedent, evolving insight and best practice. The latest version of the guidelines will be the version published on the ACCC website.

Overview of merger assessment

Why merger scrutiny is important

The purpose of the Act is to enhance the welfare of Australians through the promotion of competition and fair trading, and provision for consumer protection.[3] Preventing anti-competitive mergers is an important aspect of this objective.

As noted in the explanatory memorandum outlining the changes to Australia's merger control regime:

> While most acquisitions are unlikely to raise competition concerns, some can harm competition, which can lead to businesses increasing prices for consumers and not passing economic gains on to consumers. Australia's merger control framework plays a crucial gatekeeper role in focusing on preventing the small number of acquisitions that could substantially lessen competition, thereby harming consumers and the wider economy.[4]

Competition between businesses puts pressure on them to lower their prices, offer quality goods and services, increase the choices available, create product features that consumers value, innovate and be more efficient. The more intense the competition, the more likely it is that businesses will pursue profits in a way that works in the best interests of consumers.

Mergers are important for the efficient functioning of our open market economy. They allow businesses to achieve greater economies of scale, and to access new resources, technology and expertise.[5] Most mergers pose little or no risk to competition and are unlikely to harm consumers. In fact, many mergers are pro-competitive and enhance consumer welfare. The merger control regime aims to focus on the small number of mergers that undermine the competitive process and risk significant consumer detriment.

As was held by the Trade Practices Tribunal (now the Australian Competition Tribunal) in *QCMA*, 'the antithesis of competition is undue market power, in the sense of the power to raise price and exclude entry'.[6] A firm with market power:

- faces fewer competitive pressures
- has greater incentive and ability to increase prices or worsen non-price aspects of its goods or services offer
- has more reason, and sometimes more ability, to exclude rivals from entering the market, or hinder them from competing effectively.

In some cases, a firm may attain market power via an acquisition; in other cases a firm may already have market power, and have it strengthened or entrenched through an acquisition.

The Act prohibits mergers that substantially lessen competition.[7] The concept of a substantial lessening of competition does not mean a large or weighty lessening of competition, but one that is 'real or of substance' and thereby meaningful and relevant to the

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3 *Competition and Consumer Act 2010 (Cth)*, s 2.

4 Explanatory Memorandum to *Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024*, para 1.6.

5 Treasury, 'Merger Reform: A Faster, Stronger and Simpler System for a More Competitive Economy', 10 April 2024.

6 *Re Queensland Co-Op Milling Association Limited and Defiance Holdings Limited (QCMA)* (1976) 8 ALR 481, 512 [5].

7 *Competition and Consumer Act 2010 (Cth)*, s 51ABZH(1).

competitive process.[8] The harm to the competitive process may take various forms, including increased prices, reduced output, poorer quality, less choice or stifled innovation.

The ACCC is the administrative decision-maker at first instance for all acquisitions notified under the formal merger control regime. We may also investigate mergers, including completed mergers, that are not notified but are likely to substantially lessen competition for potential enforcement action under section 50 of the Act.

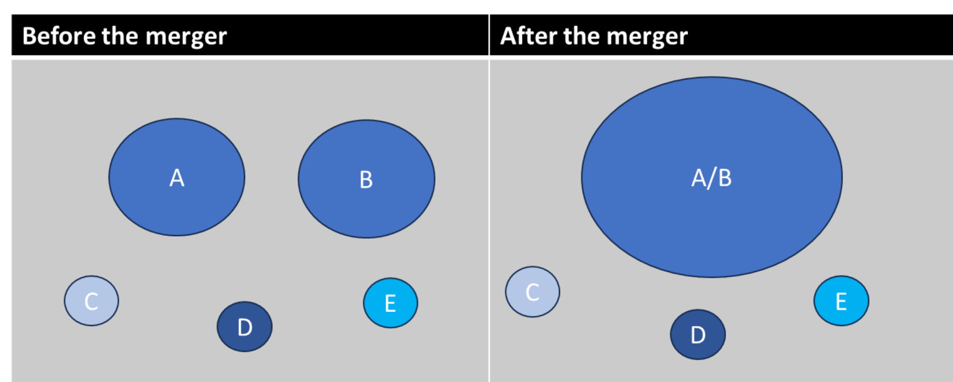
How mergers can raise competition concerns

Different mergers raise different competition risks, and the level of risk that each merger presents will be unique. Although each merger requires individual analysis, we explain below how some situations can raise competition concerns:

- a merger between close competitors
- a merger in a concentrated market
- an acquisition of a potential competitor
- an acquisition that restricts rivals' access to inputs, facilities or customers
- a merger involving the linking of goods or services
- a firm repeatedly acquiring smaller firms.

The examples below focus on the potential risks to competition that certain merger situations can present. In practice, if the ACCC identifies competition concerns with a merger, we will consider whether there are countervailing factors that are relevant to the competitive process. These include the entry or expansion by rivals, the countervailing power of customers, and rivalry-enhancing efficiencies. Countervailing factors are discussed in detail in Chapter 6.

A merger between close competitors



An example of a merger between close competitors is a merger between 2 suppliers of bread (A and B). The suppliers may be close competitors because they supply a similar quality product (e.g. long-lasting white sliced bread), or because they supply to similar locations. Although these 2 suppliers may face some competition from other suppliers of bread (C, D and E), the most important competitive constraint on A is B and vice versa.

[8] *Pacific National v Australian Competition and Consumer Commission* (2020) 277 FCR 49, [104].

Before the merger

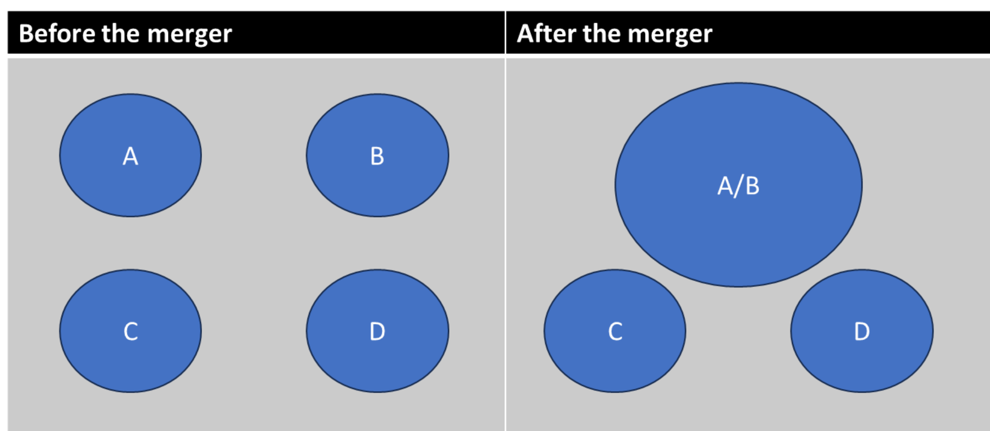
If supplier A considered raising its prices, it would face a trade-off between the increased profits from the higher margins it would earn on sales it would continue to make, and the decreased profits from the loss of margins on sales it would no longer make. This includes sales that are lost because customers might switch to other suppliers, including supplier B.

If A and B are close competitors—that is, if customers consider the bread supplied by these 2 suppliers to be close substitutes—the potential decrease in profits from customers switching to B will be greater. The risk of significant switching by customers helps to deter both suppliers from increasing their prices.

After the merger

If supplier A acquired supplier B, the constraint the suppliers exerted on each other, which deterred them from increasing their prices, would disappear. The closer the competition between A and B pre-merger, the greater the merged firm's incentive to increase prices post-merger.

A merger in a concentrated market



An example of a merger in a concentrated market is a merger between 2 of the 4 largest suppliers of cars. Even though there may be some other smaller suppliers of cars, the 4 firms (A, B, C and D) account for most of the total market for cars.

Before the merger

If supplier A considered increasing its prices, it would face a trade-off between the increased profits from the higher margins it would earn on sales it would continue to make, and the decreased profits from the loss of margins on sales it would no longer make. This includes sales that are lost because customers might switch to the other 3 large suppliers.

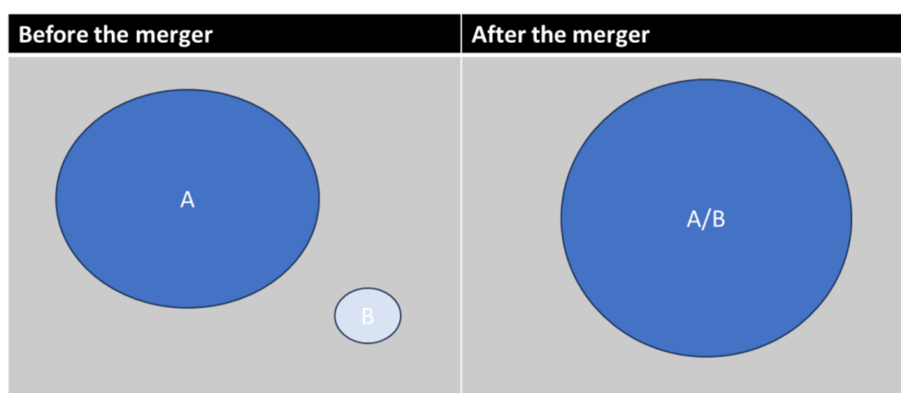
After the merger

If supplier A acquired supplier B, and considered raising its prices, the trade-off would change, since the potential decrease in profits would be reduced, as customers would have fewer suppliers to switch to. The merged firm would then have a greater incentive to increase prices.

The loss of competition between the merger parties may also provide an impetus for C and D to increase their prices as well. This risk is higher in a concentrated market because the loss of competition between 2 out of 4 suppliers significantly reduces the competitive constraints across the whole market.

Moreover, in markets with only a few suppliers that collectively account for a large portion of total supply, there may be an increased risk of the suppliers coordinating.

An acquisition of a potential or nascent competitor



An example of a merger involving a potential competitor is an established supplier of solar batteries (A) acquiring a startup company that is developing a competing solar battery (B).

Before the acquisition

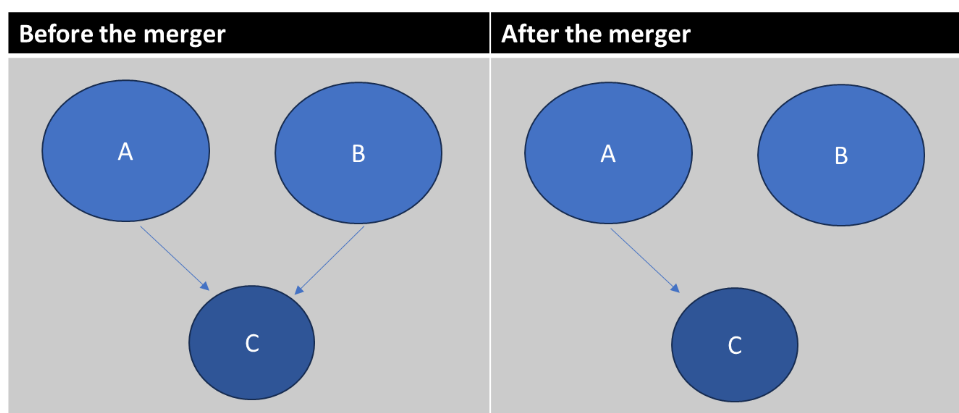
While supplier B may be small, or may have not yet entered the market, if supplier A increases its prices for solar batteries, that may provide B with the impetus to grow or enter. The prospect of this happening will constrain A from increasing its prices. In other words, even though B is not currently a close competitor to A, the potential that it will grow and become a close competitor has a constraining effect on A.

After the acquisition

If supplier A acquired supplier B, that will prevent the potential for B to enter or expand in a way that might have otherwise increased competition. A may acquire B to neutralise the competitive threat it poses, and to strengthen or entrench its position in the market.[9]

[9] In some situations, it is the startup that acquires the established company, which can have the same anti-competitive effect.

An acquisition that restricts rivals' access to inputs, facilities or customers



An example of a merger that could restrict rivals' access to inputs, facilities or customers is a manufacturer of bicycles (A) acquiring a distributor of bicycles (C) in circumstances where A's close competitor, B, also uses C to distribute its bicycles.

Before the acquisition

Distributor C will have a commercial incentive to obtain supply from multiple manufacturers, to offer a range of bicycles and to maximise sales.

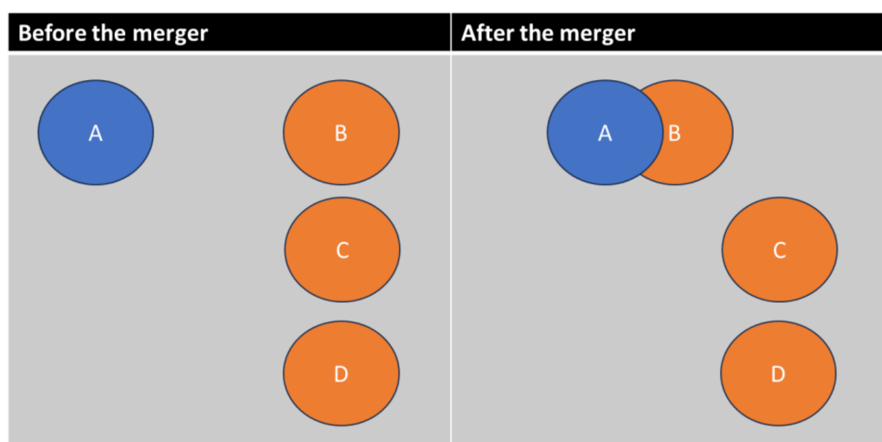
After the acquisition

If manufacturer A acquired distributor C, the merged firm may have the ability and incentive to limit manufacturer B's access to distributor C. If C is an important distribution channel for B, the effect of limiting B's access to C may be that B becomes unprofitable and exits the market, or otherwise becomes a less effective competitor.

Another issue may be that because of the distribution relationship between B and C, manufacturer A may gain insight into B's manufacturing plans (e.g. a new range of bicycles). This may allow it to use that information in its own manufacturing business, and the effect may be to undermine B's competitiveness.

A merger that increases the ability and incentives on the merged firm to discriminate against rivals or that gives the merged firm access to competitively significant information about rivals is more likely to raise competition concerns. The risk to competition in cases of this kind is that the merged firm may act in a way that has the effect of limiting rivals from competing effectively.

A merger involving the linking of goods or services



An example of a merger involving the potential linking of sales is a supplier of a real estate listings platform (A) acquiring a supplier of data analytics services (B), in circumstances where real estate agents often purchase both listings and data analytics services.

Before the merger

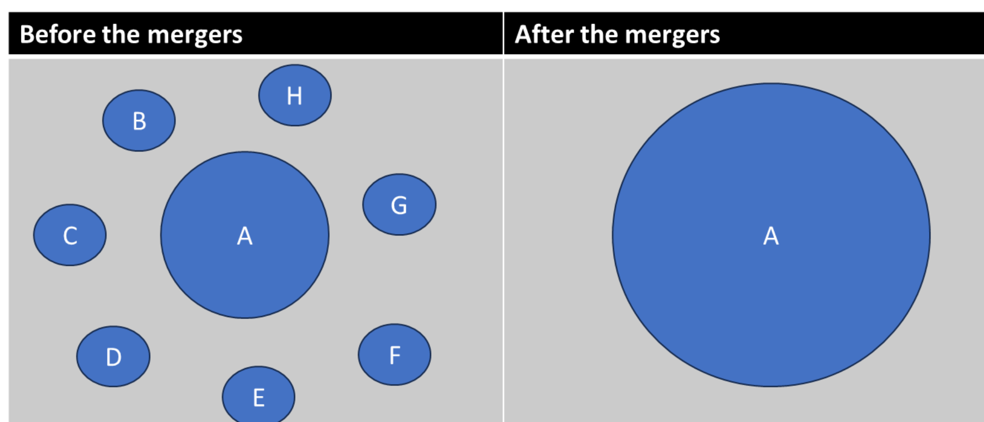
Platform A will have a commercial incentive to supply a real estate platform that real estate agents and potential property purchasers want. This may include offering attractive product features, such as making the platform compatible with a range of data analytics services.

