SUBMISSION OF THE NATIONAL GROCERS ASSOCIATION

IN RESPONSE TO THE

U.S. DEPARTMENT OF JUSTICE AND U.S. FEDERAL TRADE COMMISSION

REQUEST FOR COMMENT ON DRAFT UPDATED MERGER GUIDELINES

September 18, 2023

The National Grocers Association (NGA) welcomes the opportunity to provide comments in response to the U.S. Department of Justice Antitrust Division and U.S. Federal Trade Commission's invitation to provide comments on the July 19, 2023 draft update of the Merger Guidelines.[1] NGA represents independent community grocers across the country, as well as their wholesaler partners. Our 21,000 members are the true entrepreneurs of the grocery industry, passionately committed to their customers, their employees and the markets they serve.

NGA commends the Agencies for modernizing the Merger Guidelines to consider the anti-competitive effects of mergers involving competing buyers as reflected in Guideline 11. The draft updated Merger Guidelines reflect a proper concern about the harm to suppliers resulting from powerful buyers. However, NGA respectfully requests that the final updated Merger Guidelines should go farther and directly address the anticompetitive effects of mergers that enhance buyer-side market power that also results in economic discrimination against the merged buyers' competitors. Doing so would fully align Guideline 11 with the Draft Merger Guidelines' overall purpose—articulating a merger enforcement regime that accurately reflects market realities and the antitrust laws and protects the competitive process, consumers and producers.

The Draft Updated Merger Guidelines' Recognition of Mergers that Create Anticompetitive Buyer Power is a Welcome and Necessary Change

As Guideline 11 correctly points out, "a merger between competing buyers may harm sellers just as a merger between competing sellers may harm buyers." And NGA is encouraged that Guideline 11 recognizes that "[a] merger of competing buyers can substantially lessen competition by eliminating the competition between the merging buyers or by increasing coordination among the remaining buyers . . . [and] can likewise lead to undue concentration among buyers, accelerate a trend towards undue concentration, or entrench or extend the position of a dominant buyer." Further, Draft Merger Guidelines Section II.1 helpfully explains that "Concentration" among buyers can also reflect "the number and relative size of firms competing

[1] NGA's references to "Draft Merger Guidelines" refer to the draft Merger Guidelines released for public comment purposes on July 19, 2023, FTC Matter No. P869910.

to purchase a product or service" [2] and that "Concentration is 'high' when the market only has a few significant competitors."[3]

These changes are welcome. As NGA highlighted in its April 21, 2023 comments, the immediate prior merger guidelines[4] did not directly address the potential harms to competition between the buyer and its rivals that stem from enhancement of buyer-side market power, sometimes referred to as monopsony power. Indeed, the prior merger guidelines generally addressed "powerful buyers" only as a potential constraint on a merger's enhancement of seller-side market power, stating that such buyers "are often able to negotiate favorable terms with their suppliers."[5] Only in passing did the prior merger guidelines note that "[s]uch terms may reflect the lower costs of serving these buyers, but they also can reflect price discrimination in their favor," without any discussion of the potential anticompetitive effects of such discrimination.

The Draft Merger Guidelines, and Guideline 11, begin to address these omissions. NGA urges the Agencies to maintain Guideline 11 in the final Merger Guidelines so that the Agencies consider the potential harms to competition of mergers involving competing buyers.

The Final Guidelines Should Go Further to Fully Address the Theories of Harm that Flow from Mergers that Create Anticompetitive Buyer Power

Although NGA appreciates that the Draft Merger Guidelines reflect a proper concern about the harm to suppliers resulting from powerful buyers, the Guidelines should go farther and directly address the anticompetitive effects of mergers that enhance buyer-side market power that also results in economic discrimination against the merged buyers' competitors. NGA's members compete in markets that are increasingly dominated by a handful of national and international chains. These dominant chains have used buyer-side market power to dictate terms and conditions to suppliers, which forces suppliers to discriminate against independent grocers and drives consolidation throughout the supply chain. Buyer-side market power also harms small and mid-sized producers, such as independent farmers and ranchers, who are paid prices far below competitive levels.

