MEMO/07/258

Brussels, 27th June 2007

Mergers: Commission's prohibition of Ryanair's proposed acquisition of Aer Lingus – frequently asked questions

(see also IP/07/893)

Why has the Commission prevented a new entrant like Ryanair from expanding?

Ryanair is not prevented from expanding. It remains perfectly free to expand as it has up until now, through organic growth. It can also take over other airlines as long as it doesnot impede competition.

However, Ryanair is no longer a small new entrant airline: as regards the number of passengers served, Ryanair itself cites recent IATA statistics according to which Ryanair ranked in 2006 on the first place with 40,532,000 international passengers and thus carried more international passengers than Air France, Lufthansa or British Airways[1].

While Aer Lingus is smaller than these carriers, it carried 8.6 million passengers in 2006 (around 7.5 million on short-haul routes).

The merged entity would have a fleet of more than 150 aircraft used on short-haul (intra-European) routes, with firm orders for more than 160 additional short-haul aircraft.

The competitive effects of the transaction were analysed on individual short-haul routes between Ireland (in particular Dublin) and various European destinations. On these markets, both Ryanair and Aer Lingus are clearly the most important operators carrying together around 80% of all intra-European passengers to/from Dublin. Further, their activities directly overlap on 35 routes on which more than 14 million passengers are carried annually.

Both the Commission's market investigation and internal documents of both carriers confirmed that on these routes, Ryanair and Aer Lingus clearly represent the main competitive constraint on each other. This is also taken into account by both of them when determining their prices and other elements of their competitive behaviour. For all these passengers the transaction would lead to significant elimination of choice between available airlines.

By way of comparison, the total number of passengers carried annually on short-haul (intra-European) routes on which the Commission identified competition concerns that had to be remedied was significantly less than 4 million in both Air France/KLM (see IP/04/194) and Lufthansa/Swiss (see IP/05/837) and well below 1 million in Lufthansa/Eurowings (see IP/05/1703).

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[1] See Ryanairs press release of 13 June 2007, available on Ryanair's webpage at the following address: http://www.ryanair.com/site/EN/news.php?yr=07&month=jun&story=gen-en-130607.

What of Ryanair's claim that consumers would have saved more than €100 million in the first year?

Competition following liberalisation of the EU's air travel market has brought significant benefits to consumers. It has enabled new, low-cost, carriers to enter the market and shake up an industry that had long been dominated by national flag carriers and government-regulated fares. It is this new dynamic competition ushered in by liberalisation that has saved consumer hundreds of millions of euros.

The €100m figure relates to a proposed "remedy" by which Ryanair would commit to lower Aer Lingus' short-haul fares by 10% for a period of one year after obtaining a near monopoly position at Dublin airport. While this is a headline-grabbing figure, this type of commitment would be almost impossible to monitor. Moreover Ryanair gave no commitment on what would happen to Ryanair's own prices, or what would happen to Aer Lingus prices after the first year.

What is certain is that Ryanair proposed to end the intense competition between Ryanair and Aer Lingus at Dublin airport that has pushed prices down and brought Irish consumers an increasing choice of direct flight connections from Dublin. It is highly unlikely that Irish consumers would be better off with a near monopoly, even if it were sweetened by a temporary, hard-to-monitor price rebate. Further, it is impossible for the Commission to anticipate what would constitute a "competitive" price level at a future point in time in a market that has seen significant fluctuations in average fares and in input costs, such as fuel, from year to year.

Given Ryanair's record of low-cost fares, how can a merger be detrimental for consumers?

Ryanair saw a business opportunity though introducing competition into the airline sector: consumers benefited greatly from that increased competition. However Ryanair cannot now take that competition away again by buying its main competitor in Ireland.

The fact that Ryanair has contributed to the development of low-fares alternatives for European customers does not exempt Ryanair from EU competition rules. The EU's liberalised air transport market enables any EU-based carrier to connect any two EU airports it chooses. Ryanair, along with several other start-up airlines, seized these opportunities offered by this open skies environment. This has greatly increased competition and lowered fares for consumers. At the same time, Ryanair generates one of the highest profit margins of the airline industry.