After the merger

If platform A acquired service B, the merged firm could link its data analytics services to its platform, for instance, by making the platform only operable with B, by offering listings and analytics as a package for a lower price, or by only selling listings on the condition that customers also buy its data analytics service.

The merger may substantially lessen competition if the linking of the platform and the service prevents other data analytics service suppliers (C and D) from competing effectively. This could be the case if A's platform is a 'must-have' or is otherwise especially important to real estate agents, and the market that remains for analytics suppliers, such as C and D, is too small for them to compete effectively.

A firm serially acquiring smaller firms



An example of a firm serially acquiring smaller firms is a supplier of medicines periodically acquiring small competing suppliers of similar medicines (B, C, D, and so on).

Before the mergers

If supplier A considered increasing its prices, it would face the risk that customers might switch to the other small suppliers. While each small supplier may only exert a weak constraint on supplier A, cumulatively, they may exert a strong constraint. The small suppliers may also grow into larger suppliers, and become stronger competitors, as they attract more customers.

After the mergers

If supplier A acquires a series of small competitors, that may allow A to strengthen or entrench a substantial degree of power in the market. While each individual acquisition may not substantially lessen competition, the series of acquisitions may do so.

The ACCC may treat the effect of an acquisition as being the combined effects of the acquisition and any one or more acquisitions that were put into effect during the last 3 years.[10]

Guideline summary

These are the topics covered in each chapter of the guidelines. Depending on the merger under review, we may place more emphasis on some aspects of the guidelines than on others.

- Chapter 1 – Analytical framework: the competitive process, how mergers can lessen competition, the forward-looking nature of the assessment, types of mergers that the ACCC commonly reviews, the meaning of a 'market', the importance of concentration to merger analysis, and the clarification of the substantial lessening of competition test.
- Chapter 2 – Mergers between competitors: unilateral effects: factors the ACCC may consider when assessing the risk of unilateral effects arising from mergers between competitors, in particular the closeness of competition between the merger parties and the effectiveness of remaining rivals.
- Chapter 3 – Coordinated effects: factors the ACCC may consider when assessing the risk of coordinated effects, in particular whether the market is vulnerable to coordination, the incentives on firms to deviate from coordination, the risk of retaliation from deviation, and evidence of past coordination.
- Chapter 4 – Non-horizontal mergers: vertical effects and conglomerate effects: factors the ACCC may consider when assessing the risk of vertical or conglomerate effects arising from mergers involving businesses that are not direct competitors, in particular, the risk of foreclosing effective competitors, and the risk of leveraging power from one market to another.
- Chapter 5 – Specific merger issues: factors the ACCC may consider when assessing mergers involving a vigorous and effective competitor, mergers that eliminate potential competition, mergers involving competing buyers, mergers involving multi-sided platforms, mergers involving pricing across local or multiple markets, and mergers involving serial or partial acquisitions.

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10 *Competition and Consumer Act 2010*, s 51ABZH(6).

- Chapter 6 – Countervailing factors: countervailing factors the ACCC may consider if we identify competition concerns with a merger, including the potential for new entry or expansion by rivals, the potential countervailing power of customers, and the potential for the merger to create rivalry-enhancing efficiencies.
- Chapter 7 – Public benefits and detriments: factors the ACCC may consider if a merger party submits that the merger will result in a net public benefit.

The guidelines include appendices with more detailed information on certain aspects of merger analysis.

- Appendix 1 – Market definition tools: the tools the ACCC may use to define markets and measure concentration, and the ACCC's approach to specific issues that may arise in the context of market definition.
- Appendix 2 – Counterfactual analysis: how the ACCC identifies relevant counterfactuals when applying the 'future with and without' test.

1. Analytical framework

Competition is a process of rivalry

1.1. Competition expresses itself as rivalrous behaviour between firms to win and retain customers, and takes many forms – rivalry in terms of price, service, innovation, quality, and other factors. In a competitive market, firms engage in a continual process of improvement, experimentation, and innovation. A firm may change its pricing or product range, it may research and develop new goods or services, or it may improve efficiency in its supply chains. In response to these changes, the firm's competitors must change too, because if they stand still, they risk losing customers. Dynamic competition between firms changes market configurations over time, as firms enter, expand, merge and exit. Suppliers, intermediate buyers, and end consumers benefit from the process of competition, as firms become more efficient, agile and responsive to their demands.

1.2. One of the key mechanisms of competition is substitution:

- from a customer's perspective, by switching from one supplier to another
- from a supplier's perspective, by supplying products to customers in place of a competitor's supply.

1.3. Competing suppliers strive to bring about substitution by increasing their economic efficiency in three main ways:

- by reducing their costs of production (productive efficiency)
- by selling a larger volume of products customers want at lower prices (allocative efficiency)
- by investing in innovation with the object of creating new products that better meet the needs and wants of customers (dynamic efficiency).[11]

1.4. Both price and non-price aspects of competition are integral to the competitive process. For example, professional services firms may primarily compete on quality and experience, retailers may focus on offering the broadest range of goods or the best customer service, and digital platforms may attract users through offering the most innovative services.

1.5. Anything of value to customers is a potential point of differentiation in the competitive process. Customers may value locally based customer service, enhanced interoperability (particularly in the digital sector), a diverse range of goods or services, more staff in stores, generous returns or price-matching policies, enhanced levels of

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[11] *ACCC v BlueScope Steel Limited (No 5)* [2022] FCA 1475, [127].

privacy, or environmental sustainability. In some markets, non-price competition may be the key feature of competition.

How mergers can lessen competition

1.6. In *QCMA,* the Trade Practices Tribunal held that 'the antithesis of competition is undue market power, in the sense of the power to raise price and exclude entry.'[12] A firm with market power can act with a degree of freedom from competitors, potential competitors, suppliers and customers.[13] In other words, a firm has market power when it can 'give less and charge more'.[14]

1.7. Not all mergers that lessen competition are prohibited by the Act; only those that are likely to lessen competition substantially. Synthesising previous authorities, in *ACCC v Pacific National*, Justice Beach held that:

> [T]he concept of substantially lessening competition does not require a large or weighty lessening of competition, but only one that is meaningful and relevant to the competitive process. A short-term effect readily corrected by market processes is not substantial in this respect. But a medium to long term effect not easily corrected may amount to a substantial lessening of competition.[15]

1.8. The concept of a substantial lessening of competition is not fixed, but relative. In some cases, a firm may attain market power via an acquisition, in other cases, a firm may already have market power, and an acquisition may strengthen or entrench that power. The more market power one party already has, the more likely it is that a merger will entrench that market power and be a 'substantial' lessening of competition.

1.9. Moreover, the process of competition is not static, but dynamic. A merger can result in longer-term harm to competition, even when there is no immediate adverse impact on customers, or it initially provides some short-term benefits, such as lower prices. The ACCC will consider not just the immediate impact of the merger on customers, but also on industry dynamics and the competitive process over the long-term.

The forward-looking nature of the assessment

1.10. Merger control is a kind of competition risk management policy, and the application of that policy occurs in the real world.[16] A merger assessment is a forward-looking exercise in which the ACCC assesses the effect or likely effect of the merger on the

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[12] *Re Queensland Co-Op Milling Association Limited and Defiance Holdings Limited (QCMA)* (1976) 8 ALR 481, 512 [5].

[13] Guidelines on misuse of market power, para 2.14. See also *Boral Besser Masonry Ltd v ACCC* [2003] HCA 5; 215 CLR 374, [121] (Gleeson CJ and Callinan J).

[14] The source of the phrase "giving less or charging more" is the US Attorney-General's National Committee to Study the Antitrust Laws in its Report of 1955 (at 320) and approved by the Tribunal in *Re Queensland Co-operative Milling Association Ltd and Defiance Holdings* (1976) 25 FLR 169.

[15] *ACCC v Pacific National (No 2)* [2019] FCA 669,[1262].

[16] *Australian Gas Light Company v ACCC (No. 3)* [2003] FCA 1525, [348] (French J).

competitive process. While this forward-looking exercise involves predictions about the future, our analysis will be grounded in commercial reality.

1.11. As part of the ACCC's assessment, we may make findings of fact, based on an overall evaluation of the information before us, taking account of the significance of the expected facts and circumstances and the likelihood of such facts and circumstances occurring in the future.[17]

1.12. For a merger to be 'likely' to substantially lessen competition, that outcome must be more than speculative or a mere possibility, but it does not need to be a certainty. Importantly, a substantial lessening of competition does not need to be 'more probable than not'. It is sufficient that there is a 'real commercial likelihood' that the merger will substantially lessen competition.[18]

1.13. Fundamentally, the ACCC is concerned with finding out what the merger might change and whether that change is likely to substantially lessen competition. This involves comparing the nature and extent of competition that would be likely to exist in the market in the future with and without the acquisition.[19] The 'future with and without' test is a tool of analysis to assist in answering the question of whether the merger is likely to substantially lessen competition.[20]

1.14. The 'future without' is known as the counterfactual. More detail about the ACCC's approach to identifying counterfactuals is in Appendix 2.

Types of mergers

1.15. The ACCC may categorise a merger into one or more types to help guide our analysis. This categorisation does not indicate whether a merger is more or less likely to raise competition concerns, and the different types are not fixed or mutually exclusive. A merger may feature elements of different types.

1.16. The different merger types include:

- Mergers between competitors – mergers between actual or potential suppliers or buyers of substitutable goods or services (horizontal mergers)
- Mergers between firms in a buyer/supplier relationship – mergers between firms operating or potentially operating at different functional levels of the same supply chain (e.g. a steel manufacturer and an automobile producer, or an electricity generator and an electricity retailer) (vertical mergers)
- Mergers between firms that are neither competitors nor in a buyer/supplier relationship but are related in some way – mergers between firms that supply related products, for example, products that are complements[21] (e.g. milk and cereal), or products that customers prefer to buy together (e.g. a hospital may purchase all or

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17 *ACCC v Pacific National* (2020) 277 FCR 49, [255].

18 *ACCC v Pacific National* (2020) 277 FCR 49, [246] (Middleton and O'Bryan JJ).

19 *Australian Gas Light Company v ACCC (No. 3)* [2003] FCA 1525, [352].

20 *ACCC v Metcash Trading Ltd* (2011) 198 FCR 297,[228] (Yates J; Finn J agreeing).

21 In economics, goods and services are economic complements where the cross-elasticity of demand is negative. This means that when the price of one product goes up, the demand for the other product goes down.

most of its consumables from one supplier for cost and convenience) (conglomerate mergers).

Meaning of ‘market’

1.17. The ACCC must identify the market or markets within which a substantial lessening of competition might occur.[22] The identification of the market forms part of our assessment of the competitive effects of a merger and is not a separate exercise.

1.18. Section 4E of the Act defines ‘market’ as meaning, unless the contrary intention appears:

> … a market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are substitutable for, or otherwise competitive with, the first-mentioned goods or services.

1.19. Depending on the facts of the merger under review, the identification of the relevant market or markets may be relatively straightforward. The ACCC may simply define the market as comprising the most important constraints on the merger parties that have been identified in our competition assessment. In other cases, the ACCC may undertake a market definition exercise to identify the area or areas of competition, including potential competition, between firms, and to assess the degree of substitutability between different products and geographic areas.

1.20. Even when the ACCC undertakes a market definition exercise, it is often unnecessary to settle on the relevant market or markets for the purposes of a competition assessment. For example, there may be several plausible markets, but if the merger leads to a substantial lessening of competition in each of them, then we need not reach definitive conclusion on market definition.

1.21. The tools we may use to define markets are explained in Appendix 1.

Concentration

1.22. The degree of concentration in the market before and after the merger is often a key element to merger assessments. As a general principle, when there is already a high degree of concentration, there is an increased risk a merger will substantially lessen competition.

1.23. Market concentration provides a snapshot of market structure: the number, size and share of supply or demand of the merger parties (pre-merger), as well as the merged firm and the remaining competitors (post-merger). Changes in market concentration

[22] *Competition and Consumer Act 2010* (Cth), ss 51ABZE(2), s 51ABZF(2), s 51ABZJ(2).

over time can also reveal the frequency of new entry and provide insight into the ability of new entrants and smaller competitors to attract customers and expand.

1.24. The ACCC may use the Herfindahl-Hirschman Index (HHI) as a measure of market concentration, and considers that markets with a HHI greater than 2,000 are highly concentrated (e.g. 5 firms each with 20 percent market share), and a change in HHI of more than 100 points (e.g. a merger between 2 firms each with around 7 percent market share) is a significant increase in concentration.

1.25. Further details about the tools we may use to measure concentration are set out in Appendix 1.

Creating, strengthening or entrenching a substantial degree of market power

1.26. The merger reforms make clear that a substantial lessening of competition can include creating, strengthening or entrenching of a substantial degree of power in a market.[23] As noted in the explanatory memorandum to the merger reforms, the words are intended to increase the focus on the market power of the merger parties and to clarify that even a small change in market power may amount to a substantial lessening of competition.[24]

1.27. The addition to the legislative test reflects the economic link between a lessening of competition and an increase in market power, and should be seen as an elucidation of the ways in which a substantial lessening of competition can arise rather than a change to the meaning of a substantial lessening of competition.[25]

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[23] *Competition and Consumer Act 2010* (Cth), s 51ABZH(4)

[24] Explanatory Memorandum to *Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024*, para 4.41.

[25] Explanatory Memorandum to *Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024*, para 4.43.

2. Mergers between competitors – Unilateral effects

2.1. All horizontal mergers between competitors eliminate competition between the merger parties, and it is that loss of competition which gives rise to potential unilateral effects. Pre-merger, if one merger party increased prices, reduced output, or degraded some other aspect of the good or service offer, that might result in some customers switching, or substituting, to the other merger party. Post-merger, this possibility of substitution to the other party—and the constraining effect that has—is removed.[26]

2.2. The ACCC's approach to the analysis of horizontal mergers may differ depending on whether the merger involves suppliers of differentiated products or suppliers of undifferentiated products. There is no clear-cut distinction between differentiated products and undifferentiated products, however, broadly speaking:

- customers regard products as differentiated when they are prepared to pay more for a product from one supplier than from another supplier. Examples of differentiated products include bread, timber, home insurance, medicines, and laptops
- customers regard products as undifferentiated when they are not prepared to pay more for a product from one supplier than from another supplier. These products are generally referred to as commodities, such as wheat, coal and steel.[27]

2.3. Many of the mergers assessed by the ACCC concern firms supplying differentiated products. For this reason, this chapter focuses on mergers involving differentiated products. The factors relevant to assessing mergers involving undifferentiated products are discussed at the end.

