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Business School

Research Series
Paper 2002: 2
ISBN 1 85901 177 2

Loughborough University

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June 2002

Author Biography

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1. Introduction

Developments in Grocery Retailing and Associated Policy Issues

Retailers represent the final and therefore the most visible point of the grocery supply chain for most consumers. Developments at this level consequently have a direct effect on consumer interests in relation to price, choice and quality of products on offer. In the last couple of decades the face of grocery retailing has changed significantly with the emergence of new, large-store formats and the increased prevalence of large retail chains. These developments have offered consumers increased shopping convenience through superstores offering one-stop shopping for food and other daily consumer goods.[1] However, with consumers' shopping habits changing in favour of these large-store formats the consequence has been a sharp decline in the number of traditional and specialist retailers. This pattern of development has been common across most of Europe.

Yet it is not just consumers which have been affected by these developments. As grocery retailing has consolidated and concentrated as an activity, large chain-store retailers have emerged commanding significant shares of national markets. This development has facilitated a marked change in the nature of supplier-retailer relations where increasingly retailers hold the whip hand, with supply chains being now fundamentally retailer-driven. Here, the substantial market shares held by the leading retailers have offered them increased ability to exercise substantial buyer power over suppliers. With their control of shelf space and the greatly reduced number of competitors, therefore offering fewer alternatives for suppliers seeking a route to market, these large retailers have in effect become "gatekeepers" for access to consumers. This in turn has allowed these large retailers greater prospect of obtaining price concessions from suppliers as well as being able to charge suppliers directly for access to their stores (e.g. through listing charges or shelf-space fees) and impose other restraints on suppliers (such as exclusive supply obligations). These benefits lie in the hands of the largest retailers, reinforcing their competitive advantage over smaller retailers and enhancing their power to dictate terms and conditions to suppliers. This leads to credible concerns about detrimental effects on competition at both the retail level and at the supplier level, where the viability of small (and large) suppliers may be considerably undermined by retailer buyer power.

These issues are, of course, not new for policy makers and competition authorities. They have, for example, been considered in the context of merger decisions (e.g. the European Commission's analysis of proposed concentrations concerning *Kesko/Tuko*[2] in Finland and *Rewe/Meinl*[3] in Austria). They have also been considered in relation to monopoly investigations into supermarkets (e.g. the UK Competition Commission's (2000) investigation). The lessons are clear that while consolidation can undoubtedly offer significant efficiency improvements to the benefit of society it can equally work the other way when it leads to restricted competition.

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1 By the term "daily consumer goods" is meant the provision of items collectively referred to as "fast-moving consumer goods" sold by grocery stores which in addition to food include domestic cleaning materials, toiletries, household goods, pet food, etc.

2 *Kesko/Tuko*, Case No IV/M.784 (OJEC L110, 26/4/1997).

3 *Rewe/Meinl*, Case No IV/M.1221 (OJEC L274, 23/10/1999).

Retailer Consolidation and Collaboration
Thus far authorities have tended to take a generally benign view towards retailer consolidation. However, competition concerns must be seen as very real in view of the apparently relentless consolidation process operating whereby the largest retailers continue to gain market share at the expense of smaller retailers. Moreover, the playing field is tilted even further in favour of large retailers than indicated simply by shares of retail sales. An aspect, often overlooked, concerns the real extent of consolidation on the buying side when full account is taken of *collaboration* between retailers in purchasing supplies. This point is significant since it not just that individual retailers have increased their control of market share but that through collaborating with other retailers they can gain increased buying power as part of a buyer group or buyer alliance. There is an important Community dimension here since collaboration is increasingly of a cross-border nature.

Indeed, it is at the Community level where current developments are most noticeable. While national level consolidation continues, the major leap in the last few years has been in terms of consolidation at the aggregate EU level. This paper estimates that the ten largest retailers control 30% of all retail food sales in the European Union.[4] Yet, the real extent of consolidation on the buyer side is made more significant by the operation of cross-border retailer alliances such as EMD and AMS (see Table 5 below). In this regard, it appears that the leading seven cross-border alliances together with the three largest non-affiliated retailers account for over half of retail grocery supplies throughout the whole Union. While these alliances are presently not formal groups in the sense of complete central purchasing, there certainly appears to be moves towards greater co-ordination between members, for example over own-label contracts. The introduction of the Euro as the key currency in the Community, and the immediate price transparency that this entails for cross-country comparisons, will no doubt further facilitate moves to greater co-ordination within these alliances.

In principle, then, just a handful of organisations control or have potential to influence the bulk of purchases from producers. This is not a small matter given that the level of grocery sales is estimated at nearly E900 billion across the EU. But continued consolidation through cross-border mergers and acquisitions is serving to add to the web of relations amongst retailers by extending links across previously separate alliances. These extended links offer further potential for exchange of price information in regard to previously private negotiations with suppliers. In this sense the prospect of alliances serving the role of a buyers' cartel are increased. An additional concern would be if this purchasing co-ordination spilled over to retail price co-ordination. Previously this prospect was remote when cross-border alliances did not involve direct competitors (typically involving just one member per state). But with overlapping membership, the prospect of co-ordination in national retail markets should be seen as a concern.

Online Exchanges
Tied to these developments has been the expanded use of business-to-business ("B2B") electronic commerce and Internet-based auctions. The latter, in particular, are playing an increasingly important role in awarding supply contracts for unbranded

[4] This estimate may be on the conservative side. Other sources report higher levels of aggregate concentration. For instance M+M Eurodata (at www.mmeurodata.de) has reported the extent of control held by the ten largest retailers as approaching 40% of retail grocery sales.

and own-label products by the largest retail groups, with moves in this direction by the major buyer alliances as well. This has entailed a shift away from the development of long-term supplier-retailer partnerships in favour of short-term price-based contracting (where the lowest price offered can win the entire contract). The impact on supplier viability and damage to long-term efficiency when investment decisions may be distorted by short-term concerns (given the uncertainty of winning contracts) has thus far received scant attention by authorities and policy-makers. There are also issues raised about ensuring quality thresholds are maintained (given the pressure that suppliers are under to cut corners in the face of retailer-orchestrated ultra-intense supplier competition). The concern is that such contracting could result in instances of sub-standard or faulty products being sold which consumers may not be immediately aware of and which may initially go undetected by retailers and quality-control agencies (such as Trading Standards or the Food Standards Agency in the UK).

While the use of B2B electronic commerce is to be broadly welcomed as reducing costs and improving overall efficiency within the supply chain, there are accordingly public interest issues that need to be addressed particularly in relation to the changing nature of supplier-retailer relations. The use of Internet auctions appear socially beneficial where it leads to reduced consumer prices at no loss of product quality and without endangering the viability and long-term efficiency of suppliers. The point made here is that the system could potentially be open to abuse and supply-chain efficiency and consumer welfare may suffer as a result if appropriate measures are not put in place.

Outline

This present report explores all of these emerging features in European grocery retailing, taking account of the patterns of consolidation and collaboration amongst retailers. The paper seeks to assess the economic impact of these changes and, where appropriate, consider policy measures to ensure that healthy competition and efficiency prevails to the ultimate benefit of consumers. The key message is that there is a greater need for co-ordination between national authorities through the European Commission to develop consistent policy towards grocery retailing and procurement given the increasing Community dimension to retailing issues and the breaking down of national boundaries in economic markets served. This calls not only for consistent treatment of mergers and anti-competitive practices but also a greater awareness of the need to develop common policy against economic exploitation of dependency relationships, given the long-term economic damage this causes.

The paper is structured as follows. The next section considers the economic welfare issues involved. Section 3 provides some background detail on the pattern of retail concentration across the different member states of the European Union, highlighting the extent of market share accounted by the major retailers at both the national level and at the Community level. Section 4 builds on this to consider a fuller assessment of consolidation by taking account of retailer collaboration arising from the development of national buyer groups and cross-border buying alliances influencing procurement markets. Section 5 discusses the impact of these developments on retail competition. The implications for producers are then considered in Section 6. Section 7 sets out a policy framework for tackling the anti-competitive effects of retailer power. The paper ends with a summary of conclusions.

2. Economic Welfare Issues

Benefits v. Costs

It is undeniable that the profound changes that have taken place in food retailing over recent years have offered considerable economic advantages. Heavy investment by retailers has allowed them to reap economies of scale through the operation of large-store formats and the benefits from operating large chains of stores. This has been supported by the implementation of sophisticated logistics and distribution systems married with significant investment in new technology (such as Electronic Point of Sale). The result has been significantly improved efficiency with greater sales per outlet and per employee.

