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An Economic Analysis of the Ryanair/Aer Lingus Merger Case

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List of Abbreviations

EEA European Economic Area
EUMR European Union Merger Regulation
HHI Herfindahl-Hirschman-Index
IAG International Consolidated Airline Group
LCCs Low Cost Carriers
O&D - Approach Origin & Destination - Approach
R&D Research & Development
1 Introduction

In the last thirty years, the European aviation market has undergone significant changes which have considerably reshaped the industry. The key drivers for this development were deregulation and liberalisation which took place in the aviation market in the 1990s. These processes have encouraged the foundation and the successful entry of low cost carriers (henceforth LCCs) which have taken advantage of the new market conditions. As a result of the numerous entries of LCCs and a resulting increased competition intensity, incumbent airlines have been challenged and placed under pressure to adapt their business strategies to the new competitive environment and to develop innovative strategies (Gilroy et al., 2005, p. 203ff). Mergers have therefore become an increasingly attractive possibility to expand route networks and to achieve synergies and efficiencies while reducing the cost base. Such a transaction would thus enable the merged airline to respond to changes in customer demand and/ or economic environment more quickly (Iatrou and Oretti, 2007, p. 21).

Since 2004, 15 mergers in the airline industry have been subject to regulatory clearance under the EU Merger Regulation Guidelines (henceforth EUMR) by the European Commission (European Commission, 2013a. On 27 June 2007, the Commission prohibited the merger between Ryanair and Aer Lingus (European Commission v Ryanair/ Aer Lingus, 2007, p. 16, 345). This case was the first decision to deal with a transaction that should have taken place between two point-to-point, low frills carriers and the first attempt of a low cost carrier, here Ryanair, to acquire a former national carrier, here Aer Lingus (O'Connell and Williams, 2011, p. 123). The Commission’s 2007 Ryanair/ Aer Lingus decision can therefore be considered an important judgement which will influence future decisions regarding mergers between LCCs since the EU Courts and the European Commission make their decisions based on case law (Whish & Bailey, 2012, p. 18). The aim of this thesis is to analyse the Ryanair/ Aer Lingus merger case using the EUMR approach and to focus especially on the economic approaches used by the Commission in its 2007 decision to clear a merger between two LCCs.

This thesis is organised as follows. In chapter two, the principles of mergers will be introduced which comprises the economic theory on mergers (section 2.1) on the one hand and the EUMR for horizontal mergers (section 2.2) on the other. Thereafter, in chapter three, the European airline industry will be analysed by taking a closer look at the different airline types (section 3.1) and the market situation (section 3.2). Moreover, emphasis will be laid on the role of LCCs in the European aviation market (section 3.3). In chapter four, the Ryanair/ Aer Lingus merger case will be analysed on the basis of the European Commission’s 2007 decision. This analysis includes a brief introduction of the involved parties (section 4.1), the case’s Community
dimension (section 4.2) and the relevant markets (section 4.3) before the competitive assessment follows (section 4.4). In this assessment, market shares and concentration (section 4.4.1), the degree of competition (section 4.4.2), buyer power and the possibility to switch supplier (section 4.4.3) as well as barriers to entry (section 4.4.4) and efficiencies (section 4.4.5) will be considered. At the end of this chapter, the Commission’s decision will be discussed following the General Courts judgment (section 4.5). The last chapter deals with cases that are related to the Commission’s Ryanair/ Aer Lingus decision. This part therefore comprises Ryanair’s second and third attempt to acquire Aer Lingus (section 5.1) and the recent takeover of Aer Lingus by International Consolidated Airline Group (henceforth IAG) (section 5.2). Chapter six concludes.

2 Principles of Mergers

This chapter begins by introducing the economic theory on mergers (section 2.1) which comprises a differentiation between the different merger types and an explanation for the occurrence of mergers. Thereafter, the EUMR for horizontal mergers will be introduced (section 2.2) which will serve as the tool for the analysis of the Ryanair/ Aer Lingus merger case in section four.

2.1 Economic Theory on Mergers

Mergers are an amalgamation between two or more companies who have been independent entities before the transaction (Crede, 2010, p. 287). Mergers can be categorised into horizontal, vertical and conglomerate mergers (ibid, p. 389). In a horizontal merger, the merging entities operate in the same relevant market and can often be referred to as close competitors who are offering the same product or service (ibid, p. 407). An example for a successful horizontal merger is the transaction between Disney and Pixar. Here, both firms have been active in the movie production industry and were considered rivals pre-merger (Barnes, 2008). Subject to vertical mergers are companies who are operating on different stages of an industry’s supply chain and who cannot be considered competitors (Crede, 2010, p. 425). The merger between E.ON and Ruhrgas falls into this merger category. In this case, the roles of the companies before the transaction can be summarized as follows: Ruhrgas was a gas supply company, buying gas directly from producers such as Russia and selling it to bulk buyers such as E.ON. The latter is an energy provider who delivers gas to end consumers (Sinn, 2002, p. 2). In a conglomerate merger, companies who are producing different products or services are merging (Crede, 2010, p. 430). The merger between Procter & Gamble and Gillette is an example for a conglomerate merger. Here,
the transaction combined two large sellers of a wide range of consumer goods (Monti, 2007, p. 294).

Companies decide to merge in order to achieve a certain outcome. This outcome depends on the type of the merger. While vertical mergers can lead to lower transaction costs as they enable the producing company to secure access to either raw materials or distribution channels, conglomerate mergers can achieve cost savings through economies of scope, the reduction of uncertainty and diversification (Lipczyński et al., 2005, p. 258, 596f). A horizontal merger may lead to a cost reduction through rationalisation, economies of scale, research and development (henceforth R&D) or purchasing economies on the one hand and an enhanced market power on the other (ibid, p. 258ff). In more detail, rationalisation allows the merging entities to realise the same level of marginal costs in all production plants by shifting production from high marginal cost to low marginal cost plants. With the effects that are brought about by the economies of scale, an improved operating efficiency can be achieved as the total average costs for producing a single product tend to decrease when the scale of operations increases. When the R&D departments of two former independent entities are combined, further cost savings can be achieved if the newly created unit is able to achieve better and more efficient outcomes than the separated units. Moreover, horizontal mergers lead to improved purchasing economies that are encouraged by an increased bargaining power that allows the merged entity e.g. to extract lower prices from suppliers or to raise funds from capital markets more easily. Since mergers combine the market shares of two former independent companies such a transaction may lead to increased market power, especially if the merger leads to the elimination of a close rival\(^1\) (ibid, p. 259ff).

However, economists argue that the economies of scale advantage achieved through horizontal mergers cannot be considered as an entirely merger-specific gain. They claim that economies of scale can likewise be achieved through internal expansion. Thus, they refer to so-called *synergies* which are gains that can wholly be associated with the merger. These merger-specific gains include the coordination of joint operations, sharing of complementary skills, improved interoperability and network configuration (ibid, p. 260).

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\(^1\) This aspect will be further discussed in section 2.2.
2.2 EU Merger Regulation Guidelines for Horizontal Mergers

In 1989, the European Union introduced a merger regulation based on a system of pre-notification which came into force in 1990 (El-Agraa, 2011, p. 203). Thereafter, the guidelines have been extensively revised and extended until 2004 when the latest amendment came into force (Crede, 2010, p. 269). Based on the EUMR\(^2\) the European Commission scrutinises mergers before the actual transaction takes place. On the contrary, in cases of the abuse of a dominant position or the existence of cartels, the Commission interferes only after the exposure of the infringement (El-Agraa, 2011, p. 203). Since the amendment of the EUMR in 2004, the number of mergers that have been notified to the European Commission increased from 247 in 2004 to 402 in 2007 back to 259 in 2009 which can be associated with the eruption of the financial crisis in 2008 (Whish and Bailey, 2012, p. 811). However, with the recovery of the world economy, merger activity has augmented again to 309 notified mergers in 2011. Thus, it can be assumed that the level of merger activity is subject to economic fluctuation. In total, 5,726 mergers have fallen into the jurisdiction of the Commission since the introduction of the EUMR in 1990 and 3,376 since the 2004 amendment from which 120/ 61 have been withdrawn in phase I and 37/ 16 in phase II (European Commission, 2015a).

\[\text{Figure 1: The EU Merger Control – A Timeline (Ghosal and Stenmek, 2007, p. 314)}\]

*Figure 1* shows the different stages of the EU merger control, starting with the announcement of the merger and its notification to the Commission. Thereafter, the Commission has to decide whether the transaction can be considered to be compatible with the common market (*phase I*) within 25 working days. If the merger cannot be cleared after this stage, the Commission conducts a more in-depth analysis (*phase II*) within 90 working days. Afterwards, it has to be decided whether the merger can be declared to be cleared, whether remedies are necessary in order

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\(^2\) Regulation 139/2004
to approve the transaction or whether the merger brings about serious anti-competitive effects which cannot be outweighed and therefore has to be blocked (Ghosal & Stennek, 2007, p. 314).

The successful implementation of the EUMR empowered the Commission to interfere in planned mergers that could lead to dominance in the market before the actual transaction takes place. This procedure is a more cost and time effective approach considering the resources needed in order to break off a merger that has already created a dominant position. Moreover, an early interference is beneficial for the merging entities since a prohibition of a merger that has already led to dominance after the transaction and the integration process have already taken place, would be of the disadvantage of the merging parties. Furthermore, anti-competitive transactions do not only have an effect on the merging entities but also on the entire market including actual and potential competitors as well as consumers which makes an ex-ante merger control even more essential (Monti, 2007, p. 246).

According to the EUMR, mergers are subject to approval if they have a Community dimension and if they may lead to a concentration that aims to “significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position” (European Commission, 2004). As a transaction must have a Community dimension in order to fall into the jurisdiction of the European Commission, the merging entities have to meet a certain turnover threshold (Harvey et al., 2008, p. 9). The turnover-based threshold is a reliable tool for examining the strength of the merging enterprises (European Commission v Ryanair/ Aer Lingus, 2007, p. 5). Figure 2 outlines the circumstances under which a merger either has or does not have a Community dimension making the EUMR applicable or inapplicable. Transactions that do not have a Community dimension fall into the jurisdiction of the affected member state’s competition authority (Ivaldi & Verboven, 2005, p. 672). Above a certain size, mergers cannot take place without the Commission’s approval (El-Agraa, 2011, p. 203). Moreover, the relevant market has to be identified and defined before the competitive assessment can be conducted. This step is necessary in order to identify the competitive constraints an enterprise faces in its operating market (Whish & Bailey, 2012, p. 27).

In the competitive assessment, market shares and concentration levels are reasonable indicators for measuring dominance in a market. With the aid of these tools a decent insight into the market structure and the competitive importance of the merging parties for the market on the one hand and their competitors on the other can be gained. According to a statement made by the General Court, former Court of First Instance, “market shares of 50 per cent or above may themselves be an indicator for a dominant position” (European Commission v Ryanair/ Aer Lingus, 2007, p. 85).
For the examination of the concentration levels of a market, the Commission uses the Herfindahl-Hirschman-Index (henceforth HHI). The HHI can be calculated by adding up the squared individual market share of each company that is operating in the concerned market. In order to compare the market concentration pre- and post-merger, the Commission furthermore calculates the so-called delta which represents the difference between the pre- and the post-merger HHI. The delta can be derived by firstly multiplying the market shares of the merging entities before multiplying the derived product with the factor two or by simply calculating the subtraction. The calculated HHI can be interpreted as follows: the higher the concentration in a market, the higher the HHI and vice versa. According to the European Commission a merger does not raise anti-competitive concerns if the post-merger HHI is either below 1.000, between 1.000 and 2.000 with a delta below 250 or above 2.000 with a delta below 150 (Crede, 2010, p. 394).

Although the Commission generally takes a positive view of mergers as corporate reorganisation strengthens the EU’s position in the global market and therefore surges the competitiveness of the European Union, there are cases when a merger has to be blocked (Harvey et al., 2008, p. 7). Especially horizontal mergers can raise concerns about their anti-competitive effects as they
combine two former competitors which can therefore easily lead to the creation or the strengthening of a dominant position (Monti, 2007, p. 246). Therefore, mergers will meet with disapproval when they have the potential to create *monopoly power*. Monopoly power can be obtained when the transaction either eliminates the remaining competition or when the combination of two or more enterprises leads to the creation of a high market share. Companies who enjoy monopoly power or a sufficiently high market share tend to increase prices. Therefore, the lack of competition and substitutes imposes a restriction on consumers to switch suppliers (Crede, 2010, p. 408). However, mergers can be approved although concerns about its compatibility with the common market exist. This is the case if the economic benefits resulting from the transaction considerably outweigh the potential costs. Therefore, the merger has to bring about so-called *efficiencies* that will result in higher welfare on the one hand and have the dimension to counteract the anti-competitive effects of the transaction on the other. Nevertheless, efficiency gains can only be achieved if the merger forces the involved parties to rationalise their business activities and therefore leads to more efficient operations and lower unit costs. Consequently, if the efficiency gains outweigh the transaction’s anti-competitive effects, the merged entity is more likely to decrease sales prices instead to increase them. The latter would occur, if the transaction leads to the creation of sustainable market power which cannot be offset by efficiencies. As a consequence, the merger is likely to decrease the overall consumer surplus as well as the total welfare. In these cases, the Commission would not approve the transaction (Motta, 2007, p. 238).

According to the EUMR, the merging entities have to provide evidence that the merger will bring about the crucial efficiency gains (European Commission v Ryanair/ Aer Lingus, 2007, p. 310). Moreover, the efficiencies generated by the merger need to be to the benefit of the consumers in order to counteract the anti-competitive effects the transaction would have otherwise. However, the precondition for efficiency gains to be effectively passed to the consumers is the existence of competitive pressure exerted by the remaining firms in the market on the one hand and potential entrants on the other. It is furthermore unlikely that a merger that leads to increased market power approaching the level of monopoly will create efficiencies that can effectively counteract the adverse effects on competition. In addition, efficiency gains need to be merger-specific and verifiable (European Commission v Ryanair/ Aer Lingus, 2007, p. 310f).