Differentiated products

2.4. The ACCC will consider whether the elimination of competition between the merger parties is likely to substantially lessen competition. As part of our assessment, the ACCC will focus on the closeness of competition between the merger parties, and the

[26] Dr Jill Walker, 'Economic analysis in merger investigations – Background Note by Dr Jill Walker', OECD Global Forum on Competition, available at https://one.oecd.org/document/DAF/COMP/GF(2020)6/en/pdf, p 14.

[27] The ACCC recognises that there may be different grades of such products, and that only commodities within the same grade may be considered undifferentiated.

effectiveness of remaining competitors, including their likely responses to the exercise of market power by the merged firm.

Closeness of competition between the merger parties

2.5. A characteristic of differentiated product markets is that firms will compete more closely with some firms than with others. If one firm increases its prices, the customers who switch will be more likely to switch to firms that supply products with similar attributes, such as similar quality or features. These products are known as substitutes. Firms that supply products that are close substitutes will typically have high diversion ratios. Diversion ratio means the proportion of a firm's total lost sales that switch to a rival when it increases its price (or worsens some other term of competition). The higher the diversion ratios between two firms, the more closely they compete, and the more competition that will be lost through a merger. Because the risk of switching has a constraining effect on firms, a merger between close competitors is more likely to raise competition concerns than a merger between distant competitors.

Box 1

Example of product differentiation and diversion ratios

Supplier A manufactures a popular range of sports shoes. Customers purchase the shoes because of the high-quality designs, product range, premium brand name and celebrity endorsements. If supplier A increased its prices, customers would be likely to switch to supplier B, which manufactures sports shoes under a competing brand name, and has similar quality designs and celebrity endorsements. Customers would be less likely to switch to supplier C, which focuses on hiking and trail-running, and whose brand name is associated with outdoor apparel.

There would be high diversion ratios between suppliers A and B, and low diversion ratios between supplier A and supplier C.

2.6. To assess the degree of substitutability between different products, the ACCC may consider factors such as:

- product features and functions
- customer perceptions of the firms and their products
- customer loyalty to the firms or their products
- brand loyalty
- breadth of product lines and level of specialisation
- distribution channel coverage
- geographic presence
- internal company planning, strategy, marketing, financial and sales information
- information about advertising campaigns and other information that highlights how the merger parties perceive themselves vis-à-vis others

- studies and information regarding customer preferences and switching habits – for example, customer data that is collected by the merger parties or from external sources.

2.7. To assess the likelihood of customers switching to the other merger party, in addition to diversion ratios, the ACCC may consider other relevant factors, such as:

- the profitability of sales that would be recaptured by the other merger party
- price elasticity—how strongly buyers react to changes in price–including own-price elasticity (the percentage change in quantity demanded if a merger party raised its price) and cross-price elasticity (the percentage change in demand for one product if a merger party raised the price of another product)
- whether market features exist that prevent or hinder customers from changing suppliers — for example, switching costs resulting from exclusive long-term contracts and termination fees
- analysis of bidding patterns in markets subject to bidding to see if the merger parties bid for similar projects or are close in bidding contests
- the production capacity of the merger parties and other firms, including any capacity constraints or excess capacity
- the costs to rival firms of expanding their capacities
- impediments to rival firms altering or expanding their product mix to compete more closely with the products of the merged parties
- whether the merged parties control inputs/distribution channels, patents/other intellectual property and access to, or pricing of, different platforms.

Effectiveness of competition from other rivals

2.8. The ACCC will also assess the effectiveness of competitors that will remain after the merger. If these rivals supply products that are also close substitutes, and the merged firm risks losing a large volume of valuable sales to those rivals if it increased prices or worsened non-price aspects of its good or service offer, the merger will be less likely to substantially lessen competition. If, on the other hand, the remaining rivals supply products that are not close substitutes, the merger is more likely to substantially lessen competition, since those rivals will only provide a weak competitive constraint on the merged firm.

2.9. To assess the effectiveness of remaining rivals, the ACCC will generally have regard to the factors considered when assessing the closeness of competition between the merger parties.

2.10. It is important to note that the remaining competitors may respond to the merger in different ways. They may reposition their products, extend their product lines, or find other ways to attract customers from the merged firm. In assessing the likely responses of different rivals, the ACCC will also consider whether there are any barriers to expansion (see Chapter 6 for a discussion on the types of barriers that rivals may face). Further, the constraint exerted on the merged firm by different rivals

will be different; that is, one firm might exert a close competitive constraint on the merged firm, while another may only exert a weak constraint.

Import competition and competition from overseas

2.11. In some cases, competition from imports may provide an effective competitive constraint on the merged firm, even when there is no effective constraint from domestic rivals.[28]

2.12. The ACCC considers that imports are more likely to effectively constrain the merged firm in the following circumstances:

- independent imports can be increased in response to demand, taking into consideration any barriers to expansion including those that may be specific to imports, such as government regulations, and the likelihood and impact of anti-dumping applications on imports
- the imported product is a sufficiently close substitute for the merged firm's product, taking into account the need to meet any relevant Australian or industry standards, any increase in the complexity of customers' logistical arrangements, increased transport times and costs, the risk of adverse currency exchange rate fluctuations, and any other relevant factors
- the price of actual or potential imports, including any tariffs or other import-specific taxes and charges, is competitive with the domestic price of the merged firm's product
- the merged firm and other major domestic suppliers are not controlled or influenced by actual or potential import suppliers.

2.13. In some cases, competition from overseas markets may prevent the merged firm from increasing prices or worsening non-price aspects of products sold in Australia. This will depend on the ease and cost-effectiveness with which customers can make their purchases from overseas sellers.

Undifferentiated products

2.14. In markets involving suppliers of undifferentiated products, firms select the volume of output they supply and receive the market price. In a competitive undifferentiated product market, a firm will incur losses if it reduces its output, as customers will switch to a rival. When a merger removes a supplier that buyers would otherwise turn to as an alternative, it may be profitable for the merged firm to reduce its output so that prices rise. This will be particularly the case if rivals have little or no spare capacity. Even if rivals have spare capacity, their profit-maximising response,

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[28] The ACCC will assess buyers' willingness or ability to turn to imports, which may be affected by their tastes and preferences, and by border-related considerations. Buyers may be less willing or able to switch to foreign substitutes when faced with exchange rate risk, local licensing and product approval regulations, industry-imposed standards, or initiatives to "buy local". Conversely, buyers may be more willing to turn to foreign substitutes when they have ample information about foreign products and how to source them, when foreign sellers or their products have already been placed on approved sourcing lists, or when technology licensing agreements, strategic alliances or other affiliations exist between domestic buyers and foreign suppliers.

especially in concentrated markets, may be to replace some, but not all, of the output 'withdrawn' by the merged firm, so they can also benefit from increased prices.

2.15. For mergers involving undifferentiated products, unilateral effects are more likely to arise in the following circumstances:

- large share of supply: if the merged firm has a large share of supply, it will typically have a greater incentive to restrict output volumes, as the benefits of a higher price will apply to a greater volume than would be the case for a smaller firm. The tools for measuring market concentration and shares of supply are explained in Appendix 1
- concentrated market: when the market is concentrated among few rivals, price increases may be more likely
- rivals lack capacity: if rivals do not have spare capacity, or substantial amounts of their capacity are committed to other buyers under long-term contracts, they may be unable to expand quickly at relatively low cost
- high switching costs: customers may face costs if they switch to rival suppliers post-merger. For instance, the relevant products may be sold under terms and conditions that limit or curtail the ability of rivals to acquire customers (e.g. break fees, exclusivity or long-term contracts). The more costs faced by customers when switching, the greater the risk of the merged firm unilaterally exercising market power.

3. Coordinated effects

3.1. Coordination occurs when a group of firms, including the merged firm, interact in a way that limits competition between them. In merger analysis, coordination refers to conduct by multiple firms that is profitable only because of accommodating actions of rivals. For example, coordinated effects will occur when one firm increases its prices or degrades a non-price aspect of its good or service offer, and that is profitable because other firms act in a similar way.

3.2. A merger has coordinated effects if it makes coordination among firms more likely, more complete, or more sustainable.[29] Coordinated conduct may relate to price, service levels, customers, geographic areas, research and development, marketing, investment, or any other dimension of competition. For example, firms may coordinate on a minimum price, or the customers they will and will not target.

3.3. In *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited (ANZ/Suncorp)*, the Australian Competition Tribunal (the Tribunal) gave this description of coordinated effects:

> In merger analysis, the distinguishing feature of coordinated effects, when compared with unilateral effects, is that the effect depends on the accommodating actions of suppliers, other than the merger parties, to increase prices or reduce output and other non-price attributes. They reflect the exercise of the combined market power of firms (or a group of firms) in the market. Coordination may be tacit or explicit and will not necessarily involve any conduct that otherwise breaches the CCA.[30]

3.4. As noted by the Tribunal, coordination between firms can be tacit or explicit:

- tacit coordination is not explicitly negotiated or communicated. Rather, firms engage in cooperative behaviour or communication without reaching an arrangement or understanding. The coordination can come about simply from repeated interactions, or it may entail signalling, or other forms of communication
- explicit coordination is explicitly negotiated and communicated. This type of coordination is a serious violation of the Act.

3.5. A merger may increase the potential for coordinated effects by:

- reducing the number of competing firms
- removing or weakening competitive constraints (such as by removing a 'maverick'[31])
- making the market more vulnerable to coordination

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29 Jill Walker, 'Economic Analysis in Merger Investigations – Background Note by Dr Jill Walker', OECD Global Forum on Competition, 29 October 2020.

30 *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [375].

31 For discussion of mavericks, see Chapter 5.

3.6. Coordinated effects may also occur in addition to unilateral effects, so that the merged firm is able to exercise even more market power than it would on its own.

3.7. There are several conditions that make a market vulnerable to coordination, and these are explained below. However, it is important to note that the presence or absence of these conditions is not a reliable predictor of coordinated effects. The conditions assist to guide the ACCC's analysis but are not a checklist. Rather, the key issue is how the merger will change the conditions for coordination:

> Not all such factors need to be present for coordination to be successful and the key question for merger review is how does the merger change the likelihood of successful coordination, if at all? The question that needs to be answered is whether there is a coherent story that can be told about how the merger could make the market more vulnerable to coordination or how coordination might become more complete or more sustainable?[32]

Market conditions

Concentrated markets

3.8. As a general principle, mergers that take place in concentrated markets are more likely to result in coordinated effects. For firms to coordinate, they need to collectively have market power and be able to reach mutually beneficial terms. It is easier for firms to have collective market power if there are only a few firms, each with a large market share. Likewise, it is easier for firms to reach a common understanding on the terms of coordination if there are only a few participants.

High barriers to entry

3.9. Coordinated effects are also more likely to occur if the market has high barriers to entry. New entrants to a market can disrupt coordinated conduct by competing, and the prospect of new entry can deter incumbents from coordinating with each other. Conversely, markets with high barriers to entry can afford coordinating firms a degree of protection from the prospect of disruption by new entrants. See Chapter 6 for a discussion on barriers to entry.

Transparency

3.10. Firms can more readily coordinate if they can observe other firms' activities and general market conditions. Market transparency tends to both better enable firms to achieve a consensus on the terms of coordination (e.g. price, output, or another dimension of competition), and to detect deviations from those coordinated terms. Not all aspects of the market need to be transparent to make a market vulnerable to

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[32] Jill Walker, 'Economic Analysis in Merger Investigations – Background Note by Dr Jill Walker', OECD Global Forum on Competition, 29 October 2020, para 57.

coordination. For example, firms may coordinate on the allocation of customers, even if they cannot observe each other's prices.

3.11. Markets with a high degree of information sharing about a parameter of competition that is capable of being coordinated are more prone to coordination. Information may be readily available to firms if, for example, they actively publish their prices, hold cross-shareholdings in each other, or are members of trade associations that collate and publish market information.

3.12. Markets do not need to be fully transparent for coordinated conduct to arise, but firms must have some mechanism for monitoring and detecting deviations from the coordinated outcome. It is not necessary that firms are able to precisely identify deviations - deviations may be detected based on, for example, a general fall in prices, but transparency around firms' strategic choices can help to maintain coordination.[33]

Other product and market conditions

3.13. In addition to the above factors, a market will be more vulnerable to coordination if the following features are present:

- less differentiated products: complex products and differences in product offerings tend to it make it more difficult for firms to reach mutually profitable terms of coordination
- firms with similar cost structures: cost asymmetries make it more difficult to reach mutually profitable terms. As discussed further below, cost asymmetries also increase the risk of low-cost firms deviating from a coordinated understanding
- stability: when product innovation or fluctuations in cost or demand are common, it may be difficult for firms to know whether a change in rivals' pricing arises from these changes or constitutes a deviation from coordinated terms. On the other hand, stable market shares over a long period will make it easier for suppliers to detect deviations.

Incentives to deviate

3.14. When considering whether a merger increases the likelihood of coordination, the ACCC may consider the incentives of firms to deviate from any terms of coordination.[34] In a competitive market, profit-maximising firms have an incentive to behave independently (e.g. by offering discounts or pricing below their competitors) to induce customers to switch to them. By contrast, profit-maximising firms have an incentive to coordinate when the expected profits from coordinating are greater than the expected profits from behaving independently.

3.15. As noted above, markets are more vulnerable to coordination when firms have similar market shares, cost structures, and production capacities. Conversely, the profits

[33] The ACCC recognises that market transparency can benefit customers in a way that increases competition.

[34] *Applications by Australia and New Zealand Banking Group Ltd and Suncorp Group Ltd* [2024] ACompT 1 at [386].

from deviating from coordinated conduct (and the incentives on firms to deviate) are likely to be higher when:

- individual transactions are large and infrequent relative to total market demand
- individual transactions are large relative to a single firm's total output
- there is firm asymmetry: smaller firms or firms with lower cost structures may have more to gain from competing rather than coordinating
- markets are characterised by frequent product innovations.

3.16. Deviation may also be more likely where there is active customer switching, as firms are more likely to gain from competing by attracting new customers. Factors that affect the levels of customer switching include search or switching costs, brand loyalty, consumer behavioural biases, or risk aversion.

3.17. However, the presence or absence of these factors is not conclusive; even in asymmetric markets (with large and small firms), firms may be able to come to a consensus on specific parameters of competition, such as known pricing points or geographic strength.

Retaliation

3.18. Firms that have an incentive to deviate from a consensus may refrain from doing so due to fear of retaliation. Retaliation may simply involve a return to competitive conditions or, for example, a 'price war'. The credible threat of effective punishment from the consensus alone may be sufficient to deter deviation.

3.19. Coordinating firms have a greater ability to retaliate where:

- firms have similar cost structures: similar-cost firms are more likely to face retaliation, while low-cost firms may not fear retaliation by higher-cost firms
- firms compete against each other in more than one market: this provides additional opportunities to punish deviating firms
- some firms have excess capacity, which may enable them to increase output and reduce prices in response to a deviation (however, excess capacity may also provide firms with an incentive to deviate)
- the punishment is not likely to be delayed because, for example, market transactions are infrequent.

3.20. Retaliation requires coordinating firms to be able to detect deviations. Publicly available information on firms' pricing, product portfolio or investment decisions may enable such detection. Firms may also be able to infer their rivals' actions from market outcomes, even if they cannot observe them directly. For example, a firm's knowledge of its own or a competitor's sales volumes and capacities might, in some

contexts, provide enough information to determine whether deviation from coordination is taking place.

