

Anticipated acquisition by Tesco plc of three former Somerfield stores from Co-operative Group Limited

ME/4174/09

The OFT's decision on reference under section 33(1) given on 3 August 2009.  
Full text of the decision published 6 August 2009.

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**PARTIES**

1. **Tesco plc** (Tesco) is predominately a grocery retailer (the UK's largest) with a portfolio of stores across the UK.
2. **Co-operative Group Limited** (CGL), a grocery retailer, acquired the grocery retailer Somerfield Limited (Somerfield) on 27 February 2009. Tesco proposes to acquire three former Somerfield stores from CGL in Battersea (London), Leyland and Millom (the Acquisition Stores).<sup>1</sup>

**TRANSACTION**

3. Tesco notified the transaction to the OFT by a Merger Notice. The period for considering the Merger Notice commenced on 8 July 2009, and the (unextended) statutory deadline expires on 4 August 2009.

**JURISDICTION**

4. As a result of this transaction Tesco and the Acquisition Stores will cease to be distinct. The parties overlap in the supply of grocery retailing and together Tesco and the Acquisition Stores will account for over 25 per cent of all grocery retailing in the UK.<sup>2</sup> As a consequence the share of supply test in section 23 of the Enterprise Act 2002 (the Act) is met. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

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<sup>1</sup> The Acquisition Stores are not stores that CGL is required to divest pursuant to the undertakings in lieu of a reference that the OFT accepted from CGL on 15 January 2009 (and coming into effect on 27 February 2009) following CGL's acquisition of Somerfield.

<sup>2</sup> Tesco submitted that it accounts for 27 per cent of UK grocery sales (based on TNS data) and the Acquisition Stores account for less than one per cent.

## **MARKET DEFINITION**

5. The parties overlap in the retail of groceries in the UK. This industry has been examined extensively in recent years by both the OFT and Competition Commission (CC).<sup>3</sup>

### **Product scope**

6. In past cases the CC and the OFT have considered that grocery retailing comprises three broad product markets:
  - **One stop stores:** those with a net sales area of 1,400 square metres or above.<sup>4</sup> These stores form their own product market
  - **Mid size stores:** those with a net sales area of less than 1,400 square metres but above 280 square metres. These stores are constrained by one-stop stores and so one-stop stores must be included in any market definition with mid size stores as its focus, and
  - **Convenience stores:** those with a net sales area of less than 280 square metres. These stores are constrained by all grocery stores and so the product market focussed on convenience stores must also include mid size and one-stop stores.
7. An aspect of product market definition in previous grocery investigations has been to include in the relevant product market large grocery retailers (such as Tesco and Somerfield), regional grocers and symbol groups in the effective competitor store fascia, but to exclude limited assortment discounters (LADs), frozen food retailers and specialist retailers (one of the key reasons has been because of the relatively reduced range of products that these retailers offer).<sup>5</sup>

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<sup>3</sup> For OFT examples, see Completed acquisition by Tesco Stores Limited of Brian Ford's Discount Store Limited, Case ME/3827/08, OFT decision of 22 December 2008 (*Tesco/Brian Ford*), Anticipated acquisition by Co-operative Group Limited of Somerfield Limited, Case ME/3777/08, OFT decision of 20 October 2008 (*CGL/Somerfield*), and Anticipated acquisition by Tesco Stores Limited of a store in Paisley from Somerfield plc, OFT decision of 30 April 2008.

For CC examples, see The supply of groceries in the UK market investigation (April 2008) (*Groceries report*), Tesco plc and the Co-operative Group (CWS) Limited: a report on the acquisition of the Co-operative Group (CWS) Limited's store at Uxbridge Road, Slough by Tesco plc (November 2007) (*Tesco/CWS*), and Somerfield plc and Wm Morrison Supermarkets plc: A report on the acquisition by Somerfield plc of 115 stores from Wm Morrison Supermarkets plc (September 2005) (*Somerfield/Morrison*).

<sup>4</sup> In its market investigation into groceries, the CC considered that the floor size threshold for larger grocery stores was larger than 1,000 to 2,000 square metres (paragraph 12) but used the threshold of 1,400 square metres for much of its analysis (paragraph 13). In *Tesco/CWS* the CC also used 1,400 square metres as the threshold.

<sup>5</sup> Paragraph 14 of the *Groceries report* and paragraph 161 of *CGL/Somerfield*.

8. Tesco submitted that the exclusion of LADs and frozen food retailers was not appropriate as both compete vigorously with grocery retailers. Tesco told the OFT that partly as a result of competition from the LADs it launched a range of discount brands and an extensive marketing campaign to support these new brands.
9. However, given that the inclusion or otherwise of the LADs and frozen food specialists does not affect the outcome of the OFT's competition assessment in this case, the OFT has not found it necessary to conclude on the product market definition in this case. This also applies to the inclusion of regional suppliers since sufficient numbers of major national grocery retailers are present in the relevant local areas in this case.
10. In examining this acquisition the OFT has adopted the approach set out in *CGL/Somerfield*, that is, there are three distinct product markets distinguished by size of the sales area (as set out in paragraph 6 above) and these product markets are fascia specific (as set out in table A2 of *CGL/Somerfield*). All of the Acquisition Stores are mid size.