The prior guidelines' discussion of buyer-side market power did not reflect modern market realities in many sectors—including grocery—at the retail, wholesale, or producer levels or current economic learning drawn from these sectors. Although the Draft Merger Guidelines acknowledge certain potential harms from mergers that enhance or create buyer power—the harm to suppliers ("artificially suppressed input prices or purchase volume, which in turn reduces incentives for suppliers to invest in capacity or innovation"), the discussion does not address, at least in detail, the potential for transactions to create anticompetitive buyer-side bargaining leverage that enables discrimination against smaller rivals.

This would be a significant omission. Anticompetitive transactions threaten the competitive process at the retail level with anticompetitive effects on consumers as well as upstream on

[2] Merger Guidelines, Section II.1, 6, n. 24.
[3] *Id.* Section II.1, 6.
[4] NGA's references to "prior merger guidelines" refer to both the 2010 Horizontal Merger Guidelines and the 2020 Vertical Merger Guidelines unless otherwise specified. RFI n. 3.
[5] Horizontal Guidelines at § 8.

producers. The anticompetitive effects include reduced grocery competition at the retail level, higher prices, and reduced choice and quality for consumers. They also include increased concentration in the grocery supply chain, reducing alternatives for independent retailers, producers, and consumers as well as making the supply chain more vulnerable to disruption.

Market Realities and Economic Learning Require Stricter Scrutiny of Mergers that May Enhance Buyer-Side Market Power and Facilitate Economic Discrimination

The final, updated Merger Guidelines should include in their description of anticompetitive buyer-side market power a purchaser's ability to use its bargaining leverage to impose discriminatory terms on the purchaser's rivals—i.e., obtain price or supply concessions that are not available to its competitors.[6] The final guidelines should indicate the Agencies' intention to challenge mergers that create or enhance such buyer-side market power. Doing so would reflect market realities and current economic scholarship in the grocery sector. Basing enforcement on these principles would protect the competitive process, consumers, and independent producers.

In the grocery sector, the large national chains have significant bargaining leverage over suppliers because the national chains are critical "gatekeepers" between grocery suppliers and consumers.[7] These retailers control a substantial proportion of the shelf space—whether physical or digital—that provides the key distribution channel for suppliers' products.[8] For example, the top five national grocery retailers control approximately 60 percent of grocery sales.[9] One national chain, Walmart, controls one in four dollars spent by American grocery consumers.[10]

This bargaining leverage is asymmetric; the largest grocery retailers are not nearly as dependent on a particular supplier as the supplier is on the retailer. This is because a particular grocery supplier's products generally represent only a small fraction of a grocery retailer's sales, which may encompass tens of thousands of products.[11] And a dominant retailer often enjoys several potential branded suppliers for a particular product in addition to selling its own, private label brand versions. As a result, a dominant retailer has a substantial advantage over its suppliers in a negotiation because the risk for the retailer, if the supplier refuses its demands and no deal results, is substantially smaller than it is for the supplier.[12]

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[6] John B. Kirkwood, *Buyer Power and Exclusionary Conduct*, 72 ANTITRUST L. J. 625, 652 (2005).
[7] Sofia Berto Villas-Boas, Vertical Relationships Between Manufacturers and Retailers: Inference with Limited Data, 74 REV. OF ECON. STUDIES 625, 647 (2007) (analysis of U.S. wholesale and retail yogurt prices consistent with "high bargaining power of retailers" relative to manufacturers).
[8] Paul Dobson, *Exploiting Buyer Power: Lessons from the British Grocery Trade*, 72 ANTITRUST L. J. 2, 555 (2005).
[9] Prepared Testimony and Statement for the Record of David Smith, President & CEO, Associated Wholesale Grocers, Hearing on "Beefing Up Competition: Examining America's Food Supply Chain" Before the Senate Judiciary Committee (July 28, 2021); *see also* Claire Kelloway and Sarah Miller, *Food and Power: Addressing Monopolization in America's Food System*, Open Markets Institute, Mar. 27, 2019, http://www.openmarketsinstitute.org/publications/food-power-addressing-monopolization-americas-food-system.
[10] Stacy Mitchell, *Walmart's Monopolization of Local Grocery Markets*, INST. FOR LOCAL SELF-RELIANCE, June 2019, https://ilsr.org/wp-content/uploads/2019/06/Walmart_Grocery_Monopoly_Report-_final_for_site.pdf.
[11] *Id.*
[12] *Id.*

