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MERGER REGULATION IN CENTRAL AND EASTERN EUROPE: EVIDENCE FROM HUNGARY, ROMANIA AND SLOVENIA

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This paper shows the principal features of merger control in selected transition economies of Central and Eastern Europe (CEE), namely Hungary, Romania and Slovenia, by applying case study methodology. The presented findings are based on the analysis of Hungarian, Romanian and Slovenian competition law and merger rulings reached by the Competition Offices of these countries. A substantial part of the conclusions is drawn from a sample of 42 merger applications processed by the Office of Economic Competition of Hungary between 1994 and 2000. The results of empirical analysis demonstrate the considerable flexibility of merger control in the studied countries, its orientation towards the future of domestic markets and a close link with industrial policy. The paper also highlights the areas of interdependence of competition policy and transition and argues that merger control in the studied CEE countries may be regarded as currently adequate to the requirements imposed by transition.

Keywords: merger regulation, competition policy, transition economies

JEL classification index: O34, G18, K2, P2

INTRODUCTION

Nowadays, mergers are common business practice throughout the world. The interest of scholars and regulators in such activities originates largely from the inherently present tradeoff. On the one hand, the re-allocation of resources within the merged entity may create considerable efficiency gains. On the other hand, mergers alter the market structure and often lead to higher concentration and concomitant restrictions to competition. These latter effects reveal the scope of merger regulation.

Following the course of reforms, the process of economic transformation has stimulated mergers in the former centrally planned economies of CEE. Lacking

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the relevant experience of merger regulation, these countries adopted the main methods of merger control from the more advanced market economies. The questions, which naturally arise, are how the regulatory techniques prevalent in mature markets are "shaped" by transition, and what are the most important characteristics of merger control in the transition economies of CEE. This paper tries to answer both questions for the selected countries of the region, namely Hungary, Romania and Slovenia, and there will also be some general conclusions.

The existing (English-language) literature usually discusses merger control in CEE within a larger domain of competition policy. Fingleton et al. (1996) present the most comprehensive analysis of transition reforms and competition policy for the four Visegrád countries. Other works include mainly country studies of the region. For instance, Török (1996, 1997) and Kovács (1997) provide a thorough examination of the first and second generation competition law and its application in Hungary. Slay (1996) and Modżełewska (1997) discuss the development of competition policy in Poland. These papers, however, consider competition policy as a whole and do not cover merger control in depth. The present study intends to fill in the gap existing in competition policy research for the transition economies of CEE, and provides an extensive analysis of mergers undertaken in three countries of the region – Hungary, Romania and Slovenia. The novelty of this study is seen in its primary focus on mergers in the transition economies of CEE, and in the demonstration of the specifics of merger regulation. The latter were derived from the examination of actual case materials obtained for the countries in question.

This paper shows that the economic environment of transition determines rather broadly defined and flexible standards of merger control in the studied countries. Specifically, the results of the undertaken research demonstrate that the evaluation of the strength of actual and potential competition plays a more pronounced role than the exact delineation of relevant markets and the appraisal of market shares. Our findings also indicate that the competition authorities of Hungary, Romania and Slovenia favour economic concentration and consider the needs of industrial policy in their decisions on mergers.

Most conclusions drawn in the paper are based on the analysis of a sample of 42 merger applications processed by the Office of Economic Competition of Hungary between 1994 and 2000. Additionally, the available material on merger decisions adopted by the Competition Offices of Slovenia and Romania allowed the scope of the study to be substantially extended and the results to be generalised.

The paper is structured as follows. First, the essence of "transitional" competition policy will be discussed briefly. Second, to show some quantitative similarities, the structural patterns of merger rulings in the selected transition econo-

mies of the region will be compared to those of the EU. Subsequently, the features of merger control in the transition economies of CEE will be shown and supported by evidence from Hungary, Romania and Slovenia. The final part of the paper will discuss the relationship between transition and competition policy, and the adequacy of merger regulation with respect to the requirements of transition.