Furthermore, entry must be likely, timely and sufficiently and pose an immediate, actual threat in order to exert a sufficient competitive constraint on any anti-competitive behaviour on the part of the merged entity. According to the General Court, *barriers to entry* can be defined as either economic, commercial or financial features of the market or an established position of the incumbent firms which make it difficult for potential competitors to enter the market. The
deterrence can be associated with the high risks and costs of entrance (ibid, p. 137, 146). These costs are caused by a large number of investments that have to be made in order to win a sufficient number of customers (ibid, p. 149f). Moreover, the uncertainty of whether the entry will be successful brings about a high level of sunk costs that will occur in case of an unsuccessful entry. Sunk costs include marketing and potential start-up costs (ibid, p. 153). In addition, countervailing buyer power exercised by the customers can only exert competitive pressure on the merged entity if it remains effective post-merger and if the transaction does not lead to the elimination of a credible alternative. The customers can utilise their buyer power to off-set the potential negative effects of the merger, if they have the possibility to switch suppliers easily, to integrate into the upstream market on a vertical level or to sponsor upstream expansion (European Commission, 2004, p. 12).

Furthermore, it is possible that the Commission demands the parties to modify the transaction in order to eliminate the anti-competitive risks the merger brings about instead of blocking the transaction immediately. These remedies can either be structural or behavioural. Structural remedies demand the affected enterprises to divest parts of their business units which will lead to a reduction of their combined market share and therefore might encourage another competitor to enter the market. This type of remedy depicts a solution that successfully reduces the anti-competitive risks coming from the merged entity (Monti, 2007, p. 283). Behavioural remedies require the parties to cooperate with their competitors, for example by granting licences of intellectual property rights in order to keep them in the market post-merger (ibid, p. 286).

In summary, once a horizontal merger falls into the jurisdiction of the European Commission, the authority analyses (1) the relevant market, (2) market share and concentration, (3) possible anti-competitive effects which are likely to result when (3.1) the new entity will have a high combined market share, (3.2) the merging entities are each other’s closest competitors, (3.3) customers have no or only limited possibilities to switch suppliers, (3.4) the merged entity does not respond to an price increase with an extension in supply, (3.5) the new entity has the ability to hinder expansion by competitors, (3.6) the merger leads to the elimination of an important competitive force and (3.7) the competitors are able to monitor each other’s behaviour. Moreover, the Commission examines (4) countervailing factors such as (4.1.) possible entry into the market by a new competitor and (4.2.) the consumers’ buyer power and their possibility to switch suppliers (4.3) as well as (5) the pro-competitive benefits of the transaction (Harvey et al., 2008, p. 417).
3 The European Airline Industry

This chapter firstly introduces the existing airline types (section 3.1) before it gives an overview of how the European airline industry has developed over the years and discusses the events that shaped the current market structure (section 3.2) which will give an explanation for the occurrence of LCCs. Accordingly, the role LCCs in the European Union will be discussed further (section 3.3) as their business model is crucial for the analysis of the Ryanair/ Aer Lingus merger case where both airlines are operating this model.

3.1 Airline Types

A large heterogeneous group of airlines is currently serving the European aviation market offering scheduled passenger air transport services. These airlines mainly differ from each other regarding their operating model and the level of service they are offering to their passengers (European Commission v Ryanair/ Aer Lingus, 2007, p. 11f). According to this differentiation, airlines can be categorised in two key groups: network and point-to-point carriers. While network carriers that operate a so-called hub-and-spoke system are mostly former national flag carriers or full-service airlines such as British Airways and Lufthansa, point-to-point networks are mainly adopted by low cost, no-frills airlines such as Ryanair and easyJet. Network carriers are operating from one or more hub airports where they concentrate their traffic at, by directing flights into their network. From these hubs, passengers are dispersed to their destinations. Moreover, these airlines are mostly offering world-wide or at least trans-continental and therefore long-haul services (Burghouwt, 2007, p. 2). Furthermore, full-service airlines provide their customers with a number of complimentary services such as drinks, food, seat reservation, different cabin classes, luggage transport or newspapers (European Commission v Ryanair/ Aer Lingus, 2007, p. 14).

On the contrary, point-to-point carriers are serving routes on either regional, national or European-wide basis which are operated independently from other routes in their network. This airline type operates from a so-called base where it stores a number of aircrafts overnight and concentrates its operations at, by offering several routes from that airport (ibid, p. 93f). This strategy brings about flexibility of assets on the one hand that further encourages economies of scale and scope and provides the carrier with the possibility to spread fixed costs over many routes on the other. Furthermore, the flexibility of a base operation allows airlines that concentrate large operations at one airport to react on changes in demand or in the market place immediately. This leaves them with an advantage over carriers with no base at that airport (ibid, p. 139). Their no-
frills model indicates that these airlines have reduced their level of complimentary services in order to be able to offer cheaper fares. Additionally to the full-service and low frills airline types, an intermediate model, the so called some-fills model, exists, such as operated by Aer Lingus, which combines the features of network carriers with those of point-to-point airlines. Here, the point-to-point carriers offer some complimentary services to distinguish themselves from other airlines in the sector (ibid, p. 13f).

3.2 Market Situation

The European aviation market achieved market liberalisation in 1993 as a cause of progressive deregulation which began with the approval of the first out of three “liberalisation packages” by the European Council of Ministers in 1987. Deregulation brings about greater efficiency, decreasing air fares, higher flight frequency and wider customer choice and therefore aims to make air travel more affordable and available for a broader customer group (Gilroy et al., 2005, p. 204; Iatrou and Oretti, 2007, p. 14, 18). These outcomes have resulted in increased consumer welfare (Burghouwt et al., 2014, p. 42). Moreover, deregulation has not only increased the degree of competition in the European aviation market but has also encouraged low cost airlines to gain a foothold in this market. The deregulation process has allowed airlines to enter any route within the European Community, leaving them with full traffic rights, no limitations on fare zones, multiple designation and no capacity restrictions (Gilroy et al., 2007, p. 203f). In 1997, the last remaining restrictions in terms of cabotage limitations were abolished, making the European airline industry a fully liberalised market (ibid, p. 205).

Furthermore, deregulation has effectively encouraged the privatisation of former state-owned flag carriers such as Lufthansa (1997) and Iberia (2001) (Iatrou and Oretti, 2007, p. 33; lufthansagroup.com). Regarding the success of privatised airlines, other state-owned carriers have followed their example in the course of time. Air France for example was state-owned until 2003 when the airline merged with KLM Royal Dutch Airlines which turned the new created entity Air France KLM into a private enterprise (airfranceklm.com). Another example is Aer Lingus who was turned into a fully privatised company by merging with IAG in 2015 after the Irish government ushered the privatisation process in 2006 (McDonald, 2015). Finally, deregulation and liberalisation can be seen as the drivers for the continuing expansion of the European airline network which grew significantly with 2070 routes existing in 1995 compared to 3254 routes in 2012. 51 per cent of these routes were launched by LCCs compared to 41 per cent that were established by traditional airlines (Dobruszkes, 2013, p. 81f).
3.3 The Role of Low Cost Carriers in the European Union

The deregulation process led to an increased appearance of LCCs in the European aviation market which started with Ryanair’s adaption of the Southwest low cost model\(^3\) in 1995 (Gilroy et al., 2005, p. 209). The same year easyJet, who is currently Ryanair’s closest competitor on the majority of intra-Europe routes, entered the market (Dobruszkes, 2013, p. 75). The German Aerospace Centre (2014) identified 28 LCCs that are currently operating in the European air transportation market (p. 14). Thus, the European low cost market is highly concentrated with Ryanair and easyJet accounting for 64 per cent of all low cost seats (Dobruszkes, 2013, p. 77). Moreover, the present market situation provides a decent insight into how the presence of LCCs has affected the European air transportation industry. Table 1 shows that the market share of low cost carriers on intra-Europe routes has increased between 2005 and 2012. In fact, their market share augmented from 27.8 per cent in 2005 to 56.6 per cent in 2015 compared to the poor development of full-service carriers who faced a gradual decrease from 45.8 per cent in 2005 to 27.8 per cent in 2012 (European Commission, 2013b, p. 3).

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*Table 1: Market Share in % by Carrier Type on Intra-EU Routes (European Commission, 2013b, p.3)*

Moreover, LCCs can be considered more risk-seeking compared to traditional airlines. The former carrier type launched 721 new routes between 2004 and 2012 where they enjoyed a first-mover advantage. Airlines benefit from this first-mover advantage especially in so-called niche markets which are mostly small or thin routes that generate profit only to a certain degree due to limited traffic. This market currently represents 35 per cent of all low cost seats. Moreover, it is more difficult for a competitor to successfully enter a niche market where a first-mover is already operating as the late entrant will face restrictions in terms of profitability (European Commission v Ryanair/ Aer Lingus, 2007, p. 121). This situation explains why LCCs enjoy monopoly power in 61 per cent of all routes in their network. However, 42 per cent of these newly established routes were unsuccessful as a high share of LCCs left the market again shortly after their entrance (Dobruszkes, 2013, p. 82, 86).

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\(^3\) This model will be further described in section 4.1.1.
Nowadays, LCCs who initially targeted non-time sensitive or leisure travellers are even attracting time-sensitive travellers such as business travellers who were considered to be “totally price indifferent”. This development challenges the incumbent traditional airlines who are now in need to adapt to the new market situation in order to stay competitive (Iatrou and Oretti, 2007, p. 18f; Dobruszkes, 2013, p. 77). Time-sensitive passengers are neither flexible concerning the duration of the flight nor the time of departure or arrival. They require the aircraft to be on time and to use the fastest route to the destination airport. Moreover, the airline has to offer the possibility to change reservations at short notice to attract time-sensitive passengers (European Commission v Ryanair/ Aer Lingus, 2007, p. 74). On the contrary, non-time sensitive passengers are more likely to use secondary instead of primary airports and can often even, although not always, be referred to be “destination insensitive”. Most customers who fall in this passenger category are leisure travellers who might be looking for a short holiday somewhere in Europe without having a specific destination in mind (ibid, p. 17, 75).

According to Dobruszkes (2013), the drivers for this shift in demand have not been identified so far. He claims that (a) travel and (b) journey attributes can be seen as the key aspects that influence one’s airline choice. This means that customers take (a) the travel purpose, destination and duration as well as (b) fares, airport type served (primary or secondary airport) and the operating model (point-to-point or connecting service) of the respective airline into account before purchasing a ticket (p. 77). Especially, business travellers who are flying intra-Europe are looking for non-stop, point-to-point services that are offered at a high-frequency.

However, even LCCs are forced to re-implement some full-service features in order to distinguish themselves from the numerous competitors (Iatrou and Oretti, p. 17). Additionally, when low cost carriers entered the market, they initially focused on serving niche markets and regional airports. Nowadays, they predominantly offer services to the main European cities and tourist destinations, serving no longer only secondary but also some primary airports. The latter even started offering terminals for LCCs such as Madrid Airport or Airport Milan (Dobruszkes, 2013, p. 78f). LCCs have also begun to serve long-haul routes which allow them to expand their businesses. This adaption is necessary especially considering that the main short-haul routes connecting large cities and the profitable niche routes are already served. Nevertheless, it seems to be difficult to realise this new strategy as cost reductions can barely be achieved since long distance flights still require full-service operations (ibid, p. 80).

Since, globalisation, deregulation and liberalisation have changed the way airlines operate, both airline types, traditional as well as low cost carriers, seek to be “fast, efficient, profitable,
flexible, adaptable and future-ready” in order to improve or remain their market position. One solution for efficiently responding to market changes are mergers. They bring about synergies and efficiencies which can be achieved by reducing the cost base, thus expanding the route-network. Another solution are alliances which aim to achieve the same objectives as mergers (Iatrou and Oretti, 2007, p. 21). However, reality shows that alliances have indeed increased traffic and improved networks, but nevertheless have neither delivered the desired cost reduction nor synergies. An explanation for this situation can be found in the fear of smaller airlines to lose control which would make them more vulnerable in case of changes in the business environment (ibid, p. 20).

4 Analysis of the Ryanair/Aer Lingus Merger Case

Ryanair’s attempt to acquire Aer Lingus by way of a public bid was notified to the European Commission on 30 October 2006. The proposed transaction was subject to an in-depth investigation within the EUMR as the merger raised concerns about its compatibility with the EEA Agreement on the one hand and the common market on the other. Ryanair had already acquired 19.16 per cent of Aer Lingus shares before the Commission received the notification of the planned transaction which would have led to sole control of Aer Lingus by Ryanair. On 28 November 2006, the share capital Ryanair held in Aer Lingus added further up to 25.17 per cent (European Commission v Ryanair/ Aer Lingus, 2007, p. 2f). The Commission’s investigation revealed that the merger, which would have combined the two leading Irish airlines, would have significantly impeded competition in the common market. As a result of the transaction, the combined entity would have obtained either a dominant or a monopoly position on 35 routes. Consequently, the merger would have harmed consumers due to the concomitant reduction in choice and price increase. Therefore, the merger was prohibited on 27 June 2007 (ibid, p. 345).

Ryanair appealed against the Commission’s decision in November 2007 but was rejected by the General Court in July 2010 (Nourry et al., 2013, p. 1).

After having introduced the economic theory on mergers with a focus on horizontal mergers (section 2) and having highlighted the role of LCCs in the European aviation industry over time (section 3), this chapter analyses the Ryanair/ Aer Lingus merger case based on the European Commission’s decision that was promulgated in 2007. Therefore, the EUMR for horizontal mergers that have been introduced in section 2.2 will be used as the tool for the analysis.4 This chap-

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4 The following analysis is solely based on the market situation pre-2007.
ter ends with a discussion of the Commission’s decision which will be based on the General Court’s 2010 judgement (section 4.5).

