NERA
ECONOMIC CONSULTING

THL/Apollo: response to anonymous cross submissions

23 June 2022

Anonymous cross submission	Point made by anonymous cross-submitter	NERA response
Cross submission A	Critical loss is not without its limitations and detractors. Scheffman and Simons (2003)[1] argue standard critical loss is "just arithmetic", but more case-specific evidence is required to reach an informed conclusion on competitive effects.	Scheffman and Simons (2003) could hardly be considered a "detractor" of critical loss. They state that critical loss is "very useful" for assessing competitive effects (p.2), and that its "simplicity and ease of practical application" explain why it has been readily adopted by courts and antitrust agencies (p.3). While it is correct that more case-specific evidence is required to analyse competitive effects, critical loss is one tool that can help in that analysis.
	Critical loss does not identify whether a reduction in output will actually occur (citing Harris and Veljanovski, 2003).[2]	This is correct – calculation of the *critical* loss does not tell us anything about the *actual* loss. This is why we have showed the extent to which expansion by rivals will exceed the critical loss (see [10] of our 22 April 2022 addendum memo), and estimated what sort of market demand elasticity would imply an actual loss in excess of the critical loss (section 2 of our 31 May 2022 SoUI report). Harris and Veljanovski (2003) are also not detractors of critical loss (Barry Harris was one of the authors who developed the concept[3]). Their paper explains the critical loss concept "in the hope that greater attention will be placed on this and other empirical

[1] David T. Scheffman and Joseph J. Simons (2003), "The State of Critical Loss Analysis: Let's Make Sure We Understand the Whole Story", *The Antitrust Source*, November, 1-9.

[2] Barry C. Harris and Cento G. Veljanovski (2003), "Critical Loss Analysis: Its Growing Use in Competition Law", *European Competition Law Review*, 5, 213-218.

[3] Barry C. Harris and Joseph J. Simons (1989), "Focusing Market Definition: How Much Substitution is Enough?", *Research in Law and Economics*, 12, 207.

		tests of market definition" in EC antitrust cases (p.213).
	Huschelrath (2009)[4] notes that economic theory, particularly in differentiated markets, predicts a price rise by the merged entity will incentivize third party price rises, which risks critical loss underestimating the profitability of a price increase.	Huschelrath (2009) notes that there are three possible rival responses to a price rise by the merged entity: a price increase; a price decrease; or no change in price. He notes that there are a number of factors that determine which is the most profitable. The anonymous cross-submission has noted only Huschelrath's point about price rises. In this case, Huschelrath appears to have in a mind a differentiated Bertrand model of competition. This is not a good fit for the RV rental market, where (as described in our various reports) price is a function of market fleet capacity.
	O'Brien and Wickelgren (2003)[5] note that when margins are higher, a firm faces fewer substitutes. This leads to greater price increases when margins are high, contrary to what critical loss shows.	Higher margins are not necessarily indicative of facing fewer substitutes, as they can instead be indicative of the need to recover fixed costs.[6] O'Brien and Wickelgren (2003) also explicitly exclude consideration of the supply-side, and in the present case it is the fluidity of rival expansion that suggests the critical loss will be exceeded. We note also that O'Brien and Wickelgren (2003) do not raise any concerns with the calculation of the *critical* loss itself.
Cross submission B	NERA observe that the residual demand elasticity has not been estimated econometrically, but NERA do not reflect the results of the	The consumer survey is valuable and informative evidence. However, it is not the same as an econometric estimate of the demand

[4] Kai Huschelrath (2009), "Critical Loss Analysis in Market Definition and Merger Control", *European Competition Journal*, 5(3), 757-794.

[5] Daniel P. O'Brien and Abraham L. Wickelgren (2003), "A Critical Analysis of Critical Loss Analysis", *Antitrust Law Journal*, 71, 161-184.

[6] See, for example, Kenneth G. Elzinga and David E. Mills (2011), "The Lerner Index of Monopoly Power: Origins and Uses", *American Economic Review: Papers and Proceedings*, 101(3), 558-564, who state (at p.561) that "…a relatively high Lerner Index may reveal nothing more than the necessity of covering fixed costs". See also Robert H. Bork and J. Gregory Sidak (2013), "The misuse of profit margins to infer market power", *Journal of Competition Law and Economics*, 9(3), 511-530, noting that high margins do not indicate market power, but can be necessary for the recovery of high fixed costs.

	consumer survey. That NERA is not prepared to rely on the survey demonstrates it should be given no weight.	elasticity. For that we would require, for example, a sufficiently long time series of quantities and prices for all competitors, as well as time series of other variables that need to be controlled for.