Anticipated acquisition by Princes Limited of the canning business of Premier Foods Group Limited

The OFT's decision on reference under section 33 given on 22 June 2011. Full text of decision published 19 August 2011.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

PARTIES

1. **Princes Limited ('Princes')** is ultimately owned by the Mitsubishi Corporation. It is active in the production, marketing and wholesale distribution of food and drinks products, primarily to the retail grocery channel in the UK. Around £[ ]m ([ ] per cent of canned food sales) of Princes' sales is to the food service sector. Princes manufactures around [ ] per cent of its products at nine sites based in the UK,[1] one site in Poland, and one in Mauritius. Princes has one canned food manufacturing plant, which is based in Chichester, and this has one canned pie production line.

2. Princes' core ambient food[2] products include fish, meat, fruit and vegetables, sandwich fillings, pasta, sauces, cooking oils and microwaveable ready meals. Princes' core drinks products include bottled water, fruit juice, fruit concentrate-based squash soft drinks and carbonates. Canned food sales account for around [ ] per cent of Princes turnover.

3. **Premier Foods Group Limited ('Premier')** is active in the production, marketing and wholesale distribution of food products, primarily through

[1] Belvedere, Bradford, Cardiff, Chichester, Church Stretton, Eden Valley, Erith, Glasgow and Manchester.
[2] 'Ambient' is food that would normally require refrigeration for preservation but has been processed so that it can be stored at room temperature.

the retail grocery channel in the UK. Around £[ ]m ([ ] per cent of total sales) of the sales of Premier's canned food products business are to the food service sector. Premier's brands include: Branston, Batchelors, Hartley's, Crosse & Blackwell, Farrows, Fray Bentos, and Smedley's.[3] In the last financial year, the target business had a turnover of £[ ]m, of which £[ ]m was earned outside of the UK. [ ] per cent of the target business' ambient food offering is the sale of own label products.

TRANSACTION

4. The parties entered into a Business Sale Agreement on the 7 February 2011 pursuant to which Princes will acquire the canned food products business of Premier. The consideration for the acquisition is £182m. The target business comprises the transfer of the following key assets and contracts:

   - two canning plants based in Long Sutton and Wisbech (both in England) that are currently owned and operated by Premier
   - [ ]
   - certain related intellectual property, and
   - related customer and supply agreements.

5. As part of the transaction, Princes will acquire specific brands, be licensed to manufacture under certain brands and enter into contract manufacture arrangements in relation to certain other products.

6. [ ].

7. [ ].

8. [ ].

9. [ ].

10. The extended statutory deadline for the OFT to announce a decision in this case is 22 June 2011.

[3] The transaction involves the acquirer purchasing the intellectual property rights for some of these brands and leasing the intellectual property rights to others.

RATIONALE

11. Princes has told the OFT that the primary rationale for the transaction is to increase its manufacturing capability in canned foods. It stated that it intended to invest in existing production sites, increase efficiencies and reduce costs to the long term benefit of consumers.

JURISDICTION

12. The transaction qualified for investigation under the EU Merger Regulation. The parties made a request under Article 4(4) of the EU Merger Regulation (EUMR) for the transaction to be referred in whole to the United Kingdom. The OFT informed the European Commission on 18 March 2011 that it agreed with the referral request. The Commission then referred the transaction for investigation to the OFT on 5 April 2011.[4]

13. The OFT believes that the transaction would result in two or more enterprises ceasing to be distinct under section 23(1) of the Enterprise Act 2002 (the Act). The UK turnover of Premier exceeds £70 million; therefore the turnover test in section 23(1)(b) of the Act is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation will be created.

COUNTERFACTUAL

14. The parties overlap in relation to the manufacture and wholesale distribution of a broad range of food products. The application of the substantial lessening of competition (SLC) test involves a comparison of the prospects for competition with the merger against the competitive situation without the merger. The latter is called the 'counterfactual'. The OFT will generally adopt the prevailing conditions of competition as the most appropriate counterfactual against which to assess a merger.

15. In this case, the OFT has considered whether the merger should be assessed against an alternative counterfactual. This is because Princes' internal documents indicated [ ]. However, the parties presented additional information that was sufficient to satisfy the OFT that Princes' [ ] for the

[4] Case No Comp/M.6143 Princes/Premier Foods Canned Grocery Operations, 05/04/11

OFT to adopt an alternative counterfactual to the prevailing conditions of competition.

MARKET DEFINITION

PRODUCT MARKET

16. The parties overlap in the manufacture and wholesale distribution of a broad range of food products to both food service and retail customers, namely:

- ambient pies in the retail channel
- canned ready meals (including curries, chilli, pasta and other) in the retail channel
- canned mince in the retail channel
- canned stewed/'chunky' steak in the retail channel
- ambient corned beef in the retail channel
- ambient garden peas in the retail channel
- canned red kidney beans in the retail channel
- canned mixed beans in the food service channel
- canned chick peas in the food service channel
- canned butter beans in the food service channel
- canned mixed vegetables in the retail channel
- canned potatoes in the retail channel
- canned carrots in the retail channel
- canned prunes in the retail channel
- ambient cooking sauces in the retail channel, and
- ambient wet soups in the retail channel.

17. In the retail channel, the parties have submitted that they compete for consumers' 'centre of plate' and 'side of plate' products. They submit that this distinction forms the primary parameter for competition between their overlapping products. They have argued that they each provide to customers meat-based and vegetable-based ambient products that are substitutable with many other products. They also submit that a broad range of products are substitutable across the frozen, ambient and chilled temperature ranges and across different packaging formats and that price and convenience rather than, for example, the protein type contained in the product, are relevant.

18. In its past decisions, the OFT has not treated different 'meal genres', that is, for example, pizzas[5] or ready meals, which may make up the main part of a meal as all forming part of the same market. In part, this is because, although some foods may be considered complements to a main meal, the OFT is not of the view that they all fall within the same market. Many 'side of plate' items such as canned vegetables may be used as ingredients to a main meal. They each cater to different end consumer tastes and usages.

19. Further, and in contrast to the parties' wide starting point on market definition, the OFT's approach is first to consider whether narrow candidate product markets may be widened through demand-side substitution and then, if appropriate, to consider if substitution on the supply-side allows several products, which are not demand-side substitutes, to be aggregated into one wider market.[6]

20. When selecting a candidate market, the OFT will include at least the substitute products (narrowly defined) of the merger firms. The OFT has therefore considered the narrowest plausible candidate market for each of the overlaps – that is, segmenting where appropriate by temperature range (ambient, chilled, frozen), packaging type (canned, plastic), and own label and branded products.[7]

21. That said, market definition is an analytical framework used to begin an assessment of the relative competitive pressures that different suppliers place on one another. The OFT does not consider market definition to be an end in itself.[8] In particular, market definition is unlikely to be determinative in the present case as the parties' products are differentiated, meaning any bright-line-drawing market definition exercise runs the risk of falling foul of the binary fallacy: assuming that all products in the market exercise competitive constraints on each other in proportion to their market shares, whereas products outside the market exercise no

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[5] Completed acquisition by Dr Oetker (UK) Limited of the business and assets of Schwan's Consumer Brands UK Limited, decision of 5 May 2009.
[6] See Merger Assessment Guidelines, paragraphs 5.2.6 to 5.2.19.
[7] For two overlaps (pies and canned ready meals), the OFT also considered further segmentation by type of meat (for example, chicken, beef). However, evidence from the parties—corroborated by third parties (customers and competitors)—suggested that it would not be appropriate to define separate relevant markets by dint of both demand- and supply-side substitution.
[8] See Merger Assessment Guidelines, paragraph 5.2.2.

constraint on them at all.[9] The unilateral effects arising from a merger will be the same regardless of whether it is framed as one giving a high combined share of supply in a narrowly defined market, or as one between close competitors in a broadly defined market.

22. Arguments for widening the relevant market beyond the narrow candidate boundaries are therefore considered below in the horizontal competitive assessment of the merger in four overlaps in the retail channel:

- ambient pies
- canned ready meals (including curries, chilli, pasta, and other)
- ambient corned beef, and
- ambient garden peas.

