Easy as Pie? Assessing inter-brand mergers

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BIICL 10th Annual Merger Conference

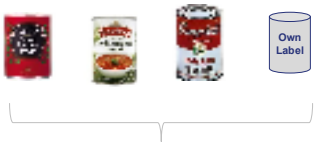
Three levels of competition: 1

Competition for consumers

Market framework

Three levels of competition: 2

Competition for shelf space



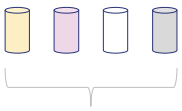
Bargaining framework

Competition for consumers

Market framework

Three levels of competition: 3

Competition to be the 'label' supplier



Bidding framework

Competition for shelf space

Bargaining framework

Competition for consumers

Market framework

Retail versus wholesale merger assessment

UPP/IPR increasingly used in assessing mergers in differentiated retail markets. Uses retail diversion ratios and retail margins. But what about wholesale mergers between branded goods?

Wholesaler incentives are related to retailer incentives…

Retailers may apply a standard mark-up on wholesale prices, or at least pass through to some extent	Switching by customers downstream will reduce sales at the wholesale level	So, retail preferences should reflect downstream preferences to some extent

…But different

Wholesalers and retailers have different margins	If the wholesaler raises its price the retailer may not pass this fully through – this depends on retail competition	If the wholesaler raises its price the retailer also has the incentive to change the retail prices of other competing products	Retailers may have bargaining power from scarce shelf space and outside option not to stock a product (bargaining framework is relevant)

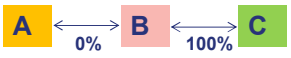
Implications of bargaining: An extreme

Retailers with bargaining power can make suppliers compete for limited shelf space

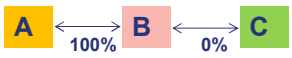
- If retailers choose not to stock products then customers find it more difficult to switch between them downstream
- This means downstream measures of competition may not directly apply and the bargaining framework should be considered directly

Market with three products (A,B,C); A is a 'must stock' brand and retailer chooses only one of brands B or C

Upstream diversion



Downstream diversion



Consider a merger between A & B

- **Downstream diversion overstates upstream competition between A&B**

Consider a merger between B & C

- **Downstream diversion understates upstream competition between B&C**

OFT cases: Using downstream data to assess upstream competition

Unilever/Alberto Culver (OFT, 2011)

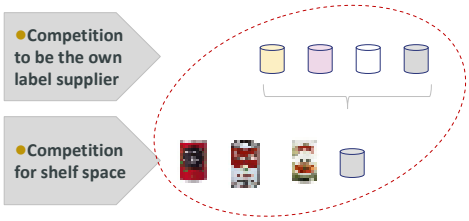
- Evidence of downstream customer switching from Kantar survey
- Retailers say their behaviour driven by end consumer behaviour
- Parties argued that retailer switching overstates wholesale switching:
  - If wholesale price of Dove raised, retailers would raise price of other soaps
  - Competition for shelf-space means retailers have wider range of products to switch to, so there is more diversion to an outside option
- OFT accepted these points, but emphasised that other arguments could go other way. Overall, considered retail level switching data is a reasonable proxy for wholesale, but mindful of limitations.

Princes/Premier Foods (OFT, 2011)

- Econometric analysis of retail scanner data to give diversion estimates
- Used both for Critical loss analysis and for GUPPI analysis
- OFT view that, since parties do not compete directly downstream in all retailers, there may be more diversion at wholesale level than is apparent from retail level diversion. And thus GUPPI is if anything lower bound.

Competition to be the own label supplier: Kerry/Headland (CC 2011)

- **Market definition: Frozen Ready Meals**



- **Market shares**
  - [50-60]% at tender stage
  - [40-50]% at wholesale stage

- **Tender analysis**
  - 25 tenders
  - In 11, Kerry was second to Headland
  - In 9, Headland was second to Kerry

- **Switching analysis**
  - Post-merger price rises!
  - But some switching, and potential for more.
  - CC concluded that customers would be able to find alternative FRM suppliers, and thus the price increase was temporary

Easy as Pie? Questions/views ?

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