

(1) Overview

Vertical relationships are those that involve an exchange between sequential stages of the value chain. Vertical integration can promote efficiency by eliminating successive monopoly mark-ups, internalizing service and mitigating contractual problems between firms. Adding to this, it can facilitate the strategic practice of market foreclosure, whereby an integrated firm denies a rival access to markets in order to gain greater market power. The first effect results in lower prices, higher traded quantities and greater consumer welfare while the second raises the prices of final goods, thereby harming consumers.

Mergers between gas and electricity companies, actual or attempted ones, seem to have been of late fashionable in the European Union. Energy mergers pose distinctive challenges for competition policy - in market definition and for modelling price impacts in markets with no storage, inelastic short run demand and transmission constraints.

Three very large mergers have captured headlines throughout the EU and drawn attention to how energy and, in particular, gas and electricity markets, function across the Union: the Takeover Bid of Endesa by Gas Natural (Spanish Regulator), the serious competition concerns about the EON-Ruhrgas merger, controversially cleared by the Ministry of economics (Germany Federal Cartel Office and Monopolies Commission) and the acquisition of GDP by EDP blocked by the EU Commission are recent examples.

The aim of my research is to empirically examine the effects of vertical integration between gas suppliers and electricity generators in order to understand the implications for European final consumers. These integration processes have raised concerns among anti-trust authorities that consumers may be harmed. Knowing this answer is vital for public policy on European energy market. There is one concern related with the best way to develop the merger policy in order to reach the European aim of full integration of energy markets.

There is no presumption in economics against the merger of large gas and electricity companies. Economic theory and evidence do not justify claims suggesting that the combination of two large companies is necessarily bad for consumer welfare (Williamson, 1968). Furthermore, economists view with suspicion claims suggesting that mergers between companies producing and commercializing products that are largely complementary (such as gas and electricity) are anti-competitive. The convergence between both industries has attracted some academic work. The empirical

records is, however, quite thin and much more analysis is needed to better assess the potential risk to competition from vertical mergers involving natural gas and electricity. The paper is organized as follows. After the introduction, section 2 reviews the relevant theories and the previous empirical studies of vertical integration and on mergers between gas suppliers and electricity generators. Section 3 describes the structure and evolution of EU energy mergers and merger policy. Section 4 describes the econometric method and data. The results are shown in section 5 and section 6 concludes the paper and gives suggestions for future research and extensions.

(2) Methods

Therefore, in this study we are interested on the average effect of the vertically integration on market outcome (prices and quantities traded). We focus on all the merger cases between 1997 and 2007 and use panel data on all the electricity final markets in Europe (for households and industrial consumers). This is opposed to some previous studies, which make use of cross sectional data. The treatment event considered is having a merger or not in the electricity - gas market. Each European market is considered as an individual and, therefore, some individuals are treated (there are mergers in the market) and some others are not.

The decision to vertically integrate or not (having the treatment) depends on the characteristics of the market, an endogeneity problem arises. For this reason we adopt a non-experimental strategy to estimate the average treatment effect of the merger.

(3) Results and Conclusions

The neoclassical efficiency theory predicts lower prices and higher quantities traded in downstream markets. Along with the results of Chipty (2001) and Waterman and Weiss (1996) our findings suggest that there is little evidence that European consumers are harmed by vertical integration between gas suppliers and electricity generators. Although each merger process has specific characteristics that can determine the final effect on market outcome so European competition regulators should be vigilant and there's scope for the role of regulation in these markets.

References

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