

Buyer power:

Understanding and assessing
its potential positive and
negative effects

Dr Nicola Mazzarotto
Competition Commission

Any views expressed during this presentation are my own and do not necessarily reflect the views of the CC or of any of its members.



Plan of the presentation

1. A framework for considering buyer power
2. Buyer power: possible adverse effects
3. Buying efficiencies and countervailing power
4. Conclusions



1. A framework for considering Buyer Power



1. Buyer power – analytical framework: what is it and how to think about it

Buyer power is “market power held by the buyer” - Context: intermediate markets.

In order to use this definition we have to be more specific...

From the point of view of economic analysis there are two broad ways of describing how sellers and buyers meet and trade. This distinction is quite important:

Market framework:

- Supply side: Fragmented and competitive;
- Trading: via a “market price”;
- Indicators of BP: buyer size relative to market might help.

Or

Bargaining framework:

- Supply side: Relatively concentrated;
- Trading: prices and terms are individually negotiated;
- Indicator of BP: buyer and seller’s “outside options”, ie their alternatives to reaching an agreement.

For a complete treatment see: R. Inderst and N. Mazzarotto “Buyer power in distribution”. In “Issues in Competition Law and Policy”, American Bar Association Antitrust Section Handbook, W.D. Collins



2. Buyer Power: possible adverse effects



2. Buyer power – Possible adverse effects

In a “market framework”

Buyer power can act as the “mirror image” of seller market power if buyers face a supply curve that “slopes up”.

With increasing marginal cost of supply, the incentive to lower input prices translates into lower quantity sold in the intermediate (and ultimately the final) market. This is referred to as:

Demand withholding

- Conditions:
 - Fragmented and competitive supply;
 - “market price”;
 - Increasing marginal cost of supply (in practice not so common?).
- } Market framework
- Indicator of buyer power: buyer size relative to the market
 - Cases:
 - Groceries inquiry: No evidence of DW in four sectors analysed (fresh fruit, meats...);
 - Stonegate/Deans (Eggs): concerns of DW effects of the merger.



2. Buyer power – Possible adverse effects

In a “bargaining framework” 1/2

Buyer power is typically seen as beneficial (*countervailing*) or neutral (transfer of rents).

However differential pricing and discounts to powerful buyers have raised concerns:

Discounts to powerful buyers: waterbeds and vicious cycles

- Conditions:
 - Prices set in bilateral bargaining (“bargaining framework”);
 - Bargaining strength derives from buyer’s size;
 - Harm to consumers in narrow set of circumstances.
- Indicators of buyer power: bargaining parties’ relative “outside options”
empirical analysis of wholesale prices paid by different buyers, etc.
- Cases:
 - Groceries inquiry: Waterbeds could harm consumers in theory but not likely in UK market;
 - EU retail mergers (eg Rewe/Meinl; Carrefour/Promodes).



2. Buyer power – Possible adverse effects

(typically) in a “bargaining framework” 2/2

Buyer power may raise concerns if it affects firms’ ability to invest and innovate

Adverse effects on investment and innovation

- Conditions:
 - Likely to be very case specific as buyer power “per se” in principle can also increase incentives to invest;
 - Need to identify a mechanism (eg a certain practice) through which buyer power adversely affects investment; dependent on type of investment, source of buyer power, etc.
- Indicators: empirical analyses more difficult as the “counterfactual” is less easily observed. Likely emphasis on the mechanism itself.
- Cases:
 - Groceries inquiry: harm identified in relation to specific practices;



3. Buying efficiencies and countervailing power



3. Buying efficiencies and countervailing power

Buyer power might lead to efficiencies or it might be held by customers who could be “strong enough” to counter detriment arising from a merger of suppliers.

Buying efficiencies:

- Should be understood and explained in the context of the input market in which they arise;
- Part of the rationale for the merger;

“Countervailing power”:

- Should be understood and explained in the context of the market in which it arises;
- Broad “shield”?
- More likely if buyer power depends on ability to integrate backwards or sponsor entry.
- Integral part of SLC analysis. No afterthought or trump card.

For a complete treatment see: R. Inderst and G. Shaffer “Buyer power in merger control”. In “Issues in Competition Law and Policy”, American Bar Association Antitrust Section Handbook, W.D. Collins



4. Conclusions



4. Conclusions: some final thoughts

In order to properly assess buyer power it is important to understand its context:
what is its source and how it manifests itself;

No easy general approach to assess the effects of buyer power “per se”;

Indicators of buyer power and possible analyses change depending on the context
and the issue under consideration;

Parties (eg sellers) can help authorities by explaining the negotiating process in
detail and the determinants of bargaining strength as well as the context of
any possible adverse effects (eg on innovation) or countervailing forces; after
all sellers are the experts on buyer power...