

Director-General

Check against delivery

## **Future conditions for independent retailer groups**

First of all I would like to thank the retailer association of the ICA retailers for inviting me to this seminar regarding the future conditions for independent retailer groups. This seminar is most topical since EU regulations in this area will be reviewed the coming years. I also note that this seminar runs in parallel to other similar ones in other EU countries.

My remarks here today will focus on some of the issues raised in the report "Leveling the Playing Field" by Professor Paul Dobson. Before going in to these issues I would like to start with some more general reflections regarding the market and the situation of independent retailer groups.

### **The competitive environment for independent retailer groups in Sweden**

The Swedish Competition Authority has for a number of years expressed concern about the situation in the Swedish food market. A number of competition problems have been visible in terms of relative high prices, a lack of new entry to the market and a high concentration in both wholesale and retail markets.

During the last couple of years we have seen that the market has become more dynamic. The result has been visible in terms of falling relative prices and new entry to the market. Part of the explanation behind this has been cross-border entry and increased efficiency due to economies of scale. By e.g. the successful use of own brands the bargaining power has increased among retailers.

During this period the independent retailers in ICA have been thriving in the Swedish market. They are now by far the largest player in the market. We have seen high profits, increased market shares and innovation at the same time as their relative position in the market has strengthened. The success is often attributed to the combination of economic strength through co-operation and entrepreneurship. It thus seems to me that ICA has managed to meet consumer needs and to provide an organization for co-operation between independent retailers. I consequently have problems to recognize the proposition in Paul Dobson's paper that the ability for independent retailers is restricted by legal

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impediments. Facts on the ground in Sweden seem to give little room for this hypothesis.

Currently we are, however, living in a period where conditions in the industry have changed. We have all seen how the industry is "talking up" prices. This is a worrying development. During summer this year trade associations for food producers engaged in an open mouth operation signaling that consumer prices would have to be raised. This was commented by the CEO of the ICA group in the following way: "We are conducting tough negotiations with producers and it is possible that we might be forced to increase prices".

Yesterday – a couple of months later – he commented once again and argued that prices on bread, meat and milk will now increase between 5 – 10 per cent. He stated that: "We have now reached the end of the road ... it will be necessary to accommodate and let some price increases be channeled through".

This means that after a benign development during the last years we are now back to a situation where it will be critical for consumers how well competition works in the market. In such a situation it is important to be vigilant regarding signs of co-ordination in markets. It is also important that the forces of competition are not unduly restricted by practices in independent retailer groups. Competition policy must be able to deal with current problems and it is against this background I would like to give some comments on current regulations.

### **Assessing competition conditions for independent retailer groups**

Paul Dobson argues that independent retailer groups have been constrained by legal impediments and that EU competition policy and law restricts the behavior and relations between members within such groups. He argues that independent retailer groups are limited in their control over retail prices and promotions which is affecting group efficiency. This results in a number of policy recommendations such as:

- The set of agreements used by independent retailer groups should be assessed on their collective and overall net effect,
- Joint purchasing arrangements and purchasing obligations should be assessed on their merits and
- Allowing fixed retail prices as either vertical or horizontal agreements should be considered when they are indispensable in providing consumer benefits from advancing inter-group competition and efficiencies.

As I mentioned earlier it is difficult to see that current policy has restricted the market for independent retailer groups in Sweden. Furthermore I would like to stress that the investigations done by the Swedish Competition Authority have recognized efficiencies? However, there are some practices where competition enforcement and policy must be strict and show a red card for practices that harm

consumers. On the other hand there are other practices where we fall into a more grey area and where there is room for reflection. I will come back to that later.

Another interesting discussion concerns the nature of independent retailer groups. Dobson argues that by being more efficient on an individual level, the independent retailers are better able to compete with larger players in their respective local markets. He also argues that when retail markets are dominated by groups of independent retailers, then not only is there the prospect of inter-group competition but there is also the possibility of a certain degree of intra-group competition.

I would agree with those comments but I would also like to add the following. A strict co-ordination of prices between independent retailers would have the effect of reducing the incentives for innovation and competition among individual retailers within a group. This translates on the macro level to a reduction in competition by the elimination of intra-group competition. This means that the comparison of independent retailer groups with integrated companies is simplified. The concept of the level playing field is not as simple as stated in the paper and independent retailer groups are a more subtle thing than that.

Let me now turn more specifically to our experiences regarding assessments under Article 81.

#### **Assessments under Article 81**

There are important differences between EU and US law that have to be recognized. The Swedish Competition Authority is aware of the development of Competition Law in the US that Erik Söderlind has referred to. We are also aware that the scope of the decision in question is under debate in the US and that legislative measures to return vertical price fixing to the *per se* area has been proposed.

However, as you are all aware, European Competition law is independent of US Competition law. There is in the EU a clear case law that vertical price fixing is a restriction by object. This is not to be confused with a *per se* infringement such as used to be the case in the US. The *per se* rule under US Competition Law eliminates the need to study the reasonableness of an individual restraint in light of the real market forces at work. There are no *per se* infringements under the EC competition rules, thus each case must be assessed on its own merits given the market in question. There are numerous examples of restrictions by object being approved based on the economic and legal context of the agreement in question.

