

Completed acquisition by Cadbury Schweppes plc of Green & Black's Limited

The OFT's decision on reference under section 22 given on 31 August 2005. Full text of decision published 6 September 2005.

PARTIES

1. **Cadbury Schweppes PLC (Cadbury)** is an international company whose principal businesses are the manufacture and sale of sugar and chocolate confectionery products and soft drinks. **Green & Black's Limited (Green & Black's)** supplies organic chocolate and chocolate related products. In the last financial year Green & Black's turnover in the UK was just over £20 million.

TRANSACTION

2. On 11 May 2005, Cadbury acquired all of the shares in Green & Black's. The administrative timetable in this case expires on 2 September 2005.

JURISDICTION

3. As a result of this transaction Cadbury and Green & Black's have ceased to be distinct. The parties have a combined UK share of supply in block chocolate of around 37 per cent; therefore 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.

RELEVANT MARKET

4. The activities of the parties overlap in the supply of the following products in the UK:
 - chocolate confectionery (block chocolate and chocolate confectionery bars);
 - cocoa-based beverages;
 - chocolate biscuits; and
 - ice cream.

5. The principal area of overlap is in the supply of chocolate confectionery, which accounts for 80 per cent of Green & Black's sales; there is also an overlap in cocoa-based beverages. Although there are overlaps in respect of the supply of branded biscuits and ice cream, the parties' combined shares of supply are low and the increments are insignificant¹, these segments are therefore not considered further.

Product market

Chocolate confectionery

6. The parties submit that the relevant frame of reference comprises the market for supply of chocolate confectionery (i.e. block chocolate as well as chocolate confectionery bars containing other ingredients such as biscuit, caramel, nuts and other foodstuffs) because of the high degree of demand side substitutability between block chocolate and chocolate confectionery bars. In this context, the parties have pointed inter alia to internal research which indicates that Cadbury's Dairy Milk (a block chocolate product) has lost sales to the following chocolate confectionery bars: Kit Kat, Aero, Kinder, Mars Bars and Mars Delight.
7. In terms of supply side substitution, third parties contacted by the OFT in this inquiry generally confirmed that there are no significant barriers to switching production between the different types of chocolate confectionery products.
8. However, since competition concerns do not arise even if one considers the narrower frame of reference of block chocolate (i.e. the main area of product overlap), it is not necessary to conclude on the point.

Cocoa-based beverages

9. The cocoa-based beverages supplied by the parties fall into two categories, namely drinking chocolate (i.e. a cocoa-based powdered product that is mixed with hot water or milk to produce a chocolate drink) and cocoa (which is mixed with sugar and hot milk to produce a chocolate drink).
10. The parties are of the view that cocoa-based beverages are part of a wider food beverages market that also includes malted drinks such as those sold under the Horlicks and Ovaltine brands. This is based on the parties' internal research relating to consumption patterns.

¹ Sales of Green & Black's branded biscuits in the first six months of 2005 accounted for around 0.06 per cent of the UK market. Cadbury's branded biscuits represent less than 4 per cent of the market. For ice cream, the parties' respective shares of supply are 0.7 per cent for Green & Black's and 6.1 per cent for Cadburys. Green & Black's licenses its brand to third party suppliers of biscuits and ice cream and is not involved in the manufacture, distribution, marketing, sale or pricing of the licensed products.

11. However, third party responses on the question of substitutability of other drinks were mixed. It is therefore appropriate to consider a frame of reference which includes cocoa-based beverages but excludes other hot or cold beverages.

Organic Products

12. Responses from both customers and competitors of the parties were predominantly of the opinion that consumers of organic chocolate products (both chocolate confectionery and cocoa-based beverages) do not view non-organic chocolate products as a close substitute. In general, third parties indicated that consumers buy organic chocolate products for reasons other than price and that very few would switch to non-organic alternatives in the event of a 5-10 per cent increase in price.
13. Since Green & Black's supplies mainly organic products and Cadbury supplies no organic products, there is no overlap between the activities of the parties if separate product markets exist for organic and non-organic chocolate products. The third party evidence referred to above, and the existence of a significant price differential between organic and non-organic products tends to lend support to this conclusion.
14. However, since our inquiries have not enabled us to come to a definitive conclusion on this point, the competitive assessment is based on a frame of reference which includes organic as well as non-organic products.
15. It should be noted that evidence obtained in this investigation indicates that there is considerable differentiation between the chocolate products supplied by the parties, which suggests that the degree of competition that existed between the parties before the merger was low.

