

Competition issues in the food markets

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ECN Report : Issues

ECN Subgroup Food, Report on competition law enforcement and market monitoring activities by European competition authorities in the food sector, May 2012

- **Structural problems:** atomistic, with many intermediate stages
- **Entry barriers to retail markets** (e.g., planning laws)
- **Contractual constraints at retail level** (e.g., limitation in the use or availability of land suitable for retail sites)
- **Buyer power:** unfair practices in the trade relationships between suppliers and buyers (i.e., retailers & wholesalers)

Buyer Power (BP)

- **Definition:** concerns with how downstream firms affect terms of trade with upstream suppliers (OECD, 2008)
- **General presumption of the benefits of BP:** benefits will be passed on to consumers if there is competition at retail level
- However, the effects of BP depends on the framework adopted:

	Market Framework	Bargaining Framework
Supply side:	Fragmented & competitive	Relatively concentrated;
Trading:	via a “market price”	prices & terms individually negotiated
Indicators BP:	buyer size relative to mkt	buyer and seller’s “outside options”
Lower prices via:	demand withholding	the threat of purchasing less

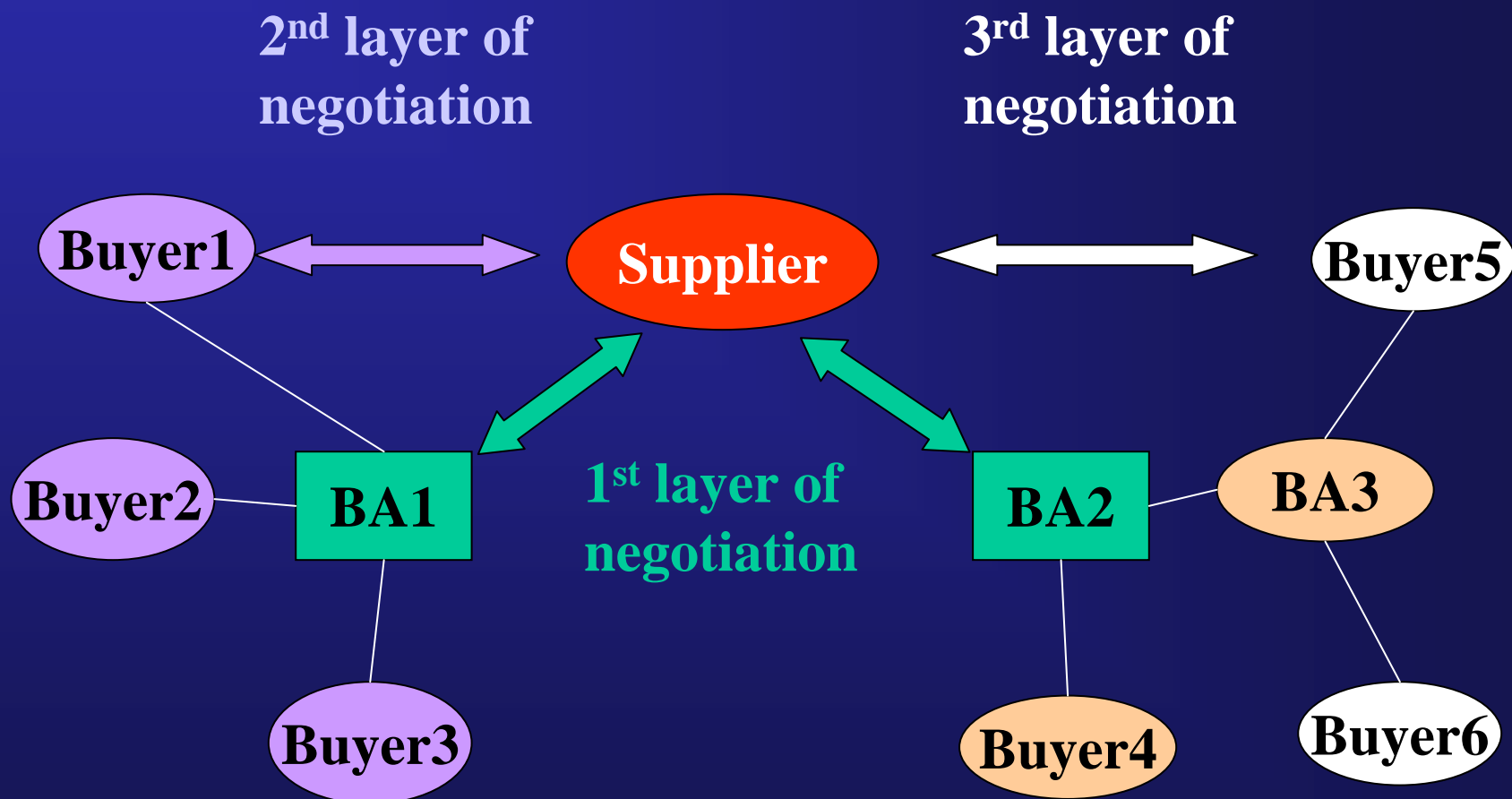
Issues with BP

- **Potentially adverse effects of BP:**
 - Tacit collusion or coordination among buyers
 - Lower supplier investment and innovation
 - Marginalization of competing fringe buyers
 - Waterbed effects
- Trade-off between short-term benefits and long-term negative effects may require a **dynamic approach**
- Should assessment mirror traditional market power analysis? **Issues for agencies and courts:**
 - same market share thresholds for screening?
 - same consumer welfare standard for assessment?

