



Provisional findings report

A response

INTRODUCTION

The British Brands Group welcomes the opportunity to comment on the Competition Commission's Provisional findings report following its investigation of the UK groceries market. The Group represents brand manufacturers in the UK and we therefore concentrate on those aspects of the findings that specifically affect our members and consumers of their products.

We focus our response therefore on buyer power, supply chain practices, competition between branded and own label goods, packaging that misleads consumers and category management.

BUYER POWER

We note the finding that all grocery retailers and wholesalers are, in certain circumstances, able to exercise buyer power in relation to at least some of their suppliers (para 8.18). Whilst we do not disagree with this assessment, we consider that it fails to strike at the heart of the issue and the conditions under which buyer power may raise important competition concerns.

As we outlined in our response to the Notice of possible remedies, buyer power is greatest when a retailer has the ability to delist a supplier or some of its products. Suppliers which are second or third in the market are at particular risk although leading brand manufacturers are also affected, consumer choice being damaged as a result. Commonly certain pack sizes or varieties are delisted and, in the case of a brand leader, it is normally its secondary brands rather than leading brands that are taken off the shelf. Delisting by a major retailer can reduce the available market for that supplier substantially and the impact of lost sales upon the supplier's profit is disproportionately large while the cost to the retailer in lost sales is relatively small. The cost to the retailer is mitigated as it can fill the shelf space with apparently close substitutes, such as other brands and own label products.

Thus the ability to exercise buyer power is greater when:

- (1) a retailer's market share is relatively large;
- (2) there is a threat of direct and significant loss of sales to the supplier (the loss in retail sales via a symbol group is not direct where the affiliation between buyer, wholesaler and retail store is loose¹);

¹ Where there are competing wholesalers the independent retailer, albeit part of a symbol group, can obtain 'delisted' products from alternative wholesalers or cash & carries. This in turn diminishes the buyer power of the symbol group.

- (3) there is the availability of apparently close substitutes, which makes it easy for the retailer to fill the “empty” shelf space.

It is important to recognise that in practice the way that retailers often exert buyer power is not necessarily to activate certain of the practices identified in the 2000 report and in the Provisional Findings but rather to use the threat of such behaviour in order to impose their will on suppliers. In the conditions outlined above, such a threat can be extremely effective in ensuring suppliers’ acquiescence to demands.

The Provisional findings do not distinguish between differing levels of buyer power (other than to state that major retailers may have buyer power in relation to more of their suppliers) yet we feel this is crucial to understand relationships between major retailers and suppliers in this market and the conditions under which competition problems may arise. This is relevant not just to the Supermarket Code of Practice (SCOP) and those retailers that should and should not be covered by it, but also to the wider climate of relationships between major retailers and their suppliers beyond practices covered by the SCOP.

SUPPLY CHAIN PRACTICES

We have analysed the practices from 2000 that the CC has assessed (Appendix 8.10, Annex 3) and while we concur with the majority of the analysis, there are some aspects that concern us.

As a general comment, we note that the discussion focuses on supplier uncertainty that may adversely affect investments and result in diminished supplier competition, all points with which we agree. However, when these practices are used by the major retailers, we consider that there must also be some concern that they will have a distorting effect on retail competition, with small retailers being disadvantaged either directly or indirectly. The dismissal of the five practices that may be used to influence the cost of supply or product availability for competing retailers (para 8.46) suggests that insufficient consideration has been given to the potential distortion of competition at the retail level (such as raising costs to smaller retailers or softening competition by allowing major retailers to further differentiate their offers) as well as at the supplier level. We urge the CC to give greater consideration to this likely harm before it reaches its final findings.

Remedy re. supply chain practices

As regards supply chain practices, we suggest it would be appropriate to include in the SCOP a requirement on major retailers to conduct their trading relationships with suppliers fairly and lawfully, in good faith and without duress, recognising suppliers’ need for certainty in relation to the risks and costs of trading.

In relation to specific practices:

ID9 (‘pay to play’ payments from suppliers): This practice concerns lump sum payments and reference is made to the CC’s concerns that such payments may represent a barrier to entry (ID2). In the case of ID2, such payments are considered a possible problem while in ID9 they are not, despite the same rationale being applied. There is an inconsistent approach here.