4.1 The Parties

Ryanair and Aer Lingus are holding about 80 per cent of all scheduled European traffic at their base airport in Dublin, making them the two largest airlines serving the Irish aviation market. Although the degree of substitutability might differ between some of the services offered by these two airlines, they can nevertheless be considered close substitutes for one another (European Commission v Ryanair/ Aer Lingus, 2007, p. 87). Being two well-established Irish airlines, Ryanair and Aer Lingus enjoy a considerable brand recognition in their country of origin which gives them a competitive advantage over other, especially non-Irish, airlines (ibid, p. 16).\(^5\) The following two sections will give a brief overview of Ryanair’s (section 4.1.1) and Aer Lingus’ (section 4.1.2) history and the development of their business models.

4.1.1 Ryanair

Ryanair is an Irish airline founded in 1985 that initially started its operations as a traditional airline that was specialising in low fares in order to dissolve the predominant duopoly market power of Aer Lingus and British Airways which existed at that point of time (Gilroy et al., 2005, p. 209). Since this business strategy did not have the desired effect, the company started to imitate the promising business model operated by the US LCC Southwest Airlines in 1991. Therefore, Ryanair’s business model was restructured by implementing low costs, low fares, no-frills, high-frequency, short-haul, point-to-point services and services to secondary airports instead to highly congested primary airports (Knorr and Arndt, 2005, p. 148). Moreover, the airline abandoned inflight services such as complimentary food or newspapers, seat allocation and business class seating, making Ryanair a wholly no-frills airline after the restructuring process (Barrett, 2004, p. 90). The foundation of Ryanair can be seen as the beginning of the low cost carrier success story that reshaped the European airline industry fundamentally (Gilroy et al., 2005, p. 209). Nowadays, Ryanair is the cost leader in the European aviation industry (European Commission v Ryanair/ Aer Lingus, 2007, p. 92).

\(^5\) This aspect will be discussed further in section 4.4.4.
4.1.2 Aer Lingus

When the Irish airline Aer Lingus was founded in 1936, the company was characterised as a state-owned, traditional full-service scheduled airline which aimed to connect Ireland with the world and vice versa. With increasing competition, especially from Ryanair, Aer Lingus was forced to transform its former full-service operating model into a low cost model in 2002. Therefore, Aer Lingus changed its operations by starting to sell flight tickets mainly through the Internet, focusing on point-to-point services, reducing its fleet size and staff numbers and therefore lowering fares (Wallace et al., 2006, p. 338). Unlike Ryanair, Aer Lingus retained some of its full-service features such as services to primary airports, frequent flyer programmes, direct links into other airline networks through an international alliance membership and enhanced product features, including seat assignment, boarding cards, and limited complimentary snacks on European flights (ibid, p. 339f). Therefore, Aer Lingus’ business model cannot be solely associated with the no-frills but rather with the some-frills model. Moreover, the airline continued to operate long-haul services to the United States. On these routes, the company retained its full-service operations as the low cost model currently still faces restrictions on long-haul flights due to the remaining demand for high level services such as offered by full-service carriers (Wallace et al., 2006, p. 338; European Commission v Ryanair/ Aer Lingus, 2007, p. 13f).

4.2 Community Dimension

Although, Ryanair and Aer Lingus neither achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State nor does their combined aggregate worldwide turnover exceed €5 billion, the merger falls within the jurisdiction of the European Commission since the other turnover-based thresholds that indicate Community dimension are surpassed (see Figure 3). In this case, the geographical allocation of turnover has to be identified in order to decide whether the relevant thresholds are exceeded in at least three Member States. The geographical allocation of turnover can either be associated with the point of sale or the so-called 50/50 ratio. The latter takes the crucial cross border character of Ryanair’s and Aer Lingus’ routes into account that are subject to this investigation by allocating the turnover to both, the country of origin and the country of destination (European Commission v Ryanair/ Aer Lingus, 2007, p. 4f).
The Commission concluded that it is difficult to apply the point of sale methodology to the business model of LCCs as the majority of tickets are sold via the Internet. Consequently, revenues cannot be reliably allocated to a specific location at the point of sale since tickets can literally be purchased from any place in the world. Another method for geographically allocating turnover is the *place of departure* methodology. This approach is most likely to identify the actual location of the customer best. The, from this method, derived information can furthermore be an indicator for an airline’s presence and therefore its strength in a specific Member State (ibid, p. 6f). However, the Commission decided that this method can only be applied if traditional return tickets, which do not exist as such in this case since airlines compete for both the out-bound and inbound flight, are treated as two one-way flights instead of a round trip. This decision is based on the bargaining power exerted by the customers which is reflected in their ability to easily compare fares via the Internet. They are therefore able to choose the more favourable flight for each leg of their journey (ibid, p. 9).

Finally, the Commission concluded that Ryanair and Aer Lingus exceed the turnover thresholds of €25 million and €100 million in at least three Member States, here Ireland, the United Kingdom and Spain, under both the place of departure and the 50/50 methodology. Both compa-
nies’ sole aggregated turnover exceeds €25 million on the one hand while their combined turnover surpasses €100 million in these three Member States on the other. Accordingly, this merger case has a Community dimension and therefore falls within the jurisdiction of the European Commission (ibid, p. 9).

4.3 Relevant Markets

The Commission has based its market analysis on the “Origin & Destination - Approach” (henceforth O&D - Approach). The O&D - Approach implies that separate markets exist for each route between a point of origin and a point of destination. Customers are more likely to purchase tickets to a specific origin and a specific destination instead of randomly choosing a route (European Commission v Ryanair/ Aer Lingus, 2007, p. 15f). Therefore, one intra-Europe route cannot be a substitute for an entirely different intra-Europe route. As part of the O&D - Approach, the Commission has moreover assessed the effects of the proposed merger on specific passenger groups on certain flights. Firstly, it was considered whether connecting flights and passengers are part of the same market. The Commission concluded that passengers flying from Ireland to a transnational destination via a connecting airport are not affected by the proposed transaction since Ryanair and Aer Lingus do not compete with each other for this type of passengers. In addition, connecting passengers might face price discrimination in comparison to point-to-point customers. The former usually have to purchase a ticket for the entire route and can therefore neither identify nor compare the prices for each limb of this route. Moreover, only Aer Lingus partly provides connecting services, but does however not adapt its flights to other airline’s schedules. Consequently, it is assumed that passengers booking a connecting flight with a different airline and therefore separately from the other limb of the route, will be furthermore referred to as point-to-point passengers in order to observe the overall effects of the proposed merger on intra-Europe routes (ibid, p. 18f).

Secondly, it is necessary to examine the substitutability of alternative airports or secondary airports to direct flights from the demand side. Alternative airports can be considered substitutable if they belong to the same catchment area as the primary airport from the consumers’ point of view. These airports are typically located in more or less remote to the primary city airports and are normally smaller, often former regional or military, airports. In order to identify substitutable airport pairs, the Commission analysed whether consumers consider services to a secondary airport as a reasonable alternative to the primary airport (ibid. p. 19f). Therefore, passengers were asked about the main factors that influence their air transport service choice. The investiga-
tion revealed that customers take travel time and total travel costs, flight times, schedules and frequencies as well as the quality of service into account when choosing an airline service. Most certainly, customers aim to minimize the travel time and costs while flight times, schedules, frequencies and quality of service are dependent on individual preferences. It can be concluded, that customers generally seek to maximise their personal utility which is restricted by their personal financial constraints. Moreover, passengers are willed to accept a longer travel time from their starting point to the secondary airport and from the secondary airport to their actual destination only, if the total travel costs are reasonably lower compared to the alternative primary airport (ibid, p. 21f).

In order to develop a suitable proxy, the Commission used the view of airports as well as available customer and competitor opinions to decide whether an alternative airport belongs to the same catchment area as the primary airport or not. The relevant customer information was obtained by way of a customer survey which was conducted at Dublin airport. For the identification of the travelling times, the 100km/1 hour proxy was taken into account using the city centre criterion. This, however, does not necessarily mean that all passengers start or end their journey in the city centre. Nevertheless, this criterion is the most suitable benchmark for determining whether customers consider a secondary airport as a substitute (ibid, p. 23f). Moreover, the Commission looked at marketing practices such as Ryanair presenting its services to secondary airports as services to the relevant larger city in the vicinity, for example Frankfurt (Hahn) or Hamburg (Lübeck). Other relevant aspects which contributed to the analysis were existing transport services from and to the airports such as bus or train connections, especially when these services were offered by Ryanair, the results of a price correlation analysis conducted by the Commission and the proportion of leisure passengers on a route (ibid, p. 25).6

It is important to stress out that although a route is considered substitutable from the demand side, it does not necessarily imply supply side substitutability due to divergent operational efficiencies and airline services (ibid, p. 66). Moreover, the Commission decided that some routes can be considered substitutes despite the fact that the 100km/1 hour methodology does not apply. In these cases, the Commission laid stress on other criteria which were considered more suitable measurements for identifying the relevant city pairs such as Ryanair’s marketing practices. Moreover, the evaluation of the customer and competitor surveys has revealed that both consulted groups agreed to the decision that routes are substitutes for one another when the Commission took that point of view (ibid, p. 68).7

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6 For a detailed analysis of the substitutability of primary and secondary airports see Table 2 in the appendix.
7 Therefore, the results of these surveys are not listed separately in Table 2 of the appendix.
Furthermore, the Commission has considered whether there is a joint market for direct and indirect flights, scheduled and charter flights and non-time and time-sensitive passengers. It was concluded that indirect flights cannot be seen as substitutes for direct flights especially with regard to Ryanair’s and Aer Lingus’ point-to-point and mainly short-haul operations. Only the latter offers a limited number of connecting flights. Therefore, indirect flights are not part of the same market as direct flights on the identified O&D pairs (ibid, p. 68). Moreover, the Commission has rejected Ryanair’s claim that charter flights belong to the same market as scheduled flights. A charter flight can be defined as a special air transport service which is not operated on a regular basis (ibid, p. 69). These flights are mostly part of package holiday sales and seats are therefore primarily sold by tour operators (ibid, p. 74). Although charter airlines are sometimes selling available seats, so-called dry seats, to end customers, this share does not have the dimension to significantly pose a sufficient competitive constraint on the affected routes served by the merging entity (ibid, p. 70). The Commission decided that it is not relevant in this case to decide whether dry seat sales should be included in the relevant market due to its limited presence and will hence not be discussed further (ibid, p. 72). Finally, the authority scrutinised a possible differentiation between non-time and time-sensitive passengers. It was concluded that a distinction between the two passenger groups cannot be made as Ryanair and Aer Lingus both sell tickets under the same terms for every passenger group. Therefore, both airlines do not price discriminate between non-time and time-sensitive passengers. Consequently, both passenger groups belong to the low cost customer sector and are thus not a market of their own (ibid, p. 78).

The Commission’s market investigation has identified the market for "direct scheduled passenger air transport services between a given point (or region) of origin and a given point (or region) of destination” as the relevant market in this case (ibid, p. 84). Consequently, the proposed merger would lead to a significant number of overlap routes, all from or to Ireland. Overall, the overlap of Ryanair’s and Aer Lingus’ services concerns 32 routes from and to Dublin, two from and to Cork and one from and to Shannon. On 16 of these 35 overlap routes, the overlap regards direct airport-to-airport routes where both airlines serve the same O&D pair while 19 further routes concern city-to-city routes where Ryanair and Aer Lingus fly from the same airport in Ireland but however serve different airports at the destination (ibid, p. 84). Moreover, the proposed transaction might raise concerns on further 53 routes from and to Dublin, 24 from and to Shannon, and 15 from and to Cork where currently only one of the merging parties is operating (ibid, p. 78f).
4.4 Competitive Assessment

This chapter analyses Ryanair’s and Aer Lingus’ market shares and the market concentration on the actual overlap routes which are subject to this investigation (section 4.4.1), the degree of competition between Ryanair and Aer Lingus on the one hand and other competitors that are active on the affected routes on the other (section 4.4.2), as well as whether countervailing factors can exert a competitive constraint on the anti-competitive behaviour of the merged entity post-merger. Therefore, the consumers’ buyer power, their possibility to switch suppliers (section 4.4.3) and the existing barriers to entry will be examined (section 4.4.4). Finally, it will be discussed whether the proposed transaction brings about efficiency gains which can outweigh the adverse effects of the merger on competition (4.4.5).

4.4.1 Market Shares and Concentration

Ryanair and Aer Lingus are by far the two largest airlines serving the Irish aviation market. They account for 80 per cent of all intra-Europe traffic from and to Ireland and the largest share of passenger traffic at Dublin, Shannon and Cork airport. At the latter two airports, the proposed transaction would create the largest short-haul airline which is operating at these two sites. The merger would therefore affect more than 14 million passengers (European Commission v Ryanair/ Aer Lingus, 2007, p. 81, 84). The Commission’s analysis revealed that the transaction would create a monopoly on 22 of the 35 overlap routes, while the merged entity would have a very high combined market share above 60 per cent on further 13 routes. Moreover, the lack of a sufficient number of competitors with a reasonable market share on almost all of the affected routes leads to a significantly increased concentration level which can be measured with the aid of the Herfindahl-Hirschman Index. The HHI level post-merger on e.g. the Dublin – Warsaw route would reach approximately 5400 compared to a pre-merger HHI of approximately 3000 with a delta of 2400.8 Thus, the HHI would even reach a considerably high level on a route where two other competitors are active. This situation indicates that the overall concentration level on each of the 35 overlap routes would be very high especially with regard to the large share of monopoly routes which would be created by the transaction. Furthermore, the merged entity would not only obtain a high combined market share on thin routes, but also on eight out of the ten most important routes from and to Dublin. This concerns flights from Dublin to Lon-

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8 The HHI levels are based on assumptions as the European Commission only published market share ranges in its decision due to confidentiality reasons (p. 82). The ranges are based on the planned weakly seat capacity for summer 2007. A detailed calculation can be found in the appendix.
don Heathrow, London Stansted, London Gatwick, Manchester, Paris Charles de Gaulle, Malaga, Birmingham, Amsterdam and Faro. Consequently, the merger would significantly affect competition due to the negative competitive effects which are brought about by a large market share and a considerably raised concentration level (ibid, p. 83f).

