# UPP-analysis, the Swedish Experience

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# Outline

» UPP in short
  - The basic UPP index
  - Common misconceptions
  - UPP a step in the right direction
  - When to UPP and when not to

» Application of UPP
  - Akademibokhandeln/Bokia (2012)

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# UPP and GUPPI

$$GUPPI_A = \frac{p_B - c_B}{p_A} d_{AB} = m_B * d_{AB} * \left(\frac{p_B}{p_A}\right)$$

- *GUPPI is the value (profit) of diverted (recaptured) sales in product B in proportion to the lost revenue in product A, assuming no efficiencies*

$$UPP_A = GUPPI_A - eff = m_B * d_{AB} * \left(\frac{p_B}{p_A}\right) - e_A$$

- *UPP factors in the downward pricing pressure of a change in product A's marginal costs (as a percentage of price $e_A = \Delta c / p_A$)*

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# Common misconceptions

» (G)UPP(I) does NOT measure price increases
  - (G)UPP(I) is a ratio of profit over revenue (potentially corrected for changes in marginal costs)

» Does NOT depend on simplistic assumptions
  - The ONLY assumption is that of profit maximizing behavior

» (G)UPP(I) is NOT a SSNIP test
  - But can potentially be applied as one if one knows what he or she is doing and makes some more assumptions

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# Common misconceptions II

» (G)UPP(I) is NOT just a screening test
  - The better estimates of its components one has the more one can trust it

» No need for a default efficiency credit
  - No reason why one should assume efficiencies and no default one-size-fits all value can exist (case by case analysis necessary)

» Assuming linear demand one can go further and estimate expected price increases
  - Proving that demand is indeed linear is near impossible within the constraints of a merger review process
  - However, linear demand assumptions are EXTREMELY standard!

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# UPP a step in the right direction

» Focuses the analysis on what matters most:
- Closeness of competition (diversion ratios)
- Market power (profit margins) or in other words, elasticity of demand

» The parts more important than the whole
- The better estimates of diversion ratios and profit margins one can attain the more one should trust UPP results
- However, one can also build the competitive assessment on just closeness of competition and market power arguments

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# When to UPP and when not to

» Do UPP!
- Differentiated products market
- Consumer goods especially
- Good estimates of diversion ratios can be acquired

» Think twice before UPP-ing
- Homogeneous goods markets
- Procurement/bidding/auction markets
- Markets concentrated both on the seller and buyer side (bargaining models)
- Difficult to acquire good estimates of diversion ratios

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# UPP-analysis in concentrations

|  | Prel. product market | Result |
|---|---|---|
| **Arla/Gefleortens (2017)** | Dairy products | Cleared |
| **Visma/Fortnox (2016)** | Business system for SME | Application to the court |
| **Kronfågel/Lagerbergs (2016)** | Poultry products | Application, withdrawn by the parties |
| **Orkla/Cederroth (2015)** | Diet products | Application, commitment from the parties |
| **Arla/Falbygdens (2014)** | Production of cheese | Cleared |
| **Komplett/Webbhallen (2013)** | Retail of computer components | Cleared after phase 1 |
| **Akademibokhandeln/Bokia (2012)** | Retail of books | Cleared |

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# Application > data

» Diversion ratio
- Internal document (market survey, win-loss analysis, strategic document)
- Sales data (e.g. scanner data)
- Customer/consumer surveys

» Margins
- Parties cost data

» Ev. efficiency gains

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# Measuring diversion ratio

» Diversion ratio measured through

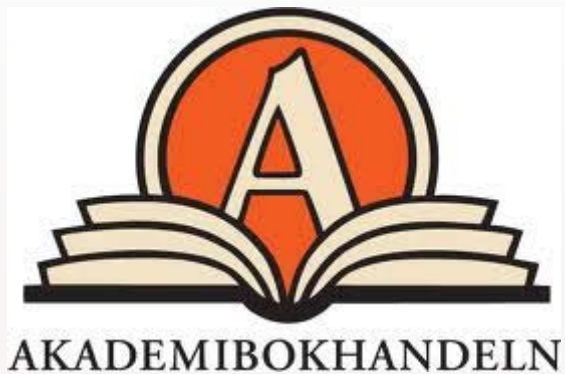- a price increase question:

  *If price of product x increases by 10%, what would you do?*

- a second choice (closure) question:

  *If the product x were not available, what would you do?*

» Choice of sample: online, telephone, face-to-face

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# Akademibokhandeln/Bokia (2012)

# Customer surveys

» Would third competition mainly from online bookstores and grocery stores be sufficient to discipline the merged entity?

» Two face-to-face interviews
- Phase 1: Gothenburg, Umeå
- Phase 2: Helsingborg, Växjö, Linköping, Malmö

» Telephone interview done by the merging parties

» Second-choice question

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# Results

» The SCA cleared the merger between Akademibokhandeln and Bokia.
- Centralised price setting
- Limited geographical overlapps
- Other factors

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# What we have learned

» The UPP-method is a useful method, when it is impossible or improper to apply the traditional approach or full merger simulation.

» UPP is a static analysis. Other factors need to be considered

» UPP is consequently a useful complement to market definition, (but not a substitute).

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