COMPETITION POLICY IN THE TRANSITION

Competition policy can be defined as a set of tools aimed at influencing market structure and conduct to ensure efficient competition. Economic transition, which implied a shift from centrally planned to market-driven resource allocation, also determined the principal tasks of competition policy. Applying the terminology of Modżełewska (1997), competition policy tasks can be creative or supportive. Creative tasks are aimed at establishing and enforcing the rules of competitive conduct of firms given large efficiency differences and the lack of previous competition among firms. The main tools are demonopolisation, privatisation and the institutionalisation of competition law. In turn, supportive tasks are needed to safeguard competition already attained in the market – in particular, via the control over anti-competitive concentrations and abuses of a dominant position. The logical development of competition policy in transition suggests that, at the initial stage of reforms, creative tasks play a more important role, whereas supportive tasks gain significance as market structure develops. However, it seems important to set both objectives from the very beginning of transition because creative tasks may not be achieved without supportive competition policy.

In both phases of competition policy defined above, competition law plays the essential role of linking policymaking, policy implementation and enforcement. At the same time, the specific tasks of competition law and hence its particular emphasis can differ in different phases. Thus, at the initial stage of transition, competition law is concerned more with establishing the legal apparatus of competition policy and combating the monopolistic behaviour of large enterprises (the so-called first-generation competition law). At subsequent stages, the focus shifts towards supportive measures – with more attention paid to restrictive agreements, and anti-competitive concentrations in particular (second-generation competition law).

Further, it should be recognised that the economic environment of transition imposes a certain pressure on competition policy. This pressure largely originates from the specific conditions in which competition policy started to emerge at the beginning of transition. These include:

- Rigid industrial structure with a large number of dominant and monopolistic enterprises, which in many cases could not compete with foreign companies (see also Pittman 1997).
- A need for substantial capital investments to undertake industrial restructuring accompanied by limited domestic financial resources.
- Underdeveloped commodity markets with no or fragile competitive fringes of smaller firms unable to substantially influence the behaviour of dominant enterprises (Fingleton et al. 1996).
- High barriers to market entry and exit further enhanced by the weakness of legislation on corporate bankruptcy, contracts and foreign direct investment (Pittman 1997) and the restricted access to credit and strategic assets for small and medium sized enterprises.
- Insufficient expertise and skills of the competition authorities' staff and limited opportunities to compare market performance of different agents.

The above conditions allow for the conjecture that transition competition policy should be more active as well as more flexible than competition policy prevalent in mature market economies. The need for a more active competition policy roots in the necessity of restructuring the enterprises and establishing competitive markets in a short period of time. A further support stems from the argument of Fingleton et al. (1996) that welfare damages from anti-competitive practices of firms might be considerably higher in transition economies than in countries with developed markets.[1] At the same time, in transition countries, competition policy should be flexible and discretionary, as it needs to account for the rapid changes of industrial structure. Specifically, the assessment of actual and potential competition on a given market might have a very short-term validity if the affected industry undergoes a process of substantial restructuring. The rest of the paper will provide evidence in support of the above conjecture for merger control as a part of competition policy.

MERGER REGULATION IN THE TRANSITION ECONOMIES OF CEE: AN EXCEPTION SUPPORTING THE RULE?

Merger regulation falls in the domain of supportive competition policy. When merger control in transition economies is studied, a question of interest is how it differs from the practices adopted in developed market economies. Do the eco-

[1] As an illustration, they note that the impact of collusion of a few large producers operating in a certain market is likely to be more harmful to competition if there is no strong fringe of small firms to impose restraints on the collusive behaviour.

nomic conditions of transition imply any specific patterns of mergers' treatment by the competition authorities? This section will compare the structure and dynamics of merger rulings in the selected transition economies of CEE and in the EU and show that actually there are common trends.

The available data on merger cases processed by the competition authorities of Hungary and Slovenia allows three characteristic features to be singled out:

- The first is the rapidly increasing number of pre-notified mergers as markets mature. While only 5 merger cases were processed by the Office of Economic Competition of Hungary in 1991, 70 such cases were appraised in 2000 (*Table 1*). In Slovenia, the number of processed mergers increased from zero in 1995 to 17 in 1999 (*Table 2*).
- The second feature is the relatively small number of blocked and conditionally authorised mergers. Between 1991 and 2000 only three mergers were refused in Hungary and only two were authorised conditionally (both in 2000). For Slovenia, the corresponding figures are two and two respectively.
- Thirdly, quite a large number of cases are out of the scope of merger control as compared with the number of blocked mergers (see *Table 1* for the evidence for Hungary).[2]

These three features are conceived to exhibit a general pattern of merger rulings in the transition economies of CEE. At the same time, quite similar trends were observed in the practice of merger control in the EU. According to the statistics of the European Commission, the number of processed merger cases was rapidly increasing between 1990 and 2000 – from 12 to 345 respectively (*Table 3*). For the whole period between 1990 and 2000, the European Commission prohibited only 13 mergers; the peak was 1996 with 3 such cases. Further, a total of 52 applications were decided to be out of the scope of merger regulation; this figure is quite substantial against the corresponding number of blocking decisions in the EU.

