Questions for the Record: The American Airlines / US Airways Merger

For Dr. Moss from Senator Blumenthal

Fares

As the witnesses noted, the overlap in exact routes is not large, but competition for direct flights between several major cities would decrease in the wake of the merger.

Mr Horton noted in the hearing, "…airlines are a network business, as you know. So even where we don't have a direct overlap, of course we're competing via connections over hubs."

Mr Parker similarly noted, "We absolutely are competitors today. We compete vigorously against each other. But we have two route networks that independently aren't as capable of competing against the larger carriers as we will be together. So I think by putting us together we create a stronger competitor to the rest of the industry."

After this merger four major airlines would control 70 percent of the US market.

> **Dr Moss, can you please report what AAI has found with regard to the city-pairs that will be most impacted by this merger? What has your analysis of price comparisons of high and low fares on the top routes found? Can low-cost carriers provide the necessary competitive discipline to keep prices in check?**

Based on AAI's analysis of publicly available data, there appear to be just over 20 routes that are potentially the most affected by the proposed merger of US Airways and American, i.e., where the merger would eliminate one of the merging carriers and result in a substantial loss of competition. These routes involve US Airways and American hubs or focus city airports, including: Charlotte (CLT), Miami (MIA), Los Angles (LAX), Philadelphia (PHL), Phoenix (PHX), Dallas-Ft. Worth (DFW), Chicago O'Hare (ORD), and Washington Reagan National (DCA), and New York La Guardia (LGA). In all cases (summarized in the table below), changes in market concentration and post-merger concentration exceed the thresholds specified in the Department of Justice/Federal Trade Commission HORIZONTAL MERGER GUIDELINES and would be presumed to lead to adverse competitive effects, including increases in fares, reduction in service, and loss of choice.

Post-Merger HHI	Pre- to Post-Merger Change in HHI			
	500-1,999	**2,000-2,999**	**3,000-3,999**	**4,000-4,999**
3,000 - 3,999	PHX-LAX, LAX-PHX			
4,000 - 4,999	DCA-ORF			
5,000 - 5,999				
6,000 - 6,999		PHX-ORD, ORD-PHX PHL-ORD, ORD-PHL		
7,000 -7,999				
8,000 - 8,999	LGA-CLT, CLT-LGA	CLT-ORD, ORD-CLT		
9,000 - 9,999		CLT-MIA	MIA-CLT	PHL-MIA, MIA-PHL, PHL-DFW, DCA-BNA, DFW-PHL
10,000				CLT-DFW, PHX-DFW, DFW-CLT, DFW-PHX

AAI also looked at routes on which US Airways and American are the high fare and low fare carriers on top airport-pair routes. It is important to note that the high/low fare data does not show rivals (or their fares) on top routes that are not the high fare or low fare carrier. Nonetheless, the data reveal potentially useful observations. Of the total number of top routes reported, about 40 percent involve US Airways and American as high and/or low fare carriers. On 44 percent of routes involving the merging carriers, either American is *both* the high fare and low fare carrier or US Airways is *both* the high fare and low fare carrier. On these routes there is therefore no difference between the high and low fares. The pricing data also indicate that the merging carriers are infrequently in situations where they aggressively undercut each other. For example, American is high fare on only 2 percent of routes when US Airways is low fare and US Airways is high fare on 10 percent of routes when American is low fare.

These comparisons reinforce the observation that American and US Airways are dominant players in the industry. The fact that each carrier offers both the high and low fare on a sizable proportion of routes might reflect limited competition on those routes and thus the ability of each carrier to set prices. Given this pattern of high pricing, reinforced by evidence that the airlines rarely undercut each other, we could expect that on routes where the merging carriers *do* compete, they are more likely to be each other's biggest rivals. This lends support to the possibility that a price increase by one carrier could divert substantial sales to the merging partner, creating upward pricing pressure and increasing the probability of post-merger price increases.

Finally, the proposed merger would occur against an industry backdrop marked by a dwindling fringe of low-cost carriers (LCCs) and growing questions as to whether legacy look-alike Southwest Airlines-AirTran Airways exerts any significant competitive discipline in the industry. The merger could hasten the metamorphosis of the domestic airline industry from one in which hub airports were designed to accommodate multiple, competing airlines to a few large, closed systems that are virtually impermeable to competition and create a hostile environment in which LCCs and regional airlines have difficulty thriving and expanding.

Increasingly concentrated hubs resulting from previous legacy mergers have enhanced barriers to LCC entry. In concentrated oligopoly markets, small fringe competitors such as LCCs and regional carriers are also less likely to effectively discipline the pricing of the resulting four powerful systems, *or* they may

walk away from the opportunity to gain market share by going along with the higher prices that often accompany diminished competition. Based on our analysis of routes affected by the Delta-Northwest and United-Continental mergers, LCCs may have a limited ability to induce price discipline among the legacy carriers that serve hub-to-hub routes. LCCs do not factor prominently on routes that could be adversely affected by a US Airways-American merger. Collectively, these factors make LCCs increasingly unreliable as a source of competitive discipline in the industry and in assuaging the concerns over adverse effects that could result from the proposed merger.

[Note: Many of the answers provided here are based on analysis contained in the AAI White Paper by Diana L. Moss and Kevin Mitchell, "The Proposed Merger of US Airways and American Airlines," (August 8, 2012), available http://www.antitrustinstitute.org/%7Eantitrust/sites/default/files/AAI_BTC_USAir-AA_White%20Paper_8-7.pdf]