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Assessing the Reality of Killer Acquisitions in Digital Platform Market

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Digital platforms have played a crucial role in fostering a platform economy. Today, we cannot imagine a world without Google's search engine. It helps us to navigate and gather diverse information related to our specific interests, from travel to academic research. We can also learn about other people's life style and exchange messages via Instagram or Facebook Messenger. We can purchase commercial goods and use cloud services through Amazon Marketplace and Amazon Web Service (AWS). There are so many functions of digital platforms that we rely on heavily in our daily lives.

Our high dependence on these digital platforms makes us think about the right level of regulation for them. If we focus on their positive role in making our lives more convenient, the government needs to remove unnecessary regulations for the platforms in order to induce more innovation achieved by them. The market for digital platforms, however, can become more concentrated if the level of regulation is reduced. Furthermore, the situation will be exacerbated when big tech companies such as GAFAM (Google, Apple, Facebook (now Meta), Amazon, and Microsoft), among others, acquire relatively small innovative firms for the purpose of eliminating their potential competitors, known as a ‘killer acquisition’. The U.S. competition authorities and Congress have paid attention to this type of acquisitions because of its negative impacts on competition in the U.S. digital platform market. Accordingly, the U.S. Federal Trade Commission (FTC) and the U.S. Department of Justice (DOJ), two representative competition authorities in the U.S., reviewed GAFA’s mergers and acquisitions (M&As) over the past 20 years to investigate whether these deals had any negative impact on market competition. Moreover, on June 14, 2021, the U.S. House of Representatives introduced a package of bills related to the regulation of major U.S. big tech companies, known as “A Stronger Online Economy: Opportunity, Innovation, Choice”.

Øverby and Audestad (2021) explain the main motivations of digital platforms. First, it strengthens internal growth strategies by accessing the core assets of the acquired company: technology, processes, practices, and intellectual property rights. Digital platforms are primarily based on information and communication technology (ICT), including artificial intelligence (AI), and high-tech manufacturing, and they need to constantly develop new products and services. The main interest of digital platforms is to develop the company's core technology, and the acquisition of startups is sometimes seen as a means to replace internal R&D. By acquiring promising startups, R&D projects can secure adequate funding in a shorter time, and gain the advantage of being a market leader. For this reason, GAFAM have strengthened their existing businesses by acquiring startups in high-tech industries. A representative example is Apple's acquisition of Beats Electronics for $3 billion in 2014.

Second, digital platforms choose M&A as means to expand their market by acquiring new products, services, and distribution channel networks as an external growth strategy. Digital platform companies seek to secure new, untapped markets, including competitors’ consumers, in order to expand their networks. The successful completion of an acquisition creates powerful network ripple effects resulting from positive market feedback. As a result, the acquiring company grows organically through a merger by increasing its market power and reducing the market share of remaining competitors. Representative examples of such network strengthening and market expansion include Microsoft's acquisition of LinkedIn ($26 billion) in 2016 and Amazon's acquisition of Whole Foods Market ($13.7 billion) in 2017.

Antitrust regulators and governments have recently paid more attention to the ever-increasing market power of digital platforms in an effort to better understand how digital markets work and promote competition. As a result, the need to regulate many corporate activities, including 'killer acquisitions' by large digital platforms, is being raised, and the direction that regulation takes will have a significant impact on the business strategies of digital platforms and the performance of the platform economy in the future. Some policy papers have expressed concern about the potential for mergers in the digital industry to become killer acquisitions aimed at potential competitors (ACCC 2019;

Crémer et al. 2019; HM Treasury 2019; Morton et al. 2019). Economists also point out that regulators are too lenient on acquisitions of small and medium-sized innovative startups by established companies, and emphasize that the practice of easily allowing them should be reconsidered. This suggests that competition authorities should take a selective approach, allowing startup acquisitions only in markets where the impact of the innovation resulting from the acquisition outweighs the benefits of preserving potential competition.

To sum up, it should be noted that the digital platform industry has the characteristics of a multi-sided market that creates indirect network effects. Horizontal mergers in the digital platform market can significantly change not only the price level but also the price structure because they can lower prices on one or more sides of the market even if there is no improvement in cost efficiency. It is generally characterized by no or low prices on the user side. Because most of GAFAM's M&A transactions do not begin to monetize only until after a large user base has been acquired, they are not challenged by the revenue criteria traditionally used by antitrust authorities in merger investigations. Therefore, restrictions under the merger control procedure have not been applied to mergers such as Google' acquisition of YouTube, Waze, Doubleclick, or Facebook's acquisition of WhatsApp, Instagram, or Microsoft's acquisition of GitHub, Linkedin. In this regard, Affeldt and Kesler (2021) and Motta and Tarantino (2021) argue that since competition in digital industries is often non-price competition for products and services, such as service quality, data collection, and innovation, merger regulation enforcement is important for these special needs. Therefore, in order to regulate corporate behavior, such as killer acquisitions, that restricts competition in the digital platform market, it is necessary to use innovation performance indicators such as patents. Furthermore, a change in mindset is needed in which the digital platform directly bears the burden of proving restraints of competition, rather than the antitrust authorities.

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