

# NSR Tech Policy: MSFT-ATVI: The Case

By [Matt Perault](#) | February 26, 2023

Microsoft's (MSFT) bid to purchase gaming company Activision (ATVI) for \$68.7 billion has the potential to shape both the future of gaming and competition in the metaverse. It has the potential to dictate new rules for mergers in the tech sector. And if it closes, it has the potential to advantage MSFT relative to rivals like Google, Apple, and Sony.

For those reasons, it has attracted the attention of antitrust authorities throughout the world, and key authorities on both sides of the Atlantic have expressed concerns about the deal. In light of the implications of the transaction, and the risks that the deal could be blocked or significantly conditioned, we are publishing a five-part series on regulatory review of the Microsoft-Activision merger.

Today, in the first note, we look at the **case**, providing an overview of the key issues that will be litigated. We examine the policy and product context, the status of regulators' reviews, the key concerns raised by regulators, the legal standard in the US, UK, and Europe, and how "litigating the fix" could affect the final result.

Over the course of the rest of this series, we will examine other key aspects of how regulators will review the deal. In the second note, we will examine the **global landscape**, looking at international regulators' review of the merger. Our third note will explore the **judge**, looking at the FTC's decision to pursue the case in the FTC's in-house administrative court, rather than in federal court. In the fourth note, we will focus on the **company**: how will Microsoft respond to the concerns raised by regulators? In our final note, we will provide our view of the most likely **outcome** in the case.

## Bottom line:

- Regulators are concerned that if MSFT acquires ATVI, it will be able to withhold or degrade ATVI content from rival consoles, like PlayStation, or rival subscription or streaming services.

- In response, MSFT and ATVI argue that they have a financial incentive to make ATVI content widely available and that they want to avoid the “reputational hit” they’d take if they degrade the content. They argue that the deal will result in wider availability of ATVI content at lower prices.
- If the case goes to trial in the United States, the judge will consider the case in light of any formal concessions that MSFT makes, which is known as “litigating the fix.”
- Here, “litigating the fix” will likely benefit MSFT, since its concessions will likely address a significant portion of regulators’ concerns about the deal.

#### **Product and policy context:**

As we noted in “M&A in the Metaverse” ([LINK](#)), the merger of MSFT and ATVI has implications for gaming, for competitive dynamics between several different industries, and for competition in the metaverse.

If the merger is successful, it will change the playing field for the rapidly growing gaming sector, which has exploded from 200 million gamers 15 years ago to 2.7 billion today. It is a sector in which every one of the Big Tech entities – Alphabet, Amazon, Apple, Meta, and Microsoft – has a stake. And it is a sector that implicates both existing players, like Sony, and other industries, like ISPs. A successful merger would also likely change the playing field for the “metaverse” where, again, Big Tech and many smaller players are making big bets.

The acquisition points to new frontiers in gaming. MSFT has emphasized the importance of the deal for its mobile gaming business, which it claims is the fastest-growing segment of gaming. The deal is also driven by MSFT’s interest in subscription services and cloud gaming. Subscription services allow users unlimited access to a library of games for a monthly fee.

Cloud streaming services allow users to play games hosted on web servers rather than their own local machines. Cloud gaming has the potential to allow gamers to play cutting-edge games without having to purchase cutting-edge hardware. Some services, such as the most expensive tier of Microsoft’s Game Pass, combine streaming and subscription services. While these services remain small compared to one-off purchases, some see great potential in streaming services that could do for gaming what Netflix has done for video.

As we noted previously, this case is the most significant opportunity to date for US antitrust regulators to showcase a governance agenda that matches their prior advocacy on merger policy ([LINK](#)). The MSFT-ATVI deal occurs against the backdrop of efforts by FTC Chair [Khan](#) and the Justice Department's Jonathan [Kanter](#) to reform how regulators review both vertical and horizontal mergers.

The confluence of these two words – product and policy – are shaping how regulators review the case, and will also shape its outcome.

