Creeping mergers – should we be concerned? A case study of hospital mergers in South Africa

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Abstract

Creeping mergers are often cited as a problem in the context of concentrated industries, but practical competition law solutions are rarely suggested. Concern typically arises from a series of mergers which increase concentration in an industry but which do not individually cause substantial anti-competitive effects, particularly where the acquisitions are undertaken by a dominant firm. In South Africa it has been suggested in several industries that creeping mergers could be a competition concern; these include retail, media and healthcare to name just three. Under the South African Competition Act, however, there is no means to tackle such a problem. This paper attempts to weigh up the possible options for dealing with this issue. It first discusses the theoretical and practical considerations related to controlling creeping mergers before reviewing international experience. Next it presents a case study of the South African private hospital market, where the creeping merger problem is often suggested to be contributing to above-inflation increases in the cost of private healthcare. The paper finds that whilst it may seem attractive to regulate creeping mergers more strictly, there are a number of theoretical and practical considerations to be taken into account. These difficulties notwithstanding, in the private hospital market the analysis suggests that a creeping merger rule may have prevented some of the concentration which has occurred in the sector.

1. Introduction

The issue of so-called creeping mergers is one that periodically gains attention in competition law circles, usually in response to growing concentration in a particular sector or industry. Concern usually arises where a large firm is involved in the acquisition of one or more smaller firms such that each individual transaction cannot be said to substantially lessen competition, but where concentration in the industry overall is steadily increasing over time. This has been summarised by the Australian Competition and Consumer Commission (ACCC) as follows:

“\textit{The term ‘creeping acquisition’ encompasses a range of situations. While it can refer to a series of acquisitions over time that individually do not raise competitive concerns, but when taken together, the acquisitions have a significant competitive impact, the term creeping acquisition also refers to a firm with existing substantial market power enhancing its market power through one (or more) acquisitions which individually do not substantially lessen competition.}” ACCC (2008)

The ACCC notes that concern around creeping mergers will be higher in markets where there are high barriers to entry. If on the other hand barriers are low and new competitors are likely to emerge then even a dominant firm purchasing smaller rivals should not be problematic since any price increase linked to increased concentration is likely to incentivise new small firms to enter the market.

A question when dealing with creeping mergers is why a series of acquisitions by a large firm which cumulatively have the same effect as one larger transaction should escape

¹ This paper represents the views of the author and not the affiliated institutions.
competition scrutiny. In South Africa this problem has been discussed by the Tribunal in a number of cases\(^2\), however, the extent to which the competition authorities can tackle the issue is limited by the Competition Act.

In terms of section 12A of the Competition Act, the competition authorities must determine whether or not a given merger "is likely to **substantially** prevent or lessen competition" [emphasis added]. Although the Act suggests that a range of factors may be taken into account when performing this assessment, including ease of entry, level and trends in concentration and whether or not the merger results in the removal of an effective competitor, it is clear that the merger must result in competition being prevented or lessened substantially. Thus it is possible that even in a highly concentrated industry with high barriers to entry, the merger of a dominant firm with an effective (or potentially effective) but small competitor may be permitted in terms of the Act. Furthermore, even if the same dominant firm has merged with three other smaller firms in the same market in the recent past, there would be no basis for prohibiting the merger under South African competition law. The combined effect of the transactions on competition, however, may be substantial.

This problem is not unique to South Africa: very few competition jurisdictions have legal provisions which aim to prevent creeping mergers. This begs the question of whether dealing with creeping mergers is undesirable in theory or in practice. In the light of on-going concern around creeping mergers in South Africa, particularly in the private hospital market, this paper aims to assess the seriousness of the problem and the pros and cons of the available solutions. The following section discusses South African cases where the issue of creeping mergers has been raised. Section 3 looks at theory and international experience, with a particular focus on Australia where the possible addition of a creeping mergers provision to their competition law was recently considered. Section 4 presents a detailed case study of the South African private hospital market which aims to establish whether creeping mergers is really a problem in this market, and whether a creeping mergers provision of the type entertained in Australia would have mitigated some of the concentration that has been seen in recent years. Section 5 concludes.

2. **Concern around creeping mergers in South Africa**

As noted above, the problem of creeping mergers has been acknowledged by the Tribunal in several cases. In the merger between Edgars and Rapid Dawn, the Tribunal stated\(^3\): "It needs to be noted however that there seems to be an increase in the number of acquisitions in which relatively small players, that claim to be financially constrained, are being bought by larger competitors. The result of this is a slow but steady increase in concentration. Cognizance should be taken of this creeping level of marginal acquisitions and the effect this might have on competition in the retail sector." The concern by the Tribunal is clear here, but the mechanism for dealing with it is not elaborated on and, as mentioned above, it is not clear whether this is even possible under the current SA Competition Act.

In the Phodiclinics/Protector merger\(^4\), one of the intervening parties raised the issue of creeping mergers in the healthcare industry, stating that creeping acquisitions by the three major private hospital groups had resulted in concentration and price increases in the private hospital market. The Tribunal found that despite sharing the intervener’s concern around increasing hospital costs, there was no evidence that the transaction in itself would have a significant effect on competition. As will be discussed in more detail in section 4, the debate around creeping mergers in this market has not abated and the issue continues to be cited

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\(^2\) See Tribunal reasons for decision in the following mergers: Edgars/Rapid Dawn, Phodiclinics/Protector, Media24/Natal Witness.

