Fair Trading Commission

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November 23, 2026

Looking into the Future: How Competition Authorities Assess Competitive Effects

When one business seeks regulatory clearance to acquire another, the public may mistakenly believe that competition authorities consider only the size of the businesses involved in the transaction. In practice, a merger review is considerably more nuanced.

An important question considered by competition authorities such as the Fair Trading Commission (FTC), is whether a proposed merger is likely to substantially lessen competition (SLC). Businesses are generally free to grow, invest, expand and pursue legitimate commercial opportunities. The Commission's concern arises where a business transaction is likely to weaken the competitive process in a way that ultimately harms consumers through higher prices, fewer choices, lower quality, reduced service or less innovation.

A merger review is forward looking. Rather than looking only at the market as it exists today, the FTC considers how markets are likely to develop in the future. The key question is what competition is likely to look like if the merger is consummated relative to what the market is likely to look like if the merger is blocked.

Hypothetical Markets (Counterfactual Analysis)

Mergers are reviewed using counterfactual analysis. It involves comparing two hypothetical evolutions of the relevant market(s) likely to be affected by the proposed merger. The first hypothetical market (the 'counterfactual market') is the future **without the merger**. The FTC considers how the businesses would likely have developed if they did not amalgamate their assets. Would either business expand into new geographic areas? Would either business introduce new products or services, invest in technology or capacity, reduce prices or become a stronger

competitive force? These questions are important because the market may change even in the absence of the merger. Businesses continue to invest, innovate, enter markets and respond to competitors.

Determining the future without the merger is often a challenging aspect of a merger review because it requires competition authorities to anticipate events that will never actually be observed if the transaction proceeds. Authorities may consider whether either business would have expanded independently, increased production capacity, entered new customer segments, developed new products or invested in technology. They may also consider whether competition between the businesses would have continued to generate incentives to lower prices, improve services and innovate.

Another important issue is whether one of the businesss would have remained in the market without the merger. If a business is genuinely failing and would likely have exited regardless of the transaction, the merger may not be responsible for the loss of its competitive presence. However, such claims require evidence demonstrating that exit was genuinely likely and that there were no realistic, less anti-competitive alternatives, such as acquisition by another purchaser. Authorities also consider whether new competitors could enter or existing competitors could expand sufficiently to replace the competitive pressure lost through the merger. The mere possibility of entry is not enough. Entry must be likely, timely and sufficient to constrain the merged business before consumers are harmed. In Jamaica, this can be particularly important because factors such as the size of the domestic market, capital requirements, access to distribution, regulation, land availability and logistics can create significant barriers to entry in some markets.

The second hypothetical market (the ‘factual market’) is the evolution **with the merger**. The two previously independent businesses become a single economic entity and make unified strategic decisions. The FTC considers whether the combined business would have a greater incentive or opportunity to exercise market power relative to the counterfactual market. For example, could it increase prices because consumers have fewer alternatives? Could service or quality decline? Could investment or innovation slow because an important rival has disappeared? The answer to whether competition is substantially lessened lies in the difference between these two futures.

Consider a market in which four supermarket chains compete. Suppose the largest chain proposes to acquire its closest rival. The current market share distribution might suggest that the transaction would simply create a larger supermarket chain. However, the more important question is what competition would have looked like without the acquisition. Suppose the target supermarket was planning to open additional stores, expand online grocery delivery and introduce more competitive pricing. If those plans were likely to materialise, the business could have become an increasingly important competitive force.

If the acquisition takes place, however, the two businesses are no longer rivals. Price competition between them disappears and their incentives for further expansion and investment may diminish. Consumers may lose an important alternative and the merged business may face less incentive to maintain competitive prices, improve service and innovate. The harm therefore does not arise simply because one business becomes larger. It arises because the merger would have removed the competitive rivalry that would have materialised in the future.

How Can a Merger Weaken Competition?

The FTC considers several possible ways in which a transaction could substantially lessen competition.

Unilateral Effects: A merger may allow the combined business to independently raise prices, reduce quality, limit choice or reduce innovation because the merger removed a competitive constraint. This is particularly relevant when the merging businesses are close competitors. If consumers regularly compare their prices and switch between them, the merging businesss constrain each other's behaviour. Once they merge, that constraint is removed, potentially increasing the combined business's incentive to increase prices or reduce competitive effort. Importantly, this does not require the combined business to become the largest business in the market. What matters is whether the transaction removes a meaningful competitive constraint.

Coordinated Effects: A merger can also change the incentives of businesss that remain in the market. Where fewer competitors remain, businesss may find it easier to recognise and respond to each other's pricing and business strategies. Competition could consequently become

less aggressive even without an explicit agreement between competitors. The FTC may therefore consider whether a transaction would make it easier for remaining businesss to avoid competing.

