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Highlights

Highlights of GAO-10-778T, testimony before the Committee on Commerce, Science, and Transportation, U.S. Senate

AIRLINE MERGERS

Issues Raised by the Proposed Merger of United and Continental Airlines

Why GAO Did This Study

Earlier this month, United Air Lines (United) and Continental Airlines (Continental) announced plans to merge the two airlines and signed a merger agreement. This follows the acquisition of Northwest Airlines by Delta Air Lines (Delta) in 2008, which propelled Delta to become the largest airline in the United States. This latest merger, if not challenged by the Department of Justice (DOJ), would surpass Delta's merger in scope to create the largest passenger airline in terms of capacity in the United States. The passenger airline industry has struggled financially over the last decade, and these two airlines believe a merger will strengthen them. However, as with any proposed merger of this magnitude, this one will be carefully examined by DOJ to determine if its potential benefits for consumers outweigh the potential negative effects.

At the Committee's request, GAO is providing a statement for the record that describes (1) an overview of the factors that are driving mergers in the industry, (2) the role of federal authorities in reviewing merger proposals, and (3) key issues associated with the proposed merger of United and Continental. To address these objectives, GAO drew from previous reports on the potential effects of the proposed merger between Delta and Northwest and the financial condition of the airline industry, and analyzed Department of Transportation (DOT) airline operating and financial data.

View GAO-10-778T or key components.
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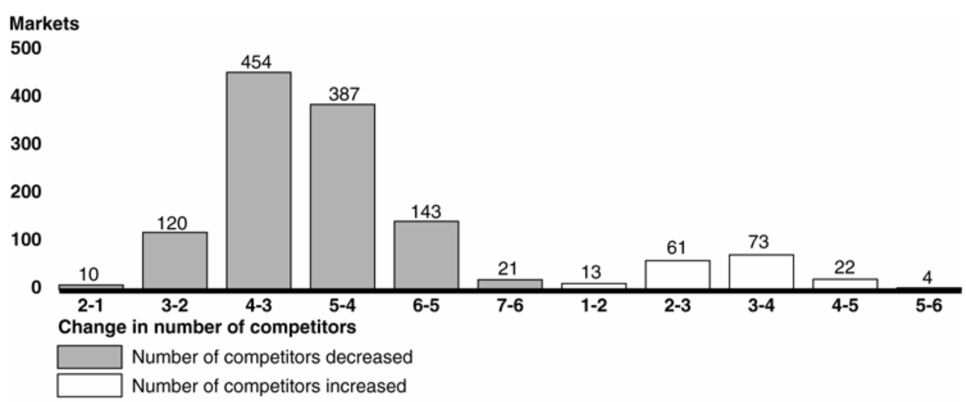
What GAO Found

As GAO has previously reported, airlines seek to merge with or acquire other airlines to increase their profitability and financial sustainability, but must weigh these potential benefits against operational costs and challenges. The principal benefits airlines consider are cost reductions—by combining complementary assets, eliminating duplicate activities, and reducing capacity—and increased revenues from higher fares in existing markets and increased demand for more seamless travel to more destinations. Balanced against these potential benefits are operational costs of integrating workforces, aircraft fleets, and systems.

DOJ's antitrust review is a critical step in the airline merger and acquisition process. DOJ uses an integrated analytical framework set forth in the *Horizontal Merger Guidelines* to determine whether the merger poses any antitrust concerns. Under that process, DOJ assesses the extent of likely anticompetitive effects of reducing competition in the relevant markets—in this case, between cities or airports. DOJ further considers the likelihood that airlines entering these markets would counteract any anticompetitive effects. It also considers any efficiencies that a merger or acquisition could bring—for example, consumer benefits from an expanded route network. Finally, it examines whether one of the airlines proposing to merge would fail and its assets exit the market in the absence of a merger.

One of the most important issues in this merger will be its effect on competition in the airline industry. For example, GAO's analysis of 2009 ticket data showed that combining these airlines would result in a loss of one effective competitor (defined as having at least 5 percent of total traffic between airports) in 1,135 markets (called airport pairs) affecting almost 35 million passengers while creating a new effective competitor in 173 airport pairs affecting almost 9.5 million passengers (fig.). However, in all but 10 of these airports pairs there is at least one other competitor.

Change in Effective Competitors for Airport-Pair Markets from United-Continental Combination, 2009



Source: GAO Analysis of DOT Origin and Destination Ticket Data.