Generally these changes have been beneficial for consumers. Greater convenience has been afforded by the development of one-stop shops offering in excess of 20,000 product lines and it is conceivable that lower prices have occurred where the cost savings from the improved efficiency have been passed on to consumers. The cost for consumers, though, has been the been the decline of traditional retailing, offering specialisation or location convenience, and a move towards greater homogenisation of retailing where fascias are fewer in number and have greater similarity in the retail offer. In some areas, the decline in competition and alternative stores for consumers has already reached the point where store choice has become very limited. This was for example evident from the EC's consideration of the Kesko/Tuko and Rewe/Meinl proposed mergers. With further consolidation at the retail level this problem of an absence of local competition may be expected to increase and become a more widespread feature across member states. This particular aspect calls for vigilance by competition authorities and consideration of whether instructed store divestments should be used to ensure that local competition remains effective.

Protecting Suppliers

While consumer welfare has been the prime focus of public concern and interest by competition authorities, the aspect of grocery retailers exercising buyer (or "monopsony") power as well as seller ("monopoly") power has come to prominence. Indeed, consideration of the effects of retail buyer power was not only a key feature of the UK Competition Commission's recent investigation but has also been an aspect of recent EC decisions on retail mergers.

The Competition Commission found that five multiples had sufficient buyer power that 30 practices identified by the Commission 'adversely affect the competitiveness of some of their suppliers and distort competition in the supplier market - and in some cases in the retail market - for the supply of groceries'. The result of the practices was that 'suppliers are likely to invest less and spend less on new product development and innovation, leading to lower quality and less consumer choice. This is likely to result in fewer new entrants to the supplier market than otherwise. Certain of the practices give the major buyers substantial advantages over other smaller retailers, whose competitiveness is likely to suffer as a result, again leading to a reduction in consumer choice' (paragraph 1.11). Although the Commission recognised some advantages in buyer power and offsetting benefits it nonetheless concluded that 27 of the practices found operate against the public interest.[5]

The practices identified by the Competition Commission covered a wide range of aspects in regard to contractual and operational relations concerning trading with suppliers. The Competition Commission usefully grouped the practices into eight different categories. Table 1 lists these categories and shows the number of different practices in each category found to operate against the public interest based on distortion to supplier competition and/or distortion to retailer competition. As can be seen, while competition concerns were raised for all categories, four categories accounted for all but two of the identified practices found to be operating against the public interest.

Table 1 - Supermarket practices related to relations with suppliers

Category of Practices	Number of Practices Against Public Interest
Payments for access to shelf space	4
Imposing conditions on suppliers' trade with other retailers	0
Applying different standards to different suppliers	1
Imposing an unfair imbalance of risk	10
Imposing retrospective changes to contractual terms	6
Restricting suppliers' access to the market	0
Imposing charges and transferring costs to suppliers	5
Requiring suppliers to use third party suppliers nominated by the retailer	1

Source: Competition Commission (2000)

At the recommendation of the Competition Commission, a code of practice has recently been established, intended to eliminate or at least restrict these anti-competitive practices with compliance required by the four largest supermarket groups (each accounting for in excess of 8% of the retail grocery market).

However, whether protection against powerful, opportunistically behaving buyers should generally be afforded to suppliers remains contentious. In some countries, notably France and Germany, so-called economic dependency laws can serve to protect suppliers against abusive exploitation, but mainly in regard to post-contractual

[5] The full list of practices identified by the Competition Commission is in a spreadsheet in Appendix 11.3 of its report. This identifies the practices (numbered ID1 to ID52) and charts which of the multiples engages in each practice and records their comments on each practice. The practices themselves are explained and discussed in detail on pages 98-136. The practices determined as being anti-competitive are listed in Table 2.14 of the CC report.

opportunism. But cases are notoriously difficult to prove and suppliers are reluctant to make complaints (for fear of reprisals).[6] The more general approach is to consider practices in regard to whether they distort, restrict or prevent competition along the lines of EC Articles 81 and 82 or their equivalents, e.g. the UK's Competition Act 1998. But thus far authorities have been reluctant to prohibit restrictive practices placed on suppliers. Even the Competition Commission's report did not lead to the recommendation that anti-competitive practices be prohibited outright but rather constrained by a Code of Practice.[7] More generally, authorities appear unwilling to prohibit retailer practices that potentially offer both efficiency benefits and anti-competitive effects even if they serve to reinforce buyer power.[8]

Consolidation throughout Europe

As to broader sector developments, it appears that the distinctiveness of national retail markets is being eroded. While national differences will continue in some aspects, mainly in relation to differences in consumer purchasing behaviour and the existing institutional set-ups, there is a clear trend indicating future convergence. Grocery retailing is increasingly becoming polarised between large hypermarket retailers and small convenience or discount store operators, with intermediate supermarket chains and unaffiliated independent retailers declining. This process is generally taking place across the EU, if at different speeds. But a noticeable feature is the rate at which markets such as Spain and Portugal, until recently highly fragmented, have consolidated as a result of multinational retailer expansion into these markets. This process is being initiated in the remaining unconcentrated markets of Italy and Greece and if effective will leave nearly all EU countries with high levels of retail concentration.

Indeed further afield, moves by the leading multinational retailers into Eastern Europe are already having a noticeable consolidating effect on countries such as Poland, Czech Republic, and Hungary. Thus, it is not inconceivable that at some future point retailers and buyer groups may be seeking to obtain supplies from producers on a fully European scale. Thus whilst retail markets remain local for consumers (with the typical catchment area represented by a 10 or 15-minute consumer drive time) on the procurement side the market may encompass the entire continent.

[6] Even if a case is taken up it may well fail because of the requirements of showing economic dependence, abuse and an effect on the market – see Ratliff (1998) and Vogel (1998).

[7] For some commentators even this is a move too far in what they regard as interference in normal business practice – see for example "Leader: A super market", *Financial Times*, 27/8/2001.

[8] An interesting case concerns slotting allowances. This practice has been extensively analysed in the US by the Federal Trade Commission and other public bodies. Thus far no action has been taken to prohibit or even discourage the practice – see Davis (2001) for a summary and Cotterill (2001) for more general discussion in the context of US grocery market developments.

3. Consolidation in European Grocery Retailing

To provide some insight into the extent of changes taking place in European grocery retailing this section provides some background information on the extent of national and international consolidation in the sector. In general, from a once largely fragmented sector, grocery retailing and procurement in Europe has become increasingly concentrated both at the national level and at the aggregate EU level. Where once retail markets were highly fragmented, consisting predominantly of traditional independent retailers, they have become highly consolidated, driven by a process of organic growth and mergers by leading retailers. The result has been the marginalisation of small independent retailers, restricted to acting as convenience stores (for so-called top-up shopping), and market domination by a limited number of large-format, multiple-store retailers that attract the bulk of consumer spending. Increasingly, the very largest retail corporations have also sought to extend their operations internationally, in the process increasing aggregate concentration across the EU.

National Consolidation Trends

The consolidation process has occurred across all countries to a greater or lesser extent but the general trend is one of apparent relentless increase over time. Table 2 shows the levels of retail concentration across EU member states for 1993-1999.

Table 2 - Five-Firm Concentration (%) in Grocery and Daily Goods Retailing for EU Member States (1993-1999)

	1993	1996	1999
Austria	54.2	58.6	60.2
Belgium+Luxembourg	60.2	61.6	60.9
Denmark	54.2	59.5	56.4
Finland	93.5	89.1	68.4
France	47.5	50.6	56.3
Germany	45.1	45.4	44.1
Greece	10.9	25.8	26.8
Ireland	62.6	64.2	58.3
Italy	10.9	11.8	17.6
Netherlands	52.5	50.4	56.2
Portugal	36.5	55.7	63.2
Spain	21.6	32.1	40.3
Sweden	79.3	77.9	78.2
UK	50.2	56.2	63.0
EU 15 (weighted av)	**40.7**	**43.7**	**48.9**

Source: Estimates based on data from Corporate Intelligence on Retailing's *European Retail Handbook* (various years)

The market share figures reported in the table are relative to all retail sales of food and daily consumer goods in each member state. Clearly market shares based just on sales in grocery retail outlets would give higher market share figures than those reported here.[9] Nevertheless, even with this broad based measure of market size, the table

[9] This point is important since it should be noted that the market base in Table 2 is the retail sales of

highlights the notable increases in the market share controlled by the five leading retailers in particular countries in just a few years. The overall (weighted) average concentration across the 15 member states increased by 20% over the six year period shown.[10]

Internationalisation and EU-wide Consolidation

However, it is not only at the national level that significant increases in concentration have occurred. Increasingly, the major retailers have sought to expand internationally. Wal-Mart, the world's second largest company with $193bn global turnover and 1,244,000 employees, has become a major player in Europe through key acquisitions in the UK and Germany. At the same time, Carrefour's recent merger with Promodès has created Europe's largest and the world's second largest retailer, consolidating its dominant position in France and Spain and increasing its position considerably in other countries. Other major retailers, notably from Germany (Rewe, Metro, Aldi and Edeka), France (ITM Intermarché, Auchan and Leclerc) and the UK (Tesco), have meanwhile strengthened their domestic and international positions.