Past conduct

3.21. The ACCC does not rely solely on elements of market structure when assessing changes in the likelihood of coordinated effects, we will also consider past conduct. This includes evidence or information on whether there was coordination in the market before the merger. For example, pre-merger trends in relation to prices, market shares, entry, capacity or margins may be consistent with coordinated behaviour. There may also be evidence or information that firms are aware of their strategic interdependence or seek to facilitate such an understanding through, for example, information sharing, public or private communications, or deepening structural links.

3.22. Evidence or information of some competition between some or all firms is not inconsistent with a finding of past coordination, as rivals may not coordinate over all competitive parameters or in all regions, coordination may not include all firms, and coordination may be characterised by periods during which the coordinating group reverts to competing.

3.23. As stated by the Tribunal in *ANZ/Suncorp*:

> Coordinated effects are most likely to be significant where coordination has, to date, been imperfect, or has broken down, such that the proposed merger could restore coordination or make it more stable or enduring, and less vulnerable to cheating and breakdown.[35]

3.24. If there is evidence of coordinated outcomes before the merger, the ACCC may consider whether the conditions for coordination will be strengthened or weakened by the merger. However, a lack of evidence or information of past coordinated conduct does not prevent the ACCC from concluding the merger will increase the likelihood of coordinated effects.

[35] *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [388].

4. Non-horizontal mergers

4.1. Non-horizontal mergers combine firms that do not directly compete, but that participate in related markets. Markets of this kind are typically classified into two sub-types:

- vertical mergers involve firms that operate at different levels of a supply chain — for example, a merger between an upstream supplier and a downstream customer where the upstream supplier supplies an input to the downstream customer's production process
- conglomerate mergers involve firms that are not active in the same supply chain but are related in another way — for example, the firms may buy or supply products that are complements, or customers may prefer to buy their products together.

Box 2

Examples of vertical mergers

- an electricity retailer acquiring an electricity generation business, which supplies electricity to multiple retailers
- a pet food manufacturer acquiring a pet food retailer
- a clothing company acquiring a textile manufacturer

Box 3

Examples of conglomerate mergers

- an online shopping platform acquiring a chain of grocery stores
- a software system provider acquiring a content streaming service
- a private hospital acquiring a company that manufactures medical consumable products

4.2. Unlike mergers between competitors, non-horizontal mergers do not involve a direct loss of competition between the merger parties. Instead, a common concern is that the merged firm may be able to use its position in one market to foreclose current or potential rivals in another market. This can weaken the constraint the merged firm faces in the related market and, as a result, harm the competitive process and ultimately customers, including consumers. The ACCC uses the term 'foreclosure' to encompass any hindrance on rivals' ability to compete effectively.

4.3. Another concern with non-horizontal mergers – vertical mergers in particular – is that the merged firm may gain access to competitively significant information about its rivals through its position as their supplier or customer. Depending on the industry, this information could include data on specific sales or bids, overall pricing strategies, algorithms, technical product specifications or innovation plans. The merged firm may use these insights to target rivals or pre-empt their competitive actions. Access to competitively significant information could undermine rivals'

ability or incentive to compete effectively, or facilitate anti-competitive coordination between rivals and the merged firm.

Vertical effects

4.4. When a merger involves an upstream supplier and a downstream customer (which in turn supplies goods or services in a downstream market), they will become vertically integrated. Competition concerns can arise when the vertically integrated firm forecloses access to products or routes to market that rivals use to compete. It is not necessary that rivals currently access the product or route to market from the merger parties. The possibility of access may be competitively significant because, for example, the availability of potential alternatives may allow rivals to negotiate better terms from other suppliers.

4.5. In the case of vertical mergers, there are typically two types of foreclosure that the ACCC considers:

- input foreclosure – when the vertically integrated merged firm decides to fully or partly restrict downstream rivals from accessing an input or offers the input on worse terms
- customer foreclosure – when the vertically integrated merged firm decides to fully or partly restrict upstream rivals from accessing its route to market (e.g. a distributor or retailer).

Box 4

Example of input foreclosure

- A rubber producer and tyre manufacturer merge, and the merged firm decides to no longer sell rubber to rival tyre manufacturers.

Box 5

Example of customer foreclosure

- A building materials producer and building materials retailer merge, and the merged firm decides to no longer sell the building materials of its rivals.

4.6. The ways that a vertically integrated firm might foreclose rivals will vary and are not limited to denying them access to an input or downstream customer. For example, as compared to a future without the merger, the merged firm might decide to:

- degrade the quality of an input or access to customers
- worsen supply terms to rivals
- limit interoperability
- limit access to data
- provide less reliable access
- tie up or obstruct routes to market

- delay access to product features, improvements, or information relevant to making efficient use of a good or service.

4.7. When considering whether a substantial lessening of competition is likely to arise from either input foreclosure or customer foreclosure, we consider three related questions:

- whether the merged firm is likely to have the ability to foreclose, that is, whether rivals have effective alternative sources of inputs or means of accessing the market
- whether the merged firm is likely to have the incentive to foreclose, that is, whether it is profitable to foreclose rivals, or whether it is relatively more profitable for the vertically integrated firm to maintain rivals' access to inputs or customers
- whether the effect or likely effect of any such foreclosure would be to substantially lessen competition.

Input foreclosure

4.8. The concern with input foreclosure is that the merged firm may restrict its competitors' access to important inputs, thereby limiting their ability to supply the relevant products competitively, to the detriment of consumers.

Ability to foreclose rivals

4.9. A vertically integrated firm that supplies an input to downstream rivals can only foreclose those rivals if they do not have suitable alternative sources for the input, and the input is important to their effectiveness in the downstream market. If there are suitable alternative inputs available, and the vertically integrated firm attempted to foreclose access to an input, rivals would simply switch to those alternatives. The presence of alternative inputs therefore acts as a constraint on the merged firm, and makes any attempt at input foreclosure less likely to occur and less likely to be effective.

4.10. To assess the availability and effectiveness of alternatives, the ACCC may consider various factors, including:

- the prices of alternative inputs
- the degree of differentiation between inputs
- their functional substitutability
- the brand and reputation of the merged firm as compared to its rivals
- any capacity constraints faced by rivals
- any switching costs faced by customers
- barriers to entry or expansion that may inhibit rivals
- control of intellectual property that may inhibit rivals
- direct or indirect network effects that may benefit the merged firm
- access to data or integration into wider ecosystems that may benefit the merged firm.

4.11. The ACCC might not place material weight on submissions that the merged firm is unable to foreclose rivals because of contractual protections. For example, a contract may require the merged firm to continue supplying an input to a downstream rival. In practice, such protections may not completely remove the merged firm's ability to foreclose rivals, given that certain rivals might not be covered by the contracts, the contracts might not protect all ways in which rivals could be foreclosed, and the contracts may be of limited duration. Moreover, over time, contracts may be renegotiated or terminated, and firms may waive their rights to enforce any breaches due to an inferior bargaining position (which may reflect the change in market structure brought about by a merger).

Incentive to foreclose rivals

4.12. If the merged firm is able to foreclose rivals, the ACCC will assess whether it also has the economic incentive to do so. A vertically integrated firm will have an incentive to foreclose if the benefit it receives outweighs the potential consequences.

4.13. An upstream supplier that denies a downstream customer access to an input will lose that customer as a source of revenue. Similarly, an upstream supplier that limits access to an input (e.g. by increasing its prices) may increase its profits from the higher margins it earns on sales it continues to make, but it will decrease profits from the sales it will no longer make. In both cases, input foreclosure will only make commercial sense if the vertically integrated firm receives sufficient benefits to offset any negative consequences.

4.14. To assess the merged firm's incentive to foreclose, the ACCC may assess whether the decreased profits from denying or limiting rivals' access to inputs will be more than increased profits from possibly increasing demand for the firm's products in the downstream market. The magnitude of these losses and gains will depend on factors such as:

- the loss in sales of the input due to foreclosure
- the margins on the reduced sales of the input
- the volume of extra sales likely to be gained in the downstream market
- the likely margin on those sales
- the extent (if any) to which margins on downstream sales can be increased by raising prices or changing some other term of trade.

4.15. The ACCC recognises that this assessment may depend on the availability of data and the quality of that data.

4.16. The ACCC may also have regard to the merger parties' past conduct, business strategies and the rationale for the merger, as well as industry factors and the

structure of the relevant markets. This will be informed by the competitiveness of the downstream market.

Customer foreclosure

4.17. The concern with customer foreclosure is that the merged firm may restrict its competitors' access to an important customer, such as a distributor or a retailer, thereby limiting their route to market and rendering them less competitively effective.

Ability to foreclose rivals

4.18. A vertically integrated firm can only foreclose upstream rivals from accessing a downstream customer if those rivals do not have suitable alternative customers, and the customer is important to their effectiveness in the upstream market. If there are suitable alternative customers available, rivals would simply switch to supplying them (or increase their existing supplies to them). The presence of alternative customers therefore acts as a constraint on the vertically integrated firm, and makes any attempt at customer foreclosure less likely to occur and less likely to be effective.

Incentive to foreclose rivals

4.19. A vertically integrated firm that decides to foreclose its rivals from making sales to its related customer will potentially lose downstream sales. For this reason, customer foreclosure will only be profitable if the profits on the lost downstream sales are less than any increase in profits from an increase in demand for the firm's upstream products.

4.20. To assess the merged firm's incentive to foreclose, the ACCC may seek information on the likely relative sizes of these possible gains and losses in profits. The magnitude of losses and gains will depend on factors such as:

- the volume of sales the vertically integrated customer is likely to lose as a result of no longer carrying its rivals' products
- the margins on those lost sales
- the volume of extra sales likely to be gained in the upstream market
- the likely margin on those extra sales
- the extent (if any) to which margins on upstream sales can be increased by raising prices or changing some other term of trade.

4.21. As noted above, the ACCC recognises that this assessment may depend on the availability of data and the quality of that data.

4.22. The ACCC may have regard to the merger parties' past conduct, business strategies and the rationale for the merger, as well as industry factors and the structure of the

relevant markets. This will be informed by the competitiveness of the upstream market.

Likely effect of input or customer foreclosure

4.23. The ACCC will also consider the likely effect of input or customer foreclosure on competition in the relevant markets. Foreclosure has competitive effects when the vertically integrated firm finds it profitable to increase the price or worsen non-price aspects of its good or service offer in the market in which rivals are foreclosed.

4.24. Foreclosure need not result in rivals being forced to exit the market to have a detrimental effect on competition. For example, rivals may be weakened by having to use more expensive alternatives to those offered by the vertically integrated firm, or they may be discouraged from expanding their operations because of concerns about access to inputs or customers, and potential rivals may be discouraged from entering the market.

4.25. Foreclosure may also lead rivals to reduce investment or change their business strategies in ways that substantially lessen competition. For example, rivals may be reluctant to invest in a market if their success depends on continued supply of an input from the vertically integrated firm. Alternatively, rivals may be forced to use expensive strategies to reduce their dependence on the merged firm, weakening their competitiveness.

4.26. Reduced investment can also occur when a merger increases the risk that the merged firm will gain access to competitively significant information about downstream rivals. For example, a downstream rival that purchases inputs from a vertically integrated supplier may be reluctant to invest in new products or production processes if the supplier will learn about those new products or processes and be able to copy them.

Conglomerate effects

4.27. With conglomerate mergers, the ACCC considers whether a merger that combines suppliers of products in related markets could allow the merged firm to profitably leverage a strong position in one market to the related market by linking the sales of different products. The merged firm may link sales by, for example:

- offering the products at a lower price if purchased together
- only making products available in a bundle
- integrating the products within a digital ecosystem
- only selling one product on the condition the customers also buy the related product

Box 6

Example of bundling

An online shopping platform acquires an online payment processing company. After the merger, the company begins to offer customers the ability to use its payment processing service for no fee, whereas if customers choose to pay with a credit card, they are charged a 2 percent fee.

4.28. In considering the possibility that the merged firm will link products to leverage a strong position in one market to a related market, the ACCC may consider whether:

- it would be profitable for the merged firm to link products. Linking the sale of products is less likely to be profitable if any increase in sales of the linked products is small relative to sales if the products are sold separately. On this issue, it may be relevant if the merged firm must offer an inducement, such as a discount on the bundle, to encourage customers to buy the products together, or incur any related costs
- customers would be likely to buy both products if the merged firm linked them. This is more likely if one of the products is a must-have or is otherwise especially important to customers, and customers see benefits in purchasing the products together. For example, customers may use the products in combination (they may be complements) or customers may reduce their costs if they buy the products together (there may be benefits in one-stop shopping)
- rivals to the merged firm could profitably replicate the combined offering through their own competing combinations.

4.29. The ACCC may also consider the effect of any leveraging by the merged firm on rivals. To have an adverse impact on competition, the linking of sales by the merged firm needs to result in rivals losing sales, and becoming less effective competitors. This is more likely to occur if the loss in sales renders them less able to achieve competitive scale to benefit from network effects.

4.30. Linking of sales may also increase switching costs for customers or otherwise raise barriers to entry and expansion for other firms, as it may become necessary for new entrants to enter both markets at once (for the supply of the primary product and related product) to compete effectively.

4.31. The net impact of any competitive effects may be a substantial lessening of competition in one or more markets. In making our assessment, the ACCC may consider the proportion and significance of firms likely to be foreclosed and the effectiveness of any firms that might remain.

5. Specific merger issues

5.1. Some mergers may raise specific competition concerns, and the ACCC has developed guidance on how we will analyse some of these concerns. The ACCC may consider these specific concerns in addition to the factors outlined in the previous chapters.

Mergers involving a vigorous and effective competitor

5.2. Some firms may be relatively small in size and market share but have a significant influence on the competitive process. For example, they may be aggressive discounters or particularly strong innovators. Such firms are known as vigorous and effective competitors or mavericks. Mavericks deliver benefits to consumers beyond their immediate supply, by forcing other suppliers to deliver better or cheaper products.

5.3. If a firm acquires a maverick, that may result in unilateral effects if the acquiring firm impedes or removes the maverick's influence on the competitive process. Likewise, the acquisition of a maverick may increase the risk of coordinated effects. The maverick might have a history of preventing or disrupting coordination, for example, by failing to follow price increases by its competitors. If the maverick is removed by a merger, the remaining firms may find it easier to coordinate, and the merger may make coordination more likely, more complete, or more sustainable.

5.4. For these reasons, the ACCC is likely to have competition concerns with an acquisition of a maverick. Some examples of the types of evidence or information the ACCC may consider when assessing whether a merger party is a maverick include:

- past competitive pricing, for example discounting and promotions
- service levels, for example opening hours and store format or after-sales service
- past and expected innovation, for example in design or production technology
- leadership in non-price competition, for example product quality.

Mergers that eliminate potential competition

5.5. Mergers can substantially lessen competition when they prevent or hinder entry or expansion by a rival that would have otherwise increased competition. Potential competition can be more important in some markets than in others. For example, in markets characterised by network effects, where users derive more value from a product if more users use the same product, the most substantial constraint may

come from potential competitors, which threaten to displace the incumbent's market position.

5.6. There are two ways in which a merger can eliminate potential competition. First, a merger may involve an incumbent acquiring a potential entrant, which eliminates future competition between the acquirer and the target. Second, the potential that firms may enter the market may incentivise incumbents, for example, to continue investing in new or improved products. A merger may result in a loss of that dynamic competition.