23. However, in relation to nine narrow candidate markets in the retail channel, the OFT was able to dismiss as less than fanciful the risk that the merger would result in a substantial lessening of competition on the basis of one or more of the following factors: the parties' combined market share and/or the increment to it were either not high enough to give the OFT cause for concern over unilateral effects, the parties do not appear to compete particularly closely with one another, no (or very few) third party concerns were raised in relation to these overlaps. As such, the following product overlaps are not further assessed in this decision:

- canned mince[10]
- canned stewed/'chunky' steak[11]
- canned red kidney beans[12]
- canned mixed vegetables[13]
- canned potatoes[14]

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[9] See Merger Assessment Guidelines, paragraph 5.3.2, first bullet.
[10] Although the parties may have a combined share of supply of up to [45 to 55] per cent in branded and own label mince there are other significant competitors in the market such as Tulip, Grants, Westers and Simpsons.
[11] The parties have a combined share of supply of [60 to 70] per cent for branded stewed steak. However, the increment is small at around [zero to five] per cent and significant players remain in the market.
[12] The parties have a high share of supply in the retail sector ([50 to 60] per cent with increment of [20 to 25] per cent) of kidney beans, but only [10 to 20] per cent of branded kidney bean sales are branded and customers were unconcerned and competitors said they could expand production.
[13] Customers were unconcerned and competitors said they could expand production.
[14] The parties deal documents notes [ ] and [ ] as close competitors and the parties appear not to have competed against each other to supply own label canned potatoes in the last three years.

- canned carrots[15]
- canned prunes[16]
- ambient wet cooking sauces[17] and
- ambient wet soups.[18]

24. The parties both supply into the food services sector. They overlap in canned mixed beans, canned chick peas and canned butter beans. The parties believe that supply to food service customers is distinct from supply to retail customers, but that, similar to the retail channel, the relevant market should include all side of plate foods regardless of the temperature range.

25. Both the parties and third parties responses suggested that it was appropriate to distinguish between sales to the retail sector and the food service sector. On the demand side, the configuration and pack sizes demanded by customers in the food service sector are likely to be different. Furthermore, food service customers are generally considered to be less brand sensitive than those in the retail sector.

26. No third parties indicated that the parties are particularly close competitors and no substantive concerns have been raised in relation to the supply of products to the food services sector. Third parties told the OFT that it is easier to enter the food service sector because branding is much less important and because the quality control required by food service customers is less exacting than that required by retailers. Supply into the food service sector is therefore not considered further.

GEOGRAPHIC MARKET

27. The parties submitted that the appropriate geographic frame of reference for all of the product overlaps was at least the UK. The parties consider

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Customers did not raise any concerns. Over [90 to 100] per cent of the supply of canned potatoes is own label which Princes is not active in.

[15] The increment in canned carrots is only [zero to five] per cent. Other significant players include La Doria , Scana Noliko and Bonduelle.

[16] The combined market share of [75 to 80] per cent in all canned prunes but increment of only [zero to five] per cent. Princes supplies only own label prunes ([ ]) whereas Premier also supplies branded prunes.

[17] The combined share does not exceed [10 to 20] per cent in all wet ambient cooking sauces or in any plausible segment ('family favourites', Indian, Italian, Mexican and Oriental).

[18] Increment of below [zero to five] per cent in all wet ambient soups. Princes supplies only own label soup whereas Premier also supplies branded soup.

that supply from outside the UK is feasible, especially for own label products. In support, they point to the presence of continental brands for some of the overlap products and suggest that the geographic frame of reference could be wider than the UK.

28. The OFT's investigation has not supported the parties' view. Third parties indicated that the main suppliers of the overlap products are based in the UK and the majority of products are sourced through UK based companies. Previous decisions involving food products have found the appropriate geographic frame of reference to be the UK since the major customers of the parties operate on a national basis.[19] In addition, several of the overlaps products are particular to the UK. Ambient pies in particular are barely consumed in other countries.

29. In view of the above, the appropriate geographic frame of reference for all areas of product overlap is considered to be the UK on a cautious basis. However, the OFT has given consideration to whether imports from overseas based suppliers may be a credible constraint, especially in the context of new entry and expansion.

HORIZONTAL ASSESSMENT

UNILATERAL EFFECTS

Ambient pies

Market shares

30. The parties have argued that ambient pies are constrained by chilled and frozen ones. Given that sales of chilled and frozen pies are much higher than sales of ambient pies, the parties submitted that their share of supply is only [zero to 10] per cent. Further, the parties submitted that even if the OFT does not consider that chilled pies are a constraint on ambient pies, they have a share of supply of ambient and frozen pies of only [25 to 35] per cent with an increment of [zero to five] per cent.

[19] For example the Competition Commission's report on the completed acquisition of HP Foods Group by HJ Heinz Company and HJ Heinz Company Ltd, 24 March 2006, and the OFT's decision in the anticipated acquisition by Premier Foods plc of RHM plc of 5 February 2007 ('Premier/RHM').

31. In measuring the parties' combined market share in ambient pies, the OFT has had to take a view on whether sales of own label pies should be attributed to the retailer or to the supplier.

32. The parties have argued that the shares of supply of own label ambient pies should be attributed to retailers and not to Princes and Premier because:

- retailers set the terms of trade
- retailers undertake own label promotional activity
- formalized contracts for the duration of supply rarely exist, and
- where there are contracts, if retailers reduce demand then suppliers would have no alternative outlet for these volumes.

33. On this basis, the parties claim they have limited brand power across all the overlaps and that none of the parties' brands are 'must stock' items.

34. Set against this, in relation to ambient pies, several of the parties' customers and other food producers indicated that the Fray Bentos name is synonymous with ambient pies and is a strong brand. Moreover, the absence of own label to a significant extent in this market is consistent with existing brand strength and was said by third parties to be a factor contributing to the historic lack of own label entry in ambient pies (see also paragraph 37).

35. The parties further referred to the OFT's decision in Symington/Cockburn[20] where own label sales were attributed to retailers. In that case the parties submitted evidence which enabled the OFT to conclude that own label and branded products should be considered in this way. By analogy, information in the present case sufficient to attribute sales of own label pies to retailers would have needed to show that:

- there was a shift from own label to branded pies over time and heavy discounting on branded pies leading to a narrower price differential between the two products

[20] Anticipated acquisition by Symington Family Estates of the Cockburn's Port brand, OFT decision of 17 December 2010.

- there was evidence of customer shifting to own label and evidence that own label was gaining its own 'brand' presence
- branding was not important for ambient pies
- there was a continuous chain of prices across branded and own label ambient pies with no significant pricing gaps, and
- there was significant evidence of customer switching between own label and branded pies, including where the de-listing or promotional activity of one had affected sales of the other.

36. In this case, the parties have not been able to provide this evidence and the evidence available to the OFT is not sufficient to conclude that own label ambient pies should be considered to form part of the same market as branded ambient pies.

37. In any event, evidence submitted by the parties suggests that own label pies are a small proportion of total ambient pie sales (with only Morrison's, Asda and Tesco very recently—stocking them)[21] and attributing them to the retailer would not significantly affect the OFT's view of the effect of the merger in ambient pies.

38. On this basis, the parties are the only suppliers of branded ambient pies and have a combined share of supply of 100 per cent with an increment of [zero to 10] per cent.[22] In the event that own label pies are considered to form part of the market the parties have a combined market share of [80 to 90] per cent with an increment of around [zero to 10] per cent.

39. These market shares and the increments are high enough to give the OFT cause for concern over unilateral effects. In assessing the unilateral effects that may arise as a result of this merger in the supply of ambient pies the OFT has relied on three principal sources of evidence:

- information provided by the parties, including from their internal documents
- from the results of the OFT's market investigation and

[21] Annex 3 to the parties' Further Submission to the Office of Fair Trading, dated 15 April 2011.
[22] The total value of the ambient pie market according to the data provided by the parties is £[30 to 35] million, of which £[zero to five] million is accounted for by Princes sales and £28.7 million is accounted for by Premier through its Fray Bentos brand.

- quantitative evidence, in particular econometric estimates provided by the parties of demand for ambient, chilled and frozen pies and analysis of switching data.

40. The evidence from these sources is discussed below.

Information provided by the parties, including from their internal documents

41. A number of the parties' internal documents identify the other as a close competitor in pies. For example as Princes' internal documents states:

[ ].

42. [ ].

43. [ ].

44. The OFT notes that the documents referred to above were not, as far as the OFT is aware, prepared in contemplation of the transaction and were prepared for business planning purposes. In any event, even if they were prepared in contemplation of the transaction, the OFT considers that they provide a good indication of the views of each of the parties' strengths.

45. Princes have also argued that the OFT has been selective in attributing weight to some comments made in documents and not others. The OFT is aware that certain statements made in the parties' internal documents may be consistent with the parties' position, however, in the OFT's view, the balance of views expressed in the parties' internal documents refer to close competition between the parties than providing an indication of little or no competition. Examples of this can be found within the [ ].

46. In the Issues Meeting, the parties told the OFT that their internal documents should be read in the context of competition for shelf space, so naturally they mention each other's brands. The OFT notes that the statements made by the parties do not only mention each other's brands but also discuss the extent and degree of competition between those brands.