\(^3\) Case number: 21/LM/Mar05

\(^4\) Case number: 122/LM/Dec05
as one of the possible reasons for above-inflation increases in the price of private healthcare.

Concern around creeping acquisitions also arose recently in the hearing into the merger between Media24 and the Natal Witness, leading the Tribunal to conclude: “The evidence in this case has shown that increased market concentration is prevalent in the relevant markets under consideration through a strategy of creeping acquisition. The familiar pattern is that of the large publishing companies such as Media24 and Caxton acquiring direct or indirect stakes in small independent publishers of community newspapers.” In this case the Tribunal was concerned that the small size of the firms being acquired often results in the mergers being classified as small mergers in terms of the Act and therefore being non-notifiable such that they were escaping competition scrutiny. For this reason, the Tribunal imposed a condition requiring Media 24 to notify all small mergers relating to small independent publishers or firms which provide printing services to small independent publishers. Although this condition ensures the Tribunal will get a chance to assess small mergers in the sector, it does not allow the Tribunal to act in situations where the impact of an individual transaction on competition is less than substantial.

3. Theory and experience in other jurisdictions

Theoretical and practical considerations

On the face of it, the discussion and examples above may seem to suggest that the lack of a creeping acquisitions provision in the merger regime is a shortcoming. However, as noted in the introduction, very few jurisdictions do have explicit provisions to deal with creeping mergers and this raises the question of whether there are theoretical or practical objections to such a development.

From a theoretical point of view it is easy to understand that while a merger that gives a large firm an extra 5% market share is unlikely to lead to substantial anti-competitive effects (depending of course on the relevant market dynamics), four similar transactions by the same large firm which increase its market share, for example, from 40% to 60% may well do so. A major attraction of a creeping merger provision would be to prevent industries from slowly becoming more concentrated over time as a result of acquisition activity by the major players.

A further point to note is that in South Africa, unlike the UK for example, the competition authorities do not have the power to address issues of anti-competitive market structure ex-post. In the UK, a market study can be used to investigate industries which are suspected to be uncompetitive and if problems are found, the authorities can impose severe remedies, including requiring firms to divest assets or business units. For example in the recent market study into the airports sector (UK Competition Commission, 2009), the Competition Commission found that the common ownership of airports in certain regions posed problems for competition and required British Airports Authority to divest several airports. In jurisdictions without that ability to deal with the problem of concentration ex-post (except to the extent that a market participant is found to be abusing its dominance), it becomes more concerning that such issues cannot be dealt with through merger control. Although the South African Competition Act has recently been amended to give the authority market inquiry powers, under the amended Act the Commission will not have the power to impose remedies in the way that the UK authorities can purely on the basis of finding that concentration in an industry is having an adverse effect on competition. It will still have to prove that an abuse of dominance (as characterised by the pre-existing provisions of the Act) has occurred.

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5 Case number: 15/LM/Jun11
Opponents of creeping mergers provisions argue that there are a number of theoretical and practical problems with such a provision. Firstly, it is argued that it would amount to penalising firms for being big, acting as a de facto market cap on firms which would prevent growth and efficiency (Law Council of Australia, 2008). To the extent that prohibiting large firms from merging will prevent them from achieving economies of scale or other efficiencies (such as if the large firm is more efficient than the target firm), this may become a welfare-detrimental exercise. There is, however, no reason why mergers where there is a failing firm defence or efficiencies that outweigh the anti-competitive effect should not be evaluated in the usual way, with the anti-competitive effects being weighed against the other concerns. Furthermore, a creeping mergers provision would not preclude firms from growing organically or gaining market share through competition on the merits. Thus it can hardly be described as a “cap” on firms’ growth.

A further question is whether a creeping merger provision which imposes more stringent rules on large firms which may have attained their position through innovation and efficiency would potentially dampen incentives for firms to innovate and grow through efficient and pro-competitive means in future. Firstly, a creeping merger rule would not necessarily target only large firms; any firm which pursues a series of transactions which together would have a substantial effect on competition would be in danger of falling foul of the rule. Secondly, even to the extent that such a rule imposed a greater burden on large or dominant firms (as do existing merger rules – a dominant firm is much more likely to have an acquisition prohibited than a non-dominant firm), an attempt to control creeping mergers does not imply that all mergers involving large or dominant firms will be prohibited, just that those which cumulatively significantly enhance its market power in a given market may be scrutinised more closely. It is an implicit principle of merger control that preventing a merger which will result in a substantial prevention or lessening of competition has benefits which outweigh any dampening of firms’ incentives to compete for market share in the first place. So why not a series of mergers which have the same effect?