5.7. For example, an acquirer may view the target as a potential competitor, and the acquirer may acquire the target as a strategy to capture and control the competitive threat before the target develops into a true rival (this is sometimes referred to as a 'killer acquisition'). When an acquirer undertakes multiple acquisitions of nascent rivals as part of a concerted strategy over time, the effect may be to strengthen or entrench the acquirer's market power, making subsequent entry more difficult. Alternatively, a company may be contemplating entering a market but may instead decide to acquire an existing player. In that case, the acquisition may remove the potential competition that the company would have brought about by entering the market.

5.8. Losses of dynamic competition are more relevant in markets when significant and long-term investments are required to reach scale. Examples include digital platforms, where the costs and time required to build up a significant user base and achieve network efficiencies might involve years of losses (with ongoing uncertainty about whether the platform will eventually be successful), or pharmaceutical companies, where investments in new products might involve years of research and development that may never come to fruition.

Loss of future competition

5.9. In assessing whether a merger involving a potential entrant leads to a loss of future competition, the ACCC may consider whether:

- either merger party would have entered or expanded absent the merger
- the loss of future competition brought about by the merger would give rise to a substantial lessening of competition, taking into account other constraints and potential entrants.

5.10. Entry and expansion will be considered more likely when a merger party has the ability and incentive to enter or expand. To assess this, the ACCC may consider:

- plans to enter or expand
- action already taken towards entry or expansion
- action taken or preparation for action by incumbents in response to anticipated entry or expansion
- a past history of entry into related markets
- financial advantages that would make entry or expansion attractive.

5.11. The ACCC recognises that merger parties may have decided to pursue a merger without creating detailed business plans on alternative routes to enter or expand. The ACCC may conclude that one of the merger parties would have entered the market absent the merger, without the ACCC forming a conclusive view on the precise characteristics of the entry (e.g. the product it would have launched, or the assets it would have acquired). However, the ACCC may place less weight on changes to plans to enter that occur around the same time as the merger transaction is negotiated.

5.12. Evidence or information relevant to the ACCC's assessment of the loss of future competition might include firms' internal documents, business forecasts or valuation models. The ACCC may consider the likely characteristics of the potential entrant's future product, and its attractiveness to customers. The ACCC may also consider whether the potential entrant has existing customer relationships or existing products that could facilitate effective entry, such as through cross-selling or bundling. The likely commercial responses of existing firms in anticipation of entry may also indicate the entrant's expected impact on competition.

Loss of dynamic competition

5.13. In a situation where an existing firm acquires a potential entrant, there may be a loss of dynamic competition if the existing firm reduces its current investment efforts. This may occur because the merger removes the risk of customers switching to the potential entrant once it enters (or if the merged firm maintains the potential entrant as a separate entity, customers may switch to the entrant, but those sales will no longer be lost by the merged firm).

5.14. Dynamic competition can put pressure on suppliers to invest in innovation and product development, and this has economic value. Accordingly, while the ACCC's assessment of dynamic competition may, in some cases, focus on entry and expansion in relation to specific products; in others, we may consider the broader impact of dynamic competition on investments for the future.

5.15. When assessing losses of dynamic competition, the ACCC may consider information regarding the ability and incentive of the incumbent merger party to respond to the threat of entry or expansion by the other merger party. The ACCC may also explore the likelihood that the potential entrant will be successful in entering, and the expected closeness of competition between it and existing firms.

5.16. The ACCC may determine that the removal of a potential entrant that is making efforts towards entry or expansion will substantially lessen competition, even when there is evidence to suggest that entry might ultimately be unsuccessful. For example, if there is evidence that the potential entrant could have a significant impact on other firms' future profits, the removal of the threat of entry may lead to a

significant reduction in innovation or a reduction in efforts by other firms to protect those future profits.

Mergers involving competing buyers

5.17. A merger between competing buyers may substantially lessen competition if it creates or enhances the merged firm's market power when buying products such that the merged firm is able to decrease the price of products below competitive levels, and there is a corresponding reduction in the overall quantity of the products supplied in the market, or there is a corresponding reduction in another dimension of competition.

5.18. When a firm can exercise market power through buying, that is known as monopsony power.[36] When a small number of firms collectively exercise market power through buying, that is known as oligopsony power. A buyer has monopsony or oligopsony power when it controls enough purchases upstream that it can affect the overall market price of a product (or a non-price aspect) by purchasing less. Suppliers might no longer be able to cover their supply costs and could then exit or reduce their supply to the market.

5.19. Suppliers may also face what is known as a hold up problem: they may be deterred from investing in their businesses, since the powerful buyer will demand that any gain from such investment is passed on to them in the form of lower prices. Suppliers may therefore decide to reduce investment in product quality, or cut costs in production, as they expect any gains from their investment will go to the buyer. Although the harm is experienced by suppliers, the reduced incentives to invest can ultimately harm consumers.

5.20. When assessing a merger involving competing buyers, the ACCC may use the analytical tools for assessing the market power of suppliers, adapted to a buyer scenario. This includes examining whether, in response to a decrease in the price of a product, suppliers could switch to effective alternative buyers or reposition or modify their products in sufficient quantities to render the price decrease unprofitable for the buyer.

5.21. Typically, if the merger parties buy only a small percentage of the total purchases of the relevant products, suppliers are likely to forgo sales to the merged firm in favour of other buyers. On the other hand, if the merger parties' purchases account for a large proportion of the total purchases, there is a higher risk the merged firm will be able to exercise monopsony or oligopsony power.

5.22. To determine whether the merged firm could exercise monopsony power the ACCC may consider whether:

- the merged firm can reduce price (or other terms) such that overall market prices are reduced (or overall market terms are worsened)

[36] In some economic texts 'monopsony' refers to a market where there is a single purchaser. However, the term is now often used to refer to a market structure where there are one or a few purchasers, each of which controls enough purchases that they can affect the market price.

- certain suppliers are likely to exit the market or otherwise reduce supply or investment in response to a price reduction, such that overall quantities are reduced
- suppliers could switch to selling their products to alternative buyers or a new buyer(s) would enter if prices decreased
- buyers of the relevant products have an incentive to restrict the quantities they purchase, taking into account the impact on their profits when they on-sell the related products
- if the merged firm reduced the amount it purchased, it would find it difficult to access adequate supply of the relevant product in the long run.

Mergers involving multi-sided platforms

5.23. Multi-sided platforms supply services to two or more distinct but related customer groups. For example, social media platforms supply services to users and advertisers, property platforms supply services to vendors and agents as well as buyers, and shopping centres supply services to shopkeepers and shoppers. Mergers involving platforms are generally analysed in a similar way to mergers involving differentiated products. However, there are some aspects of the analysis that are specific to platforms.

5.24. Multi-sided platforms generally have several attributes in common, including:

- multiple sides – on each side of a platform, participants provide or use distinct goods and services
- a platform operator – the platform operator provides the core services that enable the platform to connect participant groups across multiple sides, controls access to the platform and influences the interactions among platform participants
- platform participants – participation can vary from simply using the platform to find other participants, to building services for other participants to connect in new ways.

5.25. Platforms are often characterised by network effects, where the value of the product for customers on one side of the platform depends on the volume of users either on the same side (direct network effects) or on the other side (indirect network effects).

5.26. Network effects may operate in one direction (e.g. a social media network will be more attractive to advertisers if it has more users, but not vice versa) or both directions (e.g. a property platform will be more attractive to vendors and agents if it is accessed by many buyers, and more attractive to buyers if many vendors and agents use it to list their properties).

5.27. Where network effects are strong, the growth of a multi-sided platform may be reinforced: growth in user numbers increases network effects, and an increased network effect attracts more users. In some circumstances, the network effects may be so strong as to create a ‘tipping effect’ where one platform becomes supreme and smaller platforms only exert a weak constraint.

5.28. When assessing the potential for a merger involving a platform to give rise to unilateral effects, the ACCC may consider the impact on each side of the platform

separately, the impact on both sides of the platform, or the impact on overall competition between platforms. The ACCC considers that each side of a platform generally constitutes a separate market, while also recognising that each side may affect the other. The ACCC's approach will depend on:

- whether the merger will primarily affect one side or both sides of the platform
- the different incentives the platform operator has on each side of the platform
- the strength of any direct and indirect network effects
- the risk of a tipping effect
- the risk of amplifying market power (for instance, if interoperability or multi-homing is necessary to compete)
- the presence of any conflicts of interest
- barriers to entry and whether those barriers are increasing.

Mergers across multiple markets

5.29. This section discusses how the different approaches taken by firms active across local areas may affect the ACCC's approach to the competitive assessment. However, the broad principles set out in this section may also apply to the analysis of mergers involving firms that are active across multiple markets or segments of other types (such as product segments, customer groups, or distribution channels).

5.30. When firms operate across multiple markets, customers may consider those markets as distinct, for instance, because the product and geographic areas are not substitutes. For example, a customer located in Sydney will not typically make a retail purchase in Perth. However, there may be certain circumstances in which the ACCC might consider different markets together. In particular:

- if merger parties operate their businesses such that they set their competitive offering very similarly across all or some markets
- if competitive conditions are very similar across markets.

Similar competitive offering across markets

5.31. Firms may set their competitive offering uniformly across all markets, tailor their offering to suit the specific conditions in each area, or take a mixed approach, setting some conditions uniformly and tailoring others. How the merger parties operate their businesses will inform the ACCC's merger assessment. This includes an assessment of whether the way in which the merger parties operate is likely to change after the merger.

Box 7

Example of a merger involving pricing across multiple markets

A national supermarket may set pricing for staple products, such as packaged bread, cereal and toilet paper, on a national level, and its fruit and vegetables on a local level,

depending on supply chain costs and customer demographics. The supermarket may acquire a grocer that has outlets in three country towns and sets all prices locally.

5.32. In some cases, the price and non-price aspects of competition may depend on the conditions of competition across different geographic areas in aggregate. For example, even though buyers typically make a retail purchase in the local area in which they live (e.g. Bendigo), a retailer may set uniform prices across an entire state (e.g. Victoria). In such a case, the ACCC may consider the competitive constraint on merger parties at the state-level, as well as the local level. This involves considering the aggregate effectiveness of rivals to the merged firm across the state.

5.33. In contrast, when firms mainly compete by tailoring aspects of their offerings for the specific conditions within each local area, the ACCC's assessment will typically focus on competition at this narrower level. If important aspects of competition take place at the local and aggregate levels, the ACCC may carry out an assessment at both levels.

5.34. The ACCC may also consider how a merger might change the merged firm's incentive to set its competitive offering either on a local basis, or uniformly across different local areas. For example, a merger party may decide to move away from having a uniform competitive offering if a merger creates profitable opportunities to raise prices in individual local areas. This may be more of a risk when there is evidence the merger parties are considering changing their approach, other firms already take a different approach, or firms have been changing their approach over time. The strategies of each of the merger parties pre-merger may be relevant to this assessment. For example, one party offering uniform pricing (across local areas) might acquire a firm that does not. The ACCC may consider how the merger might affect those different strategies and the impact that will have on competition.

Similar competitive conditions across markets

5.35. The merger parties might have different prices and non-price offerings across different markets (i.e. localised offerings), but the ACCC might nonetheless assess these markets together if competitive conditions across the different local markets are sufficiently similar. In such a case, price differences between the different markets may be the result of differences in local demand, such as customer demographics, rather than differences in competitive conditions. For ease and expedience, the ACCC may consider competition in these markets in the aggregate.

Cumulative effects of mergers

5.36. In certain circumstances, the ACCC may be able to treat the effect of an acquisition as being the combined effect of the acquisition under review and certain previous acquisitions by a merger party put into effect in the 3 years prior to the notification date, regardless of whether each individual acquisition was notified to the ACCC

under the formal merger review system.[37] The timeframe of 3 years allows the ACCC to assess any strategic business behaviour and take account of dynamic competition in markets.[38]

5.37. For example, a firm may engage in a pattern of acquisitions in the same or related markets. These types of acquisitions, known as 'serial acquisitions', typically involve a firm acquiring a series of small companies over time, which the firm then consolidates. While an individual acquisition within the series may not substantially lessen competition, the combined effect of the acquisitions can raise competition concerns.

5.38. Serial acquisitions can enable firms to attain a position of substantial power in a market and erode competition. They can also be used by firms that already have a position of market power to extend or entrench that power.

5.39. Depending on the facts under assessment, serial acquisitions might raise these competition concerns:

- increased market concentration if the acquiring firm incrementally increases its market share which, over time, creates a large firm that can exercise control over price, service, quality or other elements of competition
- small or potential competitors might face increased difficulty reaching minimum efficient scale as the size of the available market is reduced
- the acquiring firm might maintain a stable of brands, which give the perception of choice, and make it harder for small rivals and potential entrants to establish a niche
- reduced competition can happen between chain stores: an acquiring firm that operates a chain might acquire a store in a competing chain, and this can impact marketing efficiencies, awareness, and the competitive presence of the competing chain
- reduced competition at different or multiple functional levels of a market can result from limiting access to a downstream customer or an upstream input. For example, a wholesaler might supply independent retail stores, and a vertically integrated firm might make a series of retail-level acquisitions, making it difficult for the wholesaler to maintain economies of scale and offer a competitive wholesale price to the remaining independent retail stores.

5.40. The ACCC may consider information or evidence regarding the merger parties' acquisition pattern and any overall strategic approach to serial acquisitions. This could include previous and future business plans, incentives behind the acquiring firm's acquisition strategy (whether the acquisitions were completed or not), and

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[37] Relevant acquisitions include those that involve goods or services that are the same or substitutable for, or otherwise competitive with, each other, irrespective of the geographic area in Australia. *Competition and Consumer Act (2010)*, s 51ABZH(6).

[38] Explanatory Memorandum to *Treasury Laws Amendment (Mergers and Acquisitions Reform) Bill 2024*, para 4.49.

evidence of the likely impact of both an individual acquisition and a series of acquisitions on the merged firm's market position.

Mergers involving partial acquisitions

5.41. In some situations, a firm could acquire a partial stake or minority interest in another firm in ways that may substantially lessen competition. While the ACCC may consider any way in which a partial acquisition may affect competition, we generally focus on four principal effects.

5.42. First, a partial acquisition can lessen competition by giving the firm making the partial acquisition (the investor) the ability to influence the competitive conduct of the target firm. For example, the investor may gain a voting interest in the target or specific governance rights, such as the right to appoint members to the board of directors, influence capital budgets, determine investment return thresholds, or select managers. Even a non-voting interest could, in some instances, provide opportunities to prevent, delay, or discourage important competitive initiatives, or otherwise impact competitive decision-making. This could include preventing or lessening the ability of the target to access capital for expansions or innovations. Such influence can lessen competition because the investor could use its influence to induce the target to compete less aggressively or to coordinate its conduct with the investor.

5.43. Second, a partial acquisition can lessen competition by reducing the incentive on the investor to compete in its own right. This may be because the investor might profit through dividend or revenue sharing, or capital gains from increased value in the target, even when it loses business to the rival. For example, an investor may decide not to develop a new product feature, because doing so could reduce the value of its investment in the rival. An investor's reduced incentives to compete can arise even when it cannot directly influence the conduct or decision-making of the target.