As we have seen, the structure and dynamics of merger rulings in Hungary and Slovenia do not differ substantially from those of the EU. This statement seems to hold for a broader selection of transition economies although some additional data would give more insight into the issue. The next section will present the results of a *qualitative* analysis of merger regulation in the transition economies of the region.

[2] The fairly large number of mergers that were not subject to authorisation in 1995–1996 is partially explained by the fact that before 1997 (according to the since then abolished Hungarian Competition Act of 1990), mergers with foreign companies, which were not initially present in the Hungarian market, were not covered by Hungarian merger regulation.

Table 1

Structure of merger decisions reached by the Office of Economic Competition of Hungary in 1991–2000 (number of cases)

Cases	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Total processed	5	8	3	3	24	25	30	49	46	70
Authorised	5	3	1	3	13	18	27	37	42	58
Conditionally authorised	–	–	–	–	–	–	–	–	–	2
Not subject to authorisation	–	5	2	–	10	7	3	8	4	9
Blocked	–	–	–	–	1	–	–	1	–	1
Total final decisions	5	8	3	3	24	25	30	46	46	70

Source: Office of Economic Competition of Hungary.

Table 2

Structure of merger decisions reached by the Competition Protection Office of Slovenia in 1995–1999 (number of cases)

Cases	1995	1996	1997	1998	1999
Total processed	–	3	1	11	17
Authorised	–	3	1	6	11
Conditionally authorised	–	–	–	–	2
Blocked	–	–	–	2	–
Total final decisions	–	3	1	8	13

Source: Šlebinger et al. (2001).

SPECIFICS OF MERGER REGULATION IN THE TRANSITION ECONOMIES OF CEE: THE CASES OF HUNGARY, ROMANIA AND SLOVENIA

Based on the study of legal framework for mergers and the available case materials from Hungary, Romania and Slovenia,[3] four features of merger regulation in the transition economies of CEE could be distinguished. In what follows, these interdependent statements will be considered separately and illustrated by representative empirical evidence.

[3] A substantial part of the conclusions presented in this section is based on the analysis of a sample of 42 merger rulings reached by the Office of Economic Competition of Hungary between 1994 and 2000. The case materials for Romania and Slovenia are taken from Domokos and Micu (2001) and Šlebinger et al. (2001) respectively.

Table 3

Structure of merger decisions reached by the European Commission in 1990–2000
(number of cases)

Cases	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	Total
Notified	12	63	60	58	95	110	131	172	235	292	345	1573
PHASE I												
Out of scope of merger regulation	2	5	9	4	5	9	6	4	6	1	1	52
Compatible	5	47	43	49	78	90	109	118	207	236	293	1275
Compatible with commitments	–	3	4	–	2	3	–	2	12	19	28	73
Referral to member states	–	–	1	1	1	–	3	7	4	4	6	27
PHASE II												
Compatible	–	1	1	1	2	2	1	1	2	–	3	14
Compatible with commitments	–	3	3	2	2	3	3	7	5	8	12	48
Prohibition	–	1	–	–	1	2	3	1	2	1	2	13
Restore effective competition	–	–	–	–	–	–	–	2	–	–	–	2
Partial referral to member states	–	–	–	–	–	–	–	–	–	1	–	1
Total final decisions:	7	60	61	57	91	109	125	142	238	270	345	1505

Source: European Merger Control – Council Regulation 4064/89 – Statistics (2001).

Feature 1:

> The exact relevant market delineation and the appraisal of market shares are less important in the transition economies of CEE than the assessment of actual and potential competition (including import competition in both cases) and a merger's justification.

The first feature of merger control is based on three interrelated findings in the practice of merger rulings in the considered transition economies of CEE:

- The definitions of relevant market are rather broad and flexible.
- Mergers can be authorised even though they create substantially large market shares.
- The prevalent argumentation for the affirmative decisions on the proposed mergers is the presence of strong actual and potential competition in the market (notably, this consideration partially explains the first two observations).