47. As noted above, in one document, the [ ]. The parties provided an explanation for this statement in order to support their argument that this did not indicate that they considered the parties were close competitors – specifically, they stated that Fray Bentos takes sales from chilled and frozen pies—inflating its market share—but not from Princes, whose market share therefore appears to fall (given that market shares must always sum to 100 per cent) even though Princes experiences no loss in sales to Premier.

48. The OFT considered that this explanation could be plausible but given the statement would require evidence to refute the more literal interpretation. The OFT therefore requested evidence to support this explanation and the parties referred to econometric evidence supplied to the OFT. This econometric evidence is discussed at paragraphs 58 to 72 below.

49. Set against this, the OFT notes that its investigation showed other evidence which indicated that the parties may be close competitors. For instance, Premier told the OFT that it tracks [ ]. This is supported by its internal documents which demonstrate that it tracks [ ]. Premier told the OFT that this was because of its strength in the supply of own-label ambient pies, however, and not because it viewed only ambient pies as competitors. That said, given the evidence supplied by the parties indicated that own label ambient pies represent a small proportion of overall ambient pie sales (see paragraph 37), it was not clear to the OFT why Premier would apparently track prices here more intensively than in areas where Premier's own label sales are a greater proportion of overall sales (ambient ready meals, for example).

50. The OFT understands that, other than for the purposes of the current investigation, neither of the parties purchases pricing or switching data pertaining to [ ]. The parties submitted that the reason for this was primarily because [ ]. [ ]. This tends to indicate that closeness of competition and not cost may be the factor determining which competitors the parties gather data on.

51. The parties also presented data in their Response to the Issues Paper, in response to an OFT request, in relation to the demographics of pie purchasers in the different temperature ranges. Though not determinative, this indicated that there were some similarities between the demographic groups buying ambient and frozen pies (largely classes D and E) and less

similarity with fresh pies. Taken at face value, this may suggest frozen pies compete with ambient ones.

52. However, this information does not indicate that actual switching between these products takes place nor that they are substitutes for one another. Moreover, this data relates to consumers rather than retailers, who are the parties' direct customers. The OFT's market investigation (summarized below) revealed retailer views that contradicted the implications that may be drawn from the demographics data.

53. On balance, then, on the basis of the above, the information provided by the parties, including from their internal documents, suggests that the parties are sufficiently close competitors for the merger to give the OFT cause for concern over unilateral effects.

Results of the OFT's market investigation

Competitors in ambient pies

54. Several third parties told the OFT that the parties are each others' closest competitors in ambient pies. The majority of customers were of the view that the parties are the only credible alternatives in this category.

55. The parties, in response to the Issues Paper, submitted that [ ] had recently obtained listings for ambient pie and pudding products in a few retailers. They also submitted that they had [ ]. Since these events were very recent, the parties were unable to provide the OFT with [compelling] information on either the number of listings and volume of distribution won by [ ] and lost by the parties and/or the share of supply won by [ ]. The OFT has insufficient evidence to support the notion that [ ] is, or will become, a sufficient credible alternative such that it would replace the pre-merger constraint provided by Princes to Premier in relation to ambient pies. The OFT also notes that this new information must be set against the concerns expressed by customers about [ ] production capacity and therefore its ability to be a credible alternative for the merger parties. On the basis of the evidence available to it, the OFT does not consider [ ] to be a strong alternative to the parties in the supply of ambient pies.

Chilled and frozen pies

56. Third party evidence, including both comments from customers and from market research reports, suggests that there are differences in consumer behaviour and choice based on the temperature format of the product, which would suggest they do not compete strongly with one another. Several third parties have informed the OFT that this is because of their significantly different pricing points, locations in store, and variation in perceptions on quality; frozen and ambient are considered to be of lower quality than chilled.

57. The evidence from third parties on the substitutability of ambient, chilled, and frozen pies—though not determinative—has for the main part, supported the proposition that chilled pies do not constrain ambient ones given their differing pricing points and quality perception. The majority of customers told the OFT that they did not believe that frozen pies acted as a constraint on ambient pies.

Quantitative evidence

Econometric estimates of demand for ambient, chilled and frozen pies

58. The parties submitted an econometric demand analysis for pies using retail level scanner data.[23] The data included the quantity demanded and average revenue (to measure prices) at the brand level for ambient, chilled, and frozen pies. Two calculations were conducted with the analysis. First, a critical loss analysis was used to directly apply the hypothetical monopolist test. Second, the diversion ratios from the demand analysis were used in conjunction with the parties' margins to calculate measures of the value of diverted sales internalised by the merger.

[23] The econometric analysis used a standard two-stage budgeting model. The first stage models consumers' expenditure between (a) chilled pies; or (b) ambient or frozen pies. The second stage models product expenditure within these two segments. The econometric specification used was the Linear Almost Ideal Demand System model. Estimation was based upon a sample of weekly pricing (that is, average revenue) and volume data for pies in the three ambient temperature ranges, between 2008w4 and 2011w4, sourced from AC Nielsen and aggregated across supermarkets and across pie fillings.

Critical loss analysis

59. Critical loss analysis uses estimates of variable costs saved in response to an arbitrary loss of business to calculate how much business would have to be lost to render unprofitable a five per cent price increase on at least one of the products in the market under consideration (here, ambient pies)—this is the 'critical loss'. If estimates of the predicted loss of sales in response to a five per cent price increase (known as the 'actual loss') exceed this critical loss, then the market may be wider than the narrow candidate market (that is, wider than ambient pies only). Estimates of variable costs saved were based on the own-price elasticities of demand in the parties' demand estimates.

60. The parties' critical loss analysis suggested that the 'actual' (that is, predicted) loss from a five per cent price increase of all ambient pies would exceed the critical loss, albeit not by much. This in turn implies that it would just be unprofitable for a hypothetical monopolist of ambient pies to raise the price of all of them by five per cent, which suggests that the market is wider than only ambient pies—but not much wider.[24]

61. Set against this, the OFT notes that the Merger Assessment Guidelines say that, when implementing the hypothetical monopolist test for market definition, the OFT will assess whether the hypothetical monopolist could profitably raise the price of at least one of the products in the candidate market but not necessarily all of them.[25] In the present case, evidence from the parties' internal documents indicated that this was a sensible thought experiment for market definition, [ ]. On this basis, the OFT therefore assessed whether the actual/predicted loss suffered by a hypothetical monopolist from a price increase on one of the merging parties' products would exceed the critical loss. In contrast to the parties' analysis, the critical loss analysis using this formulation and the parties' estimates suggested that the product market definition should be no wider than ambient pies.

[24] The parties' estimated critical loss was [10 to 15] per cent and their estimated actual/predicted loss was [10 to 15] per cent.
[25] See Merger Assessment Guidelines, paragraph 5.2.11.

Value of diverted sales internalised by the merger

62. In order to assess the extent of the loss of competition likely to occur as a result of the merger, the OFT may, when available, examine the value of diverted sales that the merging parties lose to each other (in proportional terms) following a price rise. This analysis uses two primary pieces of evidence:

- the closeness of substitution between the parties' brands, as measured by the diversion ratio between them. If the parties' brands are close substitutes, unilateral effects are more likely as the parties will recapture a significant share of the sales lost in response to any price rise post-merger, making the price rise less costly and

- the variable profit margin on sales. If the variable profit margins of the parties' brands are high, unilateral effects are more likely because the value of sales recaptured by the parties post-merger will be greater, making any price rise less costly.

63. By multiplying together the diversion ratio between Premier and Princes and Premier's variable profit margin on sales—both as implied by the parties' econometric estimates—the parties submitted that the value of diverted sales in proportional terms (known as the Gross Upward Pricing Pressure Index or GUPPI) was [five to 10] per cent. The parties argued that this is an overestimate of the likely percentage price change because Princes only been able to pass on [55 to 60] per cent of wholesale cost increases into wholesale price increases. The parties also argued that the OFT should note that Princes is [five to 15] per cent of the parties' sales and so the price increase across the parties' pie portfolio would not be substantial.

64. Set against this, the OFT believes that there are three reasons why the parties' GUPPI is an underestimate.

65. First, the diversion ratio from Princes to Fray Bentos estimated by the parties is [10 to15] per cent. This diversion ratio controls for sales lost to chilled and frozen pies but does not attribute private label sales to the parties. Moreover, despite being sold at the majority of grocers and impulse retailers (according to the parties), Princes and Premier are not

sold in all retailers. Where the parties do not compete in all retailers, aggregation across retailers (such as in the data used in the parties' econometrics) will tend to understate diversion—albeit not by much in this case. These are good reasons, on a cautious basis, to regard 15 per cent as very much a lower bound estimate.

66. Second, the variable profit margin on sales used in the parties' GUPPI calculation is [35 to 40] per cent yet the same margin used in their critical loss analysis is [40 to 45] per cent. Were they to have used [40 to 45] per cent, the parties' GUPPI would have been [five to 10] per cent.

