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# Integration contracts and asset complementarity: Theory and evidence from US data<sup>☆</sup>



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### ABSTRACT

Firms sign integration contracts to increase profits from trade and competition with third parties. An integration contract can improve complementarity among partners (productivity effect) and increase their power in the marketplace (strategic effect). We investigate three bilateral contracts: M&A, Minority Stake purchase, and Joint Venture. By using a cooperative game approach, we characterize quite general profitability conditions. To estimate the validity of those conditions, we adopt a novel complementarity index. It shows that for any kind of contract, a significant share of the integration profits is due to the “strategic effect” of increased market power. Productivity gains are relatively less important, and in some cases they are negative.

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**1. Introduction**

In the last fifteen years the American Telephone & Telegraph (AT&T) corporation, the largest provider of landline phone and broadband and television services in the US, has also become the second largest provider of mobile telephone. This position was achieved through a certain number of integration contracts. For instance, in 2000 AT&T spent \$US1.4 billion to buy a 32% share of Net2Phone, a software/services company principally specialized in Session Initiation Protocol (SIP)-based and PacketCable-based Voice over Internet Protocol (VoIP) networks. Despite the integration did not lead to the full control of Net2Phone, thereafter AT&T was able to influence strategically Net2Phone’s business with other firms in the telecommunication industry.

In 2003, AT&T Wireless and Cingular Wireless formed a joint venture (JV) to expand their Global System for Mobile Communications (GSM) and General Packet Radio Service (GPRS) wireless technologies along 3000 miles of interstate highways in Mid-western and Western states which were not covered yet. The two partners had a fifty-fifty control over the JV. At the time, AT&T and Cingular provided substitutable wireless services. The JV probably dampened detrimental competition among them, and it also reduced strategically the need for further alliances with other competitors.

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