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Sources of gains in horizontal mergers: evidence from customer, supplier, and rival firms☆

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Abstract

We investigate the upstream and downstream product-market effects of a large sample of horizontal mergers and acquisitions from 1980 to 1997. We construct a data set that identifies the corporate customers, suppliers, and rivals of the firms initiating horizontal mergers and use this data set to examine announcement-related stock market revaluations and post-merger changes in operating performance. We find little evidence consistent with increased monopolistic collusion. However, we do find evidence consistent with improved productive efficiency and buying power as sources of gains to horizontal mergers. The nature of the buying power gains, i.e., rents from monopsonistic collusion or improved purchasing efficiency, is also investigated.

JEL classification: G34; D43; L41

Keywords: Mergers; Acquisitions; Collusion; Buying power

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1. Introduction

Managers of firms undertaking horizontal mergers and acquisitions often cite improved productive efficiency as the primary source of anticipated gains to mergers.[1] On the one hand, improved efficiency in production or distribution or both could arise from greater realization of economies of scale, elimination of overlapping facilities, etc. On the other hand, antitrust authorities frequently posit that horizontal mergers enable the merging firms to gain at the expense of customers and suppliers by allowing the merging firms an opportunity to engage in anticompetitive collusion. For instance, merged firms could more easily collude with rival firms to restrict output to monopoly levels and raise prices at the expense of their customers (see Stigler, 1964). Similarly, merged firms could collude with rivals to restrict aggregate purchases to monopsony levels and thereby lower input prices at the expense of their suppliers (see Robinson, 1933).

Merging firms could gain from pooling their purchasing, without necessarily engaging in anticompetitive monopsonistic collusion with rivals. For instance, merging firms could realize purchasing efficiencies if they reduce their input usage or obtain quantity discounts from suppliers. Merging firms could also be able to use their combined purchasing to induce suppliers to compete on price to sell to the combined firm. Further, if the supplier industry is not already competitive, then pooled purchasing and the competition that it induces could allow the merging firms to effectively countervail anticompetitive practices upstream, as noted by Galbraith (1952) and Snyder (1996). If the most efficient suppliers are likely to win such price competitions, then the result is a more efficient allocation of industry resources post-merger. This is in clear contrast to the efficiency implications of anticompetitive collusion.

The gains from increased buying power or anticompetitive collusion are not mutually exclusive of improved productive efficiency. However, gains from buying power or monopolistic collusion are distinct from efficiency gains in that they are expected to affect not only the post-merger performance of the merging firms but also the performance of other firms that share a product-market relationship with the merging firms. In this paper, we investigate the relative importance of buying power (both the anticompetitive monopsonistic variety and the efficiency increasing variety) and monopolistic collusion as sources of gains to mergers. We construct a data set that identifies the important corporate customers, suppliers, and rivals of a large sample of firms that announced horizontal mergers and acquisitions between 1980 and 1997. This approach, originally suggested by Eckbo (1983), allows us to examine both the valuation impact at announcement and subsequent changes in operating performance for firms both upstream and downstream of the merged

[1] While our sample includes both mergers and tender offers, for expository purposes, we refer to all deals as mergers in this paper.