Because of this asymmetry in leverage between the largest grocery buyers and grocery suppliers, buyer-side market power in the grocery sector can exist at market shares and concentration (of purchases) that are lower than would traditionally trigger concerns over seller-side market power. For example, one national meat processor disclosed in SEC filings that Walmart would have the ability to inflict "significant setbacks in sales and operating income" if it moved its business to another supplier based on the fact that Walmart represented 18.3 percent of the processor's sales in 2018.[13] A major consumer food and beverage brand recently disclosed that maintaining Walmart as a customer was a requirement for it to "compete effectively" against other suppliers because Walmart represents approximately 13 percent of its net revenues.[14]

The indispensable buyer's leverage is particularly acute in industries such as grocery which has a long tail of relatively smaller—albeit still large, multi-billion dollar—competitors. For example, the largest private label supplier recently disclosed Walmart as essential at 22.5 percent of its net sales, noting that "no other customer accounted for more than 10 percent" of sales.[15] This market evidence of buyer-side market power through bargaining leverage is consistent with economic studies of the grocery sector, which find asymmetric bargaining leverage exists at shares as low as 10 percent.[16]

Both the prior merger guidelines and the Draft Merger Guidelines fail to account for this buyer-side bargaining leverage dynamic. The prior guidelines suggest the Agencies use their seller-side framework for analyzing market power on the buyer side.[17] For example, the 2010 Horizontal Guidelines state that "[m]arket power on the buying side of the market is not a significant concern if suppliers have numerous attractive outlets for their goods or services."[18] As the above real-world examples indicate, numerous buyers are not a palliative for buyer-side market power if even one of those buyers is significantly larger than the others. Moreover, analysis of grocery mergers' impact on grocery consumers has traditionally focused on competitive effects in local geographic relevant markets.[19] However, using the local markets to analyze buyer-side market power could underestimate the bargaining leverage that a substantial national buyer would have over national and regional suppliers.[20]

Consistent with the prior merger guidelines' relative silence on the topic, NGA is not aware of the Agencies challenging a transaction on the grounds that it would enhance the combined firm's ability to demand anticompetitive price discrimination that disfavors rivals—in retail sectors or

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[13] Tyson Foods, Inc., Form 10-K Annual Report for the Fiscal Year Ended Oct. 2, 2021 (Nov. 15, 2021).
[14] PepsiCo, Inc., Form 10-K Annual Report for the Fiscal Year Ended Dec. 25, 2021 (Feb. 10, 2022).
[15] TreeHouse Foods, Inc., Form 10-K Annual Report for the Fiscal Year Ended Dec. 31, 2021 (Feb. 15, 2022).
[16] Paul Dobson, *Exploiting Buyer Power: Lessons from the British Grocery Trade*, 72 ANTITRUST L. J. 2, 534 (2005); *see also* PepsiCo, Inc., Form 10-K Annual Report for the Fiscal Year Ended Dec. 25, 2021 (Feb. 10, 2022) ("In 2021, sales to Walmart Inc. (Walmart) and its affiliates, including Sam's Club (Sam's), represented approximately 13% of our consolidated net revenue . . . . The loss of this customer would have a material adverse effect on our FLNA, QFNA and PBNA divisions.").
[17] Horizontal Guidelines at § 12.
[18] *Id.*
[19] Daniel Hosken, Luke M. Olson, Loren K. Smith, *Do Retail Mergers Affect Competition? Evidence from Grocery Retailing*, Fed. Trade Comm'n Bureau of Competition Working Paper (Dec. 2012).
[20] FTC Letter to Albert A. Foer, President of the American Antitrust Institute (Feb. 27, 2003) (analyzing monopsony power based on local geographic markets), https://www.ftc.gov/sites/default/files/documents/cases/2003/02/ftc.gov-letterfoer.htm.