### What is the status of regulators' reviews?

- Four countries have already approved the deal: Serbia, Chile, Saudi Arabia, and Brazil.
- The UK announced it would pursue a Phase 2 investigation of the deal on September 15. On February 8, ahead of releasing the final results of this investigation, the [CMA released](#) its provisional findings, including a [notice](#) of possible remedies. It also signaled, however, that it would consider behavioral remedies as well, including one related to long-term access arrangements. It is expected to release its final report and determination on April 26th, 2023.
- The European Commission [announced](#) it was opening an in-depth investigation of the deal on November 8th. While [Politico](#) recently reported that the regulator issued a formal antitrust warning and shared a “statement of objections” with MSFT, neither has been released publicly.
- The FTC [sued](#) to block the merger on December 8. It filed the case in its in-house administrative court. We will examine the implications of this decision in our third note. The administrative hearing is [scheduled](#) to begin August 2, 2023.
- As we will detail in our next note, the deal remains under review in a handful of other jurisdictions, including [Japan](#), [South Korea](#), [Australia](#), [New Zealand](#), and [China](#).

### What are regulators' concerns and MSFT's rebuttals?

The FTC's [Complaint](#) includes a list of its concerns about the impact the deal could have on competition, and the UK's provisional [report](#) raises similar issues. We summarize those concerns here.

Complaint 1: MSFT could fully withhold ATVI content from rivals.

- The FTC argues that as a standalone company, ATVI is incentivized to make its games as available as possible across consoles and services in order to maximize revenue. Post-merger, the combined company may have the incentive to make top-shelf games, also called AAA games, exclusive to the Xbox or Xbox Game Pass in order to build demand for new consoles or subscription services.
- The FTC and CMA both observe that the most popular games, such as ATVI's *Call of Duty* franchise, are key to building demand for new consoles or subscription services.

*MSFT's response:*

- MSFT and ATVI have responded that a single AAA franchise, or even the entirety of ATVI's library, could not drive console or subscription service adoption. Moreover, MSFT argues that the economics of the acquisition require that ATVI content remain as accessible as possible: "Xbox cannot afford to take Activision's games exclusive without undercutting the basic economics of the transactions." Note that AT&T successfully raised similar issues in defending its acquisition of Time Warner.
- Finally, MSFT notes that it has already offered to keep *Call of Duty* games available on Sony and to extend availability to Nintendo. On February 21, MSFT announced that it had "signed a binding 10-year contract" with Nintendo to offer *Call of Duty* to Nintendo users "the same day as Xbox, with full feature and content parity."

Complaint 2: MSFT could limit or impair access to content for competitors.

- The FTC expressed concern that even if MSFT provides rival consoles or subscription services access to ATVI content, they could still limit or impair access to that content.
- Specifically, MSFT could adjust price, timing, or content availability in ways that would disadvantage competitors. MSFT could make ATVI more expensive on rival consoles or services. They could delay the release of games on rival platforms, giving Xbox or Xbox Game Pass users advance access to AAA games. MSFT could also reserve extra exclusive content for the Xbox or Game Pass.

*MSFT's response:*

- MSFT argues the deal will make games more affordable and accessible to consumers. Currently, ATVI does not provide its games to any subscription service. They contend that allowing ATVI content onto Xbox Gaming Pass will give users a new path to accessing their content, potentially at a lower price.

Complaint 3: MSFT could degrade the quality of ATVI content for competitors.

- The FTC argues that following the deal, MSFT and ATVI would also have an incentive to degrade graphics resolution, speeds, latency, or other technical specifications of ATVI games on competitors' platforms or services.
- They could degrade quality by intentionally reducing game performance or by not collaborating with Sony engineers to optimize games for PlayStation products.

*MSFT's response:*

- In response, MSFT argues that degrading gaming experience would result in a “reputational hit” and “alienate the millions” of gamers on competitors' consoles.

Complaint 4: MSFT could use it's broader ecosystem to “raise barriers to entry and ultimately foreclose rivals” in cloud gaming.

- The CMA argues that as the market for cloud services is “at an early state of development,” MSFT could gain an advantage over rival services by integrating ATVI content with Azure or Windows. Its market position with the Azure cloud platform and Windows operating system could enable it to strengthen “network effects” and foreclose the ability of rivals to compete.

*MSFT's response:*

- In its response to the CMA, MSFT argues that gamers could easily switch to alternate services or

subscribe to multiple services because cloud gaming does not require users to make a large upfront investment in hardware. As a result, network effects and barriers to entry are not significant concerns.

