Follow-up Questions of Senator Klobuchar
Subcommittee on Antitrust Hearing on
"The American Airlines/US Airways Merger: Consolidation, Competition, and Consumers"

For Dr. Diana Moss

1. According to a USA Today report on February 22, 2013, there were seven major price increases in 2012. More recently, only five days after American and US Air announced their proposed merger, Delta announced price increases which were immediately followed by American, US Air and United; and a day later by Southwest. The new price increases, $4 to $10 for tickets purchased within seven days of domestic travel, mostly apply to tickets popular with busy business travelers. Will increased consolidation make it easier for airlines to tacitly coordinate price increases like that?

The AAI believes that consolidation in the airline industry could increase the possibility of anticompetitive coordination, both at the national level and in airport-pair or city-pair markets where the two carriers compete. Should the proposed merger between US Airways and American be approved, the reduction in competition would result in the "Big 4" carriers (US Airways-American, United, Delta, and Southwest) nationally. At the route-specific level where the merger would significantly increase concentration, shares on US Airways-American overlap routes are concentrated largely among a few legacy carriers. A number of factors could facilitate explicit or tacit collusion at the national and route-specific levels, including high levels of price transparency, relatively homogeneous products within fare classes, and visible cost structures. With fewer national competitors, rivals would likely find it easier to signal each other and come to tacit agreement on fares or other key variables such as capacity cutbacks, which would keep fares higher than under more competitive market conditions. The same would be true at the route level. Moreover, LCCs face the key decision in increasingly concentrated markets of whether to price aggressively or to follow the pricing and capacity strategies of the dominant legacy carriers at the hub. LCCs can price their services barely below the oligopoly "umbrella," without providing the type of sharp maverick's spur needed to discipline coordinated behavior.

At the hearing, Mr. Parker said that barriers to entry into the airline industry are low, but that entrepreneurs weren't entering the market because it is so fiercely competitive. What's your response? How would the DOJ interpret that in its antitrust analysis?

The AAI believes that in regard to the proposed merger, the relevant point is not whether a potential entrant can secure financial capital and physical capital (e.g., aircraft) to engage in "greenfield" (i.e., new) entry. Rather the relevant consideration is whether existing participants in the industry find it more difficult with higher concentration and hub dominance to access the inputs (e.g., hubs, slots, gates, etc.) needed to enter and compete on airport-pair or city-pair routes that are adversely affected by the US Airways-American merger.

2. Do you believe that the DOJ should look beyond simply overlapping non-stop routes as part of their antitrust analysis?

Yes. The AAI believes that a broader view is as important at the route-specific analysis typically performed by the DOJ, for a variety of reasons. First, the merger would combine the fourth (American) and fifth (US Airways) largest airlines nationally, making US Airways-American the largest U.S. carrier with a combined share of over 20 percent, followed by Southwest with 18 percent, United Continental with 17 percent, and Delta with 16 percent. The Big 4 would therefore control over 70 percent of the national market. The dwindling stock of LCCs after maverick AirTran was eliminated by Southwest consists of JetBlue, Frontier, and Spirit Airlines. With fewer competitors with national footprints, anticompetitive coordination is easier and more likely. Rivals would likely find it easier to signal each other and come to tacit agreement on key variables such as capacity cutbacks, which would keep fares higher than under more competitive market conditions. Second, the merger would facilitate the metamorphosis of an industry in which hubs were designed to be open access facilities at which multiple, competing airlines provided service, to only a few mammoth, closed systems that are virtually impermeable to competition and provide a hostile environment in which LCCs and regional airlines have difficulty thriving and expanding.

Third, the network configuration of a merged US Airways-American has important implications for control over both connecting service and intra-regional service in the U.S. The networks of US Airways and American do not appear to be particularly complementary. There is relatively little "white space" in each network footprint that could be filled by the other carrier. Instead, combining the two networks could create regional and functional strongholds throughout the U.S. For example, the merged carrier would have a strong presence at a number of major airports on the eastern seaboard –Philadelphia (PHL), Reagan National (DCA), Charlotte (CLT), and Miami (MIA). The merging carriers would also have a presence at key Midwestern and western airports – Phoenix (PHX), Dallas Fort-Worth (DFW) and Chicago O'Hare (ORD) – that are important for providing connecting service to eastern and western destinations. Indeed, there is a resemblance to the United-US Airways merger of 2001, which was challenged by the DOJ on the basis of "solidifying control" over hubs.

Fourth, many mid-size communities have seen flight frequencies reduced, equipment downgraded or service lost altogether. Scores of airports are expected to lose scheduled service in the immediate years ahead as well as attendant local and regional economic benefits that flow from connectivity to the world's important business centers. Evidence from the Delta-Northwest and United-Continental mergers indicates that merged carriers have adjusted capacities on overlap routes where they are dominant to drive more traffic to large hubs, with the possible side effect of starving routes involving smaller cities. Similar fact patterns across these mergers and US Airways-American raises the possibility that smaller communities could be harmed by the proposed merger. Loss of consumer choice that forces consumers to use less convenient connecting service or travel longer distances to other airports represent legally cognizable adverse effects of a 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]