Another concern is that trying to control creeping mergers would also penalise other parties (the target firms) for decisions they were not party to and could not control (i.e. the large firms’ market share and previous acquisition activity). For some entrepreneurs, the attractiveness of starting a business stems in part from the potential to realise their investment by selling the business once they have built a successful enterprise. If large firms are effectively prohibited from acquiring smaller competitors, this may dampen incentives for entrepreneurial activity. In markets where barriers to entry are high, and hence a series of mergers is more likely to fall foul of a creeping mergers rule, the rule could therefore raise an additional barrier to entry through casting doubt on the ability of an entrant to realise its investment should it wish to at a later stage. How strong this disincentive to enter is in practice, however, will depend on the precise wording and interpretation of the provision. To the extent that the rule does not constitute a blanket prohibition on large firms acquiring small firms, the effect may not be particularly strong.

Finally, a range of practical difficulties may arise in the enforcement of a creeping mergers provision. Problems may arise for example if an additional analytical and evidentiary burden is created which can impact on the predictability of the regime for firms. These issues are dealt with in more detail below in the context of the Australian experience which highlights some of the main practical challenges with a creeping mergers provision.

International experience

a. Australia

On 1 September 2008, the former Assistant Treasurer and Minister for Competition Policy and Consumer Affairs issued a discussion paper to gauge the best way forward in relation to the issue of creeping acquisitions in Australia. On 6 May 2009, the Minister released a
further discussion paper calling for public comment on options to address the issue of creeping acquisitions. A significant number of submissions were received on the issue from stakeholders in the competition community and in particular from the grocery wholesale and retail industries (where creeping merger concerns had been raised). At the conclusion of the process no changes to competition laws were implemented. The debate, however, is very informative in terms of the possible mechanisms for addressing creeping mergers and some of their practical problems.

There were two main models put forward in the discussion papers. The first is an aggregation model which would give the authority the power to consider all transactions conducted by a particular firm within a certain time-period of the instant transaction and to assess these transactions in terms of their combined effect on competition. The second suggested model is the substantial market power (SMP) model which would allow the authority to prohibit any mergers which result in the enhancement of the market power of a firm with substantial existing market power. In other words, for dominant firms the relevant test would no longer be whether the merger results in a substantial lessening of competition, but whether it results in any material lessening of competition, even if not substantial. The pros and cons associated with each of the models are discussed below.

Aggregation model

The aggregation model is intuitively attractive since it tackles the problem which has been identified head-on and allows the authority to show that together a series of transactions has a significant effect. It also limits the possibility of a finding of anti-competitive effects to a situation where a firm is growing its market share over time through acquisitions. In a practical sense, however, there are challenges to the application of the rule. For example, if a transaction is problematic in the context of a series of previous of transactions, a question arises around whether measures can be taken against the earlier transactions or only the one currently under consideration. If not, the impact of prohibiting a transaction with (by definition) insubstantial competition effects will probably not be very great. However, the alternative approach would see even long-consummated transactions subject to potential unwinding which would be problematic for firms and the authorities and cause considerable uncertainty. In addition, the ACCC (2008) notes that to assess a group of transactions to ascertain their cumulative effect would be difficult analytically and evidentially, not least because market dynamics change over time to the extent that even the relevant market definition may not be the same throughout the period under review. Trying to detect which changes are due to the mergers and which are caused by other developments would be very difficult in such a context. For this reason, the ACCC did not support the imposition of this type of rule.

Substantial Market Power model

The ACCC (2008) suggested that such a provision: could look like the following:

“A corporation that has a substantial degree of power in a market must not directly or indirectly:

(a) acquire shares in the capital of a body corporate; or

(b) acquire any assets of a person;

if the acquisition would have the effect, or be likely to have the effect of, lessening competition in that market.”

In other words, the test for mergers involving firms with market power would no longer be whether the merger causes a substantial a lessening of competition, but merely a lessening of competition. This type of rule was preferred by the ACCC as it argues it is more workable
and captures the creeping acquisitions which are most likely to cause competition concern, i.e. those undertaken by firms with substantial market power. However, it does focus less on capturing the “creeping” effect of a series of mergers and more on preventing dominant firms from enhancing their market power. The ACCC argues that even though dominant firms will effectively be prohibited from merging with small competitors, they can still achieve a strong market position through innovation and efficiency. They also highlight that the effect of the transaction on competition must still be more than insignificant, so not every merger would be affected. It is also worth noting that the rule would not preclude allowing such mergers to go ahead where there is a failing firm defence or efficiencies that outweigh the anti-competitive effect. In fact given that the anti-competitive effect does not have to be significant, efficiencies also need not be terribly substantial in order to outweigh it.

From a practical point of view, this test may also increase the analytical burden on the authorities to some extent (and therefore decrease the level of certainty for firms) due to the requirement to evaluate whether or not a firm is dominant in a market. This requires a robust and conclusive market definition and accurate market shares, as well as a sound evaluation of all relevant market dynamics. These are broadly the same factors which must be analysed in assessing whether a merger results in a substantial lessening of competition, but may require a degree of certainty in some cases which is not required at present. For example, where market share accretion is very low, the authorities may not find it necessary to conclude on a market definition, but under the proposed rule it would be vital to do so.

b. Other jurisdictions

As noted above, very few jurisdictions have provisions to deal with creeping mergers. In a 2003 OECD paper titled “Substantive Criteria used for Merger Assessment”, it was found that only Finland, Hungary and Mexico gave special consideration to creeping mergers. In Finland a so-called “two year rule” allows the authority to consider other transactions involving the acquiring firm which have taken place in a two year period. This is very similar to the aggregation model described above.