67. In this regard, the parties have provided profit margins for the overlap products. Premier measures the variable profit margin on sales as total contribution after marketing ('TCAM') margin by customer and by brand. TCAM is equal to net sales[26] less prime cost, customer agreements and consumer marketing. The parties advise that TCAM margin captures the costs of customer agreements and consumer marketing; it does not include fixed costs. Premier's TCAM margins across products and customers range from [15 to 20] to [40 to 45] per cent, the latter for steak and kidney pies, which make up the bulk of Premier's sales. Consequently, GUPPI based upon a variable profit margin on sales in excess of 40 per cent seems reasonable given the parties' margin data.

68. Third, the GUPPI must be scaled by the relative prices of Premier's pies to Princes'. The ex-factory prices and quantity data for 2010 provided by the parties shows that Premier's pies are more than [15 to 20] per cent more expensive than Princes'. Consequently, were the parties to have allowed for this fact, their GUPPI (with a [40 to 45] per cent margin) would have been [five to 10] per cent.

69. Further, although the parties submitted that Princes has only been able to pass on [55 to 60] per cent of wholesale cost increases into wholesale price increases, the OFT considers that this is likely to be an underestimate of the rate of pass through. The parties' estimate of the rate of pass through is based upon Princes' 'COGS' margin (cost of goods sold), which appears to include costs other than the raw materials costs that the parties submitted had seen large increases.

[26] Gross sales less short term promotions and business protection deals.

70. Even so, with a GUPPI of [five to 10] per cent, pass through would only need to be [60 to 65] per cent before the value of diverted sales internalized by the merged (GUPPI) calibrated as a potential price rise would exceed five per cent. In previous cases, possible price effects of this magnitude have given the OFT cause for concern over unilateral effects. In this regard, the parties' own price elasticity estimates for the ambient pies segment (the appropriate elasticity to use given that the parties will be near-monopolists of ambient pies post-merger) imply a pass-through rate well in excess of [60 to 65] per cent (indeed, in excess of [90 to 100] per cent).

71. Lastly, the OFT does not consider that that fact that Princes is [five -15] per cent of the parties' sales, and that any price increase across the parties' pie portfolio would not be substantial, is a relevant factor. The OFT has always gauged its 'intervention threshold' against possible price effects on one or a few products and not on all products in a market.

72. On this basis, the OFT believes that the diversion ratio and margin evidence indicate that the parties will have the incentive to raise prices post-merger. The value of diverted sales internalized by the merged (GUPPI) calibrated as a potential price rise (that is, multiplied by the rate of pass-through) is at a level—at least eight per cent and possibly as high as 12 per cent—that gives the OFT cause for concern over unilateral effects. Moreover, the OFT notes that this finding is consistent with the results of the OFT's critical loss analysis; that is, it suggests a market no wider than ambient pies (indeed, it suggests that the narrowest market satisfying the hypothetical monopolist test contains only the parties' ambient pies).

'Switching' analysis

73. At the Issues meeting on 8 June the parties provided the OFT with recent Kantar World Panel data headed 'switching analysis'[27] covering the period of the 52 weeks up to 15 May 2011.

74. Although, the parties presented this as 'switching data', it is not clear to the OFT that it is indicative of actual switching taking place. It indicated that buyers of ambient pies also bought pies at other temperature ranges

[27] Contained with annex 2 of the parties Response to the Issues Paper.

over the period.[28] No supporting evidence was provided to show whether this was genuine 'switching' in the sense that the consumer was directly making a choice to buy pies at a particular temperature range over pies at another temperature range, for example, as a reaction to promotional activity. It is plausible that, for example, a consumer might be buying chilled pies to eat straight away and also stocking up on ambient/frozen pies to eat over a longer period, thus satisfying different needs, but not actually perceiving the two as competing directly.[29]

75. Moreover, taken at face value, the switching data suggested that some [75 to 80] per cent of ambient pie customers may be marginal shoppers. Were these shoppers marginal to price, this would imply an own-price elasticity of demand for ambient pies far in excess of the parties' estimated segment elasticity of – [zero - five]. When the OFT put this to the parties, they told us that the two pieces of evidence were not necessarily inconsistent because the switching analysis probably contained information on consumers switching for reasons other than price. They also told us that it would not be worth attempting to reconcile the two pieces of evidence any further than this. Given the great weight that the parties attached to their econometric estimates, this left the OFT unsure what weight, if any, to attach to the switching analysis.

Entry and expansion

76. The parties consider that barriers to entry are low, especially for producers of ambient meat and ready meals. The parties suggest that likely entrants include [ ].

77. The Project Orpheus deal document at page 28 states that 'Both [ ] are looking to develop a 'customer own brand' offering [ ]'. The OFT has not been able to confirm whether or how far progressed these plans are [ ].

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[28] In fact, the data presented suggested that only [zero to 10] per cent of ambient pie customers only bought ambient pies, the remainder also purchasing pies at other temperature ranges.

[29] In this regard, the OFT notes that the parties' econometric results were consistent with the existence of this kind of stocking (or 'larder loading') behaviour, as the regression errors in their analysis exhibited serial correlation.

78. The OFT notes that [ ] confirm that it does not consider the threat from own label pies to be particularly strong. It notes that Morrison's has recently introduced own label pies and that [ ].[30]

79. Third parties suggested to the OFT that canned foods sales are in long term decline and that investment in the sector is declining. Further, the OFT has received no evidence that the potential competitors identified by the parties – [ ] – had any plans to begin supplying ambient pies.

80. One retailer further told the OFT that it would be expensive for a competitor to replace Princes given the [ ].

81. On this basis, entry and expansion do not appear timely, likely and sufficient to countervail the loss of competition from the merger.

Conclusion on the supply of ambient pies

82. There are grounds to believe that the proposed transaction will result in an SLC in the supply of ambient pies to retailers in the UK. The parties are the sole suppliers of branded ambient pies. It is not clear the extent to which own label pies constrain the price of branded pies at the retail level, but in any case they account for a relatively small share of the market. Moreover, the parties are also the leading suppliers of own label pies, making it difficult for retailers to constrain the parties by threatening to switch to stocking own label instead of the parties' branded products.

83. The OFT does not consider that the evidence supports widening the market to include chilled and frozen pies. However, even on the basis of such a market definition, the parties are clearly each other's closest competitor. Even if their private label product sales are not included (an assumption favourable to the parties), the value of diverted sales internalized by the merger (the GUPPI) calibrated as a price rise raises prima facie competition concerns. Entry and expansion do not appear to be timely, likely or sufficient to countervail the loss of competition from the merger.

[30] [ ].

Ambient peas

Market shares

84. The parties have argued that 'fresh' and frozen products compete with ambient products, particularly in the case of vegetables. They have argued that temperature range is not a strong factor significantly influencing consumer choice. On this basis, the parties submit that their combined market share is [20 to 30] per cent (with an increment of just 0.2 per cent). This is not high enough to give the OFT cause for concern over unilateral effects, provided that the market is drawn appropriately narrowly.

85. In measuring the parties' combined market share in ambient peas, the OFT has had to take a view on whether sales of own label ambient peas should be attributed to the retailer or to the supplier. In this regard, Princes' deal documents indicate that it attributes the market share from the sale of own label garden peas to Premier.

86. Own label makes up the majority of the supply of ambient peas (above [85 to 95] per cent) but the parties have a high share of supply of both branded and own label ambient peas.

87. In previous decisions, the OFT has generally been cautious about the constraint that own label products are able to place on branded products, although it has accepted the existence of such a constraint in some cases.[31] In those cases, the OFT had been provided with a significant amount of evidence on the degree of competitive constraint and the competitive interaction between own label and branded products. In this case, the parties have not been able to provide similar evidence, sufficient to convince the OFT that branded should be considered as forming part of the same market as own label.

88. Third party responses overwhelmingly support the supposition that consumers and, by extension, retailers, would readily switch between own label peas and branded peas following a small but significant and non-transitory increase in prices. Premier, however, has the leading

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[31] For example, completed acquisition by Dr Oetker (UK) Limited of the business and assets of Schwan's Consumer Brands (UK) Limited, OFT decision of 5 May 2009.

position in the supply of private label ambient peas and so at least some of the diversion from branded peas will be internalized by the parties. The OFT therefore considers own label and branded peas together.

89. On this basis, the parties have a combined share of supply of branded and own label ambient peas of [85 to 95] per cent by value, albeit with an increment of only [zero to five] per cent.[32] Although this increment is small, evidence on the closeness of competition between the parties and between ambient peas and chilled and frozen ones is nonetheless examined below.