As far as the broadness and flexibility of defining relevant markets are concerned, it was found that the competition authorities were less precise in the *exact* delineation of market boundaries if there was strong actual competition either in the affected industry as a whole, or in the broadly defined relevant market. In the "Ford/Volvo" case in Hungary (1999), the merger of car manufacturers was authorised by the Office of Economic Competition despite that it would create a joint share of 51.5% in the Hungarian market of large and sports cars. The principal consideration was the existing strong competition of 35 car manufacturers on the (broadly defined) Hungarian car market, and the fact that large and sports cars account only for 1.8% of this broad market. As the case shows, *precise* market definition was regarded secondary to the intensity of competition in the broad market.

The authorisation of a substantial concentration on the relevant market appeared to depend on a merger's justification and its valuation by the regulator. Specifically, as the "Balatonboglár/Hungarovin" case in Hungary (1994) shows, a large merger (in this case, creating a joint share of 60% in the Hungarian market of champagne) is likely to be authorised if there is a proven danger that without merger one of the partners would go bankrupt. A substantial concentration can also be allowed if it serves the strategic interests of the state. For instance, if it enables technological modernisation as it was noticed in the case "RTL/PR" in Hungary (1996): a merger of two cable television services, whose combined market share was over 50% in the relevant market, was authorised. The explanation was that it would enable the modernisation of the outdated television network.

These two examples are a good illustration of one important feature of competition policy in transition: the practice of merger regulation is closely linked with industrial policy and serves its needs. This consideration seems particularly relevant in the early stages of transition. At that time, the goal of the regulators was not only to set rules and maintain efficient competition in domestic markets but also to implement industrial restructuring and modernisation, and create a sufficient number of viable market players. As transition proceeds and domestic enterprises become more competitive, the observed dependence of competition policy on industrial policy is likely to decrease.

The central argument for allowing many mergers in the studied countries was found to be the presence of strong actual or potential competition in the affected market. In principle, this phenomenon is explained by the structure of the majority of transition markets (except for the naturally monopolistic ones). These markets can be characterised by (a) a sufficiently large number of competitors within the market (which ensure strong actual competition) and (b) a relatively high degree of contestability due to low or non-existent entry barriers.

Several examples from Hungary provide an illustration of the strength of actual competition:

- 1997 – printing industry: 26 permanent and 260 temporary enterprises.
- 1998 – canned food industry: 30% of such products imported and there were about 20 large domestic manufacturers.
- 1998 – cat and dog food industry: 50% of products imported and there were 80 domestic manufacturers.

To give further illustrations, credit market, distribution of motor vehicle fuel, tobacco trading, IT services, paper industry and a number of other markets in Hungary were regarded by the competition authorities as strongly competitive. As a result, several concentration transactions proposed in these markets were authorised as not impeding efficient competition.

The high degree of market contestability can be attributed to the following factors, which appear either separately or simultaneously. The first one is the easy and likely entry of domestic enterprises as a response to price increase. A typical example is the hotel business in Budapest, where a hotel, after making certain improvements, can enter the next star category rather quickly. The second factor is the low or decreasing customs duties and fees encouraging the entry of competitive imports in some markets. To illustrate, Hungarian customs charges on the import of hollow ware products (manufacture of preserve jars and white and green bottles) decreased from 19.8% (early 1995) to zero (July 1997). The subsequent increase of import competitiveness resulted in a 67% concentration of the Hungarian hollow ware market, which was authorised by the Office of Economic Competition in 1997.

Easy import penetration may provide an additional explanation why low weight was assigned to the market shares in merger control. Starting from the mid-1990s, the domestic markets in most transition economies of CEE became open to such an extent that the boundaries of certain *properly defined* relevant markets would have far exceeded the territory of a given country. Because of the vagueness of the markets' geographic boundaries, the assessment of the strength of actual and potential competition in the defined product market proved to be more significant relative to the evaluation of the *exact* market shares.

In short, the studied merger cases suggest that competition authority decisions in the considered transition economies are not based on the *precise* delineation of relevant markets and the assessment of market shares (although these are defined for the majority of cases) but on the evaluation of:

- Actual competition in the market, namely the number and strength of market actors as well as the relevant import competition.
- Potential competition and entry barriers, namely the "timeliness, likelihood and sufficiency" of entry by both domestic and foreign enterprises in response to a price increase on the market.
- Other considerations of the given merger to see whether it is in accordance with the strategic interests of the state.

The definition of relevant markets is surely used in merger appraisals. However, the *precise* delineation can be approximated – especially if it is difficult or very expensive for the competition authorities to be precise and the considered case does not raise competition concerns in the narrowest properly defined market.