The Hungarian Office of Economic Competition can block a transaction once a series of mergers puts the acquiring group into an economic position where it can act to a large extent independently of the market. In Mexico there is no specific test for creeping acquisition but the authority can block a series of mergers to prevent an economic agent from obtaining substantial market power. Again, these rules have more in common with the aggregation rule than the substantial market power rule, although there is no specific time period set over which aggregated transactions can be considered. This is interesting, since the discussion above suggests despite being better aligned with the identified problem, the aggregation rule would be more difficult of the two to practically implement, and yet it is the only type of rule which was actually being used by any jurisdiction.

The following section attempts to shed more light on the practicality and likely effects of the two rules in the South African context through considering a case study of the private hospital market.

4. Case study: hospitals

Industry background

From 1996 to 2006, concentration in the South African private hospital market increased substantially. In 1996, the three main hospital groups (Life, Netcare and Mediclinic) accounted for 51% of acute beds. By 2006 this proportion had increased to 84% (Council for Medical Schemes, 2008). During the same period, the three major groups engaged in a substantial amount of merger activity, frequently involving the acquisition of smaller hospital groups. This trend, combined with high and increasing private healthcare costs, has led
some commentators to question whether creeping mergers are having an anti-competitive effect on the private hospital market in South Africa. The Council for Medical Schemes (CMS) in a 2008 report stated that:

“The hospital market technically became concentrated in the key national markets (major metropolitan areas) from 1999 (due to merger activity), and overall from 2002. The period when the market became concentrated coincides with a trend break in hospital costs. This report concludes that the two are causally related. Concentration increases market power, which sustains high prices, costs and inefficient behaviour.”

Figure 1 illustrates how the HHI index in different local markets and nationally has varied over time. An HHI score of between 1000 and 2000 indicates that an industry is quite concentrated whilst a score of over 2000 suggests that it is highly concentrated. The graph clearly illustrates that the national HHI has been increasing over time, but that it increased most rapidly between 1996 and 2002. In general the pattern across the major urban areas is the same, with large increases in concentration in the pre-Competition Act period and a more gradual increase post-2002.

**Figure 1: Private hospital market HHIs**

<table>
<thead>
<tr>
<th>Year</th>
<th>National HHI</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
<td>1500</td>
</tr>
<tr>
<td>1998</td>
<td>2000</td>
</tr>
<tr>
<td>2000</td>
<td>2500</td>
</tr>
<tr>
<td>2002</td>
<td>3000</td>
</tr>
<tr>
<td>2004</td>
<td>3500</td>
</tr>
<tr>
<td>2006</td>
<td>4000</td>
</tr>
<tr>
<td>2008</td>
<td>4500</td>
</tr>
<tr>
<td>2010</td>
<td>5000</td>
</tr>
<tr>
<td>2012</td>
<td>5500</td>
</tr>
</tbody>
</table>

Source: A. van den Heever, 2012

A closer look at the Tribunal decisions in private hospital mergers over the years reveals a similar trend of concentration in key markets. The tables below illustrate the concentration (due to mergers) in the Greater Durban and Pretoria markets, as measured by the Tribunal. Table 1 illustrates that through two mergers approved by the Tribunal, Life increased its market share from 10% to 50% in the affected market. Overall, the shares of the two biggest players in the market, Life and Netcare therefore increased from 41% to 82%, resulting in the market becoming concentrated.

**Table 1: Evolution of market shares in the Greater Durban market, 2001 – 2011 (%)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Post-Afrox/</th>
<th>2011</th>
<th>Post-Life/</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Table 2 tells a similar story for the Pretoria market. Through a merger involving Life and subsequent mergers involving Mediclinic and Netcare, the market share of the “Big 3” hospital groups in Pretoria increased from 46% to 90% between 2002 and 2006, effectively becoming highly concentrated.

**Table 2: Evolution of market shares in the Pretoria market, 2002 – 2006 (%)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Netcare</td>
<td>31</td>
<td>31</td>
<td>31</td>
<td>35</td>
<td>41</td>
</tr>
<tr>
<td>Curamed</td>
<td>16</td>
<td>16</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Afrox/Life</td>
<td>15</td>
<td>25</td>
<td>25</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>Wilgers</td>
<td>9</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>CHG*</td>
<td></td>
<td>6</td>
<td>N/A</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mediclinic</td>
<td>0</td>
<td>0</td>
<td>16</td>
<td>19</td>
<td>19</td>
</tr>
<tr>
<td>Other independents</td>
<td>28</td>
<td>28</td>
<td>28</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Total Big 3</td>
<td>46</td>
<td>56</td>
<td>72</td>
<td>84</td>
<td>90</td>
</tr>
</tbody>
</table>

*CHG was not accounted for separately in the market share calculations in the first two transactions. It is consequently included under “other independents”

**Market shares were not given in this decision so market shares given in the Afrox/Wilgers decision were used given that this merger occurred just a few months previously.**