Vertical Effects and Foreclosure: Not all mergers involve direct competitors. A vertical merger occurs when businesses operating at different stages of the supply chain combine. For example, when a manufacturer acquires a distributor or a supplier acquires a retailer. The FTC may consider whether the combined business could restrict competitors' access to important inputs, distribution networks, customers or other essential facilities. Such conduct is commonly described as foreclosure. A manufacturer that acquires a key distributor, for instance, could potentially make it more difficult or expensive for rival manufacturers to reach consumers. Thus, a merger can weaken competition even where the merger does not involve competing business.

Potential and Emerging Competition

Competition is not limited to businesss that are already strong competitors. Recent entrants, for example, may have the technology, investment plans, business model or other capabilities necessary to become a significant competitor in the future. A merger that removes such a potential competitor may prevent competition from developing in the future. This is particularly relevant in rapidly changing industries, including digital markets, where a relatively small business today may become a significant competitive threat tomorrow. Competition authorities may also consider whether a transaction would strengthen or entrench an already powerful position or make it more difficult for new competitors to enter or existing competitors to expand. Competitive harm can therefore arise even where an immediate effect on prices is not manifest.

Why Market Share Alone Is Not Enough

Market concentration remains an important part of merger analysis. Measures such as the Herfindahl-Hirschman Index (HHI) can help assess how concentrated a market is and how a transaction would change that concentration. However, market concentration is not a conclusive indicator of substantial lessening of competition. A highly concentrated market may still be competitive if customers can readily switch suppliers or new businesses can enter quickly. Conversely, a merger involving businesss with relatively modest market shares may raise concerns if the parties are close competitors or if one represents an emerging competitive threat.

Competition authorities may therefore examine a wide range of evidence, including pricing behaviour, customer preferences, bidding information, business strategies, financial information, investment plans and internal documents. The merging businesss' own documents can be particularly informative because they may reveal which businesses they consider to be their closest rivals and how they expect the transaction to affect their strategies. The identity and nature of competition can matter just as much as the number of businesss in a market.

Entry Barriers, Efficiencies and Public Benefits

The possibility of new entry is an important constraint on market power. If the combined business attempted to raise prices, new competitors could potentially enter and steal customers. However, this depends on whether entry is actually credible. Competition authorities may therefore consider capital requirements, access to essential infrastructure, regulatory approvals, distribution arrangements, technology, customer relationships, brand loyalty and other factors that could make entry difficult. If entry is likely, timely and sufficient to replace lost competition, concerns about a merger may be reduced otherwise the competitive constraint removed by the merger may be much harder to replace.

Mergers can produce genuine economic benefits, including economies of scale, improved logistics, increased investment, technological development, expanded production and greater research and development. However, claimed efficiencies must be supported by credible evidence. Simply stating that a merger will create "synergies" or lower costs is insufficient. The benefits should be identifiable, verifiable and sufficiently significant, and where relevant, consideration should be given to whether they are likely to benefit consumers. The fundamental question is therefore whether the transaction is likely to create a substantial difference between the future with the merger and the realistic future without it, and whether credible entry, efficiencies or other public benefits can address any resulting competitive harm.

Why the Analysis Matters for Jamaica

The counterfactual analysis is particularly relevant to Jamaica because many local markets operate within the constraints of a relatively small economy. Some sectors may naturally have relatively few businesses because substantial capital investment is required, infrastructure is costly, economies of scale are important or regulatory requirements limit entry. In such

circumstances, losing even one significant competitor can have a meaningful effect on competition. At the same time, Jamaican businesses need to be able to grow, invest, achieve economies of scale, adopt new technology, expand regionally and respond to financial difficulties.

The SLC framework therefore seeks to strike an important balance. Its purpose is to distinguish transactions that generate legitimate economic and public benefits from those that significantly weaken competition.

Conclusion

At its core, the substantial lessening of competition test is an exercise in comparing two hypothetical evolution of the relevant markets(s); one in which the challenged conduct takes place and the future in which it does not. In reviewing proposed mergers the FTC asks whether the proposed merger would increase the combined business's ability or incentive to raise prices or reduce quality, make coordination easier, restrict competitors' access to important inputs or distribution channels or eliminate a potential future competitor. It also considers whether competitors could enter or expand quickly enough to replace the competition constraints removed by the merger and whether the transaction would generate genuine efficiencies or public benefits capable of offsetting any likely harm. This forward-looking, evidence-based and economically grounded approach helps ensure that legitimate business growth can occur while preserving the competitive process that benefits consumers and businesses.

Sources and Further Reading

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