Quite similar features of not relying solely on market shares in mergers' appraisal were also found by Neven et al. (1993) in the merger rulings of the European Commission before 1992. However, an important distinction between the approach taken by the transition economies of CEE and the EU is to be made. In the EU, the authorisation of many mergers was granted "not so much because entry was easy, but rather because actual competition was considered rather strong" (Neven et al. 1993, p. 104). For transition economies, as the case of Hungary suggests, market contestability seems to play an equal or even a more pronounced role as the strength of actual competition. A possible explanation for this observation may follow from the recent opening of transition markets (in particular, to import competition). Consequently, at present the main strategic moves of firms are both *reallocation* (within a given market) and *penetration* (inside the market).

Feature 2:

> In the merger regulation of the transition economies of CEE, the mainstream theoretical dilemma of productive versus allocative efficiency[4] is often reformulated into the principle: "productive efficiency *for* allocative efficiency".

[4] On the one hand, productive efficiency might be enhanced after a merger via concomitant cost economies and synergies. On the other hand, a merger (especially a horizontal one) is likely to increase market concentration and facilitate collusion. Consequently, the *realised* possibility to profitably set prices above their competitive level might create allocative inefficiency.

It is hard to question that competition in a given market can be seriously endangered if there are only a few sufficiently large firms and no *strong* smaller companies able to counterbalance the possible anti-competitive behaviour of the dominant firms. In these circumstances, it was found that the competition authorities of the countries considered did not oppose that type of concentration, which would not result in a substantial increase of market shares but strengthen the position of weaker incumbents. Such mergers enable small firms to enjoy certain economies of scale but at the same time also to cope with their stronger competitors and safeguard allocative efficiency. As an outcome, the principle "productive efficiency for allocative efficiency" applies. This principle is inherently present in the competition law on mergers adopted in all three studied countries. The established turnover thresholds for the pre-notification of mergers allow those transactions, which do not significantly impede actual competition but might strengthen the competitive position of small companies. This way the scrutiny of authorities can be avoided.

Two typical examples of merger control in practice can be illustrated by the meat and IT industries in Hungary. According to the competition authority rulings, some authorised transactions such as the "Pick Szeged/Ringa Meat" (1997) and "Compaq/Digital" (1998) cases covered 13.7% and 8.9% of the respective markets. In both cases, in support of actual competition, the competition authorities viewed these mergers as not creating (or leading towards) dominant positions but intensifying efficient competition on the affected markets. It can be inferred that given a high level of market contestability and a large enough number of competitors, the competition authorities of the selected transition economies favour efficiency enhancing concentration, thus further strengthening the competition within the markets.

As compared with the EU experience, a stricter approach towards efficiencies associated with mergers is to be noted in the Union. On the one hand, the established turnover thresholds do allow small firms to merge without pre-notification and increase their efficiencies via economies of scale and synergies. On the other hand, if a merger is subject to authorisation by the competition authority of the EU, its attitude towards efficiency considerations is somewhat unclear. As it is shown by Neven et al. (1993, p. 116), concomitant efficiencies sometimes appear as a defence of certain mergers. At the same time, the European Commission acknowledges "the possibility that potential advantages flowing from synergies may create or strengthen a dominant position". The above distinction suggests that merger control in the EU is more "protective" towards the attained level of actual competition, while transition economies retain more "creative" features. An intuitive explanation stems from the consideration that transition

markets are still in the process of catching up. Consequently, the competition authorities recognise that they can diminish the scope of their future intervention in market processes (like combating dominant structures) by currently creating strong competitive fringes of smaller firms.

Feature 3:

Merger control in the transition economies of CEE exhibits protectionism supporting the concentration of domestic enterprises.

The regulators were found to favour the mergers of domestic enterprises in order to enable them to stand the competition of quality imports. There are protectionist clauses in the competition law on mergers in each of the countries studied. For instance, Article 24 (2c) of the recently abolished Hungarian Competition Act of 1990 prescribed to authorise a merger if it promoted activities on foreign markets that were advantageous to the Hungarian economy. Further, this Act regarded technological development and enhanced competitiveness on the external markets among the merger's advantages, which could imply anti-competitive effects of increased concentration in the relevant market (Article 17 (2e)). These provisions suggest that the Competition Act of 1990 protected Hungarian enterprises, which were generally less competitive than their Western counterparts, against increased import competition (which could be counterproductive for the domestic economy). These clauses were removed by the new Hungarian Competition Act of 1996, but certain protectionism is still retained for "internal and external competitiveness" of the merging companies during merger appraisal (Article 30 (1)). There are similar phrases in the competition laws of Romania and Slovenia. According to Article 14 (2) of the Romanian Competition Law of 1996, a large merger can be authorised if it increases productive efficiency, stimulates technological progress or enhances export competitiveness.