Felet, Lishman and Fiaudeiro (2012) investigate the relationship between increasing concentration levels in the South African private hospital sector and the profitability of the major hospital groups. The authors find that increases in market concentration in the South African private hospital market have corresponded with a period of higher profitability. Furthermore, the returns earned by South African hospital groups appear to be high in comparison to global hospital firms (a sample of 82 hospitals worldwide was used) and are above benchmarks used by UK competition authorities in their profitability analysis. They also present some possible caveats to these results, essentially explaining that correlation does not equal causation and that other factors could be driving the profitability trend such as demand shifts, efficiencies achieved and the Competition Commission’s decision to end collective bargaining in the sector in 2003.
Whilst no study has conclusively shown that frequent mergers in the sector and high prices and profits are causally related, the evidence suggests that this is at least a possibility. In the Phodiclinics/Protector merger, the Tribunal stated:

“The trend towards increasing concentration in the private hospital market and the increasing cost of healthcare in this country certainly raise concerns. But the remedy that the CMS seeks, namely that we prohibit any of the three groups to acquire any further hospitals, is one more akin to an industry sector remedy and one which this Tribunal is not empowered to grant.

This Tribunal, as an adjudicating body, is required to assess each case on its own merits in accordance with the requirements of the Competition Act. In terms of the Competition Act we are empowered to prohibit or conditionally approve a transaction only if it substantially lessens competition in a relevant market or does not fulfil any of the other requirements of section 12A. We cannot impose blanket prohibitions on specific enterprises in a particular sector. Each case has to be assessed on its own merits and circumstances.”

In this context it seems that this sector may be an appropriate case study in which to consider the question of whether existing merger regulation is sufficient to control the potential anti-competitive effects of creeping mergers.

Figure 2 illustrates the evolution of the private hospital market in South Africa from 1983 to 2012, focussing on the growth of the three major groups: Mediclinic, Netcare and Life. The light grey area of the graph illustrates the cumulative number of hospitals acquired by the major groups, whilst the dark grey bars measure the number of hospitals acquired by the groups in each year. Finally, from 1996 onwards, the line chart illustrates the movements in the national HHI for the sector.

The chart illustrates that there was a major wave of merger activity between 1995 and 1999, before the Competition Act came into force. In this period, the three major groups acquired 125 hospitals, with both the total number of hospitals owned by the three groups and the national HHI increasing steeply during this time. After that point there was a small spike in 2001/2002 and then lower levels of merger activity over the past decade.

This serves to illustrate the point that, from a concentration perspective, to some extent the damage was done by late 1999 when the new Competition Act came into force. By late 2001, when the Tribunal considered the Afrox/Amahosp merger, the industry HHI had already increased dramatically. The industry HHI did increase further from 2002 to 2006, although not as steeply, before slowing down altogether.

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6 Case number 122/LM/Dec 05, Tribunal Reasons for decision paras 170 and 171.
Figure 2: Evolution of the private hospital market 1983 – 2012

Source: Mediclinic, Netcare and Life Healthcare websites, A. van den Heever (2012), Competition Commission merger reports

Notes: 1) M = Mediclinic, N = Netcare, L = Afrox/Life
       2) It was not possible to determine hospitals divested/closed from the available information, thus the chart illustrates acquired hospitals and not total hospitals
It seems likely that if the new Competition Act had been in force from 1996, some, if not all, of the transactions which took place between 1996 and 2000 would have been prohibited, given the large increase in concentration which they occasioned. However, more pertinent to the current discussion is whether or not the mergers post-2000, when the industry had already reached a high level of concentration, should have been allowed. These transactions seem to fall squarely in the category of interest; that is, mergers which individually do not have a substantial effect on competition but which may further entrench the market power of the major players possibly to the long-term detriment of consumers.

**Applying the creeping mergers rules**

In this context, an interesting question is whether some of the mergers in later years would have been approved had they been assessed with some form of creeping mergers test rather than the usual SLC test.

In order to consider what impact a creeping mergers rule could have had on the structure of the private hospital market in South Africa, we have looked at seven mergers which were approved by the Tribunal from 2002 onwards and four mergers recently approved by the Commission and assessed whether the competition authorities could have come to a different decision under either of the rules discussed above:

1) Aggregation rule – if a firm has pursued other transactions within a 3 year period, the effect of these transactions combined can be analysed for the purposes of the merger assessment.
2) Market power rule – if a firm has market power, then a merger can be prohibited even if it has a less than substantial (but material) anti-competitive effect.

Before beginning, however, it is worth noting one complication with assessing hospital mergers, which is that competition takes place on a number of levels. The major hospital groups bargain on a national basis with funders to set prices, suggesting that, to some extent at least, competition between the major groups occurs at a national level. However, the Tribunal has also acknowledged that local competition exists in terms of non-price competition to attract patients and specialists. This may take the form of investment in equipment, improvements in quality etc. Furthermore, local market power can have an impact on national bargaining power. For example, there are some areas where one of the groups owns a “must-have” hospital and therefore holds a substantial degree of market power. In the Phodiclinics/Protector merger the CMS argued that regional dominance confers national market power in the form of leverage in tariff negotiations with medical schemes and also constrains the ability of medical schemes to negotiate preferred provider agreements. This has led the Tribunal on several occasions to consider a merger from both a national and a local perspective, for example:

>“Hospitals compete with one another on several levels. They may compete on price (tariffs) at a national level and on a non-price basis on a local level. The relevant geographical market is therefore the national and local market. A dualistic approach was followed to analyse the geographical market and to consider the national and the local market.”