otherwise.[21] A 2012 FTC retrospective study on the impact of grocery store mergers on competition did not even address retail buyer power.[22] In response to public comments on the consent decree relating to a large national chain's acquisition of a local chain in Puerto Rico, the FTC staff suggested that the FTC had not examined whether the transaction would give the combined firm increased bargaining leverage to the detriment of competing grocery stores or competition.[23]

Mergers that create or enhance buyer-side market power through bargaining leverage can have multiple anticompetitive effects. For example, disproportionate buyer-side bargaining leverage can create the ability and incentive for the buyer to impose discriminatory prices and terms on competitors through common suppliers. Because powerful retail buyers are the gatekeepers to consumers, suppliers have no leverage to resist discriminatory demands.[24] This allows the buyer to secure more advantageous terms for itself and impose higher purchasing costs or other disadvantages on its rivals, as suppliers seek to make up for the discounts and other advantages they are forced to extend to the powerful buyer with higher charges to other buyers.

Economists call this phenomenon "the waterbed effect," and have explained how it harms consumers as well as rivals:

> While a large and powerful firm improves its own terms of supply by exercising its bargaining power, the terms of its competitors can deteriorate sufficiently so as ultimately to increase average retail prices and, thereby, reduce total consumer surplus. Such consumer detriment from the waterbed effect is more likely if the adversely affected firms are already sufficiently squeezed, due to relatively higher wholesale prices and, consequently, lower market shares.[25]

Economists have observed this effect in the grocery industry, explaining that buyer power allows dominant players to enter into a "virtuous circle" in which they use their power to undercut

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[21] NGA understands that the proposed merger of Kroger and Albertsons is under investigation by the FTC and several state attorneys general and that the investigation is reportedly looking into not only the potential anticompetitive effects such a merger would have on consumers, but also its potential to enable anticompetitive price discrimination from suppliers that disfavors the buyer's rivals. *See* Diane Bartz, Focus: *FTC queries on Kroger's Albertsons deal focus on small grocers*, REUTERS (Aug. 10, 2023), https://www.reuters.com/markets/deals/ftc-queries-krogers-albertsons-deal-focus-small-grocers-2023-08-10/.

[22] Daniel Hosken, Luke M. Olson, Loren K. Smith, *Do Retail Mergers Affect Competition? Evidence from Grocery Retailing*, Fed. Trade Comm'n Bureau of Competition Working Paper (Dec. 2012).

[23] *See* FTC Letter to Albert A. Foer, President of the American Antitrust Institute (Feb. 27, 2003) (discussing the "monopsony and vertical issues" that the staff apparently considered), https://www.ftc.gov/sites/default/files/documents/cases/2003/02/ftc.gov-letterfoer.htm.

[24] *See, e.g.*, Albert Foer, *Abuse of Superior Bargaining Position (ASBP): What Can We Learn from Our Trading Partners?*, AAI Working Paper No. 16-02 (2018), https://www.antitrustinstitute.org/wp-content/uploads/2018/09/AAI-Working-Paper-No.-16-02.pdf (detailing laws related to abuse of superior bargaining position outside the United States and arguing that "a serious gap exists in the law regulating vertical relations" in the U.S.).

[25] Roman Inderst & Tommaso M. Valletti, *Buyer Power and "The Waterbed Effect,"* LIX J. INDUST. ECONOMICS 1, 2, (2011); *see also* Paul W. Dobson & Roman Inderst, *The Waterbed Effect: Where Buying and Selling Power Come Together*, 2008 WIS. L. REV. 331, 336-37 (2008) (discussing the circumstances that can give rise to the waterbed effect, and how the phenomenon can distort downstream competition and harm consumers).

smaller rivals and gain market share, which they then exploit to further undercut smaller rivals and capture even more market share.[26]

Competition authorities outside the United States have investigated the problems associated with buyer power and economic discrimination in the grocery industry.[27] For example, in 2000, the U.K.'s Competition Commission released a study of the grocery industry that identified 52 practices by dominant grocery retailers that could have potentially distorting effects on supplier and/or retailer competition. The Commission concluded:

> These practices, when carried on by any of the major buyers, adversely affect the competitiveness of some of their suppliers with the result that the 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.[28]

In the United States, wholesale prices offered to independent grocers' wholesalers can often be higher than observed *retail* prices at large national chains. This is despite the fact that these independent wholesalers purchase billions of dollars of product by the truckload and operate their own warehouses and logistics networks—offering suppliers the same efficiencies and cost savings that the national chains offer. Yet suppliers refuse to offer independent wholesalers the same terms extracted by the largest buyers. The fact that this discrimination in terms and price is not justified by efficiencies is further evidence that it is driven by naked buyer-side market power.