If we turn to the practice of merger regulation, one of the examples of state protectionism can be shown in the authorisation of a series of mergers undertaken by "Globus Canning Factory Ltd." in Hungary. On the Hungarian market of canned products, Globus had shares between 11% and 57% for the canned meal, meat, tomato and pickles product groups. Still, the Office of Economic Competition of Hungary approved the merger of Globus with Food Farms '96 (in 1998) and "Csaba Canning Factory" (in 2000), taking into account strong actual competition in the relevant market – in particular import competition (imports account for approximately 30% of the canned food market).

A more obvious case of state protectionism was found in Romania. As it was observed, the protectionism expressed by the regulators could even dominate the interests of market players. In 1997 the Competition Council of Romania conditionally authorised a merger of three tire manufacturers resulting in market share concentration up to 95% in some segments (Domokos and Micu 2001). Such an extreme level of concentration was allowed because it was though to enhance the competitiveness of Romanian tires on the global market and increase the efficiency of tire production.

The examples from Slovenia demonstrate that the protectionist goals of the state are nevertheless constrained by the considerations of preventing excessive concentration in domestic markets. As an illustration, a merger of two large trade companies "Mercator" and "Emona Merkur" was initially blocked in 1999, although it would have enhanced the competitiveness of Slovenian trade companies vis-à-vis multinational trade chains. The key argument for the resolution was the risk of limiting competition: in 1999 Mercator was among the 10 highest profit-earning companies in Slovenia and the joint share of the merged firm in the Slovenian retail market would have reached 32% (Šlebinger et al. 2001). However, the merger was allowed in 2000 due to the unfavourable financial position of "Emona Merkur" as well as to its failure to merge with some other companies to improve the situation. Thus, letting the "Mercator–Emona Merkur" merger go in 2000 seemed the second best solution to the "failing company problem", given the unfeasibility of the first best (absorption of Emona Merkur by some other trade company, preferably smaller than Mercator).

The second example from Slovenia is the conditionally authorised merger of "Luka Koper" and "Intereuropa". This transaction is regarded as the biggest merger in the Slovenian transport industry. Before the transaction, both companies held dominant positions in their own market segments – distribution and logistics, and freight forwarding and shipping, respectively. As an outcome, although the merger was vertical in effect, the market power of the merged entity was to increase. Nevertheless, the transaction was authorised because the strengthened position of the new company (which was to provide the whole range of logistic services) would be beneficial for the Slovenian economy – especially with regard to international competition. This conditional authorisation (rather than the prohibition of the merger, which further increases initially high market power) provides evidence that the competition authorities are "future-oriented" in their assessment of the structure of relevant markets and intend to "build up" strong national firms able to compete with foreign companies.

Feature 4:

In the transition economies of CEE, the regulators favour mergers except for the purely anti-competitive ones.

As it is seen from the above considerations, the practice of merger control in the selected transition economies of CEE has created factors that may justify the authorisation of a given merger. Now the fourth claim can be made, namely that the regulators favour mergers except for the purely anti-competitive ones. In all the considered countries, the provisions of the competition law support the approval of a merger if its advantages outweigh disadvantages. It becomes then the task of the regulator to determine and appropriately weigh all the possible effects of a transaction, paying special attention to market structure and entry barriers, available choices for suppliers and customers, contribution to technological progress and international competitiveness. Quite importantly, in the appraisal of a given merger, the competition law prescribes to assess not only the current structure of the relevant market and the strength of competition, but also the "prospective effects" of the transaction (Article 30 (1) of the Hungarian Competition Act of 1996). Even a large merger is likely to be authorised if it allows the consumers to enjoy the benefits of increased efficiency – in terms of lower prices, for instance (Article 14 of the Romanian Competition Law of 1996).