ID31 (delisted any suppliers of branded products in favour of your nearest own label equivalent): This directs us to Appendix 8.11 for an explanation of why this may constitute a current problem but we are unable to find an explicit explanation. This clause as worded may represent an unduly restrictive straitjacket on retailers and introduce a constraint on

competition. There may be many justifiable circumstances when a retailer may wish to replace a branded product with an own label equivalent. The concern of brand manufacturers relates more to powerful retailers using the *threat* of delisting, with the uncertainty serving to undermine brand investments and / or retailers seeking benefits that would either put smaller retail customers at a competitive disadvantage or more generally reduce the intensity of head-to-head retail competition (such as requiring exclusive brand variants or pack sizes). A SCOP that discourages relationships between retailers and suppliers that rely on intimidation and undue pressure (and which inevitably distort competition) would be a more constructive and effective approach. It is worth recalling that if a retailer were dominant then many of the practices, including ID31, would very likely be deemed to be abuses within the meaning of Chapter II of the Competition Act, either because they impose unfair trading conditions or because they limit production or markets to the detriment of consumers. The approach suggested in our proposed revised SCOP would be an effective and proportionate way to address ID31 and other harmful practices.

ID39 (over-ordered goods at a promotional price that are subsequently sold at a higher price): we remain deeply puzzled that this practice, considered a problem in 2000, is not considered a problem in 2007. Aside from the harm to suppliers (through the waste of money invested in funding promotional prices for goods), the consumer detriment is clear. The retailer is failing to pass through the special promotional price from the supplier to the consumer, so the consumer ends up paying more while the retailer clearly benefits by pocketing the difference between the promotional price from the supplier and the higher price paid by the consumer. Leaving aside the fact that in some cases such a practice could potentially be considered to be a breach of contract, we consider that this is a practice that generally harms consumers and should be stopped. If it is not discouraged, then in future consumers may see fewer promotions that give them lower prices.

COMPETITION BETWEEN BRANDED AND OWN LABEL GOODS

We are pleased that the competitive effects of retailers selling own label products have been investigated by the CC. We are concerned however that the potential *distortion* caused by own-label development on brand manufacturers' incentives to invest and innovate is not addressed to any real degree in the findings, in terms of socially detrimental *under*-investment in some instances and socially wasteful *over*-investment in others.

Specifically, there is no assessment of the actual impact that the ability of major retailers to develop product ranges that closely mimic branded products has on incentives to invest in innovation. Radical product innovation becomes increasingly risky and unlikely to achieve appropriate returns if major retailers can rapidly develop equivalent products in the knowledge that they have guaranteed access to shelves and therefore to consumers. This problem is exacerbated by the difficulty suppliers experience in enforcing their intellectual property rights in their genuinely new and differentiated products against major retail customers who are also such significant direct competitors.

In contrast, the threat of mimics obliges brand manufacturers to keep amending existing products' appearance and introduce minor formula variations to keep "one step ahead". Consumers therefore are likely to lose out on more radical product development, instead being faced with less needed product formulation and packaging redesign, all driven by retailers' ability to develop and sell very similar own label products.

Clearly, any measure that can alleviate this investment distortion, while ensuring that supplier competition remains effective and vibrant, will help consumers be better served in respect of product innovation and real product choice.

We particularly note that the single most important competitive concern arising from the simultaneous customer / competitor status of retailers (the exchange of confidential information between suppliers and retailers who compete with own label products) warrants only a passing reference (para 8.63 and Appendix 8.11, para 42).

To summarise our concern in this regard, brand manufacturers divulge crucial commercial information relating to new product launches and marketing plans to retailers many months ahead of launch. This information is required by retailers in order for them to determine their stocking and shelf allocation policies and is beneficial to suppliers (and consumers) by obtaining the retailer's input to the initiative. The competition concern however arises in those instances where the retailer has own label products. In such instances, the retailer is in effect a competing supplier, as it specifies (in every detail) the product to be produced for sale under its retail brand name. The exchange of highly sensitive commercial confidential information, while legitimate between supplier and retailer (acting as retailer), we believe may give rise to competition concerns when exchanged between supplier and retailer (acting as competitor).

Briefly, the competition issues that arise from this exchange of information are (1) the potential for retailers with own label ranges to foreshorten the period over which brand manufacturers may earn a return on their new product and marketing investment, (2) the potential to distort competition between suppliers, as the retailer (as own label specifier) is receiving details of a competitor's activity many months prior to launch, while other suppliers (ie. directly competing brand manufacturers) must wait for the product to appear on the market before being able to plan how to respond competitively and (3) the ability of the own label manufacturer to distort competition by passing this information on to its other customers (ie. other retailers with own label ranges that may be made by the same own label manufacturer).