5.44. Third, a partial acquisition can lessen competition by giving the investor access to competitively significant information about the target. Even absent any ability to influence the conduct of the target, access to competitively significant information can substantially lessen competition through other mechanisms. For example, it can enhance the ability of the target and the investor to coordinate their behaviour and make other accommodating responses faster and more targeted. The risk of coordinated effects is greater if the transaction also facilitates the flow of competitively significant information from the investor to the target. Even if coordination does not occur, the investor might use that information to pre-empt or appropriate the target's business strategies for its own benefit. If the target knows its efforts to win customers can be immediately appropriated, it might not take the action in the first place.

5.45. Fourth, a partial acquisition can lessen competition by preventing another buyer from purchasing a share in or the whole of a target. For example, business A might be a close competitor to business B in the same industry. Business A might decide to acquire a minority interest in business C, which is a smaller rival, to prevent B from acquiring a stake in C and growing to better compete with A.

6. Countervailing factors

6.1. If the ACCC identifies potential competition concerns with a merger, we will consider whether there are countervailing factors that are relevant to the competitive process. These include entry or expansion by rivals, countervailing power of customers, and rivalry-enhancing efficiencies. Each of these countervailing factors is discussed below.

Entry or expansion by rivals

6.2. Entry and expansion by rivals can provide an important source of competitive constraint on incumbents and, in certain circumstances, may mean that a substantial lessening of competition is unlikely to arise. However, the ACCC will require robust evidence, typically including previous recent examples, to conclude that entry or expansion is sufficient to offset a loss of competition.

Framework for the analysis

6.3. Entry or expansion can remedy short-term competition concerns if it is likely, timely and sufficient to provide an effective constraint on the merged firm. These conditions are cumulative and must be satisfied simultaneously. For example, it might be possible for a new entrant to enter rapidly after a merger (entry may be likely and timely), but it may take some time for the entrant to become sufficiently large to constrain the merged firm (entry may not be sufficient).

6.4. When considering the likelihood, timeliness, and sufficiency of entry or expansion, the ACCC may also consider whether there are barriers that may inhibit entry or expansion.

6.5. An assessment of the likelihood, timeliness and sufficiency of entry might differ from that of expansion, with the latter typically referring to expansion by existing market participants into new, competitively relevant geographic areas or products. Expansion may also refer to investment in infrastructure to serve existing markets if those market participants are otherwise capacity constrained, or product repositioning by an existing competitor to offer a close substitute to that of the merged firm.

Likelihood of entry or expansion

6.6. Entry or expansion must be likely to prevent a substantial lessening of competition from occurring. The degree of likelihood is relevant to the weight the ACCC will give this countervailing factor in its competition assessment. Entry or expansion that is speculative or merely a possibility will be given less weight. The ACCC assesses ability and incentive by determining whether a new entrant could expect to make a

commercial return on its investment in entry or expansion sufficient to induce entry or expansion.

6.7. Evidence or information regarding firms actively planning to enter or expand pre-merger will be a relevant consideration. However, it is not necessary that potential entrants have existing (pre-merger) plans to enter. The evidence must demonstrate that entrants consider they could operate or expand profitably, or they could quickly become profitable if the merged firm increased prices or worsened non-price aspects of its good or service offer.

6.8. Firms may encounter barriers which reduce or even prevent their ability and incentive to enter or expand in the market. The ACCC may have regard to barriers to entry or expansion where relevant, such as those listed in Box 8.

Box 8

Barriers to entry or expansion

- Sunk costs: a cost that is not recoverable if the entrant subsequently decides to exit. High initial sunk costs, such as set-up costs and costs associated with investment in specific assets increase the risks associated with entry or expansion and therefore may act as a deterrent to entry.
- Economies of scale: if effective entry needs to be on a large scale, that increases the risk associated with entry because an entrant may face a long period of losses while it builds up sufficient sales to cover its costs.
- Network effects: a need to attract a large number of customers to one or both sides of a platform in order to become an effective competitor could increase the risks and costs associated with entry.
- Customer switching: the less likely customers are to switch to an entrant's product, the lower the likely profitability of entry, and therefore the lower the likelihood of entry. Factors that might make customers reluctant to switch include:
  - Customers placing high value on the reputation and track record of suppliers. This might be especially true where the good or service being provided is important for the customer, and the quality of the products is difficult to ascertain in advance.
  - Customers are tied into long-term contracts or exclusive agreements, or face other significant switching costs. For example, in some digital markets, switching might involve giving up access to an ecosystem of goods and services, or a history of engagement.
- Market maturity: mature markets with flat or declining demand may make entry or expansion less profitable and therefore less likely.
- Legal and regulatory requirements: legal and regulatory costs are typically sunk, increasing the risk associated with entry, and often impacting on timeliness. Such requirements can include licensing conditions, environmental and other government restrictions. In the case of imports, regulatory requirements may include tariffs.
- Access to requisite inputs: a lack of access to key production or supply assets, technologies or distribution channels as a result of shortages, intellectual property rights of rivals, and interoperability requirements can prevent or delay entry or expansion.

- Strategic barriers: the strategic behaviour of the merged firm or other incumbents might limit entry or expansion. This might include temporary price cuts, exclusive dealing arrangements or long-term contracts with customers, or customer termination fees or other means of increasing customer switching costs.
- A trend towards vertical integration: A vertical merger may raise barriers to entry if, as a result of the merger, new entrants would have to enter at multiple levels of the vertical supply chain instead of just one. A conglomerate merger may result in formerly separate markets becoming one integrated market in which suppliers must offer the full range of complementary products to compete. Future entry may therefore require an offering of the full range of products, potentially increasing the sunk costs associated with entry.

Timeliness of entry or expansion

6.9. The ACCC will consider the time it would take for a new entrant to enter, or for a rival to expand, to offer customers a competitive alternative to the merged firm. It is not just the entry or expansion that must be timely, but also the effectiveness of that entry or expansion on the competitive process.

6.10. The evaluation of timeliness will vary with each merger, the relevant industry, and the market dynamics. Generally, the further in the future that entry or expansion is likely to occur, the less certainty the ACCC can place on such entry or expansion occurring.

6.11. The ACCC may consider factors that affect how long it will take to achieve the necessary scale to provide an effective constraint on the merged firm, such as:

- the frequency of transactions – the more frequently transactions occur, the more opportunities there may be for new entrants to acquire customers; conversely, infrequent transactions may mean it takes longer for new entrants to establish themselves
- the nature and duration of contracts between buyers and sellers – in a market characterised by long-term contracts with extensive and ongoing obligations, it may take longer for new entrants to establish scale, compared to one characterised by short-term, standard form, take-it-or-leave it arrangements
- lead times for production – if it takes a long time for a product to be produced and available for supply, there will be a lag between new entrants beginning production and actively competing against incumbents.

Sufficiency of entry or expansion

6.12. The likely entry or expansion must be of sufficient scale, with a sufficient range of the relevant goods or services, to provide an effective competitive constraint on the merged firm. That is, the entry or expansion needs to have the potential to succeed over a sustained period. Sufficiency to constrain the merged firm may come from a single new entrant, an existing rival expanding, or from several new entrants or existing rivals in aggregate.

6.13. Entry at the fringe of the market is unlikely to be sufficient to constrain any attempted exercise of market power by the merged firm. For example, individual entry that is

small-scale, localised or targeted at niche segments is unlikely to represent an effective constraint.

Countervailing power

6.14. The ACCC may consider whether one or more customers would have sufficient countervailing power to constrain any attempted exercise of market power by the merged firm.[39] Countervailing power might exist when a customer can credibly threaten to bypass the merged firm, such as by:

- self-supplying, by vertically integrating into the upstream market including by establishing import operations
- sponsoring new entry.

6.15. Countervailing power is more than the ability of customers to switch to alternative domestic suppliers or importers. It refers to specific characteristics of a customer, such as its size, commercial significance to suppliers, or the way it purchases, which provide it with additional negotiating leverage.

6.16. For the countervailing power to prevent any exercise of market power by the merged firm, it will usually not be sufficient if only one customer or category of customers is able to bypass the merged firm post-merger. For example, the merged firm may be able to increase prices charged to smaller customers that are unable to bypass it, while larger customers with countervailing power may be able to avoid the increase.

Framework for the analysis

6.17. In assessing whether countervailing power is likely to prevent a substantial lessening of competition, the ACCC may consider:

- whether the threat to bypass is credible on commercial grounds
- whether the customer is likely to bypass the supplier
- dynamic market conditions.

Whether the threat to bypass is credible on commercial grounds

6.18. For self-supply or sponsored entry to be commercially viable, the substituted supplier will need to operate at an efficient scale of production. If self-supplying the product or purchasing it from a sponsored firm is insufficient to underpin a commercially viable production scale, the ACCC may need evidence that the substituted supplier could readily find additional sales to sustain an efficient scale of production.

[39] In a merger between buyers, countervailing power may also be exerted by one or more suppliers if they are able to bypass the merged firm and establish alternative supply channels. In line with the approach adopted throughout these guidelines, consideration is directed towards the case where the merged firm is a supplier in the relevant market.

Whether the buyer is likely to bypass the supplier

6.19. Evidence that a customer is likely to bypass the supplier could include plans or other documents suggesting such a strategy is commercially viable, as well as previous examples when the customer or other customers have bypassed, through sponsoring entry or vertically integrating.

Dynamic market conditions

6.20. The ACCC may consider whether customers could use countervailing strategies to address the potential for the merged firm to exercise market power, and whether doing so is likely to be effective. Over time, a customer that decides to self-supply a product may be a less effective constraint on the merged firm than a third party supplier, especially if the self-supplied product is not the customer's core business. For example, if product innovation or economies of scale are important elements of competition, self-supply is unlikely to be an effective countervailing measure.

Efficiencies

6.21. The potential for improved efficiency is a common motivation for firms to merge. A merger may allow the merged firm to realise efficiencies through a range of sources. These may differ depending on the type of merger under review (e.g. horizontal, vertical, conglomerate or a combination of these) but generally may include:

- reducing the costs of production by, for example, combining the merger parties' production, distribution and marketing activities (productive efficiencies)[40]
    - increasing economies of scale
    - re-allocating production and distribution activities
    - increasing information sharing
    - enabling customers to buy related products from one supplier
    - improving interoperability between related products
    - improving corporate control
    - combining investment in research and development
- releasing new goods or services optimally over time (dynamic efficiencies)
- internalising market transactions (leading to more efficient pricing through the elimination of double marginalisation).

6.22. The ACCC's focus in merger assessments is the effect of the merger on the overall competitiveness of the market, rather than the efficiency of individual firms. A merger that removes or weakens competitive constraints will in many cases substantially

[40] The relevant cost savings are those that allow the merged firm to produce a given volume of output with fewer inputs. The merged firm may also lower its costs by obtaining a lower price for a given amount of input because of enhanced bargaining power. Such cost reductions are pecuniary benefits, not efficiency gains. In some cases, a merger of two significant acquirers of an input can substantially lessen competition for the acquisition of that input. The ACCC will explore such issues separately from the impact of efficiencies on competitive constraints in the relevant supply market.

lessen competition even if the merger results in a more efficient firm with a lower cost structure.

6.23. The ACCC will generally only consider merger-related efficiencies to be relevant to our merger assessment when there is clear and compelling information or evidence that the resulting efficiencies directly affect the level of competition in a market. That is, efficiencies that change the incentives of the merged firm and encourage it to compete more vigorously against rivals. These kinds of efficiencies are described as rivalry-enhancing efficiencies.

6.24. In cases when a merger is likely to achieve other types of efficiencies, these may be considered if a merger party makes a public benefit application. Public benefits analysis is discussed in Chapter 7.

Framework for the analysis

6.25. When assessing rivalry-enhancing efficiencies, the ACCC may consider whether:

- they are merger-specific
- they are verifiable.

Merger-specific

6.26. The ACCC may assess whether the efficiencies are attributable to the merger, or whether they would likely be brought about by another means. The ACCC may also consider whether there are significant barriers to the merger parties achieving the same improvements without the merger.

6.27. Merger parties should provide all relevant information in their possession to demonstrate that there are no less anti-competitive alternatives to achieve the claimed efficiencies (e.g. a licensing agreement between the merger parties or a cooperative joint venture instead of a merger). The ACCC is likely to consider alternatives that are reasonably practical in the business situation faced by the merger parties. The ACCC is also likely to consider the incentives of the parties to implement alternatives and whether those alternatives are reasonably practical.

Verifiable

6.28. The evidence supporting efficiencies needs to be verifiable and show that the efficiencies are likely to materialise. The assumptions and related methodology used by the merger parties to arrive at the claimed efficiencies should be made available to the ACCC. There must be a likely, clearly identifiable and evidence-based positive impact on competition.

6.29. It is important that the merger parties provide all information in their possession to demonstrate that the claimed efficiencies are merger-specific and likely to be realised. When reasonably possible, efficiencies should be quantified. Similarly, merger parties should provide clear submissions outlining the bases on which they

assert the claimed efficiencies are likely to counteract any substantial lessening of competition that might otherwise result from the merger.

6.30. Evidence relevant to the assessment of efficiency claims may include:

- internal documents that were used by the management to decide on the merger
- statements from the management to the owners and financial markets about the expected efficiencies
- historical examples of efficiencies being realised
- pre-merger external experts' studies on the type and size of efficiency gains, and on the extent to which competition is likely to be enhanced.

7. Public benefits

7.1. If the ACCC determines that the proposed merger may not be put into effect because it is likely to substantially lessen competition, or determines that the proposed merger may be put into effect with conditions, a merger party may apply for a determination that the merger should be allowed to proceed on the basis of a net public benefit.

7.2. To approve a merger based on a net public benefit, the ACCC must be satisfied that:

- the acquisition would, in all the circumstances, result, or be likely to result, in a benefit to the public; and
- the benefit would, in all the circumstances, outweigh the detriment to the public that would result, or be likely to result, from the acquisition.[41]

The weighing of benefits and detriments

7.3. In assessing whether there is a net public benefit, the ACCC will assess the magnitude of any lessening of competition and any other detriments to the public likely to result from the merger, the magnitude of the public benefits likely to result from the merger, and weigh the detriments against the benefits.

7.4. In weighing the benefits and detriments, the ACCC may place less weight on those that are less likely to occur, those for which the evidence is less strong, and those that may not be realised for some time.

Meaning of public benefit

7.5. 'Public benefit' is not defined in the Act. The Tribunal has given it a broad meaning, as including:

> "[A]nything of value to the community generally, any contribution to the aims pursued by society including as one of its principal elements (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress." Plainly the assessment of efficiency and progress must be from the perspective of society as a whole: the best use of society's resources. We bear in mind that (in the language of economics today) efficiency is a concept that is usually taken to encompass "progress"; and that commonly efficiency is said to encompass allocative efficiency, production efficiency and dynamic efficiency.[42]

7.6. In assessing the benefits that are likely to flow from a merger, the ACCC is guided by all relevant matters, including the interests of consumers, and the underlying object of the Act to enhance the welfare of Australians through the promotion of

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[41] *Competition and Consumer Act (2010)*, s 51ABZW(2).

[42] *Re 7-Eleven* (1994) ATPR 41-357 at [42,677]. See also *QCMA* (1976) ATPR 40- 012, at 17,242 and *VFF Chicken Meat Growers' Boycott Authorisation* (2006) ACompT 9 at [75].

competition and fair trading and providing for consumer protection.[43] The ACCC may consider any benefits that would result from the merger regardless of the market in which that benefit arises.