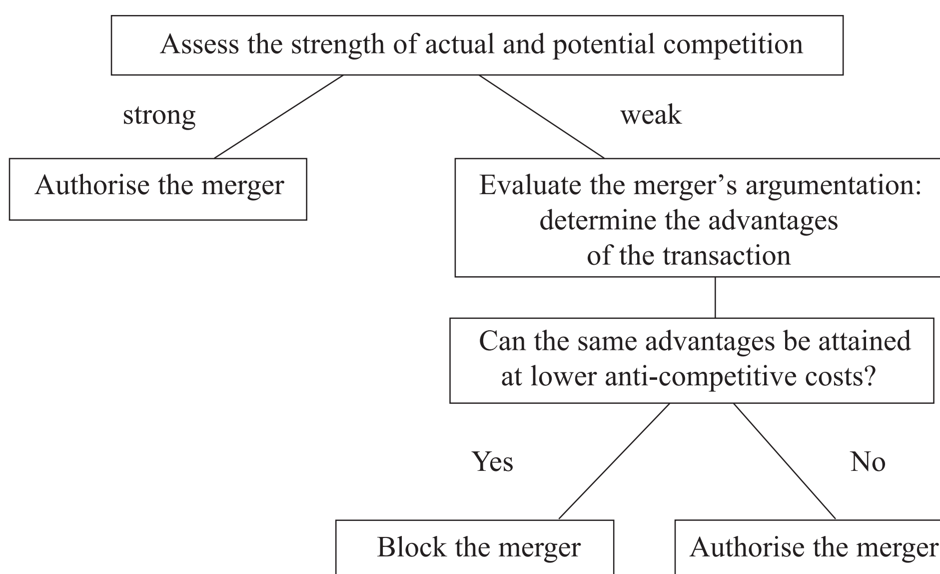
The above cases suggest that a merger must possess clear anti-competitive features if it is blocked. A typical example coming from Romania is a blocked merger, which would have resulted in a 48% concentration of the Romanian market of chemical fertilisers in 1997 (Domokos and Micu 2001). The main reason for blocking was the danger of abusing the increased market dominance. In the evaluation phase it was found that the merger's initiator had not respected the investment plans following its previous transactions – specifically, it increased output price shortly after the earlier acquisitions. Additionally, the documentation presented for the merger did not show significant production efficiencies or other positive effects sufficient to offset the negative impact of increasing concentration.

Two out of three blocked mergers in Hungary represent the failed attempts of the Hungarian telecommunication giant "MATÁV" to strengthen its dominant position in the telecommunications market. First, "MATÁV" wanted to gain control over "JÁSZ-TEL Telecommunications Development and Service Company", a local operator of public wired phone service. Second, "MATÁV" intended to acquire the local cable television network of the town Tata in Hungary. The transactions were justified by "MATÁV" as improving the quality of the services provided by "JÁSZ-TEL" and allowing for technological modernisation of the cable

television network in Tata. However, the competition authorities regarded these advantages as being local in nature, whereas the disadvantages of the strengthened dominant position of "MATÁV" in Hungary – in view of the coming liberalisation of the telecommunications market after 2001 – was considered to affect the whole country. Consequently, both mergers were blocked.

These two cases provide additional support to the claim that the authorities take into account not only the immediate impacts of a given transaction on competition, but also the likely *future* consequences, so a "forward-looking approach" can be observed in merger control. "JÁSZ-TEL" was finally acquired by two other telecommunication companies – "Magyar Telecom" and "Telholding". The conclusion is that the competition authorities tried to achieve the same positive outcomes (production efficiencies in this case) at the lowest possible anti-competitive costs.

It is now possible to formulate the *general approach* taken by the competition authorities of the considered transition economies as far as merger regulation is concerned (see the *Figure* below).[5] At the initial stage, the strength of actual and



General approach to mergers by the competition authorities of the transition economies of CEE

[5] This sequence of steps is assumed to prevail in a broader selection of CEE countries, although additional data would provide more support for this simple decision-making process.

potential competition is assessed. If competition is found to be weak or insufficient, the supporting argumentation for the merger is closely evaluated to determine the principal advantages of the transaction. Subsequently, a question of whether the same positive effects can be attained at lower anti-competitive costs is posed. Only an affirmative answer to this question makes the merger to be blocked (given insufficient competition on the relevant market). This approach serves as evidence of a generally positive view on mergers expressed by the competition authorities in the transition economies studied.

CONCLUSIONS

Based on empirical evidence, this paper highlighted the principal features of merger regulation in Hungary, Romania and Slovenia. It demonstrated the flexibility of merger control in these countries, its orientation towards the future of domestic markets and the close link with industrial policy. The features identified by this study appeared to be robust enough to the different specifications of merger legislation adopted in the considered countries. This fact allows for certain extensions of the obtained results for a broader selection of the transition economies of CEE.