Indeed, the concerted international as well as domestic expansion by the very leading food retailers has meant that they are increasingly taking a larger share of overall sales away from other retailers. The result has been a sharp increase in aggregate concentration across the EU. The top ten retailers in the EU now account for over 30% of sales of all food and daily goods. As shown in Table 3, this level has increased by some 25% in just six years. Moreover, it is clear that the top ten, or at most the top twenty, retailers are pulling away in growth terms from the rest. For instance, while the share accounted for by the leading 50 retailers was 49% in 1999, the level had only increased by 7.7% over the previous six years. As evidenced by the breakdown of rankings into decile groups, it is apparent that only the top two groups (1-10 and 11-20) increased their share, while those ranked lower accounted for reduced shares over time.

The evidence from Tables 2 and 3 clearly points to a considerably more consolidated retail sector at the national level as well as at the Community level. The leading retailers have strengthened their domestic positions and have expanded internationally to the point where a handful of leading players account for a large proportion of retail sales of food and daily products across Europe. It is on these major retailers, with their enormous buying power, that the livelihood of most suppliers depends.

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all food and all daily consumer items. Accordingly, these figures understate the level of concentration specific to items sold as prepared grocery or daily goods and predominantly identified with grocery stores. Other sources tend to show higher levels of retail concentration against this narrower base. For instance, AC Nielsen figures show that for 1999 the market shares of the five majors in grocery were in Austria 93%, Belgium 72%, Denmark 84%, Finland 83%, France 83%, Germany 76%, Greece 45%, Italy 31%, Netherlands 95%, Portugal 54%, Spain 51%, Sweden 95%, and UK 71%. Also, figures vary by store size classes, which may be relevant in defining appropriate economic markets. In the UK, for example, the Competition Commission (2000) found that the top five retailers accounted for 69.2% of sales of grocery and daily products but that the top five grocers accounted for 75.6% of stores over 600 sq.m. and 89.3% of stores over 1,400 sq.m. (i.e. of superstore/hypermarket size).

[10] Notice that there is considerable variation in consolidation patterns across the countries. Also, these national level figures, of course, hide the fact that from the consumer's perspective the relevant market is local in nature (e.g. within 15 minutes drive time), and that he/she is restricted in choice to the local stores operating in the vicinity. Here, there may be only one store (i.e. a local monopoly) but rarely more than a handful, offering retailers the possibility of exploiting local market power by setting prices according to local competitive conditions – e.g. see Competition Commission (2000, Chapter 7).

Table 3 - Aggregate Concentration in Grocery and Daily Goods Retailing for the European Union (1993-1999)				
Share of firms Ranked:	**1993**	**1996**	**1999**	**1993-1999 % change**
1-10	24.5	27.4	30.6	+24.9%
11-20	11.3	12.6	12.4	+9.7%
21-30	5.0	4.9	3.7	-26.0%
31-40	2.9	3.0	1.8	-37.9%
41-50	1.8	1.4	0.5	-72.2%
Top 50	45.5	49.3	49.0	+7.7%
Top 30	40.8	44.9	46.7	+14.5%
Top 20	35.8	40.0	43.0	+20.1%
Top 10	24.5	27.4	30.6	+24.9%

Source: Estimates based on data from CIR's *European Retail Handbook*

4. Retailer Collaboration through Buyer Groups and Alliances

While consolidation is clearly an ongoing process in European grocery retailing the above picture is in incomplete in one key respect. Tables 2 and 3, while reflecting consolidation in retail markets, do not give a full indication of the concentration facing suppliers in terms of retail procurement markets. In terms of purchasing supplies, retailers have not only sought to use their increased market share as a lever in negotiating with suppliers but have increasingly sought to collaborate with other retailers to enhance further their bargaining power. This has had a significant impact at the national level for several member states where national-buying groups operate, but is also increasing in importance at the Community level given the development of cross-border buying alliances.

National-level Buyer Groups
First, in many EU countries national-level buyer groups are prominent. In terms of operation, the key aspect is that the buyer group purchases collectively on behalf of members that remain independent retailers, striving to obtain benefits and discounts from suppliers similar to the largest integrated retailers. They tend to be in one of two forms, representing either many small retailers (e.g. Euromadi and IFA in Spain) or two or more larger retailers (such as Opera representing Casino and Cora in France). Clearly, the former type might be considered a useful counter-balance to growing retailer power of individual retailers. However, their significance should not be understated as often they represent the single largest buyers in their country (e.g. Markant in Germany and Euromadi in Spain). Moreover, in particular countries, notably Greece and Italy, buying groups dominate food purchasing, with the main players being significantly larger than any individual retail chain.

In regard to the second type of national-level buyer groups, i.e. combinations of larger retailers, a number of these have emerged in the last few years. In France, two very large buying groups have recently emerged in this manner: LUCIE (representing Leclerc and Systèm U) and Opera (representing Casino, Cora and Monoprix). In Italy, a particular feature of recent formations of buyer groups has been the involvement of multinational groups. Three instances are notable. First, RPBL involves Auchan from France (through its ownership stake in Rinascente, along with Pam, Bennet and Lombardini). Second, Mecades involves Metro (from Germany), Despar (as part of the international Spar group – of which ITM now own Spar AG) as well as Il Gigante. Third, CF consists of Finiper and GS/Carrefour (from France). Such multinational involvement is likely to spread as the wave of cross-border mergers and cross-shareholdings continues.

Taking into account the presence of national-level buyer groups, Table 4 shows adjusted five-firm concentration levels across the EU member states for 1999.[11] As can be seen, adjustments are made for eleven of the member states, in each case increasing the value of the concentration ratio. The (unweighted) average across member states now increases by 7% points to over 60%, and only Greece and Italy lie below 50%. Thus from the perspective of suppliers, national markets are noticeably

[11] It should be noted that the presence and composition of buyer groups is continually changing in some national markets, Italy being the most notable with the recent emergence of new groups consolidating the procurement market considerably.

more concentrated than that indicated simply by taking account of individual retailers' market shares.

Table 4 – Five-Firm Concentration Ratios Adjusted for Buying Groups, 1999			
	Excl BG	Incl BG	Buying groups in top 5
Austria	60.2	58.6	
Belgium/Lux	60.9	66.0	BLOC
Denmark	56.4	76.6	Supervib
Finland	68.4	70.5	Tradeka/Elanto
France	56.3	64.7	LUCIE, ITM, Opera
Germany	44.1	52.5	Markant
Greece	26.8	33.5	Elomas, Eloniki, ORA
Ireland	58.3	58.3	
Italy	17.6	26.4	ICMS, Italia Distribuzione, Intermedia, Mecades
Netherlands	56.2	71.7	SuperUnie, TSN
Portugal	63.2	67.0	Uniarme
Spain	40.3	63.7	Euromadi, IFA
Sweden	78.2	80.6	Axfood Sviege
UK	63.0	56.2	
Average	**53.6**	**60.5**	

Key: "Excl (Incl) BG" means measured excluding (including) buyer groups
Source: Based on data from CIR's *European Retail Handbook* and trade sources

Cross-Border Buying Alliances

Yet, increasingly, buyer groups are not just prominent at the national level. A number of significant cross-border buying alliances have emerged in the last few years. These alliances typically involve large retail organisations or national buying groups. As such the level of sales under their control is very significant on a pan-European scale. These alliances have been typically built up on a one-member-per-state basis, ranging from groups with three or four members to larger ones with twelve to fifteen members. Some are more formally established and open about their activities such as the two largest ones, European Marketing Distribution ("EMD") and Associated Marketing Services ("AMS"). While others, principally the ones with fewer members have a less formalised and less centralised operating structure.