#### **Geographic scope**

11. Previous CC and OFT reports into supermarkets have found that there are both national and local aspects to competition.<sup>6</sup> In respect of the local dimension of competition, the appropriate measures used<sup>7</sup> were:
  - For **one-stop stores**, 10 minutes drive time in urban areas and 15 minutes drive time in rural areas
  - For **mid size stores**, a 5 minute drive time in urban areas and 10 minutes drive time in rural areas but these stores are also constrained by one-stop stores within a 10 minute drive time (or a 15 minute drive time in rural areas), and
  - For **convenience stores**, 5 minutes drive time in all areas but these stores are constrained by one-stop stores within a 10 minute drive time (or a 15 minute drive time in rural areas) and by mid size stores within a 5 minute drive time (or a 10 minute drive time in rural areas).
12. The OFT has adopted this approach for the geographic market for its local area analysis. The Acquisition Stores in Battersea and Leyland are in urban areas while the store in Millom is in a rural area.

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<sup>6</sup> For example, *CGL/Somerfield*, *Tesco/Adminstore*, and the *Safeway report* (paragraph 2.65).

<sup>7</sup> For example, in *CGL/Somerfield* and the *Groceries report*.

## **HORIZONTAL ISSUES**

### **National competition**

13. The OFT has investigated whether there is a realistic prospect that the proposed acquisition would lead to a substantial lessening of competition at the national level.
14. One third party raised concerns that the acquisition of these stores may contribute to increasing the national market power of Tesco. No other third parties raised any concerns relating to national issues.
15. When considering the merger effect at the national level it is appropriate to consider the merged entity's share of supply across all store sizes combined, since national competition does not take place according to the size of an operator's retail stores.
16. On this measure, post acquisition Tesco will account for around 27 per cent of total UK groceries sales (based on TNS data submitted by Tesco). The increment attributable to the Acquisition Stores represents significantly less than one per cent of Tesco's UK grocery operations. Further, Tesco would continue to face strong competition from other large retailers at the national level.
17. In light of the small increment to Tesco's market share attributable to the Acquisition Stores and the presence of other larger supermarket operators, the OFT does not believe that any competition concerns on the basis of unilateral or coordinated effects arise at the national level as a result of this acquisition.
18. Nor does the OFT consider that, as a result of the acquisition, competition concerns arise at a national level through creating or strengthening buyer power to such an extent that it distorts grocery suppliers' incentives to invest in new capacity, products and production processes.
19. Consequently, competition concerns do not arise at the national level as a result of the proposed acquisition.

### **Local competition**

20. In analysing competition at the local level, detailed local level analysis was undertaken, closely following the methodological approach taken by the OFT in *CGL/Somerfield*.<sup>8</sup> The population re-centring was omitted in this case at the request of Tesco since the Census output data re-centring applies the same concept (that is, looking at the effect of the merger from

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<sup>8</sup> As described in Annex 1 of *CGL/Somerfield*.

the perspective of where the customers live) but at a finer level of detail (and therefore will not miss a potentially problematic fascia reduction that the population re-centring would identify).

21. The methodological approach uses fascia-based analysis which considers that competition concerns do not arise at the local level if four or more fascia are present (after the acquisition) in any of the differently centred isochrones.
22. On the basis of this approach competition concerns do not arise in any of the areas in which the Acquisition Stores are located.
23. Moreover, the OFT examined whether, in the local area around Millom where there is no overlap between Tesco and the former Somerfield store, Tesco has any land banks or controlled land sites. The OFT found that Tesco does not have any controlled land sites in the local area and therefore there is no possibility of competition concerns arising as a result of land sites.<sup>9</sup>

#### **Barriers to entry and expansion**

24. The OFT did not find it necessary to conclude on whether barriers to entry are high since it does not affect the outcome of this case.

#### **THIRD PARTY VIEWS**

25. Only one third party raised concerns regarding the effect of the proposed acquisition on competition at the national level (which is discussed above). Another complained about Tesco's national presence in convenience retailing (through its Express format stores) which the OFT does not consider to be relevant for this merger analysis. No third party told the OFT that the proposed acquisition raised competition concerns at the local level.

#### **ASSESSMENT**

26. The parties overlap in the supply of grocery retailing in the UK. The OFT has not identified any competition concerns at a national level, given the negligible accretion to Tesco's market share of grocery retailing and to its position relative to its suppliers. At a local level, the Acquisition Stores at Battersea and Leyland will face sufficient competitive constraints after the merger to prevent any competition problems from arising. In Millom there is no overlap between either a Tesco store or Tesco-controlled land and the former Somerfield store (and therefore no effect on local competition).

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<sup>9</sup> In local areas where one merger party is present and the other is not but controls land in the area, it may be the case that the merger lessens competition by reducing the likelihood of potential entry (either by the other merger party or by a third party using that land). See paragraph 134 of *CGL/Somerfield*.

27. Consequently, the OFT does not believe that it is or may be the case that the acquisition may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

## **DECISION**

28. This acquisition will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.