Closeness of competition

Ambient, chilled and frozen peas

90. The parties have noted OFT previous decisions which deal with the scope for substitution between products stored at different temperature ranges. In particular, they refer to a decision involving pizzas.[33] The OFT accepted that in that case there was some evidence that the retail prices of chilled and frozen pizzas seemed to follow each other 'which was indicative of there being some competitive interaction' and that they may have been substitutes. In particular, the parties note that if the acquisition were considered on the basis of both ambient and frozen peas (branded and own label), the parties' combined share of supply is [20 to 30] per cent with an increment of just [zero to five] per cent.

91. Some retailers told the OFT that frozen peas exert at least some constraint on ambient ones, although one frozen pea supplier told the OFT that the ambient canned market is 'very different' from the frozen market. Premier's internal documents also note that [ ].[34] Premier, however, regularly monitors [ ] although it has said this is more because of [ ].

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[32] If the OFT were to consider that branded supplies should be considered separately the parties have a combined share of supply of [55 to 65] per cent with an increment of [25 to 35] per cent. However, as discussed above the OFT considers that branded and own label form part of the same market – and in any case branded ambient peas only represent around [five to 10] per cent of total ambient pea sales, and therefore this figure is not viewed as instructive.
[33] ME/4033/09 dated 12 May 2009. Completed Acquisition by Dr Oetker (UK) Limited of the business and assets of Schwan's Consumer Brands Limited (paragraphs 12-16).
[34] Annexe 2I to the parties response to the OFT's first information request.

92. The parties provided the OFT with Kantar data which was presented to the OFT as evidence of 'switching' between the different temperature ranges. Although indicative that shoppers who purchase frozen peas may also buy other types, it was not compelling enough to lead the OFT to conclude that there was switching taking place of the kind relevant to market definition (that is, switching in response to changes in relative prices).

93. The parties in their response to the Issues Paper also point out the similarities between frozen and ambient peas; both being side dishes, capable of being stored for prolonged periods of time and cultivated from the same vegetable.[35]

94. Taken in the round, the evidence available to the OFT does suggest that frozen peas place some constraint upon ambient ones, but the magnitude of that constraint is unclear. As such, the OFT considered carefully the likely impact of the merger on the supply of ambient peas.

Ambient peas competitors

95. Princes has minimal sales of around £[ ] a year and the majority of these are accounted for through [ ]. The parties argue that Princes position is weak [ ] and that is compounded by the fact that Princes does not have an own label presence which makes up the bulk of sales. Its sales represent less than [zero to five] per cent of total ambient pea sales. In addition, the parties do not have any customers in common.

96. Consistent with this, the parties submitted that they do not compete at all strongly with one another – only one tender in the past three years has involved both the parties as potential suppliers.[36] Set against this, some third party respondents noted the parties as being close competitors in ambient peas.

97. The parties further submitted that a range of alternative supply options will remain post-merger. They submitted that Premier is mainly constrained by [ ] whose sales of garden peas are five times those of Princes. In addition, the parties submitted in their Response to the Issues

[35] Paragraph 5.4.4. They also give an example of a supplier of Premiers peas who supplies both ambient and frozen customers.
[36] Paragraph 5.10 of the Parties Response to the Issues Paper.

Paper[37] that customers could seek alternative supply options via suppliers with an integrated supply chain for supply into the UK or via third party supply arrangements. Retailers could source peas from other European suppliers or through UK importers with links to the UK retailers. That said, Princes' deal document noted that [ ] and [ ] have a limited presence in the UK and that these competitors are unlikely to increase their presence in the future.

98. Despite this, the parties submitted that both these parties together currently supply all of the 'Big Four' supermarkets as well as other retailers such as Waitrose and Co-op. In particular, the parties told the OFT that [ ] has a high level of distribution in Asda and [ ] has a high level of distribution at Morrison's.

Conclusion on the supply of ambient peas

99. Taking account of the low market share increment created by the merger, the relative weakness of Princes and the fact that it mainly supplies [ ], the presence of [ ] and the existence of alternative suppliers, the OFT believes that there are no grounds to believe that the proposed transaction may result in an SLC in the supply of ambient peas to retailers in the UK.

Corned beef

Market shares

100. The parties overlap in the supply of branded ambient corned beef to grocery retailers. The parties' combined share of supply of branded ambient corned beef is [65 to 75] per cent, with an increment of [zero to five] per cent. This is high enough to give the OFT cause for concern over unilateral effects.

101. Own label constitutes 30 per cent of total ambient corned beef sales. The OFT's market investigation indicates that own label does not constrain the merging parties' branded corned beef in all retailers. Evidence provided by the parties' shows that [ ] have the largest shares (between [ ] per cent and [ ] per cent each) of own label retail sales of corned beef. [ ] and [ ]

[37] Pragraph 5.13, and the Parties' Second Further Submission at paragraphs 15 – 17.

have relatively limited sales of own label corned beef; and [ ] and [ ] have none. Own label products are therefore not considered to be a constraint on the merger parties for all retailers, although they may be in relation to the retailers that stock both.

102. The supply of ambient own label corned beef is a virtual duopoly with Princes having a [40 to 50] per cent share of own label supply and Marfrig having a [50 to 60] per cent share. Premier does not supply own label corned beef. Given Princes' strength in the supply of own label corned beef, the OFT does not believe that it is appropriate to apportion the market share for own label corned beef to retailers.

103. On this basis, the parties' combined share of supply including own label is [40 to 50] per cent with an increment of below [zero to five] per cent. Although this increment is small, the OFT has nonetheless examined evidence on the closeness of competition below.

Closeness of competition

Between the parties

104. The parties submitted that Premier is a minor player in corned beef and that its position has weakened over recent years. More particularly, they argued that Premier is [ ] and that as a consequence it is appropriate for the OFT to consider the constraint that Princes places on Premier and not the constraint that Premier places on Princes.

105. Set against this, the parties' internal documents indicate that Princes is a strong constraint on Premier in the supply of corned beef, [ ]. Princes' deal document further states' [ ]'.[38]

106. The extent of competition between the parties is further evidenced by internal documents showing that [ ].

107. That said, third parties—with the exception of one—did not regard the parties as particularly close competitors.

[38][ ].

Other suppliers of ambient corned beef

108. The parties contend that post-merger the parties will remain able to supply corned beef from a range of suppliers. The parties advise that both Marfrig and JBS (who supply the majority of corned beef into the UK) have sales offices in the UK and can bypass the parties to deal directly with retailers. Apart from the constraints from these two suppliers, the parties note the constraint from other traders in canned corned beef – John West, Red Lion, and Tulip - that will remain post merger.

109. Apart from Princes, other significant branded players are John West (via a licensee, Best West Foods), with around [five to 15] per cent in branded ambient corned beef, and Ye Olde Oak. The parties' view is that these competitors could [ ]. Consistent with this, market share data for the first six months of 2011 indicates that Ye Olde Oak's share of supply has increased to [zero to 10] per cent; John West's has increased to [five to 15] per cent and Red Lion's increased to [zero to five] per cent. In this time, Princes' market share has fallen to [25 to 35] per cent. Such movement in market shares over time can indicate intense competition.[39]

110. John West, Ye Olde Oak and Red Lion all remain in the market and have higher sales in branded corned beef than Premier.

Entry and expansion

111. The parties submitted that there were a number of existing players who could credibly enter/expand into corned beef, in particular [ ]. Third party views on the timeliness, likelihood and sufficiency of expansion [ ] were mixed, however.

Conclusion on the supply of ambient corned beef

112. On the basis of the above, Premier appears to be a constraint on Princes, albeit a recently declining one. However, the increment in the share of supply resulting from the merger is limited (on whatever basis the market is assessed), third parties were generally unconcerned (apart from one) and there appear to be other credible competitors remaining in the market. The OFT does not therefore conclude that an SLC in the supply of corned

[39] See Merger Assessment Guidelines, paragraph 5.3.2, second bullet.

beef to retailers in the UK will result from the merger. Given this, the OFT has not needed to conclude on barriers to entry and expansion in ambient corned beef.

Ambient ready meals

Market shares

113. The parties are active in the supply of ambient ready meals of the following types: curries, chilli, pasta, and 'other'. The parties' combined market share over all types of branded and own label ambient ready meals is [55 to 65] per cent with an increment of [20 to 30] per cent. By individual types of branded and own label ambient ready meals, the parties' shares are below.