Geographic market

16. The appropriate geographic frame of reference in this case is the UK since many suppliers in this sector, and the major customers of the parties, operate on a national basis. This is in line with previous OFT decisions which have considered the geographic scope of the supply of consumer food products to be national.

HORIZONTAL ISSUES

Market shares

Chocolate confectionery

17. Cadbury is the largest supplier of chocolate confectionery in the UK but the increment resulting from this transaction is small at 0.7 per cent. Shares of supply in the chocolate confectionery category are set out in the table below.

Table 1: UK Shares of supply chocolate confectionery (by value) 2004 and 2005

Supplier	per cent Year to 30/04/05	per cent Year to 24/04/04
Cadbury	34.3	34.6
Green & Black's	0.7	0.5
Combined	35.0	35.1
Mars	26.9	27.1
Nestlé	18.1	19.1
Own-label	4.1	3.9
Ferrero	4.0	3.5
Kraft	3.3	3.9
Lindt	2.1	1.6
Others	6.5	5.8

Source: the parties based on A.C. Nielsen data

18. Based on the 2005 data, the HHI figure (2,324) indicates that this sector is highly concentrated. However the delta (48) is below the threshold at which OFT guidance indicates potential competition concerns may arise.
19. Furthermore, it is clear from our analysis that the parties are not each others closest competitors. Cadbury sells mass market chocolate confectionery products and its primary competitors are the other mass market producers, including Nestlé, Kraft and Mars. By contrast, Green & Black's operates at the premium end of the spectrum and so is more likely to compete with other premium chocolate producers such as, for example, Lindt. This is illustrated by reference to the price of the products supplied by the parties. As the data in Table 2 indicates, Green & Black's chocolate retails at a significant premium to other suppliers' chocolate.

Table 2: Average UK prices of chocolate per kilogram (2004)

Supplier	£ per Kilogram
Green & Black's	13.56
Lindt	10.90
Cadbury Bournville 76 per cent cocoa	9.47
Cadbury Bournville	5.88
Cadbury Dairy Milk	5.19
Sainsbury's Taste the Difference	10.06
Tesco Finest	8.60

Source: the parties based on AC Nielsen data

20. Considering the narrower segment of block chocolate, the parties estimate that Cadbury's share of this segment is 36.7 per cent and Green & Black's around 1 per cent. The increment and level of concentration are not such as to raise competition concerns.

Cocoa-based beverages

21. Green & Black's supplies drinking chocolate and cocoa under the Green & Black's and Maya Gold brands. Cadbury's branded cocoa-based beverages are the market leaders. However, Cadbury currently licenses its brand to Premier Foods; under the terms of the licence, Premier Foods is responsible for the sale, distribution and pricing of all of branded Cadbury chocolate beverage products. The parties have argued that the licensing arrangement means that there is no overlap between the activities of Cadbury and Green & Black's in this product category. However, it is expected that the licensing arrangement will terminate in the coming year; Cadbury then intends to take control of sales, distribution and marketing of chocolate beverage products sold under the Cadbury brand. The competitive effect of the transaction in this area of product overlap has therefore been considered. Shares of supply are set out in the table below.

