

“Unbundling” search engines

The upcoming resolution calling for the “unbundling” of search engines from other commercial activities raises serious concerns from the perspectives of competition policy, innovation, economic growth and the rule of law.

While Google holds a 90 per cent share of all EU searches and 31 per cent of worldwide online advertising revenue, this says little about the degree of competition in the search engine market, where rivals are just one click away. The sharp rise in the share of online ad revenues of new players such as Facebook and Twitter illustrates the dynamism of this market.

Unbundling would severely curtail the ability of search engines to innovate while also raising barriers to entry to new players and discouraging investment in the digital sector.

Unbundling would undermine the rule of law, singling out one company and justifying unprecedented intervention on the basis of a range of different issues with disparate policy implications.

Recommendation: Given the lack of evidence of anti-competitive behaviour in the search engine market, action by the European Commission is unjustified. “Unbundling” will harm innovation, economic growth and the rule of law in the EU.

The so-called “unbundling” of search engines from other commercial activities, as proposed in an upcoming resolution to be voted on by the European Parliament the week of 24th November 2014,ⁱ raises serious concerns from the perspectives of competition policy, innovation, economic growth and the rule of law. If taken on board by Member States and the European Commission, the resolution would endanger the development of the Digital Single Market, while extending anti-trust regulation beyond its proper scope and setting a dangerous precedent of unequal treatment before the law.

Competition policy

The motion notes “vulnerabilities brought about by excessive market concentration and dominant operators” in the Digital Single Market (DSM). It further calls on the Commission to “prevent excessive market concentration and abuse of dominant position [...] with regard to bundled content and services” noting “the potential development of search engines into gatekeepers and their possibility of commercialising secondary exploitation of obtained information.” As a solution, the movers call on the Commission “to consider proposals [to unbundle] search engines from other commercial activities.”

There are indeed high levels of market concentration in the search engine business, with Google holding a market share of over 90 in most EU Member Statesⁱⁱ and 88 per cent worldwide for both mobile and desktop users.ⁱⁱⁱ Google is also a leader in online advertising revenues, with a 31 per cent share which has remained roughly stable since 2012.^{iv}

However, market share only gives a partial picture of the competitive outlook in a market, and a highly distorted one at that. The fact remains that there are few lock-in effects in the search engine market and that alternative search providers are literally “just one click away.”^v Given the extremely low costs of switching and the existence of a range of alternative providers, it is hard to argue that Google’s market dominance stems from anti-competitive behaviour.

Moreover, it should be stressed that the digital sector, arguably more than any other, is subject to swift dynamic pressures and dramatic reversals in the position of established players. The case of Microsoft is illustrative in this regard: a favourite target of anti-trust bodies due to its dominant position in software,^{vi} it is now struggling to contain the fall in its market share as a result of the rise of smartphones only a few years later.^{vii} In the online advertising market, it is worth noting that newer players such as Facebook, Twitter and Amazon, while starting from a low base, have sharply increased their share of global online advertising revenue in just two years.^{viii}

Despite Google’s dominance, Twitter and Facebook have sharply increased their share of online ad revenue in two years.

Another issue raised in the motion is the potential for discrimination in search results which would undermine the diversity of sources of information on the internet. While the business of search engines by definition involves partiality in the selection and ranking of results in order to provide customers with the information they are looking for as seamlessly and quickly as possible,^{ix} the best way to ensure diversity of sources and consumer choice is to have a dynamic and competitive search engine market, which, as argued above, appears to exist. In that regard, it should be pointed out that

a wide variety of horizontal and vertical search engines are currently available to users and a growing share of searches can now be made through mobile apps, social networks and e-commerce platforms, among others.

Until and unless it becomes apparent that a dominant player in the search engine market is using its position for anti-competitive purposes, there will be no grounds for anti-trust action against it. The mere fact that one provider holds a 90 per cent share of the search market does not justify intervention by EU authorities.

Innovation and economic growth

Securing a thriving digital sector is one of the key priorities of the new European Commission, as evidenced by the Digital Agenda for Europe and as stressed by Commission President Juncker.^x Moreover, as the resolution notes, a fully developed Digital Single Market (DSM) can play a major role in economic growth across the EU by improving the efficiency and productivity of business and enabling the development of e-commerce and other innovative commercial activities.