The typical structure of these cross-border alliances is for each of them to have only one member from any state (ensuring that they are generally not direct competitors in their respective national retail markets and thereby avoiding concerns that they might directly facilitate collusion at the retail level).[12] In terms of activity, the alliances illustrate various degrees of collaboration between the sharing of buying price information and acting as a single purchasing unit, as well as often collaborating on the sourcing of private label products.[13]

Table 5 shows the constituent members of each of the seven main alliances and their estimated aggregate turnover. Their collective significance is immediately apparent in

[12] However, the potentially negative aspect of one-member per country is that it automatically results in foreclosure of competitors.
[13] See Dobson Consulting (1999, Appendix 2) for further details.

terms of their joint turnover (even though members continue at present to purchase mainly on an individual basis), estimated for the seven alliances listed at over E340bn, i.e. around two-fifths of the total EU market estimated at E845bn for 1999.

Table 5 - Cross-border alliances

Alliance (inc. members)	Combined EU turnover 1998/9 (bn Euros)
EMD	**116.8**
Markant Handels AG (Ger), ZEV Markant (Au), Euromadi (Sp), Leclerc (Fr), Delhaize Le Lion (B), ORA (Gr), Selex (It), Esselunga (It), Unil A/L (Nor), Axfood Sviege (Sw), Nisa Today's (UK), Musgrave (Ire) (+ EMD (Cz), Delvita (Cz), Honiker (Hun)) (N.B. most EMD members are national buying groups inc. wholesalers)	
AMS	**81.9**
Ahold (Nl), Casino/Opera (Fr), Edeka (Ger), Dansk Supermarked (Dk), ICA (Sw), Hakon (N), Kesko (Fi), Jeronimo Martins (P), Superquinn (Ire), Safeway (UK)	
INTERCOOP/NAF INT	**39.7**
Coop Italia (IT), Eroski (Sp), CWS (UK), FDB (Dk), KF (Sw), NLK (Nor), SOK/Tradeka (Fin), Coop Schleswig-Holstein (Ger) (+ Coop Hungary)	
EUROGROUP	**35.2**
Laurus (Nl), Rewe-Billa (Ger/Au) (+Coop Schweiz (Swtz))	
SED	**27.4**
Sainsbury (UK), Esselunga (It), Delhaize "Le Lion" (Nl)	
EUROPARTNERS	**21.4**
Superunie (Nl), Somerfield (UK), Cora (Fr) (+ Colruyt (B) – Cora (Fr), from 2000)	
BIGS	**19.0**
Spar International (Ger/Gr/Dk/Au/Sp/Ire/Fr/Nor), Spar Landmark (UK), Axfood (Sw/Fi), Despar (IT), Laurus (Nl), Unidis (B) (+Bernag Ovag (Swtz))	

Source: updated from Dobson Consulting (1999)

While the listed alliances do not include all the very largest retailers, they include many of them. Of the top ten ranked retailers only Carrefour, Tesco, Metro, Aldi and Auchan are absent from the above list.[14] Taking into account these five retailers, together with the largest five alliances, combined sales of the ten leading buying groups are estimated at E443bn, i.e. just over half of all EU grocery sales.

[14] The top 10 food retailers for 1999 ranked by sales in the EU were, in descending order, Carrefour (43.6 bn EUROs), Intermarche (29.9), Tesco (27.1), Rewe (25.3), Aldi (25.1), Auchan (24.3), Metro (23.3), Edeka (23.5), Sainsbury (18.6), Leclerc (17.7) (Source: CIR's *European Retail Handbook*).

Effects on Supplier-Retailer Relations

Seen in this light, it is not just the activity of international expansion by the leading multinational retailers that is driving greater integration of markets on the procurement side, but also alliances of nominally independent retailers. It is this combined force which food and daily goods suppliers face, affecting the prices that they can command increasingly at the international level when operating beyond the domestic level. Such moves are having important effects on the level of supplier-retailer relations as procurement shifts from being an activity at predominantly a national level to being an increasingly international one as the multinational retailers and cross-border alliances seek to strike common deals which apply across different member states.

Moreover, as the inter-linkage extends between membership of national buying groups and cross-border alliances, as well increasingly minority shareholdings and full take-overs by the multinational retailers, the potential for information exchange and price comparison increases. Indeed it is now possible to see the potential for exchange of price information across several of the cross-border alliances given the extent of either formal or informal linkages (i.e. whether by full or partial ownership, joint ventures, buying group membership or development alliances).[15]

E-Procurement

Further links arise from membership of global online exchanges. A number of online exchanges have emerged in the last few years but two retailer-initiatives stand out. GlobalNetXchange (GNX) was initiated by Carrefour (France) and Sears (US) but has since incorporated a number of major European retailers including J Sainsbury (UK), Spar (Austria), and Markant and Metro (Germany), as well as retailers from other continents. Meanwhile, World Wide Retail Exchange (WWRE) was established and has as partners Tesco and Marks & Spencer (both UK), Delhaize (Belgium), Ahold and Laurus (Netherlands), Dank Supermarked (Denmark), Edeka, Rewe, Tenglemann (Germany), Coop Italia (Italy), Auchan, Casino, Cora (France), and Hypercor (Spain), as well as numerous North American based retailers. These exchanges have thus far focused on e-procurement of commodity and private label goods as well as on "non-resaleables" (such as office equipment, office supplies and store fixtures). On-line auctions are used to award short-term contracts to suppliers, inducing ultra-intense competition where the lowest price offered wins the contract. While this has to an extent favoured low cost producers, the practice has encouraged marginal cost pricing leaving producers little or no scope to cover fixed costs with the potential damage to long-term investment and producer viability that may then be expected. Moreover, these problems can be further exacerbated if joint buying is permitted (i.e. jointly organised auctions) between major members (e.g. where their collective share exceeds 15%) or indeed such members (illegally) exchange price information (say, from equivalent auctions). Given the scale of the procurement already handled by these

[15] A number of interesting links have emerged because of new cross-border acquisitions, joint ventures and new national buying groups. For instance, Laurus (Netherlands) in principle links Bloc, Eurogroup and BIGS. While the Casino and Cora (France) joint buying venture, Opera, offers potential exchange of price information between AMS and Europartners. Furthermore, Delhaize Le Lion (Belgium) appears to be a member of both EMD and SED, offering further possibilities of exchange of information, as does Esselunga's (Italy) apparent membership of both SED and EMD. Such moves if allowed to carry on may well mean that in a short time there will be links between all cross-border alliances.

operations and the collusion possibilities that they throw up, it will be necessary for anti-trust authorities to ensure that retailers do not collaborate in either of these two respects.

5. Implications for Retailers

Benefits for Large Retailers

The result of all of these developments has been particularly favourable for the largest retailers. On the procurement side, with their control of domestic retail markets and their increasing international positions, the powerful store groups are able to wield their bargaining power to extract beneficial trading terms from suppliers pressurised into making concessions in order to gain access to their customers. The superior trading terms obtained by the leading retailers further reinforces their competitive advantage over smaller rivals, which in turn leads to further consolidation at the retail level. The process is one of a virtuous circle for the very largest retailers. Size and market share beget bargaining concessions from suppliers which reinforces cost advantages over smaller rivals enabling the large retailers to selectively reduce their retail prices which in turn increases the large retailers' sales and market share, and so on.

It is possible that national buying groups and cross-border alliances amongst smaller retailers may act to temper this advantage for the large integrated groups but the general impression is that consolidation is set to increase further at the national and Community level. In particular, multinational retailers look to be particularly advantaged where they can use their aggregate scale to penetrate new markets while continuing to consolidate their existing positions. Moreover, their advantage is even more apparent when they operate with hypermarkets and superstores against indigenous operators using small-format stores. Here, not only does the multinational operator gain through its bulk buying advantages but also gains from economies of scale advantages at the store level (where fixed costs can be more readily spread over the larger store's sales).

Smaller and Specialist Retailers

In response to these kind of advantages favouring large retail groups, it is not surprising that traditional, independent retailers have been in sharp decline in most countries over recent years. Specialist food retailers (butchers, bakers, fishmongers, etc.) have been particularly hard hit where shoppers have demonstrated their preference for the convenience of one-stop shopping offered by the supermarket and hypermarket operators. In part the rate of decline of small retailers has been lessened by restrictive planning regulations employed in many countries preventing or limiting new hypermarket store openings (e.g. the current moratorium in France). Nevertheless, small-format stores have survived operating as convenience stores for "top-up" shopping, perhaps operating through a symbol group such as Intermarché and Spar or by joining a buyer group to increase their purchasing power. On the latter aspect, most competition authorities have taken a lenient view towards the formation of buyer groups so long as they do not exceed certain market share thresholds (e.g. 20% in Sweden and 25% in Denmark).