4.4.2 Degree of Competition

Ryanair and Aer Lingus do not only operate a similar business model with a related cost structure but are also about the same size and enjoy a comparable market position in Ireland (European Commission v Ryanair/ Aer Lingus, 2007, p. 86). The Commission’s price correlation analysis shows that although price differences between Ryanair’s and Aer Lingus’ average fares still exist and amounted to €30 in 2006, it can be observed that their fares have steadily moved together over time. However, it should also be taken into account that this price difference mainly refers to the somewhat higher service level offered by Aer Lingus (ibid, p. 90f). Although, Ryanair is by far the cost leader in the European airline industry, Aer Lingus is ranked second before easyJet and Virgin Express according to the operating costs per available seat kilometre in 2004, making Aer Lingus Ryanair’s closest competitor even in terms of unit costs (ibid, p. 92f).

Moreover, both airlines have a base in Dublin and are viewed as close competitors by their customers and other market players (ibid, p. 86). In the survey carried out by the Commission, customers were asked which airline they considered when flying on routes from and to Dublin. The investigation revealed that customers generally consider Ryanair and Aer Lingus when planning a route that is served by both parties (ibid, p. 103, 106). In fact, 66.1 per cent of Ryanair’s and 32.5 per cent of Aer Lingus’ passengers who do not solely fly with Ryanair or Aer Lingus have answered that they had considered flying with the other party while only 24.5 per cent and 15.7 per cent had considered flying with another airline (ibid, p. 105). The survey’s results which are based on unweighted data, support the assumption that the degree of competition between Ryanair and Aer Lingus is significantly higher compared to other competitors as customers refer to the services offered by both parties from and to Ireland as closest substitutes (ibid, p. 104).

Another factor indicating the closeness of competition between Ryanair and Aer Lingus is that both airlines are the only active parties on 24 of the 35 routes that are affected by the proposed merger. In such a duopoly market, the operating entities are inevitably each other’s closest competitors. Although, a small number of other market players exist on the other eleven routes, their insignificant market share does not pose any competitive restraints on Ryanair’s or Aer
Lingus’ business activities. Moreover, these competitors are mainly network carriers and also charter airlines who are offering different services than the merging entities. In fact, Ryanair and Aer Lingus only face a competitor with a considerable market share on three out of the 35 routes. However, in two of these three cases that market player is mainly offering connecting services and therefore does not have the dimension to challenge the merged entity post-merger (ibid, p. 86f).

It is a common practice in the airline industry to track the pricing policy of competing airlines. This can especially be observed when airlines are close competitors and changes in the pricing behaviour of one airline leads to a price adaption by the other. Accordingly, the players in the market exert competitive constraints on each other, indicating a high degree of competition between the concerned parties. The Commission observed that airlines monitor each other’s pricing behaviour with the aid of specialised price comparison software. This software enables airlines to follow their competitors’ pricing behaviour as information about price changes can be accessed via the Internet where the majority of tickets are sold, making prices transparent. In fact, Ryanair and Aer Lingus observe each other’s pricing behaviour on a daily basis and simultaneously adapt their fares in reaction to the competitive performance of the other party (ibid, p. 107f). Moreover, the Commission’s investigation revealed that Ryanair reacts on promotions offered by Aer Lingus in such a way that it reduces its fares only until the latter’s promotion ends. Consequently, it can be concluded that Ryanair and Aer Lingus take each other’s behaviour into account when making a decision about their own pricing strategy (ibid, p. 110).

Furthermore, the Commission’s regression analysis revealed that Ryanair is inclined to enter or exit a route on which Aer Lingus is already operating which shows that the former adapts its strategy to the latter (ibid, p. 119). Finally, the Commission concluded that Ryanair and Aer Lingus are inevitably each other’s closest competitors on the affected routes. Consequently, the proposed transaction would lead to the elimination of the most important competitive force on almost 70 per cent of all routes and would therefore encourage the creation of a monopoly or a dominant position (ibid, p.107).

4.4.3 Buyer Power and the Possibility to Switch Suppliers

As the proposed transaction would lead to the elimination of the closest competitor on the majority of the affected routes on the one hand and effective competition on the other, the merged entity would gain a significant market power which is most likely to bring about increased fares (European Commission v Ryanair/ Aer Lingus, 2007, p. 120). According to the EUMR, an in-
crease in prices will particularly be the consequence of high market power when customers are not able to switch suppliers due to the lack of alternative services. In this case, the proposed merger would eliminate the alternative supplier. This would leave consumers with no, or a very limited ability to switch suppliers post-merger. Consequently, the customers would be especially vulnerable to anti-competitive behaviour when the merger causes a price increase. Moreover, the affected customer group does not have the necessary countervailing buyer power in order to offset such a price increase. This can be put down to the lack of possibilities to switch suppliers as well as to the commercially insignificance of the value of an individual ticket for the merged entity (ibid, p. 136f).

Other consequences of the elimination of the main competitor could furthermore not only be a reduction in the number of flights but also in the quantity of new routes since competition sets the incentives for airlines to enter new routes in order to secure the first-mover advantage. In fact, the Commission has observed that when Aer Lingus had significantly expanded its route network, Ryanair responded by increasing its own number of destinations and vice versa. Therefore, it can be argued that effective competition in terms of an equally strong competitor, who ideally operates from the same base, stimulates the rapid development of new routes to the benefit of the consumers. Consequently, the proposed merger would eliminate the incentives to discover new viable routes (ibid, p. 120f). Therefore, the transaction would reduce the benefits of effective competition which are low prices, high quality services, a wide selection of services and innovation. These benefits that come along with effective competitive would no longer exist as the merger would eliminate actual competition on all overlap routes. This would lead to the creation of a significantly high market power that could be used by the merged party to the detrimental of the consumers (ibid, p. 120ff). Consequently, neither the possibility to switch suppliers nor existing buyer power can counteract the transaction’s anti-competitive effects.

### 4.4.4 Barriers to Entry

The Irish aviation market is characterised by high barriers to entry that are faced especially by non-Irish carriers who do not have a base at an Irish airport. Carriers without a base neither benefit from the cost advantages a substantial operation at one airport brings about nor the flexibility which allows airlines with a base to timely respond to changes in demand or the market structure (European Commission v Ryanair/ Aer Lingus, 2007, p. 139). Ryanair and Aer Lingus both have a strong presence not only at Dublin airport, where both airlines concentrate their traffic at by way of their base, but also at Cork and Shannon airport (ibid, p. 80, 138). There are only two
other carriers who are operating from a base in Dublin. These airlines are CityJet and Aer Arann. However, CityJet’s and Aer Arann’s business models as well as their size mainly differ from Ryanair’s and Aer Lingus’. Therefore, they are unlikely to replace the anti-competitive constraint that might be exerted by the merged entity (ibid, p. 139f). Moreover, the Commission’s investigation exposed that it is doubtful that any other airline would set up a base at any of the three concerned airports. This concerns especially Dublin airport which is highly congested, making the airport an unattractive choice as building up a base that brings about flexibility in supply requires massive investments on the one hand and a sizeable fleet of large, modern and fuel efficient jets on the other (ibid, p. 141).

Furthermore, Ryanair and Aer Lingus enjoy a strong brand recognition in the Irish market due to their respectable reputation as two well-established Irish airlines. This significant position makes it more difficult for other airlines to win a sufficient amount of the crucial Irish customers for their routes from and to Ireland (ibid, p. 16f). Both, Ryanair and Aer Lingus have built up a sustainable customer and market knowledge base over the years. Therefore, they enjoy a competitive advantage over other potential, especially non-Irish, entrants. Since the target customers mainly originate in Ireland, it is significantly easier for Ryanair and Aer Lingus to win customers for their routes through their well-organised marketing and distribution system (ibid, p. 147).

Although the Internet has become an increasingly popular distribution channel, which could easily be used for reaching their target customers, competitors still need to attract passengers to visit their website. In fact, Ryanair’s Internet presence is ranked 44th and Aer Lingus’ 64th in the group of the most visited Irish websites. This observation seems to indicate that customers originating in Ireland automatically turn to either Ryanair or Aer Lingus when looking for flights from or to Ireland. Therefore they tend to compare fares solely between these two airlines. These circumstances further increase the barriers to entry for potential entrants, making entry increasingly unlikely. It can be concluded, that a new entrant has to invest excessively in marketing, advertising and promotional campaigns in order to build a similar level of brand-awareness compared to the merging entities and to win a sufficient number of customers. However, these attributes can only be developed over time and do not, in case of a successful entry, immediately affect the merged entity (ibid, p. 149f). Consequently, the level of sunk costs that occur in case of an unsuccessful entry is exceptionally high and can be associated with the incurring marketing and potential start-up costs such as the installation of ground service operations at the new airport or the purchase or leasing of new aircrafts for the new routes (ibid, p. 153).

Another barrier to entry is Ryanair’s aggressive entry deterrence strategy in order to prevent any competitor from entering an Irish route. In case of a successful entry, Ryanair tries to drive
the new entrant out of the market by temporarily reducing prices and increasing frequencies (ibid, p. 141). After having successfully forced the new entrant to exit the market by using its base-advantage, the airline has in recent cases reduced its frequencies and raised its prices back to the pre-entry level (ibid, p. 155). The Commission’s investigation supports the assumption that Ryanair engages in aggressive competition by using inter alia an example where Ryanair successfully used its entry deterrence strategy to drive out easyJet from the Gatwick-Cork route only one year after its entry (ibid, p.154). Therefore, the Commission assumes that the merged entity would deter entry even more aggressively due to its strong market position (ibid, p. 164).

Furthermore, the continuing congestion problems at Dublin airport, especially regarding the availability of runway capacity, currently deters new entrants (ibid, p. 168f). The merged entity might also use its increased size and strong position for influencing the decision-making process of the regulator at Dublin airport to their advantage which further threatens potential market players (ibid, p. 175). Finally, the Commission’s competitor survey revealed that most airlines do not even consider entering a route where they would have to engage in direct competition with either Ryanair or Aer Lingus (ibid, p. 190). Therefore, the Commission concluded that entry by another airline is unlikely on almost all overlap routes which hinders the establishment of effective competition. Consequently, competition cannot reverse the anti-competitive impact of the merger as the transaction brings about an extensive loss of competition between the merging parties and an extension of the already existing barriers to entry (ibid, p. 138).

### 4.4.5 Efficiency Gains

Finally, the Commission has investigated whether substantial efficiencies brought about by the proposed merger would have the dimension to outweigh the significant impediment of the transaction on competition. Therefore, potential efficiency gains have to be verifiable, merger-specific and to the benefit of the consumers. Since the proposed merger leads to the creation of a monopoly on 22 of the 35 overlap routes, it is unlikely that the transaction will bring about efficiencies that can effectively counteract the anti-competitive effects of the merger (European Commission v Ryanair/ Aer Lingus, 2007, p. 311). Moreover, it is assumed that companies aim to maximise their profits. The Commission’s investigation has revealed that Ryanair has in the past increased its prices in order to raise its own profit margin. Therefore, it is unlikely that Ryanair would use its improved market position and power to the benefit of the consumers (ibid, p. 317).
In the notification, Ryanair claims that the merger would bring about cost savings which will be realised in form of staff, aircraft ownership, ground operational and maintenance costs as well as airport charges and ancillary sales. These reductions are based on the improved bargaining position of the merged entity which allows them to negotiate better discounts and contracts. Moreover, Ryanair argues that a reduction in distribution and advertising costs can be achieved. These cost savings should mainly be realised by implementing Ryanair’s business model into Aer Lingus’ business structure (ibid, p. 311). The Commission questions whether Ryanair could fully maintain Aer Lingus’ brand and quality differentiation when applying its own business model to Aer Lingus. There is no evidence that the planned cost reductions in Aer Lingus would not lead to a significantly lower service quality. Furthermore, it does not seem appropriate to assume that Ryanair’s unique business model could successfully be replicated in Aer Lingus (ibid, p. 318). The other efficiency claims do likewise not respond to Aer Lingus’ business model as, for example, a reduction in airport charges seems more difficult to achieve at primary airports compared to the secondary airports Ryanair serves. Additionally, it was decided that the efficiency claims brought forward by Ryanair cannot be associated with the merger but are more a result of the airline’s already existing buyer power (ibid, p. 314).

Conversely, Aer Lingus argues that efficiency gains claimed by Ryanair in terms of cost savings do not relate to the airline’s short-haul business which is subject to the Commission’s investigation, but rather to Aer Lingus’ long-haul services. Since Aer Lingus has already achieved significant cost savings on its own in the past, it is more likely that the proposed merger would lead to either lower or even no cost savings. Therefore, the efficiency gains that were put forward are neither verifiable nor merger-specific (ibid, p. 314f).

Ryanair moreover claims that the stated efficiency gains will naturally be passed on to the consumers in terms of reduced fares, higher frequencies, an improved route network and better quality (ibid, p. 313). The Commission argued that the fix-cost efficiencies would not affect Ryanair’s price setting decisions on existing routes and would therefore not have an immediate effect in favour of the consumers. Furthermore, it was pointed out that customers would only benefit from cost savings on thin routes which are currently not viable (ibid, p. 320). Since Ryanair has not been able to provide the Commission with any supporting evidence, it is concluded that the proposed efficiencies are neither verifiable, merger-specific nor to the benefit of the consumers. Consequently, the merger does not bring about efficiencies that would offset the anti-competitive effects of the transaction (ibid, p. 321).
4.5 Discussion of the Commission’s Decision

Ryanair lodged an objection against the Commission’s decision only five months after the verdict was delivered. Ryanair argued that the prohibition of its merger with Aer Lingus was not justified. The LCC claimed that mistakes have been made in the Commission’s analysis concerning the competitive relationship between the merging entities, existing barriers to entry, the route-to-route analysis, efficiencies and submitted commitments. Initially, the emphasis of the analysis had to be laid on efficiency gains and econometric data. The Commission’s judgement was verified by the General Court on 6 July 2010 (Koch, 2010, p. 41).

