Innovation Markets Analysis: When Should This Tool Come Out of the Shed?

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Steven C. Sunshine
Jonathan M. Lave
Overview

• *Innovation is an important dimension of rivalry and engine of progress.*

• *Predictions of a merger’s effect on innovation output are uncertain.*

• *Legal and economic issues require showing of probable effect on output.*
  – Genzyme: example of insufficient evidence of effect?

• *Practical application may be infrequent and more likely in certain industries.*
Innovation markets are not easy to define with confidence

- Sources of innovation are difficult to identify
- Strength and significance of population of innovators are unclear
- Type of innovation may be relevant to confidence in market boundaries
Predicting competitive effects requires an assessment of merger’s effect on innovation and output

- **Structure as a means of predicting performance**
  - Who is right, Schumpeter or Arrow?
  - The problem and necessity of case-specific evidence

- **Innovation efforts and incentives**
  - Incremental v. revolutionary
  - Nature of competition between innovations

- **Confidence that the reduction in innovation will lead to an output effect**

- **Is the effect outweighed by innovation efficiencies?**
Enough about economics. What about the law?

• *Does Section 7’s focus on "line of commerce" of commerce doom innovation analysis?*

• *Can a plaintiff prove a nonspeculative effect in a reasonable amount of time?*

• *Burdens and do they really matter?*
  – Burden of proof always on plaintiff
  – *PNB/Baker Hughes*, burdens of production, and the *prima facie* case
Problems of the investigator

• **Investigator has a duty to evaluate proposed transactions. If innovation is a key dimension of competition, then the investigator must deal with it.**

• **The law – with the state of economic theory – requires the investigator to prove all aspects of the case, including:**
  – the innovation space in which the diminution will occur
  – the merger’s likely effect on innovation
  – the manner in which output will be reduced
  – when the output effect will be felt

• **The importance of empirical evidence from the merging parties and the market cannot be overstated.**
Suggested mode of analysis

• *Is innovation an important dimension of rivalry?*

• *Will innovation affect existing product market in a reasonable amount of time?*
  – competitive effects in a goods market
  – potential competition

• *Can the boundaries of the innovation market be determined?*
Suggested mode of analysis (cont.)

• *Does the merger lessen incentives to innovate?*
  – nature of competition between merging parties
  – nature of other downstream competition
  – efficiency analysis

• *Can harm to an output market be demonstrated?*
  – future goods markets
  – future improvements to existing goods