Ryanair's prices vary depending on the competition present on the market. It has both increased and lowered average fares in recent years depending on competitive conditions and costs. As set out in detail in the Commission's prohibition decision, Ryanair's fares are driven not only by the level of customer demand but also by the competition it meets on any given flight. The Commission's analysis shows that Ryanair reacts to competition by decreasing its fares. There is thus absolutely no reason to believe that a near monopoly at Dublin airport would make consumers better off than the current intense head-to-head competition between Ryanair and Aer Lingus.

How do the principles applied in this case relate to those used in previous cases?

The principles used in this case are the same as in the previous cases such as Air France/KLM, Lufthansa/Swiss or Lufthansa/Eurowings.

The competitive effects of the transaction were analysed on the basis of the competitive situation on individual routes while taking into account the substitutability of air transport services operated to different airports in the vicinity of the same city and other available means of transport.

Further, where the investigation found that the merger would lead to very high market shares or even a monopoly, the Commission then analysed whether there was potential for significant entry by a competitor which could compensate for the lost competition on the particular route.

It should however be stressed that the factual situation in this case was significantly different from all previous airline mergers assessed by the Commission, notably because the case concerned for the first time a merger of two "low-cost" point-to-point airlines and two airlines with significant operations at one and the same airport.

How do the facts of this case differ from previous cases?

- All previous cases concerned mainly mergers of two carriers which had their main centres of operations at **different airports**, often in different countries and raised concerns on a relatively limited number of overlapping routes. In contrast, this merger concerns the two main airlines in Ireland with significant operations at one and the **same airport**, Dublin Airport, where they are by far the two largest airlines.
- Previous airline cases dealt mainly with mergers which combined complementary networks and operating models, e.g. network carriers operating with a hub and spoke model and charter/ tour operators[2], network carriers and smaller regional airlines[3] or, in some cases, two (smaller and larger) network carriers[4]. The present transaction is the first case in which the Commission had to assess a merger combining two airlines which operate according to the low-cost/low-fares business model and which are focused on point-to-point intra-European services.
- Reflecting the significant activities of both parties in Ireland and in particular Dublin, the transaction would have led to an unprecedented large number of overlap routes where both parties currently operate directly competing services. Thus the merger would have led to competition concerns on 35 routes to/from Ireland, with 32 of these routes to/from Dublin. In case of 22 of these 35 routes, the merger would have created a monopoly as only Ryanair and Aer Lingus are active there. Further, the merger would also have eliminated the most credible entrant on a number of routes to and from Ireland where only one of the parties is currently active.

[2] See cases M.2218 - British Airways/Thomas Cook; M.1354 - Sair (Swissair)/LTU; M.1128 - KLM/Martinair;M.2093 - Airtours/FTI; M.1524 - Airtours/First Choice.

[3] Cases M.157 - Air France/Sabena; M.278 - British Airways /DanAir, M.857 - British Airways /Air Liberté; M.806 - BA / TAT; M.1855 - Singapore /Virgin; M.1494 - Sair (Swissair)/AOM; M.3940 - Lufthansa Eurowings.

[4] See cases IV/JV.19 - KLM /Alitalia; COMP M.3770 - Lufthansa/Swiss; M.562 - Swissair/Sabena, M.3280 – Air France/KLM. or M.3770 – Lufthansa/Swiss.

- The market investigation revealed significant barriers to entry to individual routes to/from Ireland (and in particular Dublin) for competitors of Ryanair and Aer Lingus. Unlike previous cases, the congestion of the airports did not play a prominent role as a barrier to entry as other barriers were significantly more important. These barriers related to the current strong position of Ryanair and Aer Lingus in Ireland, the risks and costs of an efficient entry against these two strong airlines with recognised brands on the affected routes as well as Ryanair's reputation of aggressive competition against new entrants demonstrated by a number of past examples. In fact, the Commission's investigation showed that in the past there were only a handful of successful new entrants to routes to/from Ireland and that even the second strongest low-cost carrier in Europe – easyJet – did not succeed in establishing services to Ireland and ceased flying there in 2006.

What evidence does the Commission have for its conclusions?

The Commission's analysis is based on number of different type of evidence. It has analysed replies to questionnaires sent to competing scheduled airlines, charter airlines, airports, corporate customers, slot coordination authorities, civil aviation authorities and transport authorities and other oral and written statements and studies.

Further, apart from reviewing the econometric submissions from Ryanair, Aer Lingus and other third parties, the Commission conducted two sets of regression analysis[5] based on data from Ryanair, Aer Lingus and third party data aimed at identifying the level of competitive constraints exercised between Ryanair and Aer Lingus as well as by their competitors. In addition, a price correlation analysis for individual airport pairs and city pairs provided input in particular for the market definition section with respect to substitutability of services to different airports.