The evidence that the CC has gathered does not address this practice. None of the factors assessed - levels of innovation, who is doing the innovating (brand manufacturer and / or own label supplier), shares of own label by category, the drivers of own label success – shed light on whether there is a potentially harmful exchange of information between brand manufacturers and own label retailers.

Remedy re. the exchange of information between suppliers

The anti-competitive practice to be stopped is the passing of a brand manufacturer's commercially sensitive information by a retailer to its own label supplier, in advance of that information being publicly available on the market (ie. at product launch). At present, suppliers' requests (or even explicit contractual obligations) for retailers to keep new product and marketing plans confidential tend to fall on deaf ears and often are not enforced by the supplier for fear of not securing the retailer's shelf space or support. It is a significant example of where buyer power inhibits suppliers, in this case from preventing misuse of their confidential information.

An undertaking by retailers with own label ranges to safeguard brand manufacturers' confidential and commercially sensitive information until publicly available in the market would be proportionate and realistic.

We suggest that the sharing of information beyond those to whom, and the purpose for which, it was intended should be proscribed in a revised SCOP, with the following suggested wording:

Confidentiality:

Allowing confidential information supplied by a Supplier in relation to its products, including product plans, pricing data, promotional plans and other confidential information, to be accessible to anyone other than those personnel assigned to that Supplier's account or for purposes other than that for which the information was supplied.

Such a measure, monitored and enforced by the proposed monitor / enforcer (see our response to the Notice of possible remedies, 23rd November 2007), would represent a significant step forward from the current position.

PACKAGING THAT MISLEADS CONSUMERS

There are two aspects of misleading packaging that we strongly believe warrant further investigation: (1) copycat packaging and (2) misleading claims on pack. Each is taken in turn.

(1) Copycat packaging

The Provisional findings ignore crucial evidence on this practice and do not seem to reflect a full analysis of the issue. Indeed, there is a sense of claim and counterclaim between this organisation and retailers rather than an independent assessment by the CC of the evidence and the consumer detriment.

- the CC quotes an academic study that reviewed different research on the subject. Importantly this concludes that "some degree of association appears to be drawn from the packaging". While the review dismisses as inconclusive many of the academic studies because the sample sizes were too small (around 50), it did not assess the two most significant pieces of consumer research into the practice, one by the Consumers' Association (2,000 respondents) and one by ourselves (3,994 respondents), both in 1998.

We must also question the review's judgement, where it states "only 19% felt that own labels and manufacturer brands looked so similar that they confused the two" (emphasis added). This is a significant level of confusion, potentially affecting well over 4 million shoppers.

The evidence clearly shows that the consequences of copycats for consumer welfare go beyond their free-riding aspects (on packaging design and consumer goodwill towards the brand) that serve to undermine brand manufacturers' investments.

Evidence: We consider the academic review quoted by the CC to be incomplete. We have submitted copies of all the original research to the CC (letter to Michelle Goddard, 4th June 2007) although we note that these are not referenced in the Provisional findings. We believe that the evidence of confusion is overwhelming. Given that packaging can be designed so as not to confuse, it begs the question why such packaging continues to be produced as it clearly influences consumers' buying behaviour.

- We note that the CC has rightly focused its analysis on the context of competition law (Appendix 8.11, para 16). However we strongly contest Tesco's suggestion that existing legislation addresses retailer behaviour in this area. This suggestion is totally at odds with a recent independent and highly authoritative study into the UK's intellectual property

framework commissioned by HM Treasury (The Gowers Review, 2006) which concluded that brands are insufficiently protected from this type of misappropriation.

- The two customer research reports produced for Tesco shed no light on the effects of copycat packaging (Appendix 8.110, para 15). We have never claimed that a copycat strategy is adopted wholesale (it tends to be used in a highly targeted manner, on a minority of products) so we are not surprised that some reports do not mention the practice. While we fully agree with one report's recommendation that "it's important that Tesco does differentiate its products", we note that Tesco nonetheless from time to time adopts copycat packaging designs.

Evidence: We would be happy to undertake store visits with CC officials if first hand, tangible evidence of copycat packaging is required.

- The CC explores the drivers of own label success (Para 8.70 and Appendix 8.110, para 19), noting that there are a number of these and that copycat packaging alone is unlikely to provide a sustained basis for success. We suggest that this is not an appropriate test. The mere fact that there may be a number of reasons for the success of own label products does not automatically lead to the conclusion that no individual reason is capable of giving rise to competition concerns.