The generalisation of the findings allows the areas of interdependence between transition and competition policy to be highlighted. As it was demonstrated, transition makes competition policy more flexible and forward-looking, and in this respect more cautious. A substantial degree of flexibility of competition policy originates from the fact that the competition authorities are currently still lacking the relevant experience of dealing with mergers; such economic transformations were not common under central planning. At the same time, the authorities can use the regulatory mechanisms adopted for mergers by more developed countries to a rather limited extent, acknowledging that economic conditions of transition might cause quite different and unpredictable results. In such circumstances, the competition authorities do not have "template" solutions; they deal with each case individually, paving the road for transition-specific approaches.

However, the cautious attitude towards mergers generally expressed by the regulators in the considered transition economies can only partially be explained by the lack of experience. To a larger extent, it originates from the unwillingness to regulate indirectly the new and still fragile competitive forces. It seems that the competition authorities are more cautious not to erroneously block a potentially beneficial merger than to authorise a merger, which could turn out to be anti-competitive. Such concerns complement the forward-looking policies of regulators: by not punishing the concentration of small- and medium-size enterprises,

they decrease the scope of future interventions in market processes. In this sense, transitional competition policy remains more "creative" than that operating in mature markets, even in later stages of transition.

As it was also shown, another justification for the "permissive" approach towards economic concentration arises from the necessity of competition policy to operate as a part of the "transition policy package". Opening of the markets suggested that competition policy should support not only domestic competition but also – and primarily – international competition. Consequently, certain protectionism and the allowed concentration of some domestic enterprises appeared as a response to the enhanced contestability of domestic markets.

The currently existing time lag between "advanced" and transition economies as far as the developed nature of markets is concerned is not only a disadvantage of the need of hasty restructuring but it is also a very important latecomer's advantage. At present, transition economies can observe the trends and results of merger regulation in developed market economies and omit the lengthy and inefficient regulatory paths. However, one should not overlook the costs of such learning. Advanced economies have certain interests in the still considerably underdeveloped markets of the transition countries, and here we come to the reverse influence, namely to the influence of competition policy on transition.

Competition policy, and merger regulation in particular, determines the speed of transition to a large extent, i.e. how fast domestic enterprises will be able to complete their restructuring and how competitive they will be in the years to come. As a consequence, the strength of national industries depends considerably on merger control and, specifically, on the regulation of cross-border mergers. It can hardly be disputed that foreign capital provides essential financial resources for completing the modernisation of some industries. However, foreign investors are interested in particular activities and geographic regions of the transition economies. As an outcome, the control of the mergers with foreign participation is conceived to largely determine the position of transition economies in the global markets – whether they will be equal and competing producers or just the distribution means or cheaper sources of raw materials. It can be inferred from the results of the study that the transition economies of CEE are concerned with developing their domestic production. Consequently, the competition policy of transition has to meet a dual requirement: to strengthen the position of national producers internationally and not to suppress competition on domestic markets. Thus, the influence of competition policy on the transition process implies a high level of responsibility.

Is merger control actually too flexible in the transition economies of CEE? Although it would be premature to make any extreme judgement, for the time being, the research findings suggest a negative answer to this question. First of

all, as transition proceeds, merger regulation in the CEE countries gets closer to the practices adopted in more developed market economies – both in legislation and practice. As it was shown in this paper, the structure and dynamics of resolutions concluded by the competition authorities of the selected countries from the CEE region are somewhat similar to those in the EU. Given that transitional competition policy retains more creative features than competition policy in mature markets, merger control in transition need not be stricter than that in a more developed market environment. Second, a substantial degree of flexibility in mergers' treatment by the competition authorities might be justified by the strong disciplinary impact of actual and potential competition (in particular, competition of high quality imports). Finally, the "permissive" approach towards the mergers of small- and medium-sized enterprises does not impede but, on the contrary, might strengthen efficient competition in transition markets.

The question of flexibility in transitional competition policy in CEE is still open and calls for further research. One of the suggested research areas is post-merger performance in the markets where a substantial concentration was authorised. Although obtaining reliable data in this field is quite problematic, such a study could determine whether the reliance on market contestability and strong actual competition is justified for the transition economies of CEE. Additionally, the analysis of the practice of merger control in some other transition countries would also be beneficial so as to check the robustness of the obtained results.

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