Appendices 1 and 2 summarise the analysis. For each case, details are given of the market definition, assessment of market power and the impact of the merger and the final decision of the Tribunal/Commission. The final two columns illustrate what the possible outcome of the merger assessment might have been under Rule 1 and Rule 2.

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7 These tariffs obviously only apply to patients covered by medical insurance who make up the majority of private hospital patients.
8 Case number 122/LM/Dec 05, Tribunal Reasons for decision para 14.
9 Life/Amabubesi merger, case number 11/LM/Mar10, Tribunal Reasons for decision para 7.
The tables illustrate that Rule 1 (the aggregation rule) may have had some effect on preventing further concentration in the earlier years, but this was mainly because it would have given the authorities the power to scrutinise some of the large mergers which took place before the Act was in force. In later years mergers are more infrequent and often do not take place in the same local markets, so a finding would therefore rely on a series of transactions leading to a substantial lessening of competition nationally. This in turn would be difficult to show because the later mergers are all smaller transactions, typically the acquisition of one or two hospitals, and given the total number owned by the big groups nationally it would be hard to prove that anti-competitive effects are substantial. As a result, it seems that Rule 1 would not make much difference to the level of concentration in the sector going forward. It also suffers from the problem of avoidability – firms wishing to conduct another merger which could lead to an SLC cumulatively can simply wait until the three year limit is passed. Applying a longer time horizon to the rule would increase the number of mergers which could be scrutinised together, however, a much longer time horizon would result in uncertainty for firms as well as exacerbating the problem of analysing a market where dynamics have changed over time.

The first thing to note about Rule 2 (the market power rule) is that it correlates precisely with the problem identified by the CMS and its proposed solution which was that the major hospital groups should not be allowed to pursue any further hospital mergers as this would further entrench their existing market power. Up until the end of collective bargaining in 2003, the market power rule would not have made a difference to the Tribunal’s decisions in relation to any of the mergers which were approved since in each case a large part of the Tribunal’s reasoning for the approval was the substantial countervailing power held by funders (insurers) and hence the lack of market power held by the hospital groups.

From 2003 onwards, however, the rule would have had a greater effect since the bargaining power of funders seems (from the Tribunal decisions) to have been affected by the change in the nature of price determination at this time. In later decisions, a more nuanced view of the relationship between hospitals and funders is taken. Typically a distinction is made between large medical schemes such as Discovery and smaller schemes, with the former enjoying greater bargaining power vis-à-vis the hospital groups. After this point correspondingly the Tribunal generally scrutinised the mergers which took place in more detail.

Despite this change, we cannot conclude that all the mergers which were considered by the Tribunal and the Commission would have been prohibited under a market power rule. The Phodiclinics/Protector merger would almost certainly been approved regardless, due to the parties’ successful demonstration that the target firm was a failing firm as envisaged in the Act. Evidence of a likely material (but less than substantial) harm to competition would have most likely been outweighed by this consideration.

The other eight cases considered by the Tribunal and Commission are more interesting. Broadly these fall into three categories:

1) Cases where the hospital group enjoys local market power pre-merger and the merger will lead to a material lessening of competition in a local market. This could possibly have been shown in the Netcare/CHG and Life/JMH mergers.
2) Cases where the hospital group enjoys national market power and the merger will lead to a material lessening of competition nationally. This could possibly have been shown in the Mediclinic/Wits, Life/Amabubesi, Life/Aurora, Life/Midmed, Mediclinic/Solar Spectrum and Mediclinic/Holdco mergers.
3) Cases where the hospital group enjoys national market power and through the merger gains local market power (although there is no market share accretion locally) and thus the merger will lead to a material lessening of competition nationally. I.e. when one of the major groups is purchasing an independent hospital which is a
monopoly in its local market. This could possibly have been shown in the Life/Amabubesi, Life/Aurora and Life/Midmed mergers.

Whilst at first glance this analysis may seem to imply that most of the mergers considered by the Tribunal and Commission post-2003 could have been prohibited under rule 2, several caveats apply.

Firstly, such a finding would in some cases have necessitated a more detailed examination of the relevant markets and likely competition effects. In some of the cases, the authorities did not determine a hard-and-fast market definition since the competition effects either way were not substantial. Furthermore, the lack of SLC findings in some of the cases arose partly due to a lack of demonstrable evidence of likely effects (such as the Netcare/CHG merger for example), and not just the lack of substantiality thereof, and so it is not possible to conclusively determine that the mergers would have been prohibited.

Secondly, the outcome of the Commission and Tribunal’s analysis in these cases would have been influenced by the definition of the word material. A straightforward definition of material in this context would suggest a lessening of competition that is more than negligible but less than substantial. The question is whether a market share accretion that is very small (less than 5% for example) would be classified as having a negligible or material effect on competition. In cases where the only identified harm to competition is a small increase in national market share (the second type of case noted above), it could perhaps be argued that this would have a negligible effect on competition. However, in settings where the merger under consideration would result in one of the major groups obtaining a further local market monopoly (the third type of case noted above), given the context of the bargaining relationship between hospitals and funders discussed above, this could arguably result in a material lessening of competition even if the national market share accretion is very small.