While buyer groups of small retailers have had some success in maintaining their viability there is an undeniable trend across the whole of the EU towards large retail formats employed by the large integrated groups. Moreover, as illustrated in Table 3 above, at the aggregate level it is the very leading groups that are pulling away from the rest in terms of market share. This growth has, as shown above, occurred at the domestic level but increasingly retailing is becoming international and it is this factor which is most likely to shape the future of food retailing in most countries as specialist-domestic incumbents are either taken over or outmanoeuvred by multinational rivals.

Retailer Mergers

Mergers amongst retailers, of course, accelerate the consolidation trend. As yet, though, competition authorities have appeared unwilling to deter such consolidation arising through mergers unless it results in strongly dominant positions, essentially having a clear adverse impact on a national market. For example the European Commission prohibited the proposed merger between Kesko and Tuko in Finland which would have offered the combined enterprise a national market share of 60%.[16] In the case of Rewe's acquisition of Julius Meinl in Austria, store divestments were instructed in regions where the combined enterprise would control 65% or more.[17] However, for other mergers that have had a significant concentrating effect at the aggregate EU level, notably Metro/Makro[18] and Carrefour/Promodès[19], these have been allowed by the EC to proceed relatively unhindered. Similarly, national competition authorities have generally shown little appetite for blocking or limiting greater retail concentrations. But with each successive merger taking place and concentration increasing at both the national and EU levels, there is a greater prospect of mergers resulting in either single-firm or joint dominance. Thus far the emphasis by authorities has been on consideration of unilateral effects and single-firm dominance. However, the strengthening of oligopoly positions in national markets suggests that attention may be increasingly directed at joint dominance concerns.[20]

[16] Case No IV/M.784 (OJEC L110, 26/4/1997).
[17] Case No IV/M.1221 (OJEC L274, 23/10/1998).
[18] Case No IV.M1063 (OJEC O46, 11/2/1998).
[19] Case No IV.M.1684 (25/1/2000). Here the EC focused on the procurement aspects leaving the French and Spanish authorities to consider retail market aspects. There were limited conditions agreed with the EC, including Carrefour selling its 42% stake in Cora, while the national authorities imposed a limited number of store divestments in France and Spain.
[20] Such concerns have featured in an increasing number of cases handled by the European Commission where mergers have been prevented on grounds of oligopolistic dominance. Though, as yet these grounds have not been applied by the EC to prevent a retail merger in the grocery sector.

6. Implications for Producers

Retailer-Led Supply Chains

With the substantial consolidation of retail and procurement markets, the nature of the supply chain has changed considerably over recent years. Where manufacturers may traditionally have driven distribution by developing brands and then using a network of wholesalers and retailers to sell and distribute goods to consumers it is now predominantly retailers who drive the supply chain. Large retailers have dispensed with the need for a separate wholesaling function by integrating this element into their business, in the process implementing sophisticated logistics systems based on regionalised warehousing with subsequent distribution to their own stores. At the same time, the large retail groups have become far more active in sourcing product ranges to meet consumers' needs, using electronic point-of-sale (EPoS) data to gauge demand more effectively, instructing suppliers to tailor products for their particular needs, and developing own-label product ranges to compete against manufacturer brands.

Terms and Conditions Imposed on Suppliers

The upshot of this revolution has been that producer market power has largely given way to retailer buyer power, where retailers hold the whip hand over producers. The scale of operations of the major retailers and their control of purchases means that they are able effectively to dictate terms and conditions to producers. Through aggressive bargaining strategies, including the use of de-listing tactics, and the increasing use of auctions for awarding contracts, retailers have been able to drive down the prices and margins that producers receive. Allied to these moves has been the increasing use of vertical restraints placed on producers. These buyer-induced restraints generally take one of two main forms: either aimed at further rent extraction or limiting producers' freedom or incentives to supply elsewhere. The first form includes listing charges, shelf-space fees ("slotting allowances"), promotion support payments and retroactive discounts on goods already sold. The second form includes exclusive supply obligations and other non-compete contract clauses as well as most-favoured-customer type contracts.

As the report by the Competition Commission (2000) illustrates, these practices are widespread in the UK. In its report, the Commission identified 52 practices and found that 30 of these when exercised by five leading retailers gave rise to a "complex monopoly" (i.e. they restricted or distorted competition in the market) of which 27 were considered to be against the public interest. The Commission concluded that these practices should cease and argued that a Code of Practice be introduced to prevent such policies being used. Subsequently, the Office of Fair Trading has overseen the establishment of a code binding on the four largest supermarkets (Tesco, Sainsbury, Asda and Safeway). These four companies have entered into formal undertakings that incorporate a detailed dispute resolution procedure.

Moreover, such retailer practices appear not just in the UK but in other parts of Europe as well. Spain, for instance, offers an interesting case where the large retailers commonly adopt a two-step procedure in dealing with suppliers. In the first stage prospective suppliers are selected (using as criteria price, interest in the brand, guarantee of supply and other factors). The second step is the elaboration of what is commonly called "*plantillas*", in which the retailer makes explicit the concrete conditions of the supply relationship. Standard conditions include a listing fee, slotting allowances and end-of-aisle fees for shelf space, fixed end-of-year rebates, return of unsold units, contributions to special promotions, and demands for long terms of payment that do not match product turnover.[21]

In addition to these contractual elements there have been regular moves by individual retailers in Spain to seek additional "one-off" payments after contracts have been agreed. Examples include contributions to store openings, remodelling and extensions as well as retrospective discounts over sales in the previous period in the event of mergers, acquisitions ("wedding gifts") or anniversaries. These latter practices appear as deliberate exploitation of the dependency of suppliers by large retailers and are not unique to Spain. Even in countries where prohibitions exist on practices that exploit supplier dependency such as in France (following the 1996 Galland Law) and Germany (under the 1998 Act on Restraints on Competition – *Gestez gegen Wettbewerbsbeschrankungen*) such practices may nevertheless continue given suppliers' reluctance to bring cases to court.

Impact on Supplier Competition

While the buyer power of large retailers may have distorting effects on the retail market, it is clear that its most immediate effects are likely to be on competition at the producer level, and here again competition may be distorted. Small producers, in particular, are likely to suffer when they are unable to resist retailer buyer power, forcing them to cut prices to the point which endangers their continued existence. The longer-term effect of such strong buyer power will be to threaten the viability even of the most efficient producers when investments are undermined by inability to recover fixed costs as a result of producers being forced to price at (short-term) marginal cost. Accordingly, even large producers may be deterred from making product and process investments if buyer power prevents them making an adequate return to cover the costs. As a consequence, product quality, variety and innovation may suffer.

As with the establishment of the Code of Practice in the UK, most concern has been with small suppliers that are heavily dependent on one or two key retailers for their livelihood. In such instances, retailers can have total leverage over them by threatening to de-list their products and obtain supplies from elsewhere. Threats to de-list are common and represent a credible retailer bargaining tactic where the loss for the retailer might be minimal where it can relatively easily fill its store shelves with other producers' goods. In comparison, the manufacturer may lose substantially where it cannot gain additional sales from other retailers causing it to lose volume overall and in the process raise its unit cost base considerably, placing it a competitive disadvantage with its rivals (OECD, 1998). This can even apply to apparently strong oligopolistic manufacturers with well-recognised brands commanding significant market share.[22]

[21] On the latter aspect, a typical time to payment on an invoice is around 120 days compared to other EU countries where 30 days appears the norm – see Cruz *et al* (1997) and Dobson Consulting (1999).

[22] The problem for brand producers is that consumers are more inclined to switch brands if their preferred brand is unavailable rather than switch stores to find their favourite brand (given the amount of inconvenience this causes compared to one-stop shopping). This provides the retailer with a powerful leverage over even the strongest branded goods manufacturers by raising the credibility of the de-listing threat.