The analysis misses the key damage to competition arising from the knock-on effects of retailers using copycat packaging to free ride on brand manufacturers' investments, which distorts investment and undermines efficiency and competition. Indeed, the effectiveness of using copycat packaging to draw falsely on the brand producer's reputation and packaging design skills is borne out by the continued prevalence of the practice.

Evidence: In addition to the evidence we have already supplied, we attach evidence from the British Retail Consortium² which suggests that:

- Fewer than 1 in 5 (though presumably more than 1 in 6) agree that they buy own label because of similar packaging to the branded equivalent;
- 21% of shoppers strongly agree that they buy own label because they believe it to be made by well-known brand manufacturers. Our research evidence shows that similar packaging encourages this belief while distinctive packaging discourages it.

This study (514 respondents) was also not included in the research review quoted by the CC. If between 1 in 5 and 1 in 6 (ie. 16% to 20% of shoppers) buy own label because of the similar packaging, that represents a significant sales uplift for the copycat as a result of this misleading and market-distorting behaviour.

- The CC refers to the repeat purchase nature of grocery products, suggesting that this reduces any negative effect on competition. This does not take into account the many shoppers (over 50% of shoppers, in some cases), who believe the similar packaging to indicate a connection with the familiar brand, when none exists. These shoppers are therefore likely to continue to purchase the copycat with that belief, as they will never realise – and never be told – that they are mistaken. They are therefore prevented time and again from making a fully informed decision.

² This research was undertaken in 1994 but was quoted by the BRC in 2007, so is still considered relevant by the BRC.

We are also struck by a potential inconsistency between the CC's analysis of copycat packaging and its analysis of mislabelling and the provision of misleading information. The practices are essentially similar (ie. misleading consumers regarding the nature of a product sold by a grocery retailer) but in one case a distortion of competition was found and not in the other. Tellingly, the CC notes that consumers are unlikely to be able to tell that they have been misled over packaging indicators relating to country of origin, which is exactly what we suggest is the case with copycat packaging that misleads over company of origin.

Remedy re. copycat packaging

In the case of mislabelling and the provision of misleading information, the CC has chosen to address this within the SCOP. We propose a similar approach for copycats, as the competition concern is the same (the misleading of consumers).

There are two potential approaches. The CAP Code³, with which retailers as well as suppliers abide in relation to marketing practices such as advertising, sales promotion and direct marketing but which does not cover packaging, contains a clause that could be applied to packaging via the SCOP:

Marketers should not take unfair advantage of the reputation of trade marks, trade names or other distinguishing marks of organisations or of the designation of origin of competing products (Article 20.2)

Alternatively, the IGD⁴ Dispute Resolution Procedure for packaging and trade dress disputes contains an undertaking to which all major retailers except Asda have signed up which states:

... it is accepted that a product sold in the United Kingdom should avoid using any combination of the same or similar name, colour scheme, shape, typeface, design layout or portrayed images so as to convey significant visual features which are essentially similar to the those of another product. Exceptionally, a single feature may be sufficiently significant.

Wording reflecting either of these approaches should not be contentious with retailers as most if not all have already signed up to these principles. Our proposal is to adapt the wording of the CAP Code to proscribe copycat packaging in the SCOP as follows:

Using product packaging or labelling that takes unfair advantage of the reputation of the trade marks, trade names or other distinguishing makes of Suppliers' branded products.

(2) Misleading claims on pack

We are concerned by own label products that carry misleading claims on pack such as "cleans as well as the leading brand". Under the self-regulatory CAP Code such claims must be substantiated. However, as discussed above, the Code's scope does not extend to packaging, a loophole that is exploited by some retailers. No remedies are available: there is no breach of trade marks, no basis for passing off, no malicious falsehood and, while the claim may be a false trade description and / or a misleading comparison, enforcement bodies such as the OFT and Trading Standards are too resource constrained to enforce the rules (being The Trade Descriptions Act or Control of Misleading Advertisements Regulations).

³ The British Code of Advertising, Sales Promotion and Direct Marketing, endorsed and administered by the Advertising Standards Authority (ASA)

⁴ Institute of Grocery Distribution

While it is not mentioned in either the Provisional findings or the Appendix on supply chain practices, this practice is clearly market-distorting and is very similar to the practices of mislabelling and providing misleading information which were found to raise competition concerns.

