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The valuation effects of antitrust legislation

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The authors observe that, in theory, the relationship between antitrust laws and firm value is ambiguous. One perspective, known as the “agency view,” suggests that firms hit by antitrust laws would be forced to improve their governance structures and practices, eventually increasing their market value. The idea here is that, by exposing organizational inefficiencies such as informational opaqueness and management rent-seeking practices, a healthy level of competition would encourage reform that brings value to shareholders. Just as intuitive, however, is the opposite expectation, namely, that firms exposed to greater competition would see their valuations drop. As explained in the article, the burdens imposed by competition may reduce a firm’s market share, monopolistic rents, investment in research and development, and overall revenue and profits.

To assess these rival hypotheses, the authors rely on a large panel dataset—in their estimation, the largest ever compiled in the literature on antitrust laws—containing two decades (1990–2010) of information on 90 countries and 22,000 firms. The key independent and dependent measures in the data are, respectively, the Competition Law Index, which measures the prevalence of antitrust laws that limit monopolistic practices, and Tobin’s Q, a firm valuation measure reflecting the type and size of firm assets. To account for potentially confounding causal mechanisms, the authors’ regression models also include various control variables, as well as firm and industry fixed effects.

The baseline regressions show a statistically and economically significant positive relationship between competition laws and firm value. Although this result provides some preliminary support for the agency view, it does not corroborate the specific causal mechanisms proposed by that view. To see whether these mechanisms operate in practice, the authors conduct additional statistical analyses, each based on a separate corollary hypothesis derived from the agency view. These analyses provide further support for the valuation-boosting effects of antitrust legislation, showing that these effects are (1) stronger among firms with more severe preexisting governance problems and (2) weaker in industries with a high level of preexisting firm competition. In addition, the authors find that, also consistent with a mechanism implied by the agency view, competition laws improve firm operational efficiency, especially in countries with weak investor protections.