Yet, the resolution as it currently stands would hardly promote the goals of expanding the DSM and encouraging innovation. Indeed, unbundling search engines from their other commercial activities, notably online advertising, would damage the sector by separating search engines from their main source of revenue. In order to offer an ever-improving customer experience, with more accurate search results and a wider range of options that better reflect consumer preferences, search engines rely on the economies of scale and scope provided by their ability to offer a wide range of services including advertising. Removing their ability to engage in such commercial activities would curtail their ability to do so.

Unbundling search engines will reduce innovation and the incentive for new players to enter the market.

In addition to the direct impact of unbundling on established search providers, one should consider the effect on future market entrants and other digital businesses. For the former, unbundling would reduce the incentive to enter the search engine market, given the diminished prospects to turn such activity into a profit-making enterprise. Reduced incentives for new entrants would in turn have a clear negative effect on the competition and dynamism of the search engine market. For other digital businesses, the precedent of EU authorities' ruling to separate search services from other activities would not only raise the risk of investment in a sector which is already known for being subject to significant disruption, but it would also hamper cross-subsidisation across different undertakings within the same business, a process which in the past has been critical to sustain loss-making innovations until they became profitable.

Given the current fragility of the European economy and the potential of the digital sector to spur economic growth and promote innovation, the motion's call for the unbundling of search engines would be a step in the wrong direction.

The rule of law

Transparency, a reliable institutional framework and the equal treatment of all before the law are crucial factors for the prosperity of any economy – this is true for the digital sector as much as for any other. However, the motion currently before the Parliament is hardly a case of the rule of law at work. For one, it singles out in all but name one dominant market player (Google) for action by the European Commission. And it does so by putting forward a varied set of arguments, from data protection to the development of the DSM to search engines' alleged abuse of market power, each with very different policy implications. Yet, without justification on the part of the movers, the proposed solution is one and the same: action by the European Commission to separate search engines from other commercial activities.

While each of the proponents' claims deserves consideration by the Commission (although the accusation of market-power abuse is, as argued above, doubtful at best), suggesting that all the problems currently faced by the DSM can be addressed by unbundling is implausible. Indeed, considering the controversy that has surrounded the digital sector on a number of different fronts (privacy, tax, competition) in recent years and months, it would seem that the resolution is motivated more by a political desire to punish certain companies and industries than by serious concerns about competition. To use the movers' own language, the various different arguments need to be unbundled and each of the claims considered independently to avoid unjustified action on the part of the Commission that would harm the DSM and undermine the rule of law across the EU in the process. The concerns do not stop at EU level, as any action by the Commission endorsing the movers' claims is likely to guide subsequent policy decisions by Member States.

Conclusion

There is little to be gained in terms of increased competition in the Digital Single Market through the unbundling of search engines from other commercial activities. At the same time, there is much to be lost as far as the dynamism of the European digital sector, its ability to innovate and help the growth of other sectors, and the rule of law in the EU are concerned.

Unbundling will undermine the very goals of competition, innovation and economic growth that the Parliament and the Commission have set out to achieve.

ⁱ <http://online.wsj.com/public/resources/documents/DSMresolution.pdf>

ⁱⁱ <http://returnnonnow.com/internet-marketing-resources/2013-search-engine-market-share-by-country/>

ⁱⁱⁱ <http://www.statista.com/statistics/216573/worldwide-market-share-of-search-engines/>

^{iv} <http://www.emarketer.com/Article/Microsoft-Surpass-Yahoo-Global-Digital-Ad-Market-Share-This-Year/1011012>

^v Istituto Bruno Leoni, "Comments on Google's revised proposed commitments text of 21 October 2013 (COMP/AT.39740)," submission to the European Commission.

^{vi} Cf. Institut Economique Molinari, "Five myths about the dearth of competition in the presence of 'dominant firms': The Microsoft example," Economic Note, May 2007, and "Does the tying and bundling of products harm consumers?," Economic Note, March 2006.

^{vii} <https://gigaom.com/2014/08/15/should-microsoft-be-worried-about-windows-phones-falling-market-share/>

^{viii} <http://www.emarketer.com/Article/Microsoft-Surpass-Yahoo-Global-Digital-Ad-Market-Share-This-Year/1011012>

^{ix} Massimiliano Trovato, "Google and antitrust: No evidence found," IBL Focus 220 (Milan: Istituto Bruno Leoni, 2013), 2-3.

^x http://ec.europa.eu/about/juncker-commission/docs/ansip_en.pdf and http://ec.europa.eu/about/juncker-commission/docs/oettinger_en.pdf

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