A final caveat is that a finding of the second or third type would have relied on the ability of the authorities to demonstrate that the major hospital group concerned had market power in the national market that would be materially enhanced by the merger. This could have proven tricky since nationally, none of the hospital groups has a market share of above 45% (nor even above 35%), suggesting that none of them would be presumptively dominant. The authorities would have had to demonstrate that the groups have market power beyond their market shares which may have been possible, but certainly would have presented a challenge.

In conclusion therefore, the aggregation rule would have been of limited use in tackling the problem of incremental concentration in this industry but the market power rule could have given the authorities more latitude to prevent further concentration. However, the discussion above makes clear that it is not a foregone conclusion that any or all of the notified mergers would have been prevented.

Furthermore, there are clearly a number of other dynamics at play in this market which could have had an impact on competitive outcomes. An obvious candidate is the Commission’s 2003 decision on collective bargaining. Before arguing for a new rule to tackle creeping mergers, it would be advisable to have a more definitive view on whether or not the increased concentration caused by these transactions is the reason (or part of the reason) for high prices. The forthcoming market inquiry to be conducted by the Commission may shed further light on this issue.

5. Conclusion

For the purposes of concluding on whether a new provision to tackle creeping mergers would be a positive intervention, it is necessary to reflect on whether the insights gained from the hospital case study discussed above are broadly applicable. Some factors of that
market may make it unique. For example the fact that the majority of concentration happened before the new competition regime was introduced may arguably mean that preventing further mergers now will have little effect. Further, the Commission’s decision to disallow collective price negotiations could arguably be as big a factor as a few recent small mergers for the market power enjoyed by the three major groups. Nonetheless, the analysis has suggested a market power-type rule could have slowed the pace of concentration from 2002 onwards.

The concern around increased analytical burden remains, particularly as the case analysis showed that in many cases more definitive conclusions or further information would have been required in order to make a finding under either of the rules. In the light of this, a stronger argument for a creeping mergers provision would be provided if the causal link between creeping concentration and higher prices or other anti-competitive outcomes could be shown.

An area for further research would be to look at more industries where creeping mergers are thought to be a problem, in order to obtain a broader perspective of the possible impact of such a rule. It may also be informative to consider the experiences of the few countries where some kind of creeping mergers rule has been applied.
### Appendix 1: Consideration of Tribunal cases in terms of creeping mergers rules 1 and 2

<table>
<thead>
<tr>
<th>Case number</th>
<th>Merging parties</th>
<th>Relevant market(s)</th>
<th>Market power/merger effects</th>
<th>Actual outcome</th>
<th>Outcome under rule 1</th>
<th>Outcome under rule 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>53/LM/Sep01</td>
<td>Afrox (Life)/Amahosp</td>
<td>Market for the provision of a range of private hospital services in the Greater Durban/Pinetown area or in KZN.</td>
<td>Combined market share 36% (narrow market) - biggest player, concentrated market BUT other big players, countervailing power of funders, competition based on ability to market to doctors for referrals</td>
<td>Approved without conditions</td>
<td>If market local/provincial – merger approved</td>
<td>Merger approved – lack of market power</td>
</tr>
<tr>
<td>15/LM/Feb02</td>
<td>Afrox (Life)/Wilgers</td>
<td>The provision of private hospital services in Pretoria either 20-40km radius or 100-200km radius</td>
<td>Combined market share 25% (narrow market), making it second biggest player BUT similar caveats as Afrox/Amahosp plus new capacity about to be built by third biggest player</td>
<td>Approved without conditions</td>
<td>If market local/provincial – increased scrutiny due to acquisition of Faerie Glen in 1999, but post-mergers market share still only 25%</td>
<td>Merger approved – lack of market power</td>
</tr>
<tr>
<td>74/LM/Oct02</td>
<td>Mediclinic/Curamed</td>
<td>The provision of private hospital services in Pretoria or in Gauteng</td>
<td>No overlap in narrow market, 16% combined market share in broad market</td>
<td>Approved without conditions</td>
<td>Possible increased scrutiny due to Auckland Health merger (12 hospitals acquired) in 1999</td>
<td>Merger approved – lack of market power</td>
</tr>
<tr>
<td>75/LM/Aug05</td>
<td>Mediclinic/Wits University Donald Gordon</td>
<td>The provision of private hospital services in Gauteng</td>
<td>Combined market share locally 14% (accretion 3.1%), nationally 30.4% (accretion 0.9%). No SLC.</td>
<td>Approved without conditions</td>
<td>Possible increased scrutiny due to Curamed merger but possibly different local markets (JHB vs. Pretoria). Nationally small accretion.</td>
<td>Locally not likely M has market power. Possible increased scrutiny due to national market power but 0.9% accretion material?</td>
</tr>
</tbody>
</table>

