Buyer Power in FMCG Mergers

Michael Rowe, Slaughter and May
Outline

- Buyer power in merger assessment – where does it fit?
- Criteria for establishing buyer power
- Helpful factors
- Unhelpful factors
- Is too much weight given to negative factors?
- Implications of current approach – an impossible threshold?
- An alternative analytical framework?
Buyer power in merger assessment – where does it fit?

Unilateral effects

- Current approach: establish likelihood of price increase then consider mitigating factors, and whether buyer power is sufficient to eliminate potential of price increase (Unilever/Sara Lee, BAT Skandinavisk/ Tobakskomagni)

- Alternative? Consider buyer power as one of several factors (low barriers to entry, alternative suppliers, low switching costs) in weighing up likelihood of price increase

Portfolio effects – a greater willingness to accept buyer power? (P&G/Gillette)
Criteria for establishing buyer power

The test (*Guinness/Grand Metropolitan*):

- Certain customers account for large proportion of sales **AND** have the necessary technical facilities and bargaining skills to apply advantage
- Credible alternative suppliers

Horizontal Merger Guidelines

- may need to consider retailers' incentives to resist price increase
- must not just protect one customer segment
- must continue to exist post-merger

**Very difficult to satisfy these criteria in FMCG**
Helpful factors

- Concentrated customer base
  - certain customers account for large proportion of supplier's sales
- Strong competitors
  - ability to de-list and switch to alternative suppliers
- Gatekeeper role
  - control access to consumers through shelf space
- Retailer private labels
  - ability to switch to own private labels
  - knowledge of supply margins
Unhelpful factors

- "Must-have" brands
  - Is brand loyalty so strong that customers are unable to de-list?
- Cost to retailer of applying threats (e.g. delisting)
  - Potential loss of sales and customers
  - Are there sufficient alternatives both pre- and post-merger?
- Small customers
  - Unable to exert buyer power?
- Retailer incentives – a new obstacle to proving buyer power?
  - Will customers resist a price increase if it is applied across the market?
Is too much weight given to negative factors?

- Is there any such thing as a "must-have" brand?
- What about cost to supplier?
- Can small retailers exert bargaining power?
- Evidencing buyer power and incentives – margin analysis?
Implications of current approach – an impossible threshold?

- Merger analysis arguably does not take into account the full influence of buyer power
  - May be an important factor even where does not eliminate the risk of a price increase
  - Disproportionate weight is given to unhelpful factors
- Private label arguments have been subsumed by buyer power which diminishes their importance in merger assessment as a separate competitive constraint
An alternative analytical framework?

- Buyer power as one of several cumulative factors
- Apply economic bargaining power principles to re-evaluate weight given to unhelpful factors
- Private labels as a constraint that exists independently of buyer power