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The Amazon–MGM Deal

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On Wednesday, May 26, 2021, Amazon announced a deal to acquire Metro-Goldwyn-Mayer, popularly known as MGM, for $8.45 billion. The deal represents just one of several mergers and acquisitions that are reshuffling ownership lines throughout the media, entertainment, and technology industries. The Amazon-MGM deal is still pending regulatory review before completion, but it is likely to be the first serious test for newly selected Federal Trade Commission (FTC) Chair, Lina M. Khan. At the same time, a labor coalition of four major unions representing approximately four million workers has voiced its opposition to the acquisition, claiming it would only increase Amazon's market power in the entertainment industry, which could lead to anticompetitive business practices (Spangler, 2021) In what follows, we focus on the reasons for the acquisition, as well as the associated challenges facing the FTC regulators.

MGM has a long history. The studio, founded in 1924, rose to power as one of the vertically integrated "Big Five" during Hollywood's studio era. They dominated the industry before the United States Department of Justice (DoJ) issued its landmark antitrust ruling known as the "Paramount Decree." This ordered the vertically integrated studios to separate their film distribution business from their film exhibition business. In the wake of that decree, MGM divested from its movie theater properties and entered the television business in the 1950s. Additionally, MGM made a foray into hospitality and entertainment through MGM Resorts International. One of that company's main properties, the MGM Grand in Las Vegas, drew from *The Wizard of Oz*, one of MGM's biggest blockbuster titles, to develop some of its original decorative themes. However, the move into hospitality was short-lived, as it divested from MGM Resorts International in the 1980s.

Following the 1980s, MGM continued to focus on its film and television offerings as it divested or closed down holdings in most other areas of business. The studio made additional acquisitions throughout the 1990s and early 2000s but struggled financially. One of the key moments in this somewhat complex financial history was the creation of MGM Holdings, Inc. in 1993. Originally designed to house nearly $1 billion of MGM's liabilities, it eventually became the primary parent company for all of MGM's properties. Financial struggles reached their apex in 2010 when MGM filed for bankruptcy to eliminate nearly US$4 billion in debt (Barnes, Sperling and Weise, 2021). Against this background, MGM Holdings became the parent company of MGM's assets, and ownership of MGM Holdings was transferred to the company's creditors.

After the bankruptcy, MGM continued its business operations, but its creditors seemed to be seeking ways to sell the studio. After the Covid-19 pandemic forced the closure of movie theaters and provided a boon to streaming platforms, Amazon stepped in with an offer to buy the studio.

The acquisition of MGM is the second largest in Amazon's history behind the purchase of Whole Foods in 2017 for $13.4 billion. The Senior Vice President of Prime Video and Amazon Studios Mike Hopkins stated in the press release that: "The real financial value behind this deal is the treasure trove of IP in the deep catalog that we plan to reimagine and develop together with MGM's talented team" (Amazon, 2021). Indeed, MGM holds the rights to more than 4,000 films and 17,000 television shows (Pallotta, 2021). The purchase is widely seen as a strategy for displacing Netflix as the leading provider of video streaming in the United States and worldwide (Palmer, 2021b). In the third quarter of 2021 Netflix was the largest streamer in the U.S. with a 27% market share, followed by Amazon Prime Video (21%), Disney+ (14%), Hulu (13%), HBO Max (10%), Apple TV+ (4%), Showtime (2%) and other services (9%) (Winslow, 2021). The global video streaming market size, US$376.06 billion in 2020, was projected to grow to US$932.29 billion in 2028 (Fortune Business Insights, 2021). Given the prospects for such dramatic growth in video streaming revenues, it makes sense that Amazon would want to bolster its content holdings to leverage an economy of scale against Netflix. However, Amazon has a unique position in the market, as it packages its Amazon Prime Video streaming service with its Amazon Prime membership. The latter has an existing subscriber base of approximately 200 million people. At a quarterly earnings meeting in April 2021, Amazon CEO Jeff Bezos claimed that more than 175 million Amazon Prime members had streamed shows and movies the previous year, which represented a 70% increase on the previous year (Barnes, Sperling and Weise, 2021).