Table 3: UK shares of supply of cocoa-based beverages (by value) year to April 2005

Supplier (brand name)	£m	per cent Share
Cadbury/Premier Foods	35.0	56.9
Green & Black's	1.3	2.1
Combined	36.3	59.0
Twinnings (Options)	10.0	17.0
Own-label	8.0	13.8
Nichols (Galaxy and Maltesers)	4.0	5.9
GSK (Horlicks drinking chocolate)	0.7	1.2
Café Direct (CocoDirect)	0.5	0.9
Brehme (Clipper)	0.3	0.5
Charbonnel	0.3	0.6
Prinsen	0.2	0.3
TOTAL	61.0	100

Source: the parties based on AC Nielsen data

22. The HHI figure in respect of cocoa-based hot beverages indicates that the sector is highly concentrated (4,122) and the increment is significant (250). However, as is the case for chocolate confectionery, the parties are not each others closest competitors. G&B's products are premium organic products which compete most directly with other premium brands such as for example Charbonnel and Brehme's Clipper. The price differential between premium and non-premium products has been estimated to be a multiple of 2.5², indicating that before the merger the price of Green & Black's cocoa-based beverages did not constrain the price of Cadbury's products.
23. Moreover, a number of significant competitors remain in the market post-merger and, as discussed below, barriers to entry and expansion in the supply of cocoa-based beverages are relatively low, particularly for entry in respect of niche and premium products.

Barriers to entry and expansion

24. The parties argue that barriers to entry, for supply of both chocolate confectionery and cocoa-based beverages are low because manufacture can be subcontracted to third parties. In fact, this is how Green & Black's entered the market. There are a large number of contract suppliers both in the UK and elsewhere to whom production can be outsourced, including inter alia: Prinsen, Premier Foods, Nichols Foods, Elite, Asbury's, Itallo Suisse, Grand Foods Ltd and Fine Foods.

² Source: the parties based on A.C. Nielsen data for the year to May 2005.

25. The parties maintain that the only significant entry cost relates to marketing and advertising expenditure required in order to gain initial brand recognition. Third parties commented that barriers to entry are low and that entry can occur in a six-month timeframe. Third parties stated that there are no particular barriers to expanding production either in chocolate confectionery or in drinking chocolate; they also expressed the view that in particular in the drinking chocolate segment, new brands regularly appear in the market.
26. In our view, the entry and expansion of Green & Black's itself indicates that niche entry in the chocolate confectionery and cocoa-based beverages segments can and does occur successfully and that barriers to entry for niche, premium chocolate products are relatively low. However, barriers to entry in the mass market chocolate confectionery and cocoa-based beverages sector are likely to be higher, in particular given the brand strength of the main players. It should be noted in this context that this merger results in the removal from the market of an independent niche player active in the supply of premium products. Therefore the possibility of this type of entry (and expansion) occurring in a timely, likely and sufficient manner indicates that the transaction does not lead to a substantial lessening of competition.

Buyer power

27. The parties' main customers are the national supermarket chains and large wholesalers. These customers have at least a degree of buyer power. Smaller customers are unlikely to have any market power when dealing with the merged entity. However, as other suppliers do exist, they could easily switch to one of the parties' competitors.

VERTICAL ISSUES

28. This transaction does not give rise to vertical competition issues.

THIRD PARTY VIEWS

29. The majority of third parties who responded to our inquiries in the context of this merger inquiry were unconcerned. A limited number of third parties raised concerns relating to a potential increase in Cadbury's portfolio power and its market power in certain types of chocolate. However, the small increment resulting from this transaction in respect of chocolate confectionery, and the presence of a number of significant competitors post-merger, in combination with relatively low entry barriers in respect of niche and premium products, lead us to conclude that these concerns are not warranted in the circumstances of this case.

ASSESSMENT

30. The activities of the parties overlap primarily in the supply of chocolate confectionery and in the supply of cocoa-based hot beverages. In chocolate confectionery, while Cadbury remains the largest supplier in the UK, the increment to its share of supply is very small and the parties' products are not close substitutes. Furthermore there remain a number of strong competitors to whom customers could switch.
31. In respect of cocoa-based hot beverages, Cadbury is the leading brand in the sector, and the accretion of its share of supply as a result of this transaction is significant. However, the products of the parties are not close substitutes. Moreover, the parties submit, and third parties confirm that barriers to entry in the supply of cocoa-based hot beverages are relatively low and new entry does occur, particularly in respect of niche and premium products.
32. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

33. This merger will therefore not be referred to the Competition Commission under section 22(1) of the Act.