Effects on Own-Label Producers

The impact of retailer power is particularly strong on own-label producers. Increasingly the major retailers are using on-line Internet auctions, instead of traditional invited tendering processes for long-term contracts, to allocate short-term supply contracts where supply conditions are set in advance by the retailer with the lowest price bid winning the contract. While this might encourage bidders to offer prices at marginal cost it clearly does not encourage producer investment where fixed costs cannot be recovered. Moreover, it might encourage some producers to cut corners and produce sub-standard items, so adversely affecting the welfare of consumers.[23] Such problems could potentially arise where monitoring by retailers is inherently imperfect or where product specifications are not set and enforced precisely.

For producers caught in the trap of relying on key retailers for the bulk of their sales and offering undifferentiated products (e.g. unbranded or retailer own-label commodity items) then can be expected to have little defence against retailer buyer power. As such only the most efficient will survive and producer markets will in such instances be driven towards consolidation to allow scale economies to be reaped to aid the chances of survival. As a specific illustration of this, Table 6 summarises the supplier consolidation that has taken place in household products over the last few years in the face of increasing retail buyer power.[24]

Table 6 - Recent Supplier Consolidation in the European Household Products Market

Company	Outcome	Year
Despe (Belgium)	Liquidated	1995
De Fenix (Netherlands)	Liquidated	1997
Le Nigen (France)	Liquidated	1999
Wundi (Germany)	Liquidated	1999
De Klok (Netherlands)	Acquired by Dalli	1992
Dicom (Netherlands)	Acquired by Dalli	1995
Winn Cosmetics (Germany)	Acquired by Dalli	1997
Hackmann Havi (Finland)	Acquired by Henkel	1997
Grada (Netherlands)	Acquired by McBride	1998
Jeyes (UK)	Acquired by IWP	1998
Sara Lee aerosols (Netherlands)	Acquired by Trost	1998
WK Chemolux (Luxembourg)	Acquired by Henkel	1998
Reckitt / Benckiser	Merger	1999
Dan Lind / Clean Tabs	Merger	2001

Source: Trade Sources

[23] The latter concern would be where product quality is not easily verifiable until consumed. An example would be using food unfit for human consumption (e.g. see "Tesco recalls chicken in pet food scare", *The Guardian* 25/4/2001) or the use of a chemical that breached health and safety regulations in the formula or packaging used.

[24] This case is used purely for illustration. However, it is clear that producer consolidation has occurred in other food and daily consumer goods sectors in the context of buyer power pressures. See Dobson Consulting (1999) and Dobson (2001) for studies covering household detergents, coffee, butter/margarine, and pet foods.

Producer Responses

More generally, the response to buyer power from producers must be to seek economies wherever possible. With the moves to international operations by the leading food retailers and procurement by cross-border buyer alliances there will be an added incentive for producers to operate at the multinational level as well when it allows them to secure international contracts. Given the time required to build new positions organically, producers may instead be expected to extend and adjust their international reach through strategic acquisitions. It is precisely this aspect which lies behind much of the international acquisition and sell-off activities of the leading producers (e.g. Unilever/Bestfoods, PepsiCo/Quaker Oats, and Nestle/Ralston Purina). Furthermore, the need for mergers that do not yield single-firm dominant positions has been recognised by competition authorities in their recent decisions. Moreover, in the cases considered, competition authorities have dismissed the likelihood of mergers giving rise to problems of joint dominance by the leading producers in the face of intense retailer power set against them, ensuring that producers are collectively unable to exploit any market power of their own.[25]

Farmers at the first point of the food supply chain face pressure to cut margins and remain viable businesses. This pressure comes not only from retailers directly sourcing fresh produce, but also from processed and packaged food manufacturers intent on sharing the burden that they face as a result of the exercise of retailer buying power. This in turn is likely to drive further efficiencies in farming where these are possible, and perhaps also the defensive growth of farmers' selling co-operatives. But at a general level, the effect of retail buyer power, either directly applied or working its way through the supply chain, is likely to take income and money away from rural areas and communities and have potentially long-term detrimental effects on the agricultural industry when investment becomes uneconomic.

Thus the process of retailer consolidation and collaboration in altering the nature of trading relations can be expected to have important implications for the supply chain as a whole. Efficiency improvements will be encouraged by the competitive drive to remain viable, but the longer-term implications give cause for concern where producers are deterred from making appropriate investments and innovation is accordingly retarded.

[25] See Dobson (2001) for a full discussion of these issues.

7. Policy Measures

Existing Problems

As outlined above there is existing competition law and policy appropriate to the context of grocery retailing and procurement. In principle, existing law and policy towards mergers, vertical restraints and horizontal agreements are all relevant. However, clear practical problems remain in regard to legal interpretation, appropriate jurisdiction and consistency in decisions and treatment. These problems stem from three factors: the definition and measurement of buyer power, lack of clear policy guidelines, and vested national interests.

First, there is no consensus at present on the economic and legal meaning of buyer power. A number of alternative definitions have been put forward but no single one has been universally accepted and adopted.[26] Following on from this, there has been no clear agreement on the appropriate measurement of buyer power. Even in terms of the required market share for retailers to be able to exert significant buyer power there is wide disparity in levels used. The UK Competition Commission (2000) suggests that 8% of the relevant market may afford buying power, the OECD (1998) suggests 15%, while recent merger decisions of the European Commission imply 22%.[27] The only apparent consensus is that buyer power might have detrimental effects well below the usual level of dominance associated with 40% market share.[28] This is clearly an unsatisfactory situation and until definition and measurement is resolved there is likely to remain the prospect of inconsistent treatment between similar cases.

Secondly, while it is entirely appropriate to treat mergers and restrictive practices (either in a horizontal or vertical form) on a case-by-case basis, there is a notable absence of appropriate guidelines and consensus on appropriate treatment for particular instances. Case-by-case analysis arises from the need to consider and weigh possible efficiency gains against anti-competitive effects. But economics has yielded clear insights on the situations when mergers and practices are likely to be pro- or anti-competitive. Unfortunately, while these insights have been applied to the drawing up of guidelines on the diagnosis and treatment of seller power, there has been little movement towards developing corresponding guidelines on the treatment of buyer power. For instance, the European Commission's Merger Regulation (ECMR) focuses predominantly on output market considerations and seller power, while the EC's Vertical Restraints Guidelines focus almost entirely on vertical restraints arising from seller power with no clear guidance and analysis offered on buyer-induced restraints. Moreover, the EC Notice on the definition of the relevant

[26] The array of definitions thus far proposed are discussed by OECD (1998), Dobson Consulting (1999), Bloom (2000) and Collins (2000), *inter alia*.

[27] On the EC merger decisions, see the discussion by Lücking (2000).

[28] The usual reason cited in support of this claim is down to differences in relative switching costs for suppliers and retailers (e.g. OECD (1998)). For a supplier to be delisted by a major retailer there will few, if any, alternatives to make up extra sales elsewhere. For the retailer, filling up the shelf space is relatively more straightforward given that alternative suppliers are available or indeed shelf space can be allocated to other product lines with little damage to overall sales. The implication is not only that this situation places all the bargaining advantage with the retailer but that the retailer can force the supplier to accept terms that are anti-competitive. Such terms might be non-cost-related discounts and vertical restraints that serve to restrict or distort retail competition by placing other retailers at a competitive disadvantage or facilitate collusion.

market fails to address the question of how to define procurement markets.[29] It is then perhaps not surprising that the weight of importance attached by competition authorities and courts to buyer power is usually considerably less than that attached to seller power. This view is reinforced by the lack of agreement amongst authorities on the economic significance of buyer power, unlike seller power where there is greater consensus on the situations where it is likely to be anti-competitive and against the public interest.[30]

Thirdly, retailing has traditionally developed at the national or sub-national (i.e. regional or local) level. Developments on these lines have responded to, and thereby reflect, national culture and history and where national and local policy towards retailing has shaped the retail environment considerably. This background helps to explain the determination of national authorities and policy markers to retain control over decisions affecting retail developments in their country. This accounts for persistent differences between member states in regulations concerned with planning restrictions, zoning laws, shop opening hours, retail pricing policy, and other matters concerned with retail operations when economic and social objectives are mixed.

However, while retail markets persist in being at most national in geographic scope, the past couple of decades have seen the decline of traditional retailing in most EU countries and the emergence of common retail formats and so a move towards more similar retail environments. This move has been accelerated by the internationalisation of retailing with the development of cross-border retailers. However, as yet, the EC has played a very limited enforcement role, continuing to leave policy decisions in the hands of national authorities. Only with exception of a handful of merger investigations and the general application of EU competition policy has the Commission acted on retail developments. Nevertheless, with moves towards Europe-wide procurement markets and more international retail markets resulting from the introduction of the Euro and the continued development of Internet-based shopping, it appears increasingly appropriate that the Commission should take a more central role in ensuring consistent competition policy towards retailing throughout the EU. This will inevitably entail the Commission, rather than national authorities, handling an increasing proportion of merger cases and investigations of possible anti-competitive practices employed by retailers.