The purpose of the re-examination carried out by the General Court was to scrutinise whether the Commission had based its decision on valid and logical arguments, whether any important argument by the concerned parties were disregarded or whether their procedural rights had been dishonoured during the legal proceedings. Therefore, each argument put forward by Ryanair was carefully examined. Firstly, the Court investigated Ryanair’s claim that the Commission had deduced an impediment of competition from the high market share that would have been created by the merger. It was concluded that the Commission had in fact carried out an in-depth analysis according to the assessment structure set out in EUMR. Thereby not only market shares but also the concentration level in the market, the actual competition between Ryanair and Aer Lingus, available customer and competitor opinions as well as the actual situation on each affected route were taken into account (ibid, p. 42).

Secondly, the Court supported the Commission’s judgment on closeness of competition. Here, the Commission had decided that competitors have to share major business elements and that a mere threat of entry has to exist in order to counterweight the anti-competitive effects of the merger (ibid, p. 42). Thirdly, the Court extensively examined whether the efficiency claims put forward by Ryanair had correctly been addressed by the Commission. However, it did not fall into the jurisdiction of the Court to decide whether efficiencies actual existed in the case. The re-examination revealed that the arguments put forward by the Commission, which led to the rejection of Ryanair’s efficiency claims, have been assessed correctly. Moreover, the Court emphasised on the importance of meeting the formal requirements by denying Ryanair’s statement that the Commission had made significant mistakes rejecting the proposed remedies since Ryanair did not meet the deadline for handing in remedies (ibid, p. 43).
Additionally, the Court confirmed that the approaches utilized by the Commission such as the route-by-route analysis\(^9\) which was used to examine the effects of the mergers on the basis of individual routes as well as the framework developed by the Commission for deciding whether airports are substitutes for one another, were conducted in an appropriate manner. The Court also welcomed the differentiation between mergers that concern airlines operating from different airports and mergers that affect carriers operating from the same airport, their so-called base, due to the advantages that come along with this strategy. Furthermore, the Court investigated whether the data that was obtained through the passenger survey carried out at Dublin airport by an independent consultancy was accurate regarding its gathering, scale, use and presentation. The Court’s analysis supported the accuracy of the survey data used by the Commission as well as the selective analysis of the data in terms of its relevance (ibid, p. 43). Moreover, Ryanair’s claim that technical evidence derived from econometric studies should have been the tool for analysing the anti-competitive effects of the merger was dismissed. The Court decided that the use of quantitative and econometric studies in the Commission’s investigation have been reasonable (ibid, p. 44). Finally, the General Court announced that the Commission’s decision can be fully endorsed and can furthermore be seen as a prime example for the accurate use of economic approaches within the EUMR. Consequently, Ryanair’s appeal was rejected (ibid, p. 42).

5 Related Cases

This chapter briefly discusses the cases that are related to the European Commission’s 2007 decision. Ryanair was the first firm to try to resurrect a transaction that has been prohibited by the European Commission before. In fact, Ryanair tried to acquire Aer Lingus twice after the initial prohibition in 2007. However, in 2015, Ryanair finally agreed to the acquisition of Aer Lingus by IAG (Parker et al., 2012). The following two sections will give an overview of Ryanair’s second and third attempt to acquire Aer Lingus (section 5.1) and the recent takeover of Aer Lingus by IAG (section 5.2).

\(^9\) Due to the limited scale of this thesis, the detailed route-by-route analysis could not be discussed further in the competitive assessment. However, it is necessary to highlight its importance for analysing mergers in the airline industry. For the individual route analysis, the Commission takes into account the same criteria as already discussed in section 4.4. In the Ryanair/ Aer Lingus merger case, the results of the route-by-route analysis supported the Commission’s assumption that the transaction would lead to a significant impediment of effective competition as a result of very high market shares on the majority of the overlap routes which would have been created by the merger (see European Commission v Ryanair/ Aer Lingus, 2007, p. 191 – 310).


5.1 Ryanair/ Aer Lingus II and III

In December 2008, Ryanair announced a second takeover bid for Aer Lingus. At this point of time, Ryanair already held 29.8 per cent of share capital in Aer Lingus. However, this time, the offer was already turned down in January 2009 by Aer Lingus itself. This decision was especially pushed through by the Irish government who then owned 25.1 per cent of the company and Aer Lingus’ employees who held 14.2 per cent of shares in the airline (O’Connell and Williams, 2011, p. 121).

On 24 July 2012, the Commission was informed about Ryanair’s intention to acquire Aer Lingus by way of a public bid similar to its unsuccessful initial attempt in 2006. On 27 February 2013 the Commission prohibited the proposed transaction once again after having conducted an in-depth investigation under the EUMR. In this re-examination, the Commission especially took the changes in the market since 2007 into account. Almost six years after the Commission’s first prohibition, the merger would even have led to the creation of a monopoly on 28 routes compared to 22 in 2007 and a dominant position on further 19 compared to 13 routes in 2007 where Ryanair and Aer Lingus compete with each other. Moreover, both parties’ positions in Ireland have even become stronger with a combined market share of 87 per cent in 2012 compared to 80 per cent in 2007 in the market for short-haul flights from and to Dublin. This situation has furthermore increased the already existing high barriers to entry. Consequently, it has become increasingly unlikely that any airlines would enter the market post-merger and could therefore exert a sufficient competitive constraint on the even more powerful merged entity (European Commission, 2013a).

Consequently, the proposed transaction would have brought about less choice and increased prices to the detrimental to the consumers by eliminating the closest competitor on 46 routes. Moreover, the Commission decided that additionally to Dublin, Cork and Shannon airport, which have already been subject to concern in the 2007 decision, customers travelling from and to Knock would now also be affected by the merger. The Commission has furthermore rejected the remedies claimed by Ryanair as they were insufficient to effectively counteract the anti-competitive effects of the transaction and therefore could not guarantee that customers would not be harmed (ibid).

5.2 Aer Lingus/ IAG

When IAG, the parent company of British Airways, Iberia and Vueling declared its interest in merging with Aer Lingus, the largest shareholders in Aer Lingus were the Irish government with
25.1 per cent and Ryanair with 29.9 per cent (Hollinger and Thomas, 2015). According to the Forbes 2000 Index of 2015, IAG is currently the third largest airline in the world. The airline group owns its favourable position mainly to a large number of mergers that took place after the turn of the century. IAG’s proposal to acquire Aer Lingus was subject to approval by three parties: the Irish government, the shareholders, especially Ryanair due to its large shares in Aer Lingus and the European Commission due to the case’s Community dimension and the concern that the transaction might impede effective competition in the EU (Chari, 2015). IAG stated that it would only proceed with its proposal if it meets with general approval from all involved parties.

The Irish government made its approval conditional on a guarantee from IAG to keep Aer Lingus’ valuable London-Heathrow slots for Irish routes for the next ten years, which was then reduced to seven years by mutual agreement. Additionally, IAG claimed that it will continue to serve routes between London-Heathrow and Irish regional airports such as Shannon and Cork on the one hand and that it will maintain jobs and create further vacancies on the other. Moreover, IAG aims to continue the expansion of Aer Lingus’ long-haul network. On 26 May 2015, the Irish government approved IAG’s proposal to acquire Aer Lingus and therefore agreed to sell its share (McDonald, 2015). However, Ryanair was at that point of time still fighting the British Competition and Market Authority’s decision to sell its share in Aer Lingus and therefore seemed to be reluctant to approval (Hollinger and Thomas, 2015). Finally, on 10 July 2015, Ryanair officially accepted IAG’s offer after the deal was unanimously accepted by the board (Newenham, 2015).

On 14 July 2015, the European Commission approved the acquisition of Aer Lingus by IAG after having conducted an in-depth investigation under the EUMR. Before, the transaction had raised concerns about the creation of high market shares on the following three routes: Dublin – London, Belfast – London and Dublin – Chicago. On these affected routes the remaining competitors would not have been able to exert a competitive constraint on the merged entity which would therefore have led to a price increase to the detriment of the consumers. Moreover, the Commission questioned whether Aer Lingus could continue to transport passengers to connecting long-haul flights of competing airlines post-merger (European Commission, 2015b).

Consequently, the Commission declared its approval to be conditional upon two commitments. Firstly, IAG would have to release five pairs of its daily landing slots at London-Gatwick airport in order to encourage entry on routes from London to Dublin and Belfast. Secondly, Aer Lingus would have to continue to provide traffic to long-haul flights of competing airlines out of London-Heathrow, London-Gatwick, Manchester, Amsterdam, Shannon and Dublin (ibid).
Therefore, IAG would have to enter into agreements with its long-haul competitors. Moreover, the Commission added, that the airline buying the slots, would have to continue to provide traffic from London-Gatwick to Dublin and Belfast (Paul, 2015). Accordingly, IAG submitted sufficient commitments which satisfactorily addressed the Commission’s concerns. Therefore, the company made the requested slots available and entered into agreements with competing airlines in order to ensure the continuation of Aer Lingus’ long-haul connecting services. Consequently, the Commission decided that the proposed merger would not significantly impede effective competition with regard to the commitments that have been made (European Commission, 2015b). Finally, IAG took sole control over Aer Lingus on 2 September 2015 (Zeit, 2015).

6 Conclusion

The Ryanair/ Aer Lingus merger case fell into the jurisdiction of the European Commission as the proposed transaction did not only exceed the relevant turnover thresholds which gives a merger the necessary Community dimension but also raised concerns about its compatibility with the common market and the EEA Agreement (European Commission v Ryanair/ Aer Lingus, 2007, p. 2f, 4f). In its in-depth analysis, the European Commission comprehensively used economic analysis models to investigate the proposed merger. This method has simultaneously been adapted in this thesis for analysing the case. The analysis has revealed that the proposed transaction would not only have combined the two leading Irish airlines but would also have been a significant impediment on competition due to the large number of overlap routes. In fact, the merged entity would have obtained a monopoly position on 22 of the 35 overlap routes and a very high combined market share above 60 per cent on the remaining 13 routes. Furthermore, Ryanair and Aer Lingus are the only active airlines on 24 of the affected routes. Therefore, the transaction would have led to the elimination of the closest competitor on the majority of overlap routes.

Moreover, neither countervailing factors nor efficiencies would have outweighed the negative anti-competitive effects of the transaction. In addition, a large number of barriers such as the strong brand recognition of the merging entities in Ireland, aggressive entrance deterrence strategies exercised by Ryanair and the congestion problem at Dublin airport, successfully deter entry by potential competitors which made effective competition post-merger increasingly unlikely. Consequently, the merger would have harmed consumers due to the concomitant reduction in choice and increase in prices and could therefore not be approved.
Accordingly, the European Commission prohibited the merger. Its decision was fully endorsed by the General Court in 2010. The latter especially highlighted the exemplary use of economic analysis tools within the EUMR and its accurate adaption to mergers between LCCs (Koch, 2010, p. 42). After Ryanair had tried to take over Aer Lingus twice after the initial prohibition, the case was closed when Ryanair agreed to sell its shares in Aer Lingus to IAG and therefore enabled the merger between the latter two (Parker et al., 2012). Differently to the merger between Ryanair and Aer Lingus, the Commission approved the acquisition of Aer Lingus by IAG after sufficient commitments have made. Here, it was concluded that the proposed transaction does not impede effective competition and will be to the benefit of the consumers (European Commission, 2015b).
Appendix

A1. HHI Calculation for the Dublin-Warsaw Route

<table>
<thead>
<tr>
<th>Market players</th>
<th>Ryanair</th>
<th>Aer Lingus</th>
<th>LOT</th>
<th>Norwegian Airline Shuttle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market share in % pre-merger</td>
<td>40</td>
<td>30</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td>Market share in % post-merger</td>
<td>70</td>
<td>10</td>
<td>20</td>
<td>20</td>
</tr>
</tbody>
</table>

Table 2: Market Players with Market Shares on the Warsaw-Dublin Route
(based on European Commission v Ryanair/ Aer Lingus, 2007, p. 82)

\[
\text{HHI}_{\text{pre-merger}} = (40)^2 + (30)^2 + (10)^2 + (20)^2 = 3000
\]

\[
\text{HHI}_{\text{post-merger}} = (70)^2 + (10)^2 + (20)^2 = 5400
\]