7.7. The ACCC will assess (among other things):

- whether the anticipated benefit is specific to the merger
- to whom the benefit accrues and how widely it is shared in the community
- whether the benefit is ongoing or a one-off
- when the benefit is likely to arise
- the likelihood that the benefit will be realised
- the magnitude of the benefit.

Attaching weight to public benefits

7.8. The ACCC generally considers whether benefits are of value to the community generally and, if so, how much weight society attaches to those benefits.

7.9. Cost savings or productive efficiency gains achieved can constitute public benefits in cases where it ultimately leads to public outcomes including a reduction in prices to customers or dividends to a range of shareholders.[44] However, the weight to be given to such cost savings 'depends on the extent to which they are passed through to consumers'.[45]

7.10. The weight to be given to a particular benefit requires an assessment of its nature, characterisation and the identity of the beneficiaries to it.[46] This includes considering who obtains the benefit to the public, and the period over which the benefits are received.[47] It is not always necessary for the savings to be passed on in the form of

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43 Competition and Consumer Act (2010), s 51ABZW(3).

44 *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [77], citing *Re Qantas Airways Ltd* [2004] ACompT 9 at [189]-[190].

45 *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [77], citing *Re Qantas Airways Ltd* [2004] ACompT 9 at [189]-[190].

46 *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [80], citing *Re Qantas Airways Ltd* [2004] ACompT 9 at [188].

47 *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [80], citing *Re Qantas Airways Ltd* [2004] ACompT 9 at [189].

lower prices. The community at large may have an interest in resource savings because these resources may be released for use elsewhere in the economy.

The meaning of public detriments

7.11. 'Public detriment' is not defined in the Act, but the Tribunal has defined it as including:

> [A]ny impairment to the community generally, any harm or damage to the aims pursued by the society including as one of its principal elements the achievement of the goal of economic efficiency.[48]

7.12. The ACCC considers that all public detriments likely to arise from the merger can be taken into account.[49]

7.13. It may be appropriate for the ACCC to assess detriments that occur outside of the market or markets in which a lessening of competition has been identified. For example, if the merger was likely to increase pollution or reduce public health and safety, the ACCC would take this into account in balancing the public benefits and detriments.

7.14. In most cases the likely identifiable detriments will be those constituted by a lessening of competition. However, in the context of a public benefits assessment, a lessening of competition does not have to be substantial to comprise a detriment to the public.[50]

Quantifying public benefits and detriments

7.15. The Act does not require the ACCC to quantify the level of public benefits and detriments likely to result from a merger. However, where possible, and particularly with complex applications, the ACCC encourages applicants to quantify the size of claimed benefits and detriments.

7.16. Quantification can provide guidance on the relative weight to be attributed to particular benefits and detriments in the ACCC's balancing exercise. Where

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[48] *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [78], citing *Re 7-Eleven* (1994), ATPR 41-357 at [42,683]; *Application by Medicines Australia Inc* [2007] ACompT 4 at [108]; (2007) ATPR 42-164.

[49] See *Re Australian Association of Pathology Practices Incorporated* (2004), ATPR 41-985 at [93]-[94].

[50] See, for example, *Australian Competition and Consumer Commission v Australian Competition Tribunal* [2017] FCAFC 150 at [11]: 'a mandatory consideration in the Tribunal's assessment of an acquisition will include any non-trivial competitive detriment which will result, or is likely to result, from the acquisition whether it occurs on a market-wide basis or not.'

applicants provide monetary estimates of the value of the benefits or detriments, they should also provide the ACCC with extensive details, including:

- the data relied on
- the methodology used
- the assumptions and reasoning upon which the estimates rely
- the bases for the assumptions and reasoning.

Without the detail and transparency behind the modelling used in the calculations, it may be difficult for the ACCC to place much weight on the magnitude of the claims.

7.17. The ACCC recognises that in many cases it will not be possible to precisely quantify public benefits and detriments and therefore welcomes both quantitative and qualitative evidence. The assessment of benefits and detriments does not necessarily involve an arithmetical or accounting exercise.[51] Claims of this nature will usually need to be qualitatively assessed and there must be a sufficient basis for concluding that the benefits and detriments are likely to result from the merger.

7.18. In practice, a qualitative assessment involves making a judgment about the likelihood and size of the public benefit and detriment, having regard to all the information the ACCC has considered.

7.19. In all cases, the ACCC expects applicants to provide robust evidence of benefits and detriments when applying for a public benefits assessment.

7.20. Where an applicant considers its efficiency will improve, it should provide evidence to substantiate these claims. Such evidence could include accounting statements, internal studies, strategic plans, integration plans, management consulting studies, consumer surveys or research, and other available data.

7.21. The Tribunal in *ANZ/Suncorp* provided the following summary of further principles governing public benefit analysis, which were originally set out in Qantas Airways at [203]-[209]:

> an accurate, objective quantification of public benefits is difficult, in part because benefits have to be estimated for some period in the future and so their magnitude becomes a matter not only of empirical estimation based on assumptions but also one of statistical likelihood;
>
> the nature of public benefits should be defined with some precision, a degree of precision which lies somewhere between quantification in numerical terms at one end of the spectrum and general statements about possible or likely benefits at the other end of the spectrum;

51 *Australian Competition and Consumer Commission v Australian Competition Tribunal* [2017] FCAFC 150 at [68].

any estimates involved in benefit analysis should be robust and commercially realistic, in the sense of being both significant and tangible;

appropriate weighting will be given to future benefits not achievable in any other less anti-competitive way, and so the options for achieving the claimed benefits should be explored and presented;

the Tribunal is not assisted by fanciful and speculative modelling of benefits where the underlying assumptions are not clearly spelled out, where the estimates have not been subject to rigorous sensitivity analysis, and where the estimating process is not wholly transparent;

while detailed quantification of benefits is the best option, quantification is not required by the CCA and benefits should be quantified only to the extent that the exercise enlightens the Tribunal more than the alternative of qualitative explanation; and

where benefits cannot be quantified in monetary terms, they can still be claimed in qualitative terms.[52]

[52] *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [81] citing *Re Qantas Airways Ltd* [2004] ACompT 9 at [203]-[209].

Appendix 1 – Market definition

The ACCC's approach to market definition

1. The Act requires that a substantial lessening of competition occur in a market for goods and services in Australia, or a state, territory or region of Australia.[53] Accordingly, in assessing whether a merger substantially lessens competition, the ACCC will examine the competitive impact of the transaction in the context of the markets relevant to the merger.
2. The ACCC's experience is that in many mergers, the evidence and information gathered as part of the competition assessment, which includes an assessment of the constraints on the merger parties, captures the competitive dynamics more fully than formal market definition.
3. In some cases, the ACCC may take a simple approach to defining the market – for example, by describing the market as comprising the most important constraints on the merger parties that have been identified in the ACCC's competition assessment. Evidence and information on the closeness of competition between different firms can often be interpreted from documentary and oral sources, such as internal documents discussing competitors, views from customers or competitors on the closest substitutes to the merger parties' products, analyses of bidding data, evidence on diversion between different firms, and data on customers won and lost.
4. However, formal market definition, in the sense described below, can sometimes be helpful in developing certain types of evidence that may be relevant to the competition assessment. For example, the ACCC may define the market as a basis to calculate market shares or for developing other measures of concentration, which may be helpful in some cases (especially where products are undifferentiated). On the other hand, measures of concentration can often be interpreted without concluding on a bright-line market definition. For example, the ACCC may assess concentration measures on multiple different bases, including and excluding different products, depending on which products the ACCC wishes to compare. The ACCC may attach greater weight to concentration measures that include firms whose products are more substitutable, and less weight to concentration measures that include firms whose products are less substitutable.
5. While market definition can sometimes be a useful tool, it is not an end in itself. The outcome of any market definition exercise does not determine the outcome of the ACCC's competition assessment in any mechanistic way. The ACCC may take into account constraints outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. In many cases, there is no 'bright line' that can or should be drawn around a market. Rather, it can be more helpful to describe the constraint posed by different categories of products as sitting on a continuum between 'strong' and 'weak'. The ACCC will generally not need to come to precise judgements on what is inside or outside the market. Not every firm in a market will be equal and the ACCC will assess how closely the merger parties compete with different firms. The constraint posed by firms outside a putative market will also be considered.

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[53] *Competition and Consumer Act (2010)*, s 50(6).

What is a market?

6. Section 4E of the Act defines a market as including goods or services that are substitutable for, or otherwise competitive with, the goods or services under analysis. Accordingly, substitution is the essential concept of market definition.[54]
7. In *QCMA*, the Trade Practices Tribunal described a market this way:

> A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them … Within the bounds of a market there is substitution — substitution between one product and another, and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long-run, if given a sufficient price incentive.[55]

8. Market definition establishes a relevant field of inquiry for merger analysis, identifying those sellers and buyers that may potentially constrain the commercial decisions of the merger parties pre-merger and the merged firm post-merger. It also identifies those participants, particularly customers, that may be affected if the merger lessens competition.
9. However, the ACCC may not draw a clear line around a field of inquiry. The concept of a market is not susceptible to 'precise comprehensive definition'.[56] Market definition is 'not an exact physical exercise to identify a physical feature of the world' and 'there is often little or no utility in debating or identifying "the precise physical metes and bounds of the market"'.[57]
10. As noted by Justices Kiefel and Gageler in Flight Centre:

> The question does not necessarily admit of a unique answer. Because "[t]he economy is not divided into an identifiable number of discrete markets into one or other of which all trading activities can be neatly fitted", the identification and definition of a market for particular services will often involve "value judgments about which there is some room for legitimate differences of opinion".[58]

11. Market definition is purposive, meaning that it is a tool to assess whether a merger might have competitive effects. The definition of a relevant market cannot be separated from the merger under investigation. In Air New Zealand, Gordon J described market definition as a 'focusing process', used to orientate the analysis of the competitive effects of a merger.[59] It will always depend on the specific facts and circumstances of the merger under review, and current evidence from market participants will be critical. Decisions relating to market definition in previous, albeit similar, merger reviews will provide only limited guidance.
12. The purposive nature of market definition means that the market or markets that will be relevant to the ACCC's assessment will depend on the potential competitive effects that the ACCC is investigating. In practice, the ACCC does not define the market or markets in the abstract, and then investigate potential competitive effects, but rather defines the

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[54] *Applications by Australia and New Zealand Banking Group Limited and Suncorp Group Limited* [2024] ACompT 1 at [62].

[55] *QCMA* (1976) 8 ALR 481 at [513].

[56] *Air New Zealand v ACCC* [2017] 262 CLR 207 at [59] (Gordon J).

[57] *Air New Zealand v ACCC* [2017] 262 CLR 207 at [59] (Gordon J)].

[58] *ACCC v Flight Centre Travel Group Ltd* [2016] HCA 49 at [69].

[59] *Air New Zealand v ACCC* [2017] 262 CLR 207 at [57]-[59] (Gordon J).

market or markets for the purpose of assessing whether the merger under review is likely to result in competitive effects.

Defining markets

13. The ACCC's starting point for delineating relevant markets is to identify the products and geographic regions actually or potentially supplied by the merger parties.[60] The ACCC focuses on defining markets in areas of activity where competitive harm could occur. This must be assessed on a case-by-case basis. Generally, the ACCC focuses on overlaps between the products or geographic regions supplied by the merger parties, or some other meaningful economic relationship — such as an actual or potential vertical relationship or where the products supplied by the merger parties are complementary in nature. It is not uncommon for more than one market to be identified.
14. The ACCC then considers if any other products and geographic regions constitute relevant close substitutes. Importantly, the ACCC defines markets by reference to products and regions not by reference to the firms supplying those products or regions at the time of the merger.

Hypothetical monopolist test

15. The degree of substitutability between different products and regions is best tested by asking if there would there be a significant switch in demand or supply in response to a relatively small price increase (all other competitive variables being unchanged).[61] In practice, this is reflected in the test known as the small but significant and non-transitory increase in price (SSNIP) and the hypothetical monopolist test (HMT).
16. The HMT determines the smallest area in product and geographic space within which a hypothetical current and future profit-maximising monopolist could effectively exercise market power. In general, the exercise of market power by the hypothetical monopolist is characterised by a profitable imposition of a SSNIP, assuming the terms of sale of all other products are held constant. In appropriate cases, instead of using a SSNIP, the ACCC may consider an equivalent reduction in the value offered to customers in quality, range or service.
17. The process of applying the HMT starts with the focal product and geographic space, which is where competitive effects may arise. If a hypothetical monopolist supplier of this product cannot profitably institute a SSNIP because customers would switch to alternative products in sufficient quantity to render the price increase unprofitable, the next closest demand substitute is added. If a hypothetical monopolist supplier of this extended group of products cannot profitably institute a SSNIP for at least one product in the group, because customers would switch to alternative products in sufficient quantities to render the price increase unprofitable, the next closest demand substitute is added. The collection of products is expanded until a hypothetical monopolist supplier of all those products could profitably institute a SSNIP over at least one product.
18. The critical issue is that, if there was a SSNIP, or equivalent degradation in a non-price aspect, a significant volume of customers would switch, such that the change would be

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[60] There need not be trade in a product for a separate market to exist — the potential for exchange can be sufficient. See, for example, *Queensland Wire Industries Pty. Ltd v The Broken Hill Proprietary Company Limited & Anor* [1989] HCA 6; (1989) 83 ALR 577; ATPR 40–925, Dawson J at [591] (ALR).

[61] Maureen Brunt, 'Market Definition Issues in Australian and New Zealand Trade Practices Litigation', *Australian Business Law Review* (April 1990), pp 93-94.

rendered unprofitable. In cases where such a small proportion of customers are likely to switch that a price increase would not be profitable, it may be unlikely that the alternative product is part of the relevant market.

Applying the HMT

19. As a general principle, when applying the HMT, the ACCC typically focuses on the product and geographic dimensions in which market participants compete. In both cases, there are two types of substitution that the ACCC considers:

    - demand-side substitution, which takes the perspective of customers and explores their substitution possibilities
    - supply-side substitution, which takes the perspective of suppliers and explores their substitution possibilities.

20. The product and geographic dimensions of the market are identified primarily by considering demand-side substitution. The views, strategies and behaviours of customers are often reliable indicators of whether customers would be likely to switch in response to a SSNIP. The ACCC may examine what customers have done in the past and what they would be likely to do in the future. Information from industry participants, such as competitors and manufacturers of the product, will also be taken into account.

21. The ACCC may rely on several types of information or evidence to define the product and geographic dimensions of a market, for example:

    - business records showing what the merger parties and other market participants regard as the field of competition
    - patterns of substitution in response to changes in relative prices
    - patterns of substitution from natural experiments when, for example, a business closed for repairs or an upgrade
    - competition between the merger parties
    - the exercise of market power.

Product dimension

22. A relevant product market consists of a given product of the merger parties and all substitutes required for a SSNIP to be profitable.

23. It will often be possible on the demand-side, to some degree, to substitute a wide variety of products for the products of the merger parties. Not all these substitutes will be included in the relevant market. For instance, some customers might view seemingly remote products as substitutes under some circumstances. This simply illustrates that an economy is essentially 'a network of substitution possibilities'.[62]

24. On the other hand, substitution does not have to be complete or instantaneous, and products do not have to be perfect substitutes to form part of the same market. To be included in the relevant market, the ACCC's view is that a product in a particular geographic region (or a group of products or regions) must be a close substitute in demand.