Role for European Commission
In view of these three factors and the need for consistency and transparency in the development of competition policy and case decisions, the role of the Commission appears fundamental. There is an urgent need to develop appropriate guidelines on the definition, implication and treatment of buyer power in regard to mergers, buyer-induced vertical restraints and horizontal agreements. This would necessarily entail new market definition guidelines that set out how procurement markets should be

[29] Commission Notice on the definition of the relevant market for the purpose of Community competition law, O.J.C. 372/3 (1997).

[30] Here the UK authorities appear to be inclined towards the extreme view that retail buying power in isolation is likely to be of social benefit where it leads to lower prices for consumers but is anti-competitive when it serves to reinforce retailer selling power – see Bloom (2000), for instance. Such a view fails to recognise the long-run damage that buyer power on its own can cause from undermining supplier viability and supplier investment, potentially detrimentally affecting product quality, variety and innovation. Such considerations appear to be present in those countries that have developed economic dependency laws, e.g. France, Germany, Greece, Portugal, and Spain.

defined. Guidelines should also be clear on how economic trade-offs between pro-efficiency effects and anti-competitive effects should be evaluated. The challenge would be to develop guidelines that are led by the need to preserve and/or enhance competition but capable of taking account of relevant social factors.[31] The five-step appraisal procedure advanced by Dobson Consulting (1999) is designed to take account of pro-competitive and anti-competitive effects, as well as economic dependency arguments if appropriate, but this needs adapting to move from being a theory-derived construction to being a practical policy tool. Implicit to this approach would be the acknowledgement that buyer power can be exerted at less than traditionally dominant levels of market share and that joint dominance may be a particular concern in view of common practices employed by grocery retailers (as witnessed by the UK Competition Commission (2000)).

Economic Dependency Laws

In terms of perspective, while it is tempting to consider the extension of economic dependency laws as presently employed in several member states to the European Union as a means of tackling buying power abuse there are fundamental weaknesses in this approach. First, the approach relies on the need to distinguish "fair" from "unfair" practice (as opposed to distinguishing between a practice that is or is not anti-competitive). This is an inherently normative and judgmental aspect (concerned with the division of economic profits between the parties concerned) as distinct from the more robust concept of defining what is "anti-competitive" (by virtue of decreased economic welfare to all society). Second, on a practical level, firms are reluctant to make complaints and/or instigate court cases for fear of reprisal (resulting in lost business) and the uncertainty of winning a case when it is notoriously difficult to show (i) dependence, (ii) abuse and (iii) an effect on the market.

Experience indicates that such laws have had little effect in controlling abuse of buyer power. Their place appears best suited to national situations in the context of existing commercial law where cases can be made more effectively to cover particular abuses concerned with post-contractual opportunism. This would cover cases where retailers have sought to use their power to change agreed terms when suppliers are already committed to existing arrangements. Examples might include demand for so-called "wedding gifts" (where, following two retailers merging, suppliers are instructed to offer increased discounts or increased lump-sum payments for slotting allowances) or demand for retrospective funding of retailer promotions not previously agreed. They might also take the form of unilateral variation of terms (e.g. over quantity or product specifications) without reasonable notice or reimbursement of costs or the common practice of delaying payments to suppliers outside of agreed contractual periods (say 30 days from the date of invoice). A more extreme example would be the severing of an ongoing supply arrangement without reasonable notice. It is these instances of post-contractual opportunism on the part of retailers that might be most effectively tackled by economic dependency laws or a statutory supported code of practice for the industry.

[31] These might include the position of small shopkeepers and out-of-town shopping, the preservation of rural communities, and the interests of farmers and other small suppliers.

Application of Existing EC Framework

At the Community level the most effective way of tackling abusive buyer power remains the current competition framework represented by Articles 81 and 82 of the EC Treaty. Yet crucial to establishing a successful approach will be appropriate interpretation of these articles. In particular, dominant and jointly dominant retailer positions should be seen as emerging not simply from overall market shares but relative to the extent of supplier dependency. Specifically, it needs to be recognised that buyers can abuse dominant positions when suppliers have no alternative economically viable route to market for their products given their present scale and given the existing contracts in the market. Each case may be expected to differ but, as argued by the UK Competition Commission, buyer power can be associated with a grocery retailer having a share as low as 8% of a procurement market. Since, even at this level suppliers may have little alternative but to comply with retailers' demands for fear of losing critical sales which would seriously undermine their competitive position (given the higher unit costs which might result from reduced scale). Similarly, in regard of buyer-induced vertical restraints (such as listing fees, slotting allowances and insistence on exclusive supply) account needs to be taken of not just the individual share of each retailer employing these restraints but their collective share (given that cumulative effects are likely to exacerbate anti-competitive outcomes).

Policy on Joint Buying

In addition to developing appropriate policy to tackle anti-competitive behaviour of individual firms holding dominant or jointly dominant buying positions, a clear policy is required towards joint buying and the establishment and operation of buying groups.[32] These should be treated essentially as horizontal agreements and not vertical agreements.[33] A common EU-wide approach is increasingly required in light of increased cross-border purchasing activity and the extended collaboration of buying groups in international alliances. At present, different countries have adopted different laws and policy positions on the matter of national buying groups. A clear role exists for the EC to take a view on the appropriate conditions for national buying groups to receive exemption from present regulations. This requires not only identifying an appropriate upper market share threshold (say, 15%) but also practices to be prohibited or exempted.[34] A key requirement must be that the members of the alliance are not required to purchase goods through the alliance (i.e. they are free to negotiate individually with suppliers), thereby encouraging choice for consumers and supplier access to the retail market. In addition, arrangements must not deter individual members from marketing their own retail businesses and lowering their prices directly or indirectly (i.e. no alliance induced price maintenance) or support

[32] Some alliances have been notified to the Commission for an individual exemption under Article 81(3) but so far no formal Commission decision has been issued (i.e. other than responses through the issuing of so-called "comfort letters" to the notifying parties).

[33] Presently the horizontal aspects of buying alliances are analysed under the horizontal blocked exemption but vertical arrangements (i.e. with suppliers and customers) are analysed under the vertical restraints block exemption. Article 2(2) of the vertical restraints block exemption makes it clear that the block exemption only applies to buying alliances if the total aggregate turnover is less than E50m.

[34] Combined market share thresholds presently differ across different member states. In Denmark chain co-operation may be allowed with 25% market share while in Sweden the upper threshold is 20% - see Ratliff (1998). In Germany it appears acceptable for market shares of 10-15% to be pooled (Section 4(2) of the ARC – see Böge (2000)). With conversion to an upper limit of 15% this would call into the question the present exemptions granted to a number of significant national-buying groups.

other forms of collusion serving to restrict retail competition. These principles should apply equally to international buying groups as well as national buying groups.

In the case of international buying alliances, additional restrictions appear warranted. First, multiple membership of buying groups should be prohibited when it raises the prospect of cross-alliance exchange of price information. This means that individual members of a national buying group should not be members of different national or international buying alliances. Secondly, to ensure that the prospects of retail collusion are minimised a rule of one member per country should be enforced.[35]

In regard to online exchanges it is important that the economic benefits are allowed to flow from these, i.e. arising from economies of scale and reduction of transaction costs, as potentially there are considerable cost-savings for the industry as a whole. Yet joint buying by members should be prohibited (other than for members of an existing sanctioned buying group or where application of EC horizontal agreement regulation applies, i.e. up to 15% combined market share), to ensure that exchanges do not simply act as some super-large buying group to the benefit of already large individual members. It is also crucial to ensure that retail members are not permitted to exchange price information (applying to both commodity items and branded goods). Furthermore, to ensure that these exchanges do not operate as monopolies, through gaining "essential facility" status, access should be open and user/member costs (particularly for small retailers and small suppliers) should be kept to an absolute minimum (preferably on a pro-rata basis rather than a lump-sum fee). At present the degree of openness is unclear. If exchanges work by invitation only then this may simply serve to benefit large firms. Effective exclusion of smaller firms from these exchanges will have the effect of further consolidating the industry.

