Klick
Antitrust
Final Exam
Summer 2015

You may use your casebook, notes, and commercial outlines in the completion of this exam, but you may not confer with anyone else about it during the exam period (June 19 – June 22). You have 8 hours to complete the exam starting once you download it, but it must be submitted by 11:59 pm on June 22. Each question (1, 2, and 3) is equally weighted subject to your choice in question 4. Good luck.

1. In Gary Becker's famous model of discrimination, he concluded that discrimination against employees of a disfavored class based on an owner's animus against that class was not sustainable in a competitive equilibrium. Essentially, Becker reasoned that such discrimination would raise the employer's costs relative to non-discriminating employers (since the discriminating employer would not be choosing the best available workers), and this cost disadvantage would raise the prices charged by the discriminating employer, leaving that employer unable to compete in a market where other firms did not experience such a cost disadvantage. However, in a monopolistic market, this conclusion does not hold; thus, one way to counter employment discrimination is to ensure that markets are more competitive. What about the case where employers in a given market are not directly discriminatory (i.e., the employer feels no animus toward a given class of people), but an overwhelming number of consumers in that market do prefer that the good in the market is not served/produced/serviced/etc. by members of the disfavored group? What is the likely effect of competition on the resulting level of employment discrimination observed in a market such as this in equilibrium? Could the insights of such a model be used by the parties in a merger or monopolization case?

In a market where consumers are discriminatory, increasing competition may increase the discriminatory behavior of the firms serving those consumers. In the case where it is the firm owners who have a taste for discrimination, hiring only individuals from the favored class will increase those firms' labor costs which means they will have a difficult time competing against any non-discriminatory firms. Over time, this will make it difficult for discriminating firms to survive. However, in the consumer-bias case, a monopoly would be able to refrain from discrimination without losing a large number of its customers, whereas firms in competitive markets would push each other to indulge the consumer bias, all other things equal. As for whether these insights could be used by a defendant in a merger or monopolization case, the answer is likely no. The courts have suggested that such normative concerns lie outside of the scope of antitrust law, and so would likely be ignored here. Even if the court were willing to take a very broad view of consumer welfare (of which utility derived from the consumers' biased preferences would be included), the competitively-driven discrimination would improve consumer welfare.

2. A merger is proposed involving two companies, Full o' Fructose and Chock Full o' Calories. Each company produces a single product, and both of the products involved in the merger are sandwich spreads. In the materials submitted as part of their pre-merger notification are the following data involving the current 2015 market shares in the sandwich spread market:

Company	Market Share	Company	Market Share
Two Chins for the Price of One	32	At Least It Tastes Good	4
Full O' Fructose	21	Mostly Natural	3
Completely Cloying	15	Somewhat Natural	2
Chock Full o' Calories	13	Looks Natural	2
Delightfully Diabetes	7	At Least It's Cheap	1

Also included in the pre-merger notification are the following data regarding average nationwide price (in dollars) and total nationwide quantity (in 100s of millions of units) for the previous 10 years.

	Full O' Fructose		Chock Full o' Calories	
	P	Q	P	Q
2014	1.15	34	1.17	10
2013	1.13	36	1.16	15
2012	1.08	40	1.15	20
2011	1.07	41	1.14	22
2010	0.99	48	1.12	35
2009	1.12	36	1.13	28
2008	1.16	32	1.14	24
2007	1.18	30	1.15	19
2006	1.16	32	1.14	25
2005	1.16	32	1.14	26

You are the FTC staffer assigned to the initial review of this merger. Draft a memo outlining your initial conclusions regarding the merger, including an intuitive explanation of the reasoning behind your conclusions, and whether any additional data should be sought from the parties, including specific requests and the rationale behind the requests.

On first inspection, this merger seems problematic in that the market is moderately concentrated (Herfindahl index before = 1942; Herfindahl index after = 2488) and the merger would increase the Hefindahl index by 546. The Horizontal Merger Guidelines suggest that such an increase in a moderately concentrated industry "potentially raise significant competitive concerns and often warrant scrutiny." However, if one examines the year to year price and quantity data, it appears as though the cross price elasticity is negative. That is, when the price of Full o' Fructose goes up, the quantity of Chock Full o' Calories consumed goes down and vice versa. This implies that the products of the two companies are complementary. In such a case, the merger is unlikely to result in an increase in prices (reduction in output) and might actually lead to a decrease in prices (increase in output). If this is indeed the case, this merger should not be challenged. That said, the simple cross price elasticity calculation that can be performed on the data provided above may be misleading. It might be the case that other background variables are changing year to year (such as consumer income or the prices of raw materials) which change the price/output decisions of both firms in the same direction, which may be obscuring the true cross price elasticity. Given this possibility, it would

be necessary to perform some kind of regression analysis to control for the relevant background variables. While some of these variables may be generally available (such as consumer income) others may require an additional request for information (such as raw materials prices). If, after controlling for these common background variables, the regression analysis still implies a negative cross price elasticity between the products of the two firms, there is little reason to scrutinize this merger further.

3. Assume that the market for fast food is dominated by three companies (each of which has multiple restaurant lines operating under it), McDowell's, King Burger, and HoagieWay. In many areas, these companies account for as much as 90 percent of all fast food sales. The restaurants in these chains tend to be very profitable. In addition to substantial demand for their products, their profit margins tend to substantially exceed those of their competitors due to the economies of scale they enjoy in logistics and the substantial bargaining power they wield with suppliers. In most markets, other fast food restaurants are small operations that do not have much capital, relying mostly on unskilled labor that is paid a low wage. These competitors also face very small profit margins.

   During the course of the annual meeting of the fast food trade association, of which McDowell's, King Burger, and HoagieWay are the primary members, McDowell's offers the proposal for the association to mount a campaign to lobby the federal government to pass a $15/hour minimum wage law. Each of the three large fast food companies pledge support for this campaign, providing substantial funding for the lobbying activities. Discuss the potential for this scenario to give rise to a claim that McDowell's, King Burger, and HoagieWay have violated US antitrust laws. Also, discuss any legal defenses to the claim(s) you identify.

Given the market characteristics provided in the question, McDowell's, King Burger, and HoagieWay are in a better position to absorb higher labor costs than are their competitors. Their higher profit margins suggest that they might be earning returns that exceed their cost of capital, in which case, they could survive the increase in costs, while their competitors appear to be just covering their existing costs. Further, these higher profit margins may allow the three firms to invest in labor saving capital (self-serve order screens, robots, etc) that are beyond he financial reach of their competitors, allowing the main firms to avoid the higher labor costs to some extent.

Such a scenario could give rise to a raising rivals' costs claim. However, such a claim would run into a few potential problems. First, any court will be hesitant to suggest that firms may not lobby in this way on first amendment grounds. At a minimum, the potential (anti)competitive effects will need to be balanced against this infringement. Second, a court examining this theory could consider the plausibility of this monopolization claim since the firms would be increasing their own costs (at least in the short term) for the mere possibility that the action will improve their market power for a long enough period to recoup those lost profits without new entrants (who perhaps can exploit the labor saving capital in the way that McDowell's et al. would) pushing prices back down. Further, the lobbying effort is presumably limited by the fact that each of the main firms bear the full cost of their lobbying efforts, while having to split the potential gains of pushing the other firms out of the market. This kind of public good problem may lead the court to believe the raising rivals' costs scenario is implausible.

4. Choose one of the questions 1-3 to count double in the calculation of your final exam score, or choose to have each question count the same (i.e., multiple the score for each question by 1

1/3) in determining your final exam score. Make your choice clearly; failure to do so will result in an automatic loss of 25% of the potential points available for the exam.