**Commission outlaws collective bargaining in 2003**
<table>
<thead>
<tr>
<th>Case number</th>
<th>Merging parties</th>
<th>Relevant market(s)</th>
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</tr>
</thead>
<tbody>
<tr>
<td>122/LM/Dec05</td>
<td>Phodiclinics (Mediclinic)/Protector</td>
<td>The provision of private hospital services nationally or in the Vaal and Kathu regions</td>
<td>Combined market share in Vaal region – 53% or 71%. But some bargaining power held by medical aid schemes. No significant enhancement of market power locally or nationally Failing firm.</td>
<td>Approved without conditions</td>
<td>Possible increased scrutiny due to Mabopane merger but 40km from Pretoria (nearest Protector hospital) so may not have been same relevant market.</td>
<td>Some anti-competitive effects were likely although not substantial BUT ultimately failing firm defence would still have outweighed effects</td>
</tr>
<tr>
<td>68/LM/Aug06</td>
<td>Netcare/CHG</td>
<td>Not defined</td>
<td>Market shares: Pretoria 41%, East Rand 40%, Cape Town 24%. Difficult to gauge likely effect due to prior implementation. Merging parties argued hospitals not closest competitors. Nationally, would not significantly affect bargaining power</td>
<td>Approved without conditions</td>
<td>Merger approved – no other transactions within 3 years</td>
<td>Possible that a likely lessening (not substantial) of competition could have been shown but market definition would have had to be more conclusive</td>
</tr>
<tr>
<td>11/LM/Mar10</td>
<td>Life/ Amabubesi (Bayview hospital)</td>
<td>The provision of private hospital services locally and nationally</td>
<td>No overlap in local market, market share accretion very small in national market</td>
<td>Approved without conditions</td>
<td>Merger approved – no other transactions within 3 years</td>
<td>Possible change in finding due to market power of Life nationally. Merger could increase Life’s bargaining power vis-à-vis funders</td>
</tr>
<tr>
<td>74/LM/Sep11</td>
<td>Life/JMH</td>
<td>The provision of private hospital services in the Greater Durban Metro area</td>
<td>Combined market share 50% in the local market. Pricing unlikely to increase, SLC unlikely as Life already owns minority stake - JMH would not compete strongly</td>
<td>Approved without conditions</td>
<td>Possible increased scrutiny due to Amabubesi merger but different local markets – would depend on finding SLC nationally</td>
<td>Possible change in finding – could have been a material lessening of competition</td>
</tr>
</tbody>
</table>

Source: Tribunal merger decisions
Note: Green=likely approved, Orange=possibly prohibited, Red=most likely to be prohibited
### Appendix 2: Consideration of some recent hospital mergers assessed by the Commission in terms of creeping mergers rules 1 and 2

<table>
<thead>
<tr>
<th>Case Number</th>
<th>Merging parties</th>
<th>Relevant markets</th>
<th>Market power/merger effects</th>
<th>Actual outcome</th>
<th>Outcome under Rule 1</th>
<th>Outcome under Rule 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011Apr0015</td>
<td>Life/Aurora</td>
<td>The provision of acute rehabilitation services in Port Elizabeth</td>
<td>No geographic overlap at a local level (Life has an acute rehabilitation unit in East London, but separate markets)</td>
<td>Approved with conditions</td>
<td>Possible increased scrutiny due to JMH and Amabubesi mergers but no local market overlap so would depend on national market shares</td>
<td>Possible increased scrutiny due to national market power – Life acquiring a second monopoly provider of acute rehabilitation services could increase its market power vis-à-vis funders</td>
</tr>
<tr>
<td>2011May0041</td>
<td>Life/Midmed</td>
<td>The provision of private hospital services in Middelburg/Mpumalanga (not necessary to conclude)</td>
<td>Market shares not high enough to cause concern</td>
<td>Approved</td>
<td>Possible increased scrutiny due to Aurora, JMH and Amabubesi mergers but no local market overlap so would depend on national market shares</td>
<td>Possible increased scrutiny due to national market power – Life acquiring potential monopoly provider of private hospital services in Middelburg could increase its market power vis-à-vis funders</td>
</tr>
<tr>
<td>2012May0025</td>
<td>Mediclinic/Solar Spectrum</td>
<td>The provision of private hospital services in Centurion</td>
<td>Low market shares and market share accretion</td>
<td>Approved with conditions</td>
<td>Merger approved – no other transactions within 3 years</td>
<td>Difficult to show market power locally. Possible increased scrutiny due to national market power but small accretion material?</td>
</tr>
<tr>
<td>2012Dec0730</td>
<td>Mediclinic/Holdco</td>
<td>The provision of private hospital services in radius of 10-30km from the target hospital (Boksburg)</td>
<td>Low market shares and market share accretion</td>
<td>Approved</td>
<td>Possible increased scrutiny due to Solar Spectrum merger, although Commission analysis placed them in different markets</td>
<td>Difficult to show market power locally. Possible increased scrutiny due to national market power but small accretion material?</td>
</tr>
</tbody>
</table>

Source: Commission merger reports

Note: Green=likely approved, Orange=possibly prohibited, Red=most likely to be prohibited
References

Australian Competition and Consumer Commission (ACCC) submission to the Assistant Treasurer and Minister for Competition Policy and Consumer Affairs regarding creeping acquisitions, October 2008


OECD, Substantive Criteria used for Merger Assessment, DAFFE/COMP (2003), a copy of which can be found at: http://www.oecd.org/dataoecd/54/3/2500227.pdf.

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