Delta = 5400 – 3000 or 40 x 30 x 2 = 2400

A2. Analysis of the Substitutability of Primary and Secondary Airports

<table>
<thead>
<tr>
<th>City</th>
<th>Airports</th>
<th>City Centre Criterion</th>
<th>Private Car</th>
<th>Public Transport</th>
<th>Ryanair’s marketing practices</th>
<th>Substitutes</th>
</tr>
</thead>
<tbody>
<tr>
<td>London</td>
<td>Stansted (STN)</td>
<td>59 km</td>
<td>85 min</td>
<td>bus: 75 min</td>
<td>London (Stansted)</td>
<td>Ryanair bus service</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 45 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Heathrow (LHR)</td>
<td>28 km</td>
<td>65 min</td>
<td>bus: 65 min</td>
<td>Not served by Ryanair</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 55 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Gatwick (LGW)</td>
<td>46 km</td>
<td>85 min</td>
<td>bus: 90 min</td>
<td>London (Gatwick)</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 60 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Luton (LTN)</td>
<td>54 km</td>
<td>44 min</td>
<td>bus: 60 min</td>
<td>London (Luton)</td>
<td>Ryanair bus service</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 25 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>London City (LCY)</td>
<td>14 km</td>
<td>20 min</td>
<td>rail: 22 min</td>
<td>Not served by Ryanair</td>
<td></td>
</tr>
<tr>
<td>Manchester</td>
<td>Manchester (MAN)</td>
<td>16 km</td>
<td>15 min</td>
<td>rail: 20 min</td>
<td>Manchester</td>
<td></td>
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<tr>
<td></td>
<td>Liverpool (LPL)</td>
<td>52 km</td>
<td>41 min</td>
<td>rail: 67 min</td>
<td>Liverpool</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Ryanair bus service</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Leeds-Bradford (LBA)</td>
<td>72 km</td>
<td>55 min</td>
<td>rail: 80 min</td>
<td>Leeds Bradford</td>
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<tr>
<td>Birmingham</td>
<td>Birmingham International (BHX)</td>
<td>13 km</td>
<td>15 min</td>
<td>bus: 20-25 min</td>
<td>Birmingham</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 11-17 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>East Midlands (EMA)</td>
<td>64 km</td>
<td>52 min</td>
<td>N/a</td>
<td>East Midlands</td>
<td></td>
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<tr>
<td>Newcastle</td>
<td>Newcastle NCL)</td>
<td>11 km</td>
<td>10 min</td>
<td>metro: 23 min</td>
<td>Newcastle</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Durham Tees Valley (MME)</td>
<td>63 km</td>
<td>52 min</td>
<td>bus+train: 70 min</td>
<td>Durham (Tees Valley)</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Glasgow</td>
<td>Glasgow International (GLA)</td>
<td>15 km</td>
<td>14 min</td>
<td>bus: 25 min</td>
<td>Not served by Ryanair</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 40 min</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Prestwick (PIK)</td>
<td>51 km</td>
<td>45 min</td>
<td>bus: 45 min</td>
<td>Glasgow (Prestwick)</td>
<td>Ryanair bus service</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 44 min</td>
<td></td>
<td></td>
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<tr>
<td>Paris</td>
<td>Paris Charles de Gaulle (CDG)</td>
<td>23 km</td>
<td>31 min</td>
<td>bus: 55 min</td>
<td>Not served by Ryanair</td>
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</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 35 min</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Beauvais-Tillé (BVA)</td>
<td>80 km</td>
<td>60 min</td>
<td>bus: 75 min</td>
<td>Paris (Beauvais)</td>
<td>Ryanair bus service</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>rail: 70 min</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Airport</td>
<td>Secondary Airport</td>
<td>Distance (km)</td>
<td>Time (min)</td>
<td>Service</td>
<td>Notes</td>
<td></td>
</tr>
<tr>
<td>---------</td>
<td>-------------------</td>
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<tr>
<td>Lyon</td>
<td>Lyon St Exupéry (LYS)</td>
<td>25</td>
<td>28</td>
<td>bus: 30 min</td>
<td>Not served by Ryanair</td>
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<td></td>
<td>Grenoble (GNB)</td>
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<td>50</td>
<td>bus: 50 min</td>
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<td>Toulouse Blagnac (TLS)</td>
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<td></td>
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<tr>
<td>Nantes / Rennes</td>
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<td>79</td>
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<td></td>
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<td>46</td>
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<td>Hahn (HHN)</td>
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<td>Hamburg</td>
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<td>9</td>
<td>35</td>
<td>bus: 25 min</td>
<td>Not served by Ryanair</td>
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<tr>
<td></td>
<td>Lübeck Blankensee (LBC)</td>
<td>75</td>
<td>60</td>
<td>bus: 75 min</td>
<td>Hamburg (Lübeck) Ryanair bus service</td>
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<tr>
<td>Vienna / Bratislava</td>
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<td>73</td>
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<td>Barcelona (BCN)</td>
<td>13</td>
<td>26</td>
<td>rail: 17-30 min</td>
<td>Not served by Ryanair</td>
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<tr>
<td></td>
<td>Girona-Costa Brava (GRO)</td>
<td>100</td>
<td>80</td>
<td>bus: 70 min</td>
<td>Barcelona (Girona) Ryanair bus service</td>
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<tr>
<td></td>
<td>Reus (REU)</td>
<td>80</td>
<td>70</td>
<td>bus: 80 min</td>
<td>Barcelona (Reus) Ryanair bus service</td>
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<tr>
<td>Alicante</td>
<td>Alicante (ALC)</td>
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<td>19</td>
<td>bus: 35-40 min</td>
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<td>Murcia San Javier (FCO)</td>
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<td>Murcia (Alicante)</td>
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<td>Bilbao</td>
<td>Bilbao Sondica (BIO)</td>
<td>13</td>
<td>17</td>
<td>bus: 60 min</td>
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<td></td>
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<tr>
<td></td>
<td>Vitoria (VIT)</td>
<td>67</td>
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<td>N/a</td>
<td>Vitoria (Bilbao)</td>
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<td>Tenerife</td>
<td>Tenerife Norte Los Rodeos (TFN)</td>
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<td>12</td>
<td>N/a</td>
<td>Tenerife North</td>
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<td>Tenerife Sur Reina Sofia (TFS)</td>
<td>60</td>
<td>47</td>
<td>N/a</td>
<td>Not served by Ryanair</td>
<td></td>
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<tr>
<td>Rome</td>
<td>Rome Ciampino (CIA)</td>
<td>15</td>
<td>26</td>
<td>bus: 40 min</td>
<td>Rome (Ciampino) Ryanair bus service</td>
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</tr>
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<td></td>
<td>Rome Fiumicino (FCO)</td>
<td>32</td>
<td>32</td>
<td>rail: 31 min</td>
<td>Not served by Ryanair</td>
<td></td>
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<tr>
<td>Milan</td>
<td>Milan Linate (LIN)</td>
<td>7</td>
<td>45</td>
<td>bus: 20 min</td>
<td>Not served by Ryanair</td>
<td></td>
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<tr>
<td></td>
<td>Malpensa (MXP)</td>
<td>50</td>
<td>56</td>
<td>bus: 50 min</td>
<td>Not served by Ryanair</td>
<td></td>
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<tr>
<td></td>
<td>Bergamo (Orio al Serio) (BGY)</td>
<td>45</td>
<td>50</td>
<td>bus: 60 min</td>
<td>Milan (Orio al Serio) Ryanair bus service</td>
<td></td>
</tr>
<tr>
<td>Venice</td>
<td>Venice (VCE)</td>
<td>16</td>
<td>51</td>
<td>water bus: 75 min</td>
<td>Not served by Ryanair</td>
<td></td>
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<td></td>
<td>Treviso (TSF)</td>
<td>20</td>
<td>45</td>
<td>bus: 45 min</td>
<td>Venice (Treviso) Ryanair bus service</td>
<td></td>
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<tr>
<td>Bologna</td>
<td>Bologna Guglielmo Marconi (BLQ)</td>
<td>6</td>
<td>24</td>
<td>bus: 20 min</td>
<td>Not served by Ryanair</td>
<td></td>
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<td></td>
<td>Forli (FRL)</td>
<td>84</td>
<td>60</td>
<td>bus: 85 min</td>
<td>Bologna (Forli) Ryanair bus service</td>
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</tr>
</tbody>
</table>

Table 3: Analysis of the Substitutability of Primary and Secondary Airports (based on European Commission v Ryanair/ Aer Lingus, 2007, p. 82)
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Airfranceklm.com [no date] ................................................................. 2
Barnes, B. (2008) .............................................................................. 3
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European Commission (2013b) ....................................................... 8
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Zeit (2015)...................................................................................... 25


For the first time, Pixar is also scheduled to deliver two movies in a single year: "Brave," the story of a salamander's search for love, and "The Bear and the Bow," an action-adventure starring an impervious Scottish princess; both films will arrive in multiplexes in 2011.

How Disney and Pixar are making the integration work holds lessons for other executives faced with the delicate task of uniting two cultures. Tactics that have served the companies will include the obvious, like effectively communicating changes to employees. Other decisions, including drawing up an explicit map of what elements of Pixar would not be changed, have been more unusual.

"None of this has been easy," said Richard Cook, chairman of Walt Disney Studios, "but it helps when everyone has tremendous respect both professionally and personally for one another."

Mutual respect was sorely at the two companies just three years ago.

Pixar, based in Emeryville, Calif., and Disney, with its headquarters in Burbank, Calif., had a notoriously strained relationship. Pixar's chairman and chief executive, Steve Jobs, abruptly called off talks to continue a lucrative partnership with Disney, which had helped to finance and distribute such Pixar films as "Monsters, Inc."

Mr. Jobs, who, like the chief executive of Apple, had bitterly clashed with Michael D. Eisner, who was then running Disney, had long expressed doubts about the firm's commitment to the films. During the talks, Mr. Jobs had displayed his usual directness, comparing Pixar's situation at Disney to that of a "prisoner of war" in an Asian country.

The end result was that Mr. Jobs and others at Pixar didn't place much faith in what their Disney counterparts told them.

After Mr. Iger took the reins at Disney, he restarted acquisition efforts and won some early support at Pixar by talking candidly and clearly about the lessons he learned when his previous employer, the A.B.C. television network, endured two takeovers. Pixar executives recall Mr. Iger joking that if he ever decided to write a book, it would be titled "I've Been Bought," because the two merger experiences were so formative for him.

Edwin Catmul, the president of Pixar who was also put in charge of Walt Disney Animation Studios, said, "It became very clear to us that Bob Iger had been through mergers before, both positive and negative."

Mr. Iger also agreed to an explicit list of guidelines for protecting Pixar's creative culture. For instance, Pixar employees were able to keep their relatively plentiful health benefits and wasn't forced to sign employment contracts. Mr. Iger even stipulated that the sign on Pixar's front gate would remain unchanged.

Still, Mr. Catmill conceded that trust didn't come easily, especially in an age when some companies promise one thing before a merger and then seem to do another once the deal is done.

"It took about a year before there was a collective letting down the guard," he said. "Initially people were thinking, 'Is something going to happen?'"

Regarding Disney's list of promises, Mr. Catmul said: "We've never had to go back and look at it. Everything they've said and they would do they have done up to." Mr. Jobs, who became Disney's largest shareholder and a board member as a result of the transaction, did not respond to interview requests.

In most acquisitions, the conqueror typically reigns supreme. When NBC bought Universal Studios, executives at the movie studio in Los Angeles were — overnight — required to start commuting to New York for grueling financial planning meetings at the behest of N.B.C.'s owner, General Electric.

Employees were also startled to wake up on the morning after the acquisition announcement to find that their e-mail addresses had already been altered to "ebørn."

An N.B.C. Universal spokeswoman declined to comment. Although analysts generally think that Universal Pictures has been well served by the G.E. takeover, they cited the company's aggressive handling of the merger as one reason the studio's respected chief executive, Stacey Sheriff, quit the company.

But in the Pixar acquisition, Disney, despite its legendary corporate identity and strong will, held back. Pixar kept its e-mail system. Nobody was shipped to Walt Disney World in Florida to work a shift, part of the initiation that other executive must endure. No switchboard operators at Pixar were asked to end telephone calls with the words "Have a magical day," as they do elsewhere in the company.

And, of course, Mr. Lasseter continued to wear whatever he wanted, Hawaiian shirts and all.

In fact, a deep Disney "introduction and visit" didn't come until this spring, when a random selection of 200 of Pixar's 800 employees spent the day in Burbank touring the live-action studio and consumer products division.

"There is an assumption in the corporate world that you need to integrate swiftly," Mr. Iger said. "My philosophy is exactly the opposite. You need to be respectful and patient."

Key to the successful integration, analysts say, has been Mr. Iger's decision to give incoming talent added duties. Instead of just buying Pixar and moving on, Mr. Iger understood what made the acquisition valuable, said Mr. Price, the author. "If you are acquiring expertise," he said, "then dispatch your newly purchased experts into other parts of the company and let them stretch their muscles."
In Disney’s case, Pixar was assigned the difficult task of turning around a storied animation department that had fallen into disrepair as it struggled to find its footing in a new world of computer-generated pictures. At a low point, the 2003 film “Treasure Planet” flopped so badly that Disney was forced to take a $50 million write-down.

A window into how the rebuilding effort is going will come on Nov. 26, with the release of “Ratatouille,” the tale of a Hollywood dog star who becomes lost in New York and has to make his way back to California. Mr. Lasseter and his team have heavily reworked the project, including playing up a wickedly funny side character, a hamster.

Although some bloodletting has been involved in Pixar’s efforts to rebuild the studio — the original director of “Ratatouille” was replaced, resulting in some hurt feelings — Mr. Lasseter said he was pleased with the way the transformation was progressing. “We were very nervous coming in, but to see the change has been amazing,” he said. “Disney has become a filmmaker-led studio and not an executive-led studio. We are very proud of that.”

The relationship could still sour, of course, and big tests loom.

Still very much a work in progress is the turnaround of Walt Disney Animation Studios, where it has taken Mr. Catmull and Mr. Lasseter longer than investors anticipated to sort through the pipeline of existing projects and begin greening-lighting new ones.

Disney’s plans for hand-drawn animation are unclear, with only one project currently announced: “The Princess and the Frog,” a musical set in New Orleans that is scheduled for its premiere in December 2009. A Disney spokeswoman said animators were deeply immersed in mastering older hand-drawn techniques with new technology for future movies, adding that plans for a new headquarters for Disney’s Burbank animators were slowly progressing.

PIXAR’s list of coming movies includes some with unusual concepts that might not lend themselves to the kind of merchandising tie-ins that have made “Cars” a juggernaut. “Up,” the next big Pixar film after “Wall-E,” is a comedy about a cranky, case-waddling 78-year-old who transports his home to exotic locales by attaching hundreds of helium-filled balloons.

With the exception of “Up,” which is being directed by Pete Docter (“Monsters, Inc.”), Pixar is placing some of its biggest new projects in relatively untapped areas. Brenda Chapman, the director of Pixar’s first fairy tale, “The Bear and the Bow,” served as a story supervisor on modern classics like “The Lion King” but has only one previous directing job under her belt, for “The Prince of Egypt.”

Of course, Mr. Lasseter will be helping to guide the way, but he must cope with extreme demands for his time. Aside from overseeing an ambitious slate of movies, Mr. Lasseter, who now Shuttleburs, near Los Angeles, and Emeryville, outside San Francisco, is involved in everything from approving special effects for the coming “Cars” ice tour to helping design theme park attractions.

He also has new corporate responsibilities, from schmoozing with important investors to helping to push Disney’s efforts with high-definition Blu-ray DVDs. All of this juggling, some people say, has made him somewhat inaccessible. One Pixar insider, who requested anonymity because he was not authorized by the company to speak, joked that scheduling a meeting with Mr. Lasseter has become harder than “lining up a shot with the pope.”