As passenger views are important in this case, the Commission assigned an independent consultant to carry out a customer survey at Dublin Airport to obtain a representative sample of responses from customers who departed from Dublin.

The Commission has several times indicated that it supports consolidation in the European air transport sector. Is the decision in this case in line with this Commission's policy?

The Commission's previous decisions show that consolidation can be wholly compatible with merger control rules that are there to protect consumers. While the Commission supports consolidation in the sector, that consolidation cannot come at the expense of millions of consumers' facing monopolies and higher prices on a large number of routes.

The facts of this case clearly showed that the transaction would lead to a significant impediment of effective competition on numerous routes which would affect a large number of passengers.

[5] One set of the regression analysis was based on comparisons of fares across routes (the "cross-section" analysis) and the other involved an assessment of price variations over time and across routes (the "fixed-effects" analysis).

Why were Ryanair's commitments insufficient to remove the identified competition concerns in this case?

As indicated above, different to previous airline mergers assessed by the Commission, the barrier to entry due to the lack of slots played, due to the specific facts of this case, a less prominent role than in the previous cases. The investigation showed that, for this case, transfer of slots (i.e. landing and take-off rights at airports at specific times) alone was not sufficient to lead to a required likelihood of new entry which would provide significant competitive constraints to the merged entity on all the overlap routes.

In all cases remedies based on the divestiture of slots must be linked to the likelihood of entry. In previous cases the Commission demonstrated that entry of a new competitor was, on the basis of the facts known to the Commission at the time of the decision, sufficiently likely to provide competitive constraints to the merged entity. This approach was confirmed by the judgment of the Court of First Instance in the case T-177/04 – easyJet v. Commission (relating to the Commission's decision in the Air France/KLM case).

In contrast to the previous cases approved subject to slot divestiture commitments, the Commission had no clear evidence in this case that entry by one or more competitors on the basis of the proposed commitments would be sufficiently likely and of a sufficient scope to remove the identified competition concerns on the overlap routes. The extensive market test of the proposed commitments, as well as the results of the in-depth market investigation, clearly showed that entry of a significant competitor which would replace the competitive constraints between Ryanair and Aer Lingus lost due to the merger is unlikely. Under these circumstances, the Commission could not approve the transaction subject to slot divestiture commitments aimed at mere reduction of barriers to entry consisting in airport congestion.

Did other elements of the proposed commitments not compensate for the insufficiency of the "traditional" slot divestiture?

Ryanair tried to address the insufficiency of the slot commitments by proposing a so-called “up-front” solution, i.e. a commitment that Ryanair would acquire control over Aer Lingus only after a suitable new entrant was found. It should be noted that it is a standard practise of the Commission to use "up-front buyers" in cases where viability of the divested assets depends to a large extent on the identity of the purchaser[6].

However, apart from various formal shortcomings of this commitment, the scope of the guaranteed new entry was clearly insufficient to address all the identified competition concerns. The market test clearly indicated that a new entry with at least 12 to 16 aircraft for routes to/from Dublin would be necessary to ensure that the merged entity would face sufficient competitive constraints on all routes where competition concerns were identified. However, the commitments proposed by Ryanair provided a guarantee of only up to 8 aircraft. In addition, the proposed commitments suffered from numerous other shortcomings which taken together significantly reduced the likelihood that these commitments would be successfully implemented and provide for a sufficient likelihood of a significant new entry. In these circumstances, the Commission had an obligation to declare the concentration incompatible with the common market.

[6] See paragraph 20 of the Commission Notice on remedies acceptable under Coucil Regulation (EEC) No 4064/89 and under Commission Regulation (EC) No 447/98, OJ C 68, 2.3.2001, p. 3., as well as cases such as COMP/M.3796 – Omya/Huber PCC of 19 July 2006; Case COMP/M.2972 – DSM/Roche Vitamins of 23 July 2003; Case COMP/M.2060 – Bosch/Rexroth of 13 December 2000; Case COMP/M.2337 - Nestlé/Ralston Purina of 27 July 2001; COMP/M.2544 Masterfoods/Royal Canin of 15 February 2002; COMP/M.2947 Verbund/Energie Allianz of 11 June 2003.