Another anticompetitive effect of unchecked buyer-side market power is increased concentration upstream in the grocery supply chain. Power buyers' demands on suppliers for lower costs are forcing consolidation among food and consumer goods manufacturers.

Supply chain concentration is particularly acute in private label manufacturing—the grocery supply sector that manufactures store brand versions of food products and consumer goods, such as paper products and packaged foods. Store brands are important alternatives to branded products for consumers and retailers alike. But under pressure from dominant retailers, the private label sector is consolidating dramatically. For example, today there is only a single major private label manufacturer of canned soups, and there is significant consolidation in

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[26] *See* Dobson, *supra* note 16 (noting that the circle is only "virtuous" for the dominant retailer but "vicious" for the smaller, independents).

[27] *See, e.g.*, OECD, Competition issues in the Food Chain Industry (2013) (incorporating submissions from over 30 competition authorities).

[28] U.K. Competition Comm'n, *Supermarkets: A Report on the Supply of Groceries From Multiple Stores in the United Kingdom* at 7, https://web.archive.org/web/20070109000906/http://www.competition-commission.org.uk/rep_pub/reports/2000/fulltext/446c1.pdf. The 2013 OECD survey of market conditions in the food supply chain across 30+ countries concluded that "increasingly dominant retail firms" was an already common but increasing trend across many countries. OECD 2013, *supra* note 27, at 36.

private label manufacturing in a diverse list of other products from canned fruit and pasta, to snack foods, and paper products.

Concentration in the grocery supply chain does not insulate it from retailer buyer power; it makes suppliers even more beholden to leverage. As manufacturers consolidate, they become more dependent on the largest buyers, who represent a substantial portion of their sales. Small and mid-sized grocers actually see their relative value to manufacturers decline, even when they pool their purchasing through wholesalers. As a result, the largest retailers effectively dictate supply decisions to grocery suppliers. This has become particularly acute in the private label sector. For example, private label manufacturers are forced to prioritize runs ordered by their biggest buyers, limiting capacity for products sought by independents. They have also narrowed their available products in order to serve demand from the largest buyers, reducing product diversity and consumer choice.

Invariably, products sought by small and medium-sized grocers are the ones eliminated. Some private label manufacturers have largely dedicated their capacity to dominant national chain grocers, foregoing independents' business almost entirely. Not only does this harm independent grocers and their customers directly, through loss of these popular products especially for cost-conscious consumers, it also reduces independents' bargaining leverage with branded suppliers by eliminating alternative sources of product supply to which independents might switch. As a result, independent grocers are even less able to push back on discriminatory treatment imposed by retailers with buyer-side market power.[29]

In addition to reduced product choice and increased prices for independent grocers and their consumers, greater supply chain concentration can result in anticompetitively low prices paid to independent producers, such as ranchers and farmers. And manufacturer concentration can make the grocery supply chain more vulnerable to disruption due to natural disasters or a pandemic.

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Merger enforcement under Section 7 of the Clayton Act and Sections 1 and 2 of the Sherman Act is a critical tool to deter and prevent the enhancement and creation of buyer-side market power. The Agencies should use this tool together with others in its law enforcement toolbox—including the Robinson-Patman Act and Section 5 of the FTC Act—to remediate and prohibit the anticompetitive effects of buyer-side market power, such as economic discrimination that harms the competitive process. NGA is encouraged by the Agencies' work to modernize the Merger Guidelines to better reflect the competitive harms that result from mergers among powerful buyers. NGA appreciates the opportunity to provide further comments on the Draft Merger Guidelines and looks forward to continuing to engage with the Agencies on these important issues.

[29] *See* Dobson, *supra* note 16 (describing private label as an important negotiating level for grocery retailers).