Complaint 5: MSFT is likely to attempt to lessen competition, even if it makes commitments to the contrary.

- The [FTC](#) argues that MSFT's past practices suggest that it will renege on public commitments after the acquisition closes.
- It claims that after “disavowing the incentive to make ZeniMax content exclusive” to EU regulators ahead of MSFT acquisition of ZeniMax, MSFT now plans to make three new ZeniMax titles exclusive to Xbox and Xbox Game Pass.
- The FTC argues this example should “cast more suspicion on its non-binding public commitments to keep *Call of Duty* available on PlayStation consoles through the end of Activision's existing agreement with Sony.”

*MSFT's response:*

- MSFT has [committed](#) to make its commitments legally enforceable.
- [MSFT](#) and [ATVI](#) also distinguished the ZeniMax case by saying that they never made binding commitments to the EU regarding all ZeniMax content. Rather, they note that all ZeniMax titles discussed with EU regulators ahead of the acquisition have been made available on the PS5. They contend that the three titles they will make exclusive are new games that were not discussed in the acquisition negotiations.
- Interestingly, in a statement to an [Axios reporter](#), one EU official pushed back on the FTC's version of events. The official noted that “Microsoft did not offer any commitments to the Commission,” and the Commission had approved the deal unconditionally.

### **The legal standard**

The law on merger review in the three key jurisdictions reviewing the deal will help to shape the final outcome. The laws in the US, UK, and Europe are similar, with the US and UK both prohibiting mergers that

“substantially lessen” competition and the EU prohibiting mergers in which competition is “significantly impeded.”

- US law prohibits a merger where the effect “may be substantially to lessen competition, or to tend to create a monopoly.”
- UK law prohibits a merger that “has resulted, or may be expected to result, in a substantial lessening of competition within any market or markets.”
- EU law prohibits a merger that “creates or strengthens a dominant position as a result of which effective competition in the common market or in a substantial part of it would be significantly impeded.”

#### “Litigating the Fix”

The legal standards in each jurisdiction will serve as the foundation for how each one will evaluate the case. But one critical component of the evaluation will be what permutation of the deal they review. Specifically, will judges and regulators consider MSFT’s commitments as part of the analysis of whether the deal will lessen competition?

The answer is yes, due to a practice known as “litigating the fix.” Litigating the fix means that if MSFT makes a concession to try to address a regulators’ concerns about the deal, a judge will review the merger as if that concession is a part of it. The term is used in the US context, but similar evaluations occur during the merger review process in the UK and the EU.

MSFT has already offered several concessions that will be litigated as part of a “fix.” For instance, it offered to make *Call of Duty* games available to both Sony and Nintendo consoles. MSFT will likely propose additional concessions in advance of court proceedings (see part four of this series for a more detailed list of potential concessions MSFT may offer).

Historically, the government has a strong track record in cases that involve litigating the fix, likely because antitrust agencies would reject weak concessions and take cases to trial when significant concerns about a mergers’ impact on competition remain.

Here, we think that “litigating the fix” may advantage MSFT rather than the government. MSFT can offer commitments that address a substantial portion of the concerns raised by regulators (which we will describe in more detail in our fourth note). Litigating those commitments may remove much of the risk that the deal will result in “substantially lessened” competition. For instance, the FTC’s assertion that MSFT could withhold ATVI content from rivals could be addressed by a MSFT commitment to make all ATVI available on all platforms. Lesser commitments -- such as making ATVI content available on PlayStation for a 10-year period -- address some of the risk, even if they do not mitigate it entirely.

In the US, because the ability to “litigate the fix” will increase the chances that MSFT prevails in court, it also increases the chances that the MSFT will reach a negotiated settlement with the FTC before going to trial. The FTC will want to avoid a loss in court, and MSFT will view concessions as a mechanism for avoiding a trial and bringing resolution to the case.

### Stay tuned...

- **Note 2: The Global Landscape.** Our second note will examine international regulators review of the deal.
- **Note 3: The Judge.** Our third note will focus on the FTC’s decision to pursue the case in its in-house administrative court.
- **Note 4: The Company.** Our fourth note will look at how Microsoft might respond.
- **Note 5: The Outcome.** Our final note will provide our prediction for how the case will resolve.



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