25. The ACCC will often consider qualitative evidence and will not always seek to produce quantitative estimates of what customers would do in response to a SSNIP, or how such

[62] *Re Tooth & Co Ltd* (1979) 39 FLR 1, at [38]-[39].

responses would affect the profitability of a supplier or suppliers. Nevertheless, the ACCC may still consider conceptual aspects of the HMT when defining markets. The ACCC may also require a variety of information from the merger parties and market participants to examine various substitution possibilities.

Geographic dimension

26. As with the product dimension, the ACCC's focus in defining the geographic dimension of a market is on demand-side substitution and identifying the most important alternatives to the merged firm. The ACCC will investigate the willingness of customers to switch from a product supplied in one location to the same product supplied in another location in response to a SSNIP or an equivalent degradation in a non-price aspect.
27. The ACCC may consider evidence such as:
    - information on the competitive performance of firms supplying from different geographic areas or over different distances
    - information on differences in pricing, sales, advertising and marketing strategies by area, as well as information on delivery costs or barriers to supplying into an area or over different distances or across borders
    - the views of market participants on consumer preferences
    - product characteristics such as perishabili

Supply-side substitution

28. The boundaries of the relevant product market are generally determined by reference to demand-side substitution. However, there are circumstances where the ACCC may consider possible substitutes in supply.
29. A product (or group of products) may be a supply-side substitute for a focal product if, in response to an increase in the price of the product, suppliers can adjust their production plans, substituting another product in their output mix for that product or substituting one geographic source of supply for another.
30. To be a supply-side substitute, the firm must be able to switch production relatively rapidly, using existing assets and without incurring significant expenditure. This is to be distinguished from opportunities for new entry, which may require significant expenditure or the acquisition of new assets. Whether substitution is feasible or likely can depend on factors such as customer attitudes, technology, distance, and cost and price incentives.[63] Another consideration is whether it would be profitable for suppliers to switch production; that is, the profits earned on the assets in their current use would be less than if they were switched to supply a substitute for the products of the merger parties.
31. In most cases, entry or expansion by rivals that could supply substitutable products to the merger parties will entail some challenges and costs, and so should be considered as part of the competition assessment, as discussed in Chapter 6, and not as a form of supply-side substitution.

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[63] *Applications by Telstra Corporation Limited and TPG Telecom Limited (No 2)* [2023] ACompT 2 at [113] citing *QCMA* (1976) 8 ALR 481 at [513].

Specific issues that may arise in the context of market definition

Discrimination and customer-specific markets

32. Where substitution possibilities are not uniform across customer groups, it may be appropriate to define separate markets for different customer groups.[64] For example, some customers might view two products to be highly substitutable while other customers might consider the same products to be, at best, weak substitutes.

33. The ability of suppliers to discriminate between different customer groups will depend on their ability to:

    - distinguish between those customers that have the option of substitution and those who do not, and

    - prevent resale or arbitrage between customer groups.

34. If suppliers can discriminate, a customer that has limited substitution possibilities may receive different terms and conditions to a customer that has strong substitution possibilities. It may be appropriate in this situation to consider separate markets. The number of relevant markets will depend on the number of customers or groups of customers that face different prices as a result of facing different competition conditions.

35. If suppliers are unable to discriminate between customer groups, they will provide the same prices and levels of service to all customers, regardless of their substitution possibilities. In this situation, there are unlikely to be separate markets based on different customer groups. Customers that are unable to substitute to an alternative product will be protected to the extent that suppliers cannot distinguish them from customers that are able to switch.

Asymmetric substitution

36. Substitution possibilities are not necessarily symmetric. Asymmetric demand-side substitution occurs when substitution between two products only occurs in one direction. For example, buyers of luxury cars may substitute to more standard cars in response to an increase in the price of luxury cars, but the opposite may not be the case.

37. The relevant pattern of substitution is substitution for the focal product. For example, if the concern is with the supply of luxury cars, standard cars may be relevant substitutes, but if the concern is with the supply of standard cars, luxury cars may not be relevant substitutes.

Platforms and other multi-sided markets

38. As discussed in Chapter 5, platforms intermediate between two or more groups of customers. For example, food delivery apps are platforms that intermediate between customers and restaurants. The number in each group can affect the profitability of the services supplied by the platform, because the value that one group realises from using the platform can depend on the volume of users in the other group (also called indirect network effects).

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64 *ACCC v Pacific National* [2020] FCAFC 77 at [137]-[139].

39. The price that platforms charge to each group of customers takes account of the need to get both sets 'on board'. It may therefore be difficult to conduct the HMT because:
    - there is no single price to both sets of customers to which to apply a SSNIP
    - the effect of a SSNIP on the demand of one group of customers may be exacerbated by indirect network effects
    - the constraints on the merger firms' products may come not only from other platforms but also from 'one-sided' firms serving one set of customers (e.g. restaurants offering take-away services).
40. The relevant question therefore becomes whether a hypothetical monopolist would find it profitable to increase prices by a SSNIP to one customer group, given the impact on purchases from these customers and other customer groups. In these cases, the ACCC may consider the interdependencies in demand between different groups of customers when defining the relevant market on each side of the platform.

Market shares and concentration

41. The ACCC may use market shares as an early indication of whether a merger is more likely to give rise to competition concerns, for instance, because the merged firm would have a very high market share, or the market is already concentrated. However, the ACCC approaches market share data with caution. The accuracy of market shares depends on the market definition, and high market shares are not necessarily an indicator of market power.[65] Conversely, a firm with a low market share might nevertheless be significant to the competitive process, for instance, because it is a maverick.
42. Consequently, while the ACCC pays attention to market shares, they are not determinative of a merger assessment.

Calculating market shares

43. How market shares are calculated depends on the characteristics of the market and the availability of data. When interpreting shares based on historical data, the ACCC may consider whether significant recent or reasonably foreseeable changes to market conditions suggest that a firm's historic shares overstate or understate its current and future competitive significance. The ACCC may measure market shares on multiple metrics that are commercially relevant. For example:
    - revenues in a relevant market often provide a readily available basis on which to compute shares and are often a good measure of attractiveness to customers
    - unit sales may provide a useful measure of competitive significance in cases where one unit of a low-priced product can serve as a close substitute for one unit of a higher-priced product. For example, a new, much less expensive product may have great competitive significance if it substantially erodes the revenues earned by older, higher-priced products, even if it earns relatively low revenues
    - revenues earned from recently acquired customers (or paid to recently acquired buyers, in the case of merging buyers) may provide a useful measure of competitive significance of firms in cases where trading partners sign long-term contracts, face switching costs, or tend to re-evaluate their relationships only occasionally

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65 Rhonda L. Smith, 'Mergers', *Research Handbook on Methods and Models of Competition Law*, Deborah Healey, Michael Jacobs, Rhonda L. Smith (eds.) (Edward Elgar), 2020, p243.

- measures based on capacities or reserves may be used to calculate market shares in markets for undifferentiated products where a firm’s competitive significance may derive principally from its ability and incentive to rapidly expand production in a relevant market in response to a price increase or output reduction by others in that market (or to rapidly expand its purchasing in the case of merging buyers)
- non-price indicators, such as number of users or frequency of use, may be useful indicators in markets where price forms a relatively small or no part of the exchange of value

Measuring concentration

44. The Herfindahl-Hirschman Index (HHI) is one measure of market concentration the ACCC may use. We may also consider other measures, such as concentration ratios.
45. The HHI is a formula model for measuring the degree of concentration in a market based on market shares. The HHI produces a number by squaring the market share of each firm in the relevant market, including the merger parties, before and after the proposed merger, and adding the results to produce a final number. The higher the resulting number (10,000 being the highest possible), the more concentrated the market. The HHI then subtracts the pre-merger number from the post-merger number to determine the likely increase in concentration, expressed numerically. The increase is called the ‘delta’.
46. The ACCC considers markets with an HHI greater than 2,000 are highly concentrated, and a delta of more than 100 points is a significant increase in concentration. The accuracy of the HHI and delta calculations depend on the accuracy and availability of the information before the ACCC and the definition of the relevant market. HHI may be used as a tool by the ACCC where appropriate, but it is not determinative of market concentration.

Appendix 2 – Counterfactuals

What are counterfactuals?

1. A merger assessment involves a comparison between the circumstances that are likely in the future if the merger proceeds and the circumstances that are likely in the future if the merger does not proceed. The latter is known as a counterfactual, and the comparative exercise is called the 'with and without' test. This is a 'tool of analysis' to assist in answering the question of whether the likely effect of the merger is meaningful and relevant to the competitive process.
2. A counterfactual may consist of the prevailing, or pre-merger, conditions of competition (status quo counterfactual), or conditions of competition that involve stronger or weaker competition than in the status quo (alternative scenario counterfactual). The assessment of the future without the merger may affect the ACCC's views about whether there is likely to be a substantial lessening of competition in the future with the merger.

The ACCC's approach to counterfactuals

3. The ACCC will consider the range of possible counterfactuals and consider two issues as part of a single evaluative judgment: first, whether it is commercially realistic that a counterfactual will eventuate, and second, the intensity or degree of competition (and in the case of a public benefits assessment, the intensity or degree of public benefit and public detriment) that would materialise if events did or did not eventuate.
4. Typically, the best starting point for the counterfactual analysis is the prevailing conditions of competition, that is, the conditions of competition existing before the merger was anticipated. This is known as a 'status quo' counterfactual.
5. In some cases, it may be necessary to consider likely and imminent changes in competition to accurately reflect the nature of rivalry in a future without the merger, such as:
   - entry, expansion or exit plans by competitors
   - significant expansion by one or both merger parties
   - exit by one or the other of the merger parties.
6. Establishing appropriate counterfactuals is an inherently uncertain exercise and evidence relating to future developments absent the merger may be difficult to obtain. However, uncertainty about the future will not in itself lead the ACCC to assume the pre-merger situation is an appropriate counterfactual. The ACCC may consider the likelihood of the merger parties pursuing alternatives to the merger. This may may involve reviewing evidence of specific plans or documents evidencing their intentions where available.
7. As was observed in the joint judgment of Justices Middleton and O'Bryan in Pacific National:

> In the usual case, predictions about the nature and extent of competition in the future with and without the acquisition will be rooted firmly in past and present market conditions, which are susceptible of proof in the ordinary way. Most markets have a history from which an assessment of substitution possibilities, concentration, barriers to entry and other commercial behaviours and conditions can be undertaken and reliable predictions about the future can be made. Further,

some future facts are more certain than others. For example, commercial firms and governments make plans about investment or entry into markets, which are observable facts able to be proved in the ordinary way.[66]

8. The identification and assessment of counterfactuals is not distinct from the assessment of whether a merger would have or would be likely to have the effect of substantially lessening competition. Counterfactual analysis is one part of the single evaluative judgment the ACCC applies to assess any change in the state of competition. The analysis involves multiple elements: identifying the likely future(s) with and without the merger, identifying the effect on competition of each and making a comparison, as part of considering the ultimate question of whether a merger substantially lessens competition. Conceptually, the counterfactual has no separate purpose, other than as an aid to detect the existence and extent of change in the state of competition.[67] The elements of the analysis form a single evaluative judgment.

Alternative scenario counterfactuals

9. As noted above, in some cases, there may be information or evidence to suggest that the conditions of competition are likely to materially change regardless of the merger, and those changes would not be accounted for in a status quo counterfactual. In these circumstances, the ACCC may consider an alternative scenario counterfactual.

Potential competition

10. The prevailing state of competition could understate the future state of competition without the merger in situations where one of the merger parties would have entered the market or expanded if the merger did not take place. For example, one merger party might be a start-up company or newly active in a market, and without the merger, may continue to grow. Alternatively, an established firm might decide to enter a new market through acquisition, when it otherwise would have invested in organic entry by developing its own products. In both scenarios, a merger may eliminate potential competition between the merger parties.

Failing firms

11. The state of competition prevailing at the time of a merger may overstate the future state of competition without the merger in situations where one of the merger parties is likely to exit the market. In those cases, the ACCC compares the likely future state of competition with the merger against the likely future state of competition without the merger (where the firm exits or fails).

12. In our assessment, the ACCC will consider whether each of the following features are present:

    – absent the acquisition, the firm is likely to exit (through failure or otherwise)

    – there is not an alternative purchaser of the firm or its assets that raises lesser competition concerns

    – the likely state of competition with the merger would not be substantially less than the likely state of competition after the target has exited and the target's customers have moved their business to alternative sources of supply.

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66 *ACCC v Pacific National Pty Ltd* (2020) 277 FCR 49 at [218].

67 *ACCC v Metcash Trading Ltd* [2011] FCAFC 151 at [228] (Yates J; Finn J agreeing).

Glossary and shortened forms

Term	Meaning
ACCC	Australian Competition and Consumer Commission.
Act (the)	Competition and Consumer Act 2010 (Cth), formerly the Trade Practices Act 1974 (Cth).
complementary products	Products are complementary in either demand or supply where a change in the demand for one generates demand for the other. If the price of one product rises, demand for both products may fall. Similarly, if the price of one product falls, demand for both products may increase.
conglomerate merger	A merger between firms that are not active within the same supply chain, but are related in other ways — for example, the firms may buy or supply products that are complements, or customers may prefer to buy their products together.
differentiation	Differences in the features of a range of products that all serve the same function.
economies of scale	The economic principle whereby a product's average total cost of production decreases as its output increases.
failing firm	A firm that is likely to exit a particular market in the foreseeable future (generally within one to two years) with its productive capacity leaving the market — that is, not simply a change in ownership.
foreclosure	When a firm hinders a rival firm from competing effectively.
HHI	Herfindahl-Hirschman Index — a metric used to estimate the post-merger level of concentration of markets, as well as changes in the concentration of markets as a result of a merger. The HHI is calculated by adding the sum of the squares of the market share of each firm in a particular market.
HMT	Hypothetical monopolist test — a conceptual tool used for defining relevant markets. It identifies the smallest group of products and the smallest geographic area in which a hypothetical monopolist could profitably impose and sustain a significant and non-transitory price increase/decrease above/below levels that would likely exist in the absence of the merger.
horizontal merger	The merging of firms that are competitors.
market	A market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are substitutable for, or otherwise competitive with, the first-mentioned goods or services.
market participant	A firm that operates in a particular market or markets, such as a supplier or customer.
maverick firm	A firm with a relatively small market share that is considered a vigorous and effective competitor, which generally drives significant aspects of competition, such as pricing, innovation and/or product development.
minimum efficient scale	The level of output at which a firm can produce a product at the lowest average cost.

multi-sided platform	A platform that supplies services to two or more distinct but related customer groups.
niche segment	A portion of a differentiated market serviced by small, specialised suppliers and often involving products that are in some way distinct from the products of larger suppliers.
product	A product encompasses a good or service.
notification threshold	The threshold established in legislation that identifies which mergers must be notified to the ACCC.
SSNIP	Small but significant and non-transitory increase in price.
sunk costs	Costs that cannot be recovered on exiting the market.
switching cost	The cost for customers to switch suppliers (including search costs, transaction costs and market specific behaviour).
Tribunal (the)	Australian Competition Tribunal.
vertical merger	A merger involving firms operating or potentially operating at different functional levels of the same vertical supply chain.