Table 1: Parties' share of supply in ambient curry ready meals

	Branded (per cent)	**Own label (per cent)**	**Combined (per cent)**
Princes	40 to 50]	[20 to 30]	[25 to 35]
Premier	0 to 10]	[40 to 50]	[30 to 40]
Combined	**[45 to 55]**	**[60 to 70]**	**[55 to 65]**
Simpsons	[20 to 30]		[5 to 10]
Ye Olde Oak	[0 to 10]		[0 to 5]
Grants	[0 to 5]		[0 to 5]

Source: AC Nielsen data provided by the parties

Table 2: Parties' share of supply in ambient chilli ready meals

	Branded (per cent)	Own label (per cent)	Combined (per cent)
Princes	[5 to 15]	[25 to 35]	[10 to 20]
Premier	[0 to 5]	[40 to 50]	[10 to 20]
Combined	**[10 to 20]**	**[60 to 70]**	**[30 to 40]**
Tulip	[70 to 80]		[50 to 60]
Simpsons	[0 to 5]		[0 to 5]
Westler	[0 to 5]		[0 to 5]

Source: AC Nielsen data provided by the parties

Table 3: Parties' share of supply in ambient pasta ready meals

	Branded (per cent)	Own label (per cent)	Combined (per cent)
Princes		[0 to 10]	[0 to 5]
Premier	[0 to 5]	[60 to 70]	[10 to 20]
Combined	**[0 to 5]**	**[60 to 70]**	**[20 to 30]**
HJ Heinz	[90 to 100]		[70 to 80]

Table 4: Parties' share of supply in ambient 'other' ready meals

	Branded (per cent)	Own label (per cent)	Combined (per cent)
Princes	[20 to 30]	[20 to 30]	[25 to 35]
Premier	[0 to 10]	[40 to 50]	[25 to 35]
Combined	**25 to 35]**	**[60 to 70]**	**[55 to 65]**
Tanfield	[20 to 30]		[0 to 10]
Grants	[10 to 20]		[0 to 5]
Simpsons	[10 to 20]		[0 to 5]

114. In the branded segment of the market, both parties are active. However, Premier is a relatively small player in this market, with Princes (where it has a significant market position) typically facing at least two other competing suppliers which are larger than Premier pre-merger. This is true

even in the branded ambient curry ready meal segment, where the parties have a combined market share of [45 to 55] per cent (increment [zero to 10] per cent), but there are three significant competitors remaining in this segment post-merger, two of which are larger suppliers in this segment than Premier.

115. As such, the OFT is satisfied that the merger does raise significant competition concerns for the supply of branded ambient ready meals alone.

116. However, whether types of ambient ready meal are taken together or separately, the data shows that parties are the leading suppliers of own label ambient ready meals. In the case of all four categories, the combined shares are at a level which would typically give the OFT cause for concern over unilateral effects.

117. Further evidence is therefore examined below.

Closeness of competition

Ambient, chilled and frozen ready meals

118. The parties submitted Kantar data[40] showing that [90 to 100] per cent of ambient ready meal consumers also purchase chilled or frozen ready meals. The parties interpret this data to mean that consumers switch between ready meals in the three temperature ranges. However, for the reasons explained above in other product overlaps, although this may indicate that consumers buy across different temperature ranges, its value in showing actual switching of the type relevant to market definition is limited.

119. In a similar vein, other internal documents were consistent with, but not probative of, the proposition that ambient ready meals may be constrained by other products. For example, one Premier internal document [ ]'.[41]

120. Likewise, the parties also argued that market research reports, for example, one compiled by Mintel,[42] are supportive of the proposition that

[40] Annexes 14A to 14C of Form RS.
[41] Form RS paragraph 82

ready meals are constrained by other products and other temperature ranges.

121. Set against this, there was virtually no evidence in the parties' internal documents to indicate that they actively monitor or react to the actions of chilled and frozen ready meal suppliers. Moreover, there was no evidence from the parties' internal documents that the information in market research reports was considered by the parties let alone acted upon. In support of the competitive constraint from other producers Premier provided the OFT with tracking data [ ].

122. Consistent with this, third parties were generally of the view that ambient ready meals are not constrained by chilled or frozen ready meals. Further, one customer told the OFT that the purchase of ambient ready meals was carried out entirely independently of the purchase of ready meals at other temperature ranges and that, by way of illustration, if there was a promotion on products at one temperature range, they would not expect any effects on other temperature ranges and would not monitor this.

123. On balance, the evidence in the parties' internal documents and from third parties does not support the view that chilled and frozen ready meals place a sufficiently strong constraint upon ambient ready meals to place them in the same relevant market, notwithstanding some limited evidence of competitive interaction between them.

Bidding data

124. Consistent with the parties' high shares of ambient own label ready meals, bidding evidence submitted by Princes[43] suggested that the parties have recently or currently been in direct competition for shelf space at [ ] and at [ ]. However, other bidding data submitted by the parties suggests that each of the parties' largest customers has at least one or two choices other than the parties as suppliers for each type of ambient own label ready meal. This suggests that, although there is evidence that the parties have competed head-to-head, they also compete with other suppliers.

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[42] Mintel Market Report: Canned Meals and Meats – UK – Market Intelligence Report (March 2010).

[43] Annexe 6A to the parties response to the OFT's first information request.

125. In this regard, three of the four main retailers mentioned, as either having bid for own label contracts or as potential suppliers of them, [ ]. Retailers also thought that they may be able to turn to other smaller competitors specialising in particular types of ambient ready meal such as Westlers, Grants and Red Lion.

126. On the basis of the above, the OFT considers that the parties will continue to face a competitive constraint from a variety of existing players post-merger.

Entry and expansion

127. One retailer commented that the competitors that are the next best alternatives to the parties are Simpsons and Westlers, although it was concerned that they might not have spare capacity. One third party, that supplies three of the four ready meals categories, told the OFT that it is currently operating at [ ] per cent capacity. The third party also advised that it is considering exiting canned ready meals because of recent steel price increases – although this is a factor facing all canned goods manufacturers. Given the mixed evidence received the OFT is not able to conclude that entry would be timely, likely, or sufficient. In any case given that it has found no SLC in this market it has not been necessary to do so.

Conclusion on ambient ready meals

128. The parties have combined shares of supply in ambient ready meals at a level sufficient to raise prima facie concerns. Although, the parties' bidding data suggested that they compete head-to-head, other data also identified several other strong ambient ready meal suppliers. However, the bidding data is supportive that there are several other credible suppliers of ready meals (although not all of them produce all varieties of ready meals). The bidding data indicates that most of the parties largest customers have a choice in who supplies them and the majority of them had no concerns that the transaction would substantially lessen competition in ready meals. Given that there is sufficient existing constraint on the parties it has not been necessary for the OFT to conclude on entry and expansion.

Ambient meatballs

129. The parties do not overlap in the supply of ambient meatballs. Premier holds a [70 to 80] per cent market share in ambient meatballs. Princes does not have a presence in ambient meatballs.[44] However, there was some evidence in Princes' recent internal documents indicating that [ ]. [ ].[45]

130. The Merger Assessment Guidelines[46] state that there are two ways in which the removal of a potential entrant could lessen competition by weakening the competitive constraint on an incumbent supplier. The first is where the merger involves a potential entrant that could have increased competition. Such 'actual potential competition' is a constraint only if and when entry occurs. The second is where the merger removes a firm which is not in the market, but which nevertheless imposes an existing constraint because of the threat that it would enter if existing firms in the market raised their prices. A constraint from such 'perceived potential competition' may arise even though the OFT do not believe that entry would actually occur.

131. Given [ ], in this case the OFT was concerned about a loss of actual potential competition. In assessing whether a merger leads to unilateral effects from a loss of actual potential competition, the OFT considers the following questions:

(a) Would the potential entrant be likely to enter in the absence of the merger?

(b) Would such entry lead to greater competition?

132. In respect of (b), the supply of ambient meatballs is highly concentrated. The other brand in this category is 'Tyne', a Westlers brand. [ ] notes that [ ] was not considered a constraint on Premier pre-merger:

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[44] [ ]Premier has a [50 to 60] per cent market share in meatballs (taking branded and own label together) and own label accounts for [25 to 35] per cent of sales. Further, Premier supplies around [80 to 90] per cent of own brand meatballs.

[45] The OFT has considered actual potential competition in ambient meatballs as the narrowest candidate product market where the parties could overlap.

[46] See paragraphs 5.4.13 to 5.4.18.

'[ ]'.[47]

133. On this basis, it seems clear that entry would lead to greater competition, inasmuch as Premier currently appears to face very little.

134. However, in respect of (a), the parties submitted that Princes does not [ ], [ ].

135. In support, the parties submitted [ ].

136. In addition, the parties provided evidence to the OFT that Premier perceives there to be two other strong competitors in branded meatballs, [ ],[48] as well as [ ] in own label meatballs with several multiple retail customers. On this basis, the parties argued that Princes was not particularly well placed to be an actual potential competitor to Premier, let alone uniquely well placed.