The EC competition rules expressly acknowledge that restrictive agreements may generate objective economic benefits so as to outweigh the negative effects. The efficiencies that can arise through cooperation or distribution schemes must be weighed against the risk for consumer harm. Article 81 provides an appropriate legal framework for this assessment, recognizing the distinction between anti-competitive and pro-competitive effects:

- Article 81(1) prohibits those agreements which appreciably restrict or distort competition,
- while Article 81(3) allows for exemption of those agreements which confer sufficient benefits to outweigh the anti-competitive effects.

When the pro-competitive effects of an agreement outweigh its anti-competitive effects, the agreement is on balance pro-competitive and compatible with the objectives of the competition rules.

The parties to a restrictive agreement must show that the pro-competitive effects of the agreement, to a sufficient degree of certainty, outweigh its anti-competitive effects. Should the parties manage this task the authorities will not take action against the agreement. Let me illustrate this with some recent examples from our Authority.

#### *The ICA investigation*

In 2006, the Authority closed the file on a long lasting investigation into the cooperation structure of ICA AB and its retailer association. In so doing, we closed the file on several of the questions that the paper of Professor Dobson refers to. However, when saying this, it should be noted that the decision was taken without any reference to the vertical block exemption. Questions of exemption under Article 81 (3) are now an integrated part in competition law assessments at every level, from the European Commission through the national courts and NCA:s and down to the day to day conduct of businesses and their legal counsels. The modernization reform has also brought about other changes such as a changed role of the NCA:s. A lot of the focus of our Authority used to be on examining vertical relationships and multi faceted business deals. When the process of negative clearance and exemption was abolished this put the focus of competition authorities on the fight against cartels.

An important aspect to bear in mind when it comes to retail trade is that consumers face supermarkets in a local environment and that local cartels could be just as detrimental for the consumer on the local market as national cartels can be in a European perspective. Beneficial cooperation schemes should therefore not be allowed to become local cartels.

The investigation into the cooperation scheme of the ICA retailers was due to the fact that we felt a great uncertainty in how the mixed relationships within the ICA network functioned with regard to competition law and consumer welfare. At the start of the investigation our focus was with the vertical relationships but with time and increased knowledge the focus of our investigation shifted to the horizontal aspects. This is most assuredly due to the fact that we recognize the benefits of functioning distribution systems.

The result was that not only vertical aspects were reviewed. Horizontal aspects were reviewed as well. The need to preserve and protect brand image through

joint advertisement, internal control mechanisms and last but not least, the need of independent retailers to cooperate in joint purchasing schemes were all considered as pro-competitive aspects, acknowledged by us in light of the fact that we did not intervene.

Furthermore, a short term national wide scheme of maximum pricing with the outspoken aim of lowering consumer prices also passed unchallenged since we found that this particular scheme was connected to preserving brand image and increasing inter brand competition.

However, we challenged some of the horizontal aspects of a system of price recommendations. The reason for this was our assessment of the potential effects on competition and consumers. ICA adjusted their practices when we showed the red card for practices that we judged would harm consumers.

#### *The ACNielsen investigation*

This brings me to the recent decision to close the investigation on the information exchange scheme between all the major retail chains in Sweden through ACNielsen. This information exchange scheme was examined in light of the risk of the information exchange leading to collusion with regard to consumer prices. The investigation showed that the information in question in its current form was presented in such a form and that it would be unlikely to lead to collusion on the local markets of the retailers in Sweden. This is a good example of how the Authority assesses the possible effects of a conduct in light of the market structure in question.

#### *The service shop investigation*

In another recent case of ours we put the focus on a price fixing scheme within two franchise networks in Sweden. The investigation was carried out through an open dialogue with the parties. The price fixing scheme could have eliminated all competition between the two biggest chains of service shops/kiosks in Sweden. The parties did not show any possible efficiencies gained by the price fixing scheme that would outweigh the negative effects of the scheme. However, the investigation was closed with commitments intent on preventing the risks in question.

#### **Concluding remarks**

So to sum up, we believe that the focus of competition authorities should lie in the fight against cartels. At the same time it is important to recognize the efficiencies that can arise through cooperation or distribution schemes. This being said we have not seen evidence of vertical price fixing being instrumental to consumer welfare and we are intent on intervening against vertical price fixing and other kinds of cooperation schemes that are likely to lead to consumer harm. In so doing we always try to see all aspects of the agreement in question and we would never intervene in a case where it would be obvious that the pro competitive aspects outweigh the anti competitive effects necessary for the efficiency aspects in question.

We do recognize the need of legal certainty for organizations such as ICA. But it is important to note that competition law evaluation must be made on a case by case basis with due account to the market power of the parties and the economic and legal context of the agreement.

The last review of the vertical block exemption was a great step forward and signaled a more economic approach both by the European Commission and the NCA's. The block exemption expires in 2010 and the EU Commission's review starts next year. The Swedish Competition Authority is looking forward to be a part of this process. The topic for our annual Pros and Cons conference next year will be "The Pros and Cons of Vertical Restraints". We are looking forward to important contributions to the policy debate regarding competition policy and regulations connected with the challenges we meet in today's markets.