Mr. Lasseter, speaking by cell phone during a commuter hour, said: “The toughest part of my job is probably just managing my schedule. But I think everything is going pretty well.” He added that there have been times in the past — such as when he was directing “Cars” — that his walk — around time at Pixar was limited. “It elbs and flows,” he said.

For now, attention is focused on “Wall-E.” Directed and written by Andrew Stanton, the creative force behind “Finding Nemo,” the picture tells the story of a cuddly trash-compacting robot who lives on an abandoned, heavily polluted Earth 700 years in the future. His sidekick is a goofy cockroach named Hal.

“Wall-E,” which features long sequences without dialogue, is under extra pressure to perform at the box office because of such initial receipts for a recent Disney film, “The Chronicles of Narnia: Prince Caspian.” Adding to the weight are Pixar’s last three films; though all were blockbusters, they have gradually trended downward at the domestic box office. A reversal would quiet critics who say the studio’s best days are behind it (Disney notes that an increase in foreign box office sales has offset the slide).

As with “Cars,” Disney is counting on “Wall-E,” set for release on June 27, to take off with a tough crowd: little boys. It has prepared a collection of 300 robot-themed consumer products that will arrive on store shelves over the next month.

“There are some great toys, and we are working on a variety of potential applications for our parks,” said Mr. Iger in a conference call with analysts on May 6. “So we are poised to take advantage of broad and deep success when it comes.”

(He added that he has particularly high hopes for a “Wall-E” remote-controlled robot. “Having played with it, I think it’s going to be a hot seller for Christmas,” he said.)

Wall Street, which closely monitors major animated movies because of their huge cost, is not yet sold on the robot, which was criticized by some as looking too much like the star of the 1996 film “Short Circuit.”

“I can see how it could work and be huge and I can see how it could not,” said Richard Greenfield, an analyst at Pali Research.

By contrast, the competing DreamWorks Animation has received applause for its coming “Kung Fu Panda,” featuring the vocal talents of Jack Black and Angelina Jolie. Ingrid Chang, a media analyst at Goldman Sachs, recently said that she found the film’s concept and execution “strong enough to create a franchise.” When it came to Pixar, Ms. Chang declined to comment.
In order to understand the creation of world champions that merge and acquire, should one look less at what goes on in business and more at the political firms face in global markets?

Let’s consider developments in Aer Lingus between 2006 and 2013. Privatized in 2006, the state nevertheless retained a 25% stake. Since the privatization, Dublin-based Ryanair, led by Michael O’Leary and which now has several other bases throughout the liberalized European economy, made 3 unsuccessful bids for full takeover of Aer Lingus (the last of which was in 2013). The main explanation of Ryanair’s failed takeover bids lies in the role of the Irish state, which wanted the acquisition blocked. It also lies in the role of European Commission’s regulatory authorities in DG Competition that blocked the proposed deals, despite the various remedies proposed by Ryanair. Politics – at the domestic level and at the supranational level in Europe – ultimately mattered.

Now, let’s fast forward to 2015 where IAG is trying to takeover Aer Lingus. With the recent green light indicated by the Irish government on May 26, the deal appears to be set. Yet, beyond the price offered, the Irish state is happy that IAG has given a commitment to the slots in Heathrow and offered a guarantee for smaller airports beyond Dublin that Aer Lingus flies out of (Cork and Shannon). At this stage, the deal is still subject to both other shareholder approval (including Ryanair which owns close to 30% of Aer Lingus) and, perhaps more importantly, regulatory approval of the European Commission. But considering that the Commission has never rejected a deal involving BA/Bea/AEG as examined in the book, it is likely to approve the deal of the ‘trusted friend’ it has in IAG.

To be fair, talented operators who lead firms – such as Willie Walsh of IAG – are important, if not crucial, in explaining firms’ vision for global expansion.

But such leaders who envision having their firms enter into other parts of Europe or the world by merging and acquiring only have to ask three essential questions that have less to do with business and more to do with politics. Do the rules allow for it? Will states facilitate it? And will regulators ultimately approve it?

If the answer to these is ‘yes,’ then it is smooth flying going forward. If the answer is ‘no’ to any of them, expect significant turbulence.

When it comes to IAG’s takeover of Aer Lingus, sit back and relax. It’s unlikely to be a bumpy flight.

Raj Chari is an Associate Professor of Political Science at Trinity College Dublin. He is also the author of Life After Privatization (OUP 2015). Read the introductory chapter, freely available for a limited time.
Miriam Ettel  
An Economic Analysis of the Ryanair/Aer Lingus Merger Case


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**European Commission**

**PRESS RELEASE**

Brussels, 27 February 2013

Mergers: Commission prohibits Ryanair’s proposed takeover of Aer Lingus

The European Commission has prohibited, on the basis of the EU Merger Regulation, the proposed takeover of the Irish-flag carrier Aer Lingus by the low-cost airline Ryanair. The acquisition would have combined the two leading airlines operating from Ireland. The Commission concluded that the merger would have harmed consumers by creating a monopoly or a dominant position on 40 routes where, currently, Aer Lingus and Ryanair compete vigorously against each other. This would have reduced choice and, most likely, would have led to price increases for consumers travelling on those routes. During the investigation, Ryanair offered remedies. The Commission assessed them thoroughly and carried out several market tests. However the remedies proposed fell short of addressing the competition concerns raised by the Commission.

Commission Vice President in charge of competition policy Joaquín Almunia said: “The Commission’s decision protects more than 11 million Irish and European passengers who travel each year to and from Dublin, Cork, Kerry and Shannon. For them, the acquisition of Aer Lingus by Ryanair would have most likely led to higher fares. During the procedure, Ryanair had many opportunities to offer remedies and to improve them. However, those proposals were inadequate to solve the very serious competitive problems which this acquisition would have created on no less than 46 routes.”

Ryanair and Aer Lingus are by far the most important carriers operating out of Ireland. They compete directly on 46 routes. It was the third time that the proposed acquisition of Aer Lingus by Ryanair was referred to the Commission. In 2007 the Commission prohibited Ryanair’s first attempt to acquire Aer Lingus (see COMP/M/1908) and the decision was upheld by the EC General Court (T-199/08). In 2009, the second referral for Ryanair was withdrawn.

The Commission took into account the changes in market circumstances since 2007, for example the fact that the market positions of Ryanair and Aer Lingus have become even stronger, with their combined market shares going up from 55% in 2007 to 87% in 2013 for short haul flights out of Dublin. The number of routes to and from Ireland operated in competition by Ryanair and Aer Lingus has increased from 33 in 2007 to 46 in 2012.

The combination of Ryanair and Aer Lingus would have led to very high market shares on all of these 46 routes:

- On 28 routes the proposed merger would have created an outright monopoly.
- On 11 further routes, the only alleged competitive constraint to the merged entity would have come from charter airlines. However, this constraint would have remained weak because charter airlines have a very different business model.
- Finally, on 7 routes Ryanair and Aer Lingus operate alongside other scheduled carriers. In addition to their very high market shares Ryanair and Aer Lingus are very close competitors - for each other's closest competitors - on those routes. The reason is that the business model of competing scheduled operators tends to focus on bringing connecting passengers to their own network hubs - typical examples are British Airways (to London Heathrow), Lufthansa (to Frankfurt) and Air France (to Paris Charles de Gaulle) – as opposed to the point-to-point connection that Ryanair and Aer Lingus offer.

The proposed merger would therefore have removed the currently vibrant competition between Ryanair and Aer Lingus on all these routes where their activities overlap.

Moreover, the Commission’s investigation confirmed the existence of high barriers to entry stemming, in particular, from Ryanair’s and Aer Lingus’ strong market positions in Ireland. The market investigation showed that there was no prospect that any new carrier would enter the Irish market after the merger, in particular by the creation of a base at the relevant Irish airports, and challenge the new entity on a sufficient scale.

In short, customers’ travelling options would have been substantially reduced and it is unlikely that competitors would have been able to sufficiently constrain the merged entity in its market behaviour. Higher prices for passengers would have been the likely outcome.

**Remedies proposed by Ryanair**

Ryanair offered several sets of remedies during the procedure. The final remedies package consisted mainly of the divestiture of Aer Lingus’ operations on 43 overlap routes to Flybe and the cessation of take-off and landing slots at Big/British Airways at London airports, so that IAG/British Airways would operate on 3 routes (Dublin-London, Shannon-London, and Cork-London). Flybe and Jet2 committed to operate the routes for 3 years. Additional slots divestitures on London-Ireland routes were also offered.

However, the Commission’s investigation demonstrated that these remedies were insufficient to ensure that customers would not be harmed, taking
However, the Commission’s investigation demonstrated that these remedies were insufficient to ensure that customers would not be harmed, taking into account the scope and magnitude of the competition concerns raised by the proposed transactions on the 46 routes. In particular, the Commission found that Flybe was not a suitable purchaser capable of competing sufficiently with the Ryanair/Aer Lingus merged entity. The investigation also showed that SAS/KLM/Iberia would not constrain the merged entity to a sufficient degree and would have little incentive to stay on the routes beyond a 3 year period. In addition, the Commission could not conclude with the requisite degree of certainty that the proposed commitments could actually be put in place in a timely manner. Nor was it certain that they would work in practice and for a sustained period of time.

During the investigation, the Commission gathered views from a large number of market participants in Ireland and internationally, including competitors, customers, travel agents, consumer associations, public authorities and airport operators. The Commission carried out such market tests on Ryanair’s successive remedies proposals three times.

Background
The deal was notified to the Commission for regulatory clearance under the European Union’s Merger Regulation on 24 July 2013. On 29 August 2013, the Commission started an in-depth investigation (see IP/13/617). The deadline for a decision was extended to assess the remedies submitted on 7 December 2013. The parties were informed in the Statement of Objections sent in November 2013 that the merger raised serious concerns and could be prohibited.

Since 2004, the Commission has examined 13 mergers and several alliances in the air transport sector. This decision is the third prohibition. The first prohibition related to the initial attempt by Ryanair to acquire Aer Lingus in 2007. The second prohibition decision was about the proposed acquisition by Olympic Air of Aegean Airlines in 2011 (see IP/11/1108). All the prohibition decisions were related to transactions involving two airlines having large bases at the same “home” airport.

When assessing airline mergers, the Commission first analyses the effects of the proposed transaction on the routes on which both companies operate. In addition, the Commission takes into account whether the merger would affect the possibility of one airline to discipline the other one by entering a certain route at such a moment. Both questions require particular attention when the merging airlines have large bases at the same "home" airport.

Companies and products
Ryanair is a low-fare carrier operating point-to-point scheduled air services essentially in Europe. The company has a fleet of 305 aircraft and 51 bases across Europe, with the most important bases being London Stansted, Bristol Charlottes, Milan Bergamo, and Dublin. In the IAS summer season 2012, Ryanair operated in particular 52 short-haul routes in Dublin.

Aer Lingus is an Irish-based carrier. It offers essentially point-to-point scheduled air transport services. Aer Lingus is based principally at Dublin Airport.

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Merger control rules and procedures
The Commission has the duty to assess mergers and acquisitions involving companies with a turnover above certain thresholds (see Article 1 of the Merger Regulation) and to prevent concentrations that would significantly reduce effective competition in the EEA or any substantial part of it.

The vast majority of notified mergers do not pose competition problems and are cleared after a routine review. From the moment a transaction is notified, the Commission generally has a total of 25 working days to decide whether to grant approval (Phase I) or to start an in-depth investigation (Phase II). There are currently two ongoing phase II investigations. The first one examines the proposed combination of Ryanair and the European label and processing business of Whitemare, in the paper industry (see IP/12/13759), with a deadline on 16 May 2013. The second phase II investigation concerns Ryanair’s project to acquire easyJet in the data housekeeping sector (see IP/12/14589), with a deadline on 30 May 2013.

More information on the case is available at:

See also MEMO/13/144

Contacts:

The transaction was notified to the Commission on 27 May, 2012.

Companies and products:

International Consolidated Airlines Group (‘IAG’) of the United Kingdom, is the holding company of British Airways, Iberia Linhas Aéreas de España S.A. and Vueling Airlines S.A.

Aer Lingus of Ireland is currently mainly owned by the Republic of Ireland and Ryanair, a competing airline. Other significant shareholders include Bidhaa Airways.

Both IAG and Aer Lingus provide air transport for passengers, air transport for cargo, airport ground handling services and landside cargo handling services.

Merger control rules and procedures

The Commission has the duty to assess mergers and acquisitions involving companies with a turnover above certain thresholds (see Article 2 of the Merger Regulation) and to prevent concentrations that would significantly impede effective competition in the EEA or any substantial part of it.

The vast majority of mergers do not pose competition problems and are cleared after a routine review. From the moment a transaction is notified, the Commission generally has a total of 30 working days to decide whether to grant approval (Phase I) or to start an in-depth investigation (Phase II).

The commitments offered by the Parties will be made available as of 26 July under the case number M.7541. More information is available in the Commission’s public case registry on the competition website.

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Regulated public inquiries.
A compromise on the Heathrow guarantees would mark a U-turn for IAG after Mr Walsh’s insistence in February that no new offer would be made. Responding to questions on the pledge from Irish MPs, Mr Walsh said back then: “I can tell you for definite that I am not prepared to increase it.” The IAG boss on Thursday refused to comment.

While a compromise appears within reach, there are a number of hurdles and legal technicalities to be overcome before a formal bid is launched and a takeover could be completed.

It is unclear whether the Irish government will make its acceptance conditional, for example on backing from Ryanair. The low-cost carrier has been ordered to sell its stake by competition authorities but it is still fighting the ruling. While there have been discussions with IAG about a potential sale, Ryanair could still play a role.

The government’s recommendation will also have to be voted on in parliament, which could spark further public controversy. Though political momentum has been moving towards a sale, the ruling coalition is facing an election next year and the government needs to be seen to extract maximum concessions from IAG.