137. On the basis of the above, there was little evidence that Princes' [ ] [ ], nor that—given potential competition theories of harm are easy to allege but hard to rebut—Princes was particular well placed to enter. In addition, there was no evidence that [ ]. The OFT does not therefore consider that the merger gives rise to a realistic prospect of an SLC on the basis of unilateral effects from the elimination of actual potential competition in the supply of ambient meatballs.

CONGLOMERATE EFFECTS

138. The merger will enable the parties to supply a far broader range of products. As well as the overlap products, the parties produce a wide range of other ambient products.

139. The parties have stated that their products are not bundled but supplied separately; therefore trading conditions will not change post merger. However, several third parties raised concerns that as a result of the merger the enlarged entity will be able to leverage its power through the supply of many products to disincentivise customers from multi-sourcing

[47] Princes' internal document [ ].
[48] Paragraph 8.2 of the parties Response to the Issues Paper.

and taking products produced by the parties from a range of producers. One third party commented that the merged entity will have a wide portfolio of products and brands across the canned sector. In terms of brands post-merger it would hold the majority of brands in the canned sector. It was argued that this may allow the parties to ensure better trading terms for their products, in terms of shelf space, listing of products and brands outside this category, higher promotional and cross promotional activity.

140. The OFT takes into account a number factors when considering conglomerate effects:[49]

- whether sellers have market power, by dint of high market shares or a 'must stock' product or products, for example. In this regard, on the basis of the assessment above, the merger gives the parties market power in ambient pies and Fray Bentos was mentioned as having a strong brand. Set against this, none of the parties' brands were mentioned in a recent survey of the top 100 FMCG (fast-moving consumer goods) brands. Further, the merger will actually narrow the range of products sold by Premier

- whether customers have a demand for more than one product and whether the products are complements. In the current case, the parties supply a range of products, including non-overlap products such as canned tuna. However, the mere fact that retailers may prefer to purchase these from one supplier does not imply that they are complements on the demand-side. Indeed, the OFT received no evidence that (say) canned tuna and ambient pies are complements in the view of retailers

- customer preferences for variety and one stop shopping. Retailers and competitors told the OFT that, unless a supplier is selling a niche or must-stock product, it is important for suppliers to be able to provide several products in order to minimise the time and cost in delivering products. Consequently, retailers told the OFT that they rarely take products in a 'bundle'

[49]Joint OFT and CC Merger Assessment Guidelines, Para 5.6.13

- whether rivals are able to replicate any putative 'bundle'. The majority of the parties' competitors are active in discrete segments of ambient foods, for example canned vegetables, and may be unable to provide the range of products provided by the parties.

141. On balance therefore, the OFT does not consider that the merger gives rise to a realistic prospect of an SLC on the basis of conglomerate effects.

BARRIERS TO ENTRY OR EXPANSION

142. Barriers to entry and expansion have largely been discussed above in respect of the most significant overlap markets. In respect of pies, entry was not found to be timely, likely and sufficient enough to override the competition concerns arising due to the merger. In respect of the other markets, the evidence was mixed, albeit the OFT was not able to identify a competitor with existing plans to enter in any of the markets. Nevertheless no conclusion was necessary on this point, given the absence of competition concerns in these markets.

143. Further, general support for relatively high barriers to entry and expansion in this sector is provided by Princes' deal document which notes that [ ]'.[50] Indeed Princes explains that this is the reason that it has taken it so long to gain traction in the ambient pie sector.

144. Moreover, the parties' competitors who responded to the OFT did not generally express an intention to expand their capacity and commented on the costliness of doing so, especially if this would require a new facility. In relation to corned beef and pies in particular there appears to be a need for brand strength for successful expansion.

BUYER POWER

145. Third parties told the OFT that global commodity price inflation was forcing up input costs for food manufacturers, and that this pressure on input costs was being passed on, to some degree, into retail prices. One retailer provided the OFT with graphs showing the rise in prices charged by the merger parties to that retailer over time.

[50] [ ].

146. The parties submit that the parties' activities are significantly constrained by buyer power, in particular that of the 'Big Four' grocery retailers that account for the majority of the parties' sales. As a consequence of having such a concentrated customer base, the parties argue that demand is consolidated in a small number of players, each of which individually accounts for significant sales for each of the parties. The parties further argue that because they are suppliers of products for which branding is unimportant, customers are able to easily switch as they are not trying to satisfy an end consumer demand for a particular recognizable branded products.

147. The parties state that the transparency of commodity prices means that price negotiations are constrained, as supermarket customers can easily work out the parties' margins and resist price increases.

148. The parties were invited to provide pricing information showing the pattern of pricing to supermarkets over the last three to four year period. The OFT was particularly interested in evidence which could demonstrate that cost price increases, and not low sales values, were responsible for delisting.

149. The parties have provided the OFT with evidence of e-mail negotiations between the parties and grocery retailers. Many of these e-mails did not pertain to overlap products and some pertained to non-overlap products and delisting because of poor sales rather than because of attempts by the parties to raise prices.

150. Just one of the e-mails supplied by the parties in response to the OFT's Issues Letter pertained to pies.[51][ ].

151. Moreover, even accepting that buyers in this market have a degree of buyer power, this does not imply they are protected from the impact of the merger. The key question is rather how the merger impacts on their buyer power.

152. Retailers advised the OFT that, post-merger, they would not possess sufficient buyer power to countervail the parties' market power. On the basis the parties have not demonstrated from their internal documents

[51] Annex 1R to the parties' submission to the OFT dated 27 May 2011.

that retailers have buyer power in relation to pies, and because of retailers' concerns about the impact of the merger on their buyer power, the OFT is unable to conclude that retailers have sufficient buyer power to prevent the SLC.

VERTICAL ISSUES

153. The merger does not give rise to any vertical issues.

THIRD PARTY VIEWS

154. Third party views have been referenced in the relevant sections of the competitive analysis above.

ASSESSMENT

155. The parties overlap in the supply of a broad range of food products to both food service and retail customers, namely:

- ambient pies in the retail channel
- canned ready meals (including curries, chilli, pasta and other) in the retail channel
- canned mince in the retail channel
- canned stewed/'chunky' steak in the retail channel
- ambient corned beef in the retail channel
- ambient garden peas in the retail channel
- canned red kidney beans in the retail channel
- canned mixed beans in the food service channel
- canned chick peas in the food service channel
- canned butter beans in the food service channel
- canned mixed vegetables in the retail channel
- canned potatoes in the retail channel
- canned carrots in the retail channel
- canned prunes in the retail channel
- ambient cooking sauces in the retail channel, and
- ambient wet soups in the retail channel.

156. In relation to nine narrow candidate markets in the retail channel, the OFT was able to dismiss as less than fanciful the risk that the merger would

result in a substantial lessening of competition on the basis of one or more of the following factors: the parties' combined market share and/or the increment to it were either not high enough to give the OFT cause for concern over unilateral effects, the parties do not appear to compete particularly closely with one another, no (or very few) third party concerns were raised in relation to these overlaps.[52]

157. The parties both supply into the food services sector. They overlap in canned mixed beans, canned chick peas and canned butter beans. The parties believe that supply to food service customers is distinct from supply to retail customers. Both the parties and third parties responses suggested that it was appropriate to distinguish between sales to the retail sector and the food service sector. No third parties indicated that the parties are particularly close competitors and no substantive concerns have been raised in relation to the supply of products to the food services sector. Third parties told the OFT that it is easier to enter the food service sector because branding is much less important and because the quality control required by food service customers is less exacting than that required by retailers. Supply into the food service sector was not considered further.

Ambient Pies

158. There are grounds to believe that the proposed transaction will result in an SLC in the supply of ambient pies to retailers in the UK. The parties are the sole suppliers of branded ambient pies. It is not clear the extent to which own label pies constrain the price of branded pies at the retail level, but in any case they account for a relatively small share of the market. Moreover, the parties are also the leading suppliers of own label pies, making it difficult for retailers to constrain the parties by threatening to switch to stocking own label instead of the parties' branded products.

159. The OFT does not consider that the evidence supports widening the market to include chilled and frozen pies. However, even on the basis of such a market definition, the parties are clearly each other's closest competitor. Even if their own label product sales are not included (an assumption favourable to the parties), the value of diverted sales

[52] Canned mince, canned stewed/chunky steak, canned red kidney beans, canned mixed vegetables, canned potatoes, canned carrots, canned prunes, ambient wet cooking sauces and ambient wet soup.

internalized by the merger (the GUPPI) calibrated as a price rise raises prima facie competition concerns. Entry and expansion do not appear to be timely, likely or sufficient to countervail the loss of competition from the merger.