Behavioural Remedies

While all such measures targeting firm behaviour are likely to be useful as individual steps to ensure that competition remains healthy there is a general need for these to be consolidated in the form of a set of agreed rules covering all the above elements. One approach to this might be in the form of code of practice governing firm behaviour. However, codes of practice are notoriously difficult to establish (for they need to be comprehensive in scope and rigorous in wording to avoid legal loopholes). They also can be expensive to monitor and oversee if they are to be properly implemented and followed. Moreover, without appropriate means of redress suppliers are unlikely to make any complaints against large retailers when they face the prospect of being punished through losing future orders. However, as a desirable way of controlling retailer buyer behaviour and a means of avoiding the worst forms of abuse associated with buying power, a comprehensive code of practice, backed up with a tight enforcement system, has many advantages. Furthermore, such a code should be determined unilaterally by the relevant competition authority to avoid compromise of the principles and be designed to terminate practices that are judged to be anti-competitive.[36] Ideally a common code would apply across the EU, usefully

[35] An exception should be considered when one member per state results in foreclosure to competitors which may potentially arise if the buying alliance gains near-essential facility status. More generally, the measures considered here imply that the Commission needs to revisit the cases of EMD, AMS and Eurogroup where clearance has been implicitly given through comfort letters being issued.

[36] This centres on a particular criticism of the way that UK Code was established through consultation only with the supermarkets and the weakness of the wording to rule out practices which the

drawing on (and learning from) the UK experience of developing a code with a suitable dispute resolution procedure.[37]

Striking at the Root of Retailer Power

Nevertheless, for all its potential benefits, an underlying weakness of a code of practice, or indeed any individual prohibition, is that blocking particular practices does not necessarily solve the problem of buyer power: it attacks certain symptoms but not the underlying causes. Faced with being prevented from using particular practices, retailers would have an incentive to search for new ways to exert buyer power giving rise to new forms. Thus even if a code of practice were effective in ending certain practices all this may do is encourage retailers to develop new practices with similar effects. This could potentially give rise to cat-and-mouse cycles where the code has to be continually updated to take account of new practices. In such an event, striking at the causes of buyer power must seem to be more attractive in terms of ensuring that regulation is effective and that regulatory and compliance costs are restricted. This inevitably calls for more direct action on the permitted extent of consolidation and collaboration in retailing. Structural remedies imposed as a result of monopoly or merger investigations would help to ensure that retail competition remains effective (possibly through enforced store divestments or merger prohibition in appropriate cases) as these strike at the causes of retailer power. But to be thoroughly effective, behavioural remedies (such as a comprehensive code of practice) have an important complementary role to play in treating the existing symptoms. Such a two-pronged attack is likely to offer the best prospects of ensuring that the anti-competitive effects of retail buyer power are controlled, if never entirely eliminated, to the overall benefit of the industry and consumers.

Competition Commission had condemned as being against the public interest.

[37] For details of the UK's Code of Practice see "Hewitt backs good behaviour code for supermarkets & suppliers", DTI Press Release, P/2001/606, 31 October 2001. The undertakings for the four supermarket groups having in excess of 8% market share (Asda, Safeway, J Sainsbury, and Tesco) required to comply with the Code are available online at www.dti.gov.uk/cp/pdfs/codeofpractice.pdf

8. Summary of Conclusions

- The profound changes that have taken place in food retailing over recent years have offered considerable economic advantages. Heavy investment by retailers has allowed them to reap economies of scale through the operation of large-store formats and the benefits from operating large chains of stores. This has been supported by the implementation of sophisticated logistics and distribution systems married with significant investment in new technology (such as Electronic Point of Sale). The result has been significantly improved efficiency with greater sales per outlet and per employee.

- Generally these changes have been beneficial for consumers. Greater convenience has been afforded by the development of one-stop shops offering in excess of 20,000 product lines. It is also conceivable that lower prices have occurred where the cost savings from the improved efficiency have been passed on to consumers, even if the choice of stores available for them at a local level has been considerably reduced.

- With further consolidation at the retail level the problem of an absence of local competition may be expected to increase and become a more widespread feature across member states. This particular aspect calls for vigilance by competition authorities and consideration of whether instructed store divestments should be used to ensure that local competition remains effective.

- At the aggregate level, grocery retailing continues to consolidate at a rapid pace in Europe. The market share controlled by the largest five grocery retailers in each EU country has on average increased by 20% in a six-year period. Internationalisation of retailing has meant that ten retailers account for in excess of 30% of all grocery sales in the EU (up by 25% in the same six-year period). Present trends seem set to continue with the continued growth of the very largest retailers through further mergers and organic growth at the expense of smaller retailers.

- Along with the growth of individual retailers, significant collaboration exists between nominally independent retailers through affiliation to national buyer groups and cross-border alliances. The growing significance of the latter is reflected by the observation that the members of the seven leading alliances account for over two-fifths of all grocery sales in the EU (presently approaching one trillion Euros). Added to this is the emergence of online exchanges, facilitating e-procurement and in the process offering further possibilities of collaboration amongst retailers.

- Powerful positions in retail markets allow the key retail groups to take control of supply chains, dictating terms and conditions on suppliers enabling them to gain further competitive advantage over smaller rivals, which in turn leads to further consolidation at the retail level. The process is one of a virtuous circle for the very largest retailers.

- Through aggressive bargaining tactics and the increasing use of auctions for awarding contracts, retailers have been able to drive down the prices and margins that producers receive to levels that potentially endanger the latter's long-term viability and incentives to invest. Anti-competitive concerns also arise in regard to the increasing use of vertical restraints by retailers; e.g. practices imposed on producers aimed at further profit extraction or limiting producers' freedom or incentives to supply elsewhere.

- Existing policy measures and law have thus far had little effect in restricting retail buyer power. Economic dependency laws have generally been ineffective in protecting suppliers subjected to opportunistic behaviour by powerful retailers. Competition authorities have only in a few cases sought to prohibit retailer-induced vertical restraints. Moreover, authorities have generally shown little appetite for blocking retailer mergers thereby allowing for further retail consolidation.

- At present there is little consistency between the approaches taken by individual EU countries. A role exists for the European Commission to establish a comprehensive framework for tackling retailer power when it serves to prevent, restrict or distort competition in retail and procurement markets. As a first stage, this requires establishing appropriate guidelines on the definition, implication and treatment of buyer power in regard to mergers, buyer-induced vertical restraints and horizontal agreements.

- The present EC competition framework, represented by EC Treaty Articles 81 and 82, remains the most effective way of tackling abusive buyer power. Yet in regard to interpretation, dominant and jointly dominant retailer positions should be seen as emerging not simply from overall market shares but relative to the extent of supplier dependency. Similarly, in regard of buyer-induced vertical restraints account needs to be taken of not just the individual share of each retailer employing these restraints but their collective share (given that cumulative effects are likely to exacerbate anti-competitive outcomes).

- All joint buying arrangements need to be viewed as horizontal agreements and not vertical agreements. A common EU-wide approach is required in light of increased cross-border purchasing activity and the extended collaboration of buying groups in international alliances. This requires not only identifying a permitted upper market share threshold (e.g. 15%) but also specified practices to be prohibited or exempted.

- In the case of international buying alliances, multiple membership of buying groups should be prohibited as it raises the prospect of cross-alliance exchange of price information. This means that individual members of a national buying group should not be members of different national or international buying alliances. In addition, to ensure that the prospects of retail collusion are minimised a rule of one member per country should be enforced.

- In regard to online exchanges it is important that the economic benefits are allowed to flow from these yet have in place measures ensuring that retail members do not engage in joint buying or exchange price information. Furthermore, to ensure that these exchanges do not operate as monopolies, through gaining "essential facility" status, access should be open and user charges minimised to encourage participation by small firms.

- Developing a comprehensive code of practice has merits as a behavioural remedy to curb abusive retailer power and eliminate key anti-competitive practices. Crucial to its effectiveness would be the establishment of an enforcement system operated by the relevant competition authority to ensure that compliance was met. Ideally, a common code would apply across the EU.

- To strike at the roots of retailer power, a behavioural-remedy approach needs to be combined with more direct action on the permitted extent of consolidation and collaboration in retailing. This calls for greater use of structural remedies through tightening merger policy and ensuring that retail competition remains effective (possibly through enforced store divestments or merger prohibition in appropriate cases). Such a two-pronged attack is likely to offer the best prospects of ensuring that the anti-competitive effects of retail buyer power are controlled to the overall benefit of the industry and consumers.

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