Remedy re. misleading claims on pack

A proportional and effective remedy would be to include a provision in the SCOP, under the heading “product mislabelling or other practices that might mislead consumers regarding the nature of a product sold by a grocery retailer”. Again we suggest that wording is taken from the CAP Code as this represents a remedy to which retailers have already agreed for other marketing practices. The wording we propose is:

Including comparisons on product labelling that identify competitors or competing products explicitly or implicitly but are likely to mislead consumers as to the elements of comparison and provide an artificial advantage to the product in question.

CATEGORY MANAGEMENT

The Provisional findings review in some detail the category management practices among retailers and suppliers across three sectors, concluding that “there is no direct evidence of tacit co-ordination at present”. However the CC goes on to state that there might be an adverse effect on competition in the future, on a theoretical basis (Summary, para 37 and Appendix 7.1, para 33). Only passing mention is given to the key purpose of category management which is to serve as a critical driver to improve retailer and supplier efficiency, allowing more efficient product stocking, improved category product mix and better matching of product ranges to consumers’ needs and expectations, leading to significant cost savings in the supply chain which have tended to reduce consumer prices⁵.

We are concerned that the views and conclusions as currently expressed by the CC may introduce uncertainty and have a disproportionate, negative effect both on category management itself and on those companies that undertake it.

The two conclusions in the findings (that there is no current anti-competitive effect, but that there may be in the future) are somewhat contradictory. This could lead to the inference, for which there is no evidence, that there must after all be some problem with the practice for the CC to make any kind of adverse comment, even on a speculative basis.

For the following reasons we submit that it would be an unusual and incorrect outcome were the CC in its final report to discourage category management:

- The European Commission broadly endorsed the practice in its merger control decision of 15 July 2007 in *Procter & Gamble / Gillette (M3732)*;
- The enquiry is directed at the retailing of groceries, yet the Report’s comments could result in material losses to suppliers who have invested significantly in category management, including suppliers of products other than groceries;
- The potential effect of such comments (a reduction in category management practices and a potential resulting loss in efficiencies) could create a cost burden on industry participants and thereby represent a disproportionately negative outcome with consequential adverse

⁵ The benefits of category management are outlined in Chapter 1 of the ECR Europe Category Management Best Practices Report (1997) found under “publications” at www.ecrnet.org.

effects on consumer prices. The CC's guidelines (CC 3 – Market Investigation References, para 4.10) specify that its remedies must be a reasonable and proportionate reflection of actual adverse effects identified;

- Lastly, suppliers which carry out category management in conjunction with retailers have not been given an opportunity fully to comment on the CC's veiled criticisms of this practice.

For these reasons, we ask that the CC considers the unfortunate implications, when producing its final report, of predicting potential future harm from category management where no evidence exists of a problem and no adverse finding has been made. Category management raises the platform by which retailers compete to better serve customers through lower prices and improved product choice and quality and is thus inherently a pro-competitive practice. Any assessment of the practice should consider the counter-factual of what would occur in the absence of the practice, ie. a significantly less efficient and effective supply system and a poorer retail offer to consumers.

30th November 2007

**BRITISH RETAIL
CONSORTIUM**

**SUMMARY OF RESULTS OF THE MORI
RESEARCH COMMISSIONED BY THE
BRITISH RETAIL CONSORTIUM**

To support its belief that consumers are not confused by 'lookalike' products the British Retail Consortium commissioned research from Market and Opinion Research International (MORI). This fieldwork was carried out on Wednesday, April 13 1994 in 21 locations among 514 shoppers who buy own label products. A summary of the findings are outlined below:

- 79 per cent of shoppers deny ever being confused by retailers' own label equivalent of major brands.
- 51 per cent actually find such similarities useful visual cues to help identify own label alternatives.
- 59 per cent claim they help in price comparisons between branded goods and 'lookalike' versions.
- 69 per cent of shoppers regularly buy own label goods. One in fifty never buy anything else except own label.
- Main reasons for buying own label are:-
 - Cheaper than manufacturers' brands - 42 per cent strongly agree
 - Offer better value for money - 33 per cent
 - Quality is as good as manufacturers' brands - 26 per cent
- Fewer than one in five strongly agreed that they buy own label because of similar packaging to the branded equivalent.
- Only 21 per cent strongly agree that they buy own label because they believe it is mostly made by well-known manufacturers.

∴ 21% admit to confusion

-20%

Presumably more than 1 in 6 (16%) strongly agreed.



- ends -