The proposed deal, however, faces some hurdles before approval. The deal is currently being reviewed by the FTC and was announced less than a month before President Joe Biden appointed Lina M. Khan as its youngest head at the age of 32 (McCabe and Kang, 2021). Khan, Associate Professor at the Columbia Law School, rose to prominence in 2017 when she published a widely cited paper in the Yale Law Journal titled *Amazon's Antitrust Paradox* (Khan, 2017). The paper tackles the inability of U.S. antitrust law to challenge Amazon's market dominance and power. She outlined Amazon's long-term business strategy of pursuing growth over profits and considered its favorable position among shareholders and investors unaffected by company's thin profit margins. Amazon achieved its position primarily through predatory pricing and vertical integration, strategies that escape outdated interpretations of U.S. antitrust legislation based upon consumer welfare. Aside from her influential paper, Khan, more importantly, served as counselor for the 16-month investigation of competition in digital markets conducted by the House Judiciary Committee, Subcommittee on Antitrust, Commercial and Administrative Law. The investigation resulted in a 450-page report (Investigation of Competition in Digital Markets, 2020). It emphasized, among many other issues, that Amazon's "dual role as an operator of its marketplace that hosts third-party sellers, and a seller in that same marketplace, creates an inherent conflict of interest." (Investigation of Competition in Digital Markets, 2020: 16).

In response to Khan's appointment as the head of the FTC, Amazon filed a petition with the agency for recusal of Khan from any antitrust investigation, adjudication, litigation, or other proceeding in which Amazon is a subject, target, or defendant (In Re Motion to Recuse, 2021). The petition states,

> She has on numerous occasions argued that Amazon is guilty of antitrust violations and should be broken up. These statements convey to any reasonable observer the clear impression that she has already made up her mind about many material facts relevant to Amazon's antitrust culpability as well as about the ultimate issue of culpability itself (In Re Motion to Recuse, 2021: 2).

The FTC rules say that it is up to the commissioner to recuse him or herself. If he or she declines to do so, the full commission votes on the matter without the participation of the commissioner who is subject to the recusal request. Khan leads a three-vote Democratic majority on the five-member commission (McLaughlin, 2021).

The acquisition is clearly heading in the direction of growing Amazon Prime to compete in the video streaming market. Additionally, however, the fact that Amazon is also a leading provider of other digital services complicates the issue from the perspective of vertical integration. To run any streaming service, companies require massive computational power. Amazon Web Services (AWS) is the global leader accounting for 40.8% of the cloud computing market in 2020, followed by Microsoft (19.7%), Alibaba (9.5%), Google (6.1%), Huawei (4.2%), and others (19.8%) (Gartner, 2021). According to the House Judiciary report, in the first quarter of 2020, AWS accounted for 13.5% of Amazon's total revenues but 77% of its operating income (Investigation of Competition in Digital Markets, 2020, p. 317). Many of Amazon's competitors are heavily dependent on AWS. Netflix, for example, paid AWS US$500 million in 2018 to store its streaming video library there (Investigation of Competition in Digital Markets, 2020: 252). Reliance on Amazon's infrastructure [1] was highly visible when outages in the United States affected major AWS customers across different industries, Netflix and Disney+ included, in late 2021 (Palmer, 2021a).

As the House Judiciary report concluded, "Cloud computing customers like Netflix and Target are in the position of competing with Amazon while also relying on AWS. Firms in their position effectively have to choose between switching to one of the alternative cloud infrastructure providers or funding their primary competitor" (Investigating Competition in Digital Markets, 2020: 322). Untangling the nuances of the MGM acquisition provides a true test for Khan and her resolve to tackle anticompetitive behavior. In order to challenge, or stop the MGM acquisition, she will need to leverage existing antitrust mechanisms poorly adapted to digital ecosystems and to change longstanding practices of consumer welfare interpretations of antitrust. Changes to existing merger rules have already been announced by the FTC and the DoJ (Feiner, 2022) but they will not be in place before the Amazon-MGM merger is reviewed and the final decision reached in March 2022. In addition, the EU is preparing to fully approve the merger (Chee, 2022). Thus, major challenges to Amazon's rising power across different industries, and continents, is unlikely at this point in time.

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Endnotes

[1] Netflix is keenly aware of this dependence. As stated in Securities and Exchange Commission (SEC) 10-K filing for 2020: "Currently, we run the vast majority of our computing on AWS. Given this, along with the fact that we cannot easily switch our AWS operations to another cloud provider, any disruption of or interference with our use of AWS would impact our operations and our business would be adversely impacted. While the retail side of Amazon competes with us, we do not believe that Amazon will use the AWS operation in such a manner as to gain competitive advantage against our service, although if it was to do so it could harm our business." https://d18rn0p25nwr6d.cloudfront.net/CIK-0001065280/db7a47ea-a2fa-47e9-be79-2cec06c28232.html

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