Buying Alliances (BAs) in Italy ⁽¹⁾

- BAs are a manifestation of BP through joint purchasing agreements: positive element for the quite long Italian food chain (2,5 intermediaries on average between producers and consumers)
- Members of BAs are typically supermarket chains, pure wholesalers, wholesalers with a network at retail outlets in franchising or similar agreements, and other smaller BAs
- BAs negotiate “general” terms & conditions for all its members (e.g., discounts off the listed prices), but a second layer of negotiation – bilaterally - occurs between suppliers and individual BA members (and a third layer is BA member is a BA itself)

Buying Alliances (BAs) in Italy (2)



BAs in Italy: Facts & Figures

- **High concentration:** 6 BAs grouping 21 supermarket chains account for the 54% of the total retail grocery sales at national level. Higher concentration at regional/local level
- **Instability of BA composition:** frequent switching of BA member & personnel
- **Heterogeneity of BA composition:** BA members differ in terms of chain size, revenue and cost structure, geographical coverage, outlet types, strategic positioning, pricing policy
- **Negotiations between BAs and suppliers** increasingly cover other aspect **beyond prices** (promotions, category management, sales performance, co-marketing and sponsorship)

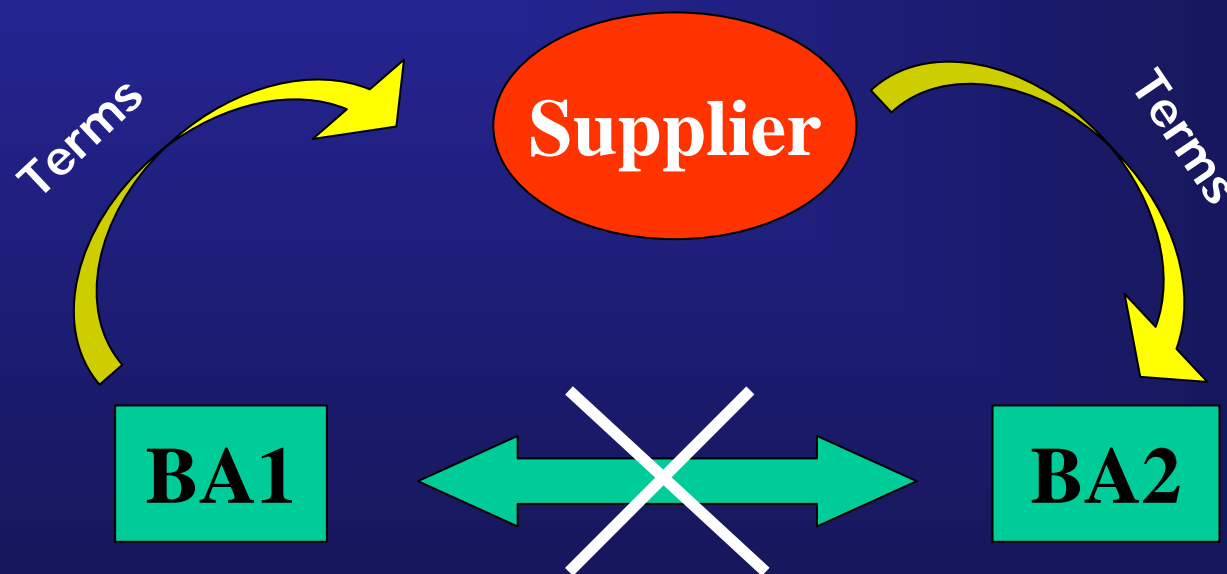
BAs: Competition Concerns (1)

Risk of coordination

- **Frequent switching of BA members and personnel:**
 - Transparency of conditions and strategic information
 - Standardization of negotiating terms on prices and other strategic variables
- **The “triangular” collusion:**
 - BA may enforce their pricing strategies indirectly via their suppliers

BAs: Competition Concerns (2)

Exchange of information on terms & conditions via supplier



BAs: Competition Concerns (3)

Additional long-term adverse effects:

- Membership to a BA may reduce the incentive in pursuing efficiencies
- Increasing dependencies between members of the buying alliance
- Purchasing agreements may ‘rigidify’ the market e.g., damaging innovation in buying practices
- Increase in the market power of BA members in regional retail markets

ICA Survey on Trade Practices

- **Written form of contracts:** 1° layer of negotiation in 82% of the cases, second layer of negotiation only in the 32% of cases
- **Unilateral request of change of terms:**
 - “often” for about 18% of respondents
 - 74% of respondents perceive them as “binding”
 - In case of opposition, 75% of respondents experienced some negative consequences at least once: delisting, worsening of terms and conditions in the next period
- **Buyers comply with their terms of payment:**
 - “Always” in the 18.3% of cases, “often” in the 34.4% while “sometimes” for the 50.3% of respondents. The issue of non-compliance appear to affect especially big suppliers
 - 40% of respondents say that buyers require higher discounts if they are to comply with the terms of payments

New Powers on Unfair Practices

- ICA to enforce three new provisions on contractual relations between suppliers and retailers in trading agricultural and grocery products:
 - Contracts valid only in the written form
 - “Unfair practices” forbidden (no dominance test required)
 - Statutory deadlines for payments: 60 days for non perishable goods (30 days for perishable goods)
- ICA can impose fines up to €0.5m

Implementing Regulation

ICA proposals

- Identification of unfair practices in accordance to the principles and good practices outlined by the Commission in the *High Level Forum for a better functioning of the food supply chain* (29 November 2011)
- Restricting the scope of the prohibition of unfair practices to include only those circumstances where there is an imbalance of the contractual power between the parties which leads to an “abuse”

In any event, in applying these new provisions, ICA will be mindful of any potential spillover effects on competition

THANK YOU!