Labour, the junior party in the coalition, also wants to ensure that Aer Lingus unions are on side.

EU competition authorities will also have to clear the bid. Nevertheless Mr Walsh’s comments will be interpreted as a signal that those obstacles can be overcome.

Meanwhile IAG unveiled the airline group’s first operating profit in a traditionally also first quarter since its creation through the merger of British Airways and Iberia of Spain in 2011.

The results reinforced confidence that IAG would meet its forecast to generate an operating profit of more than £550m this year, compared with £353m in 2014. During the three months to March 31, IAG generated an operating profit of £503m, compared with a £353m loss during the same period last year. Revenue rose 12 per cent to £4.7bn.

Fuel costs were 4.5 per cent lower during the first quarter, but Mr Walsh said these were likely to go up in the second quarter due to hedging and currency effects.

IAG shares closed down 2.7 per cent at 543p.

**RELATED TOPICS**
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The owner of British Airways is set to take over Aer Lingus in a deal that values the Dublin-based flag carrier at €1.4bn after the Irish government agreed to sell its stake to International Airlines Group.

Pascal Donohue, Ireland's transport minister, confirmed that the sale of the former Irish state carrier to IAG can now go ahead.

The Dublin government owns 25% of the airline but its agreement, after six months of consideration, was critical for the deal to progress.

Following a Cabinet meeting on Tuesday evening, Donohue said: “IAG has provided additional information and certain commitments in relation to its proposal. Following detailed consideration of this and all of the issues surrounding a potential disposal of the state's stakeholding in Aer Lingus, the government has decided that it will support IAG's proposal.”

IAG has further extended guarantees about routes to Ireland from Heathrow, from five to seven years, although they remain some way short of the decade-long commitment Dublin had sought. The guarantees also are dependent on airport charges being limited to inflation.

Donohue added: “This proposed offer has been the subject of very detailed discussions and negotiations with IAG since the board of Aer Lingus indicated on an informal basis that they are prepared to recommend the offer. The government now...

57 January that it was prepared to recommend the offer. The government has secured important guarantees in respect of Ireland’s future connectivity, particularly to London Heathrow, and on the maintenance of Aer Lingus’ iconic brand and of its head office in Ireland.

“IAG has set out ambitious growth plans for the company and the government is confident that supporting IAG’s offer for Aer Lingus is the best way of securing Aer Lingus’ future in an increasingly competitive global airline market and of enhancing Ireland’s connectivity with the rest of the world and our potential for growth and development into the future.”

Earlier on Tuesday, Aer Lingus chief executive officer Stephen Kavanagh wrote to the minister with some assurances over protecting existing Irish jobs at the airline in the event of the takeover. Kavanagh and the Aer Lingus board had backed IAG’s plans once it took control of the carrier.

Kavanagh told the minister that “the airline’s preference is to continue to use Irish crew bases - provided it continues to be as competitive and efficient as at present - and to only restructure its business when required.”

Later on Tuesday evening, an IAG spokesman confirmed that the takeover was going ahead.

A spokesman for Ryanair, which owns 29% of the shares - but has been told by competition authorities that it must sell down its stake after its own takeover bids were blocked - said the its position remained unchanged. “The board of Ryanair...
were blocked - said the its position remained unchanged. “The board of Ryanair has not received an offer and will consider any offer on its merits, if and when an offer is made.”

The sale of the Irish state’s 25% share in Aer Lingus has been opposed by the two main opposition parties – Fianna Fáil and Sinn Féin – along with a host of left-wing deputies in the Dáil.

Reports in the Irish media earlier on Tuesday suggested that IAG gave the Fine Gael-Labour coalition commitments about routes, regional airports and jobs in its takeover bid. The commitments also include the continued use of Cork and Shannon airports for routes principally to the UK.

There were further claims that IAG had promised to introduce four new transatlantic routes from Ireland creating a further 635 jobs by 2020. SIPTU, the largest trade union at Aer Lingus, had, alongside the Labour party, sought these concessions if it was going to accept the takeover deal.

The 24 landing slots Aer Lingus controls at Heathrow are among the most lucrative for Willie Walsh, IAG chief executive, to capture in the takeover with the Dublin-to-London route the busiest intensity air connection in Europe.

The Dublin route is highly profitable, with a projected 28 million passengers expected to pass through Ireland’s premier airport by 2022.

The takeover would see Walsh again at the helm of the airline where he made his name as chief executive – and started his aviation career as a pilot. He has championed consolidation in the European airline market, and created IAG with the union of British Airways and Iberia in 2011 – with the latter finally turning a profit on the back of a savage cost-cutting and redundancy regime this year. Walsh has since added Vueling, a Spanish low-cost carrier, to the group.
Miriam Ettel  

An Economic Analysis of the Ryanair/Aer Lingus Merger Case

IAG’s bid for Aer Lingus had been conditional on agreement from Europe’s biggest budget airline Ryanair, which holds a 30 per cent stake in Aer Lingus.

“Removing the uncertainty of Ryanair playing kingmaker should be taken positively for IAG shares today. Also positive for Ryanair stock given likelihood over any return to shareholders of up to €400 million,” said Jefferies analyst Mark Irvin-Ferriolence.

Shares in IAG climbed 3.8 per cent to 599 pence in early trade, making the company, which also owns the Iberia and Vueling airlines, one of the top risers on Britain’s bluechip index. Shares in Ryanair were 1.8 per cent higher. Aer Lingus’s were up 2.7 per cent.

Ryanair had fully written down the value of its Aer Lingus stake, built up during several failed takeover attempts of its own dating back to 2006. That means the proceeds, slightly more than Ryanair spent accumulating its stake, will boost its finances.

Minister for Transport Paschal Donohoe welcomed Ryanair’s decision. He said it marked an important development for Aer Lingus that would help secure its future.

Meanwhile, Ryanair on Friday confirmed it will shift its Copenhagen staff to Lithuania next week in response to planned industrial action by Danish trade unions over working conditions.

The unions want Ryanair’s staff in Copenhagen to work under a Danish collective agreement, offering what they say are more attractive conditions than those the airline sets for its workers.

Ryanair, which deployed one aircraft in Copenhagen in March to fly to cities such as London and Cologne, has said previously that its pilots and cabin crew in Denmark enjoy high pay and job security.

The airline has said it would continue to fly out of Copenhagen, but with the aircraft and staff based in Lithuania.

Reuters

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Investigation of the renewed acquisition: The CAT (in August 2012) and the Court of Appeal (in December 2012) both dismissed Ryanair’s challenges and the Supreme Court refused permission to appeal further in April 2013.

Following an in-depth investigation, the Commission prohibited the second proposed acquisition on 27 February 2013 (www.commission.europa.eu/13-962-9723). The CC then conducted its investigation.

CC Findings

In its final report, the CC considered that Ryanair’s minority shareholding of 28.8% had less or may be expected to lead to a substantial lessening of competition between the two airlines on routes between Great Britain and Ireland.

The CC considered that, in light of the importance of scale to airlines, Aer Lingus’s commercial policy and strategy were likely to be affected by Ryanair’s minority shareholding, in particular because it was likely to impede or prevent Aer Lingus from being acquired or combined with another airline.

The CC was also concerned that the minority shareholding might affect Aer Lingus in various other ways, including by giving Ryanair the power to block special resolutions or restrict Aer Lingus’s ability to issue shares and raise capital, and to limit Aer Lingus’s ability to manage effectively its portfolio of Heathrow slots.

The CC considered that the minority shareholding also increased the likelihood of Ryanair utilizing takeover bids for Aer Lingus, which could disrupt Aer Lingus’s ability to implement its commercial strategy.

According to the CC, Ryanair and Aer Lingus compete intensely for passengers traveling between Great Britain and Ireland, and there was a tension between Ryanair’s position as a competitor and its position as Aer Lingus’s largest shareholder. Ryanair had an incentive to weaken Aer Lingus’s effectiveness as a competitor.

The CC considered that the effective and proportionate remedy that would address these concerns was to require a partial divestment of the Ryanair minority shareholding from 28.8% to 5%, facilitated by the appointment of a dissidence trustee.

Consistent with its previous approach in this case, Ryanair has announced that it intends to appeal the CC’s findings.

Implications of the decision

The CC’s findings, and the path that Ryanair has traveled to reach this stage, highlight the difference between the “material influence” test used by the UK competition authorities under the 2002 Act and the “decisive influence” test used by the Commission under the EUMR.

While it is relatively easy for minority shareholders to give rise to material competition concerns, the UK material influence test may be satisfied by a lower level of control than “decisive influence” and therefore allows the assessment of such interests by the UK competition authorities.

The CC’s decision also comes at a time when the Commission is consulting on options for the possible widening of its powers to allow for the review of certain non-controlling minority shareholdings (www.competition.law/9.524-9349). This is based on the Commission’s view that, in some specific instances, the acquisition of a non-controlling stake can harm competition and consumers, for example, by reducing the acquirers’ incentives to compete because it weakens the target’s profits.

Aer Lingus is a partner, Gwira Wilmot is a senior associate, and Chandima Ghoosh is an associate, at Clifford Chance LLP.

Decisive vs material influence tests

Under the EU Merger Regulation (139/2004/EC) (EUMR), the European Commission has the power to review transactions that lead to the acquisition of direct or indirect “control” over an undertaking. For control, it is sufficient that one party acquires the possibility of exercising “decisive influence” over the other undertaking concerned (Articles 7 and 8, EUMR). This may arise by the ownership of all or the majority of the company’s voting rights or assets, or of rights that confer decisive influence on the strategic decision-making process of the company such as vote rights over the budget or business plan.

In contrast, under the UK material influence test, the authorities focus on the acquirer’s ability materially to influence policy relevant to the behaviour of the target in the marketplace. This includes the management and strategic direction of the business, and its ability to define and achieve its commercial objectives. Material influence can arise, for example, through minority board representation or a voting interest as low as 10% to 15%.
Miriam Ettel        An Economic Analysis of the Ryanair/Aer Lingus Merger Case

Creating a bigger Irish airline group with significant investment and employment plans, could go down well with some people in recession-battered Ireland.

Aer Lingus has some obvious attractions to Ryanair. Christoph Mueller has made progress with the carrier’s turnaround since he became chief executive in 2009, when it was loss-making. Last year Aer Lingus reported pre-tax profit of €34.4m and at March 31 had a net cash position of €445.9m.

But while Aer Lingus is profitable, it looks sub-scale in the context of industry consolidation. By combining with Ryanair, Aer Lingus would secure its long-term future, with the budget airline able to apply its cost-cutting expertise across the enlarged group.

Mr O’Leary says Ryanair and Aer Lingus would operate as two separate brands. Aer Lingus would focus on short-haul routes to large European airports that Ryanair does not fly to, such as London’s Heathrow.

There are risks for Ryanair. Some of Aer Lingus’s cash may be needed to fix large deficits in two pension schemes that the carrier’s current and former employees are members of.

Of more immediate concern will be the attitude of the Irish government and the competition authorities.

Ryanair’s new bid might have some appeal in Dublin, given it was priced at a 38.3% premium to Aer Lingus’s undisturbed share price on June 19.

The government has a 25% stake in Aer Lingus, which it is planning to sell under the terms of the Irish bailout agreed with the European Union and the International Monetary Fund.

But Enda Kenny, the Irish prime minister, on Wednesday expressed concerns about the anti-competitive issues raised by Ryanair’s bid, although he stressed the government did not have a veto.

Ryanair has notoriously poor relations with the Commission, which mainly assesses airline mergers on a route by route basis to see if competition will be diminished.

Andrew Lobbenberg, analyst at HSBC, highlights how Ryanair and Aer Lingus together operate 79% of long-haul departures from Dublin airport.

Gerald Ronan, analyst at Espirito Santo, says Ryanair’s offer may have reduced the risk that it is forced to make a distressed sale of its stake in Aer Lingus; the UK Competition Commission could delay its new investigation into the sharing of the bid.

He adds that even if the bid fails, Ryanair may well get a better exit from Aer Lingus if it flashes out an alternative bidder.

But apart from Ryanair, it is difficult to see who would pursue a takeover of Aer Lingus. Air France-KLM, IAG and Lufthansa are seen as unlikely suitors.

Etihad, the fast-growing Abu Dhabi-based carrier that announced last month it had bought a 3% stake in Aer Lingus, has held talks about buying the Irish government’s stakeholding. But foreign ownership rules are likely to prevent Etihad from having a controlling stake in Aer Lingus.
The proposed €2.36 billion takeover of Aer Lingus by IAG, the parent company of British Airways and Iberia, has cleared its last major obstacle after the European Commission conditionally approved the deal yesterday evening.

IAG has committed to offering for sale five pairs of landing slots at London Gatwick, specifically for flights to Dublin and Belfast, to get the deal over the line. IAG has also promised the commission it will enter into agreements with IAG’s long haul rivals to maintain route link-ups with Aer Lingus’s network.

The commission said it had concerns that the original terms of the merger would have lead to “insufficient competition on several routes”, including Dublin-London, Belast-London and London-Dublin. It said it also feared that IAG might try to prevent Aer Lingus from connecting its flights with those of IAG’s long haul rivals. Since the deal was first notified to the commission on May 23rd, however, IAG returned with specific competition remedies proposals to sway Margrethe Vestager, the competition commissioner, to rubber stamp the merger.

“By obtaining significant concessions…the commission has ensured that air passengers will continue to have a choice of airlines at competitive prices,” said Mr Vestager.

Under the terms of the approval, the merged IAG Aer Lingus will have to offer for sale the five Gatwick slot pairs, although it is understood these will not necessarily be existing Aer Lingus slots. Iberia and British Airways, both owned by IAG, also own Gatwick slots. The commission has stipulated that whoever buys the slots will have to consult to see them for flights to Dublin and Belfast.

Aer Lingus and IAG confirmed to the stock market last night that at least two of the slot pairs must be used for flights to Dublin, while one must be used for Belfast. Aer Lingus shareholders are to vote tomorrow to approve measures designed to facilitate a commitment to the Government that connectivity will be maintained between Dublin and London Heathrow.

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