Corned Beef

160. The parties overlap in the supply of branded ambient corned beef to grocery retailers. The parties' combined share of supply of branded ambient corned beef is [65 to 75] per cent, with an increment of [zero to five] per cent. This is high enough to give the OFT cause for concern over unilateral effects. Premier appears to be a constraint on Princes, albeit a recently declining one. However, the increment in the share of supply resulting from the merger is limited (on whatever basis the market is assessed), concerns from third parties were very limited and there appear to be other credible competitors remaining in the market. The OFT does not therefore conclude that the merger will give rise to an SLC in the supply of corned beef to retailers in the UK. Given this, the OFT has not needed to conclude on barriers to entry and expansion in ambient corned beef.

Ambient ready meals

161. The parties have combined shares of supply in ambient ready meals at a level sufficient to raise prima facie concerns, in particular in the supply of own label ambient ready meals. The parties' bidding data suggested that they compete head-to-head. However, the bidding data indicates that there are several other credible suppliers of ready meals (although not all of them produce all varieties of ready meals). The bidding data also indicates that most of the parties' largest customers have a choice in who supplies them and the majority of them had no concerns that the transaction would substantially lessen competition in ready meals. Given that there is sufficient existing constraint on the parties it has not been necessary for the OFT to conclude on entry and expansion.

Ambient peas

162. The parties have argued that 'fresh' peas and frozen peas both compete with ambient peas, and that temperature range is not a strong factor significantly influencing consumer choice. Whilst the available evidence

provided some support for the parties' claim that frozen peas place a constraint upon ambient ones, the magnitude of that constraint is unclear. As such, the OFT further considered the impact of the merger on ambient peas.

163. On this basis, the parties have a combined share of supply of branded and own label ambient peas of [85 to 95] per cent by value. However, Princes is a very small player in the market, with just [zero to five] per cent of this narrow market and primarily only supply one supermarket. A stronger player than Princes is [ ] which sells around [ ] times the peas as Princes and remains a constraint on the parties. It is also possible that other existing competitors of peas who import from outside the UK could expand their supply into the UK. Therefore, the OFT concludes that there can be no substantial lessening of competition in relation to ambient peas as a result of the merger.

Meatballs

164. The parties do not overlap in the supply of ambient meatballs. Premier holds a [70 to 80] per cent market share in ambient meatballs. Princes does not have a presence in ambient meatballs.[53] However, there was some evidence in Princes' recent internal documents indicating that [ ].

165. Following some investigation, there was little evidence that [ ], nor that—given potential competition theories of harm are easy to allege but hard to rebut—Princes was particular well placed to enter. In addition, there was no evidence that [ ]. The OFT does not therefore consider that the merger gives rise to a realistic prospect of an SLC on the basis of unilateral effects from the elimination of actual potential competition in the supply of ambient meatballs.

166. Overall, the OFT believes that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom, specifically in the supply of ambient pies.

[53] According [ ] Premier has a [50 to 60] per cent market share in meatballs (taking branded and own label together) and own label accounts for [25 to 35] per cent of sales. Further, Premier supplies around [80 to 90] per cent of own brand meatballs.

UNDERTAKINGS IN LIEU

167. Where the duty to make a reference under section 33(1) of the Act applies, pursuant to section 73(2) of the Act the OFT may, instead of making such a reference, and for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which has or may have resulted from it or may be expected to result from it, accept from such of the parties concerned undertakings as it considers appropriate.

168. Princes offered certain undertakings in lieu of a reference. The OFT has therefore considered whether these would address the competition concerns outlined above. The OFT's *Exceptions and Undertakings Guidance* states that undertakings in lieu of reference are appropriate only where the remedies proposed to address any competition concerns raised by the merger are clear cut and capable of ready implementation.[54]

169. Princes offered [ ].

170. The OFT's guidance explains its preference for structural divestments.[55] In exceptional circumstances, quasi-structural undertakings, such as a long-term brand licences or re-branding agreements may meet the clear-cut standard (see Unilever/Alberto Culver) even where they involve some form of brand splitting. For such remedies to be accepted, the OFT will seek to ascertain whether the incentives of the parties who would share the brand would be aligned. A strong indicator of such alignment is the structure of brand equity. If the brand equity to be divested is small in comparison to the retained brand equity, or where a high proportion of the revenues generated using the brand is in markets outside those where competition concerns have been identified, then there would be, absent other factors, few reasons to believe that the licensor (or licensee if there is licence back arrangement) would seek to devalue the brand. In contrast, where the brand equity to be divested is large and a high proportion of revenues generated from the brand are obtained in the market concerned by the remedy, then it may be that the incentives between the purchaser and the licensor will not align and the divestment offered would therefore not be

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[54] See OFT Mergers – *Exceptions to the duty to refer and undertakings in lieu of reference guidance* OFT1122, paragraph 5.7.
[55] OFT – Mergers – Exceptions to the duty to refer and undertakings in lieu guidance (OFT1254), paragraph 5.20.

clear-cut.

171. In applying these considerations to this case, the OFT notes that the majority of the sales under the Fray Bentos brand are generated from the market in which the OFT considers there to be a realistic prospect of an SLC (that is ambient pies). In addition, the retained brand equity (or the equity to be licensed back if there were a sale of the brand) competes with existing Princes products. These two factors mean that the OFT cannot, based on the information available to it, dismiss the possibility that the merged entity would have the ability and incentive to devalue or degrade the Fray Bentos brand. Such considerations cast doubt on the clear-cut nature of a brand split in the present case, and therefore prevent such a remedy from being acceptable at first phase. For these reasons, the OFT was not able to accept this remedy offer.

172. The OFT therefore considered whether to accept Princes offer of a more comprehensive remedy comprising the following main elements:

(i) the sale of the whole Fray Bentos brand covering all Fray Bentos branded canned products (that is, pies, puddings, corned beef, ready meals and meatballs) without a licence back to Princes in respect of any Fray Bentos brand canned products and

(ii) the sale of the Fray Bentos ambient pie manufacturing assets and

(iii) to the extent possible, the transfer of existing retail customer contracts for Fray Bentos branded canned products to the purchaser and

(iv) transitional manufacturing arrangement for a limited time (that is, until such time as the transfer or relocation of any manufacturing assets to the purchaser have been effected).

173. In assessing whether this package of assets would be sufficiently clear cut to address the concerns arising from the merger, the OFT considers that the sale of the entire Fray Bentos brand is appropriate in order to remedy the SLC in a clear-cut manner. Such a remedy package would provide a purchaser with a commercial incentive to manufacture and distribute ambient pies under the established Fray Bentos brand alongside a range of other canned food products.

174. Depending on the exact requirements of the purchaser, a transfer of the contracts related to the sale of products other than ambient pies would also be appropriate since it provides the purchaser with a range of products to manufacture and distribute to retailers, this is the case even though it extends beyond the area in which competition concerns have been identified. As such, the OFT considers that this offer is a clear-cut solution to the competition concerns.

175. The OFT has also considered whether the remedy offered is capable of ready implementation by reference to the following factors.

(i) The severability of the pie manufacturing assets. The OFT understands that the current pie manufacturing assets consist of two manufacturing line at Premiers' Long Sutton plant which, itself, was an addition to that plant. In so far as any pie manufacturing assets would need to be re-sited, Princes has explained that they could be easily severed from their current physical location and transferred to a potential buyer.

(ii) No transfer of manufacturing assets in relation to Fray Bentos products other than pies. The OFT considered whether a potential purchaser might require additional manufacturing assets in order to produce all the Fray Bentos products branding being transferred. Princes informed the OFT that in relation to canned ready meals and meatballs no special canning was required. Corned beef is manufactured and canned by a third party supplier and neither Princes nor the target business have manufacturing facilities in relation to corned beef. The only other Fray Bentos product being transferred which required specialist canning is puddings and they are produced on the same line as pies.

176. Length of transitional arrangement. The OFT was concerned to ensure that transitional arrangements are put in place to ensure that a purchaser is able to continue to meet contractual obligations with customers. Princes has offered a transitional manufacturing arrangement, at the election of the purchaser, for a period of six – 12 months to deal with this concern [should the buyer require this].

177. The OFT therefore considers, based on the above, that the offer of the sale of the Fray Bentos brand and certain pie manufacturing assets is a clear-cut solution and capable of ready implementation.

Up-front buyer

178. The OFT considered whether it is appropriate in the circumstances of this case to require that the relevant divestments are made in whole to an up-front buyer.

179. An up-front buyer requirement means that the proposed purchaser will have committed contractually, subject to formal OFT approval of the undertakings in lieu, to acquiring the relevant divestment before the OFT accepts undertakings in lieu. This means that the OFT will accept undertakings in lieu only where a provisional sale has been agreed, thereby demonstrating that a sale to a suitable purchaser is achievable. It also means that the OFT may consult publicly on the suitability of the proposed divestment purchasers, as well as any other aspects of the draft undertakings, during the public consultation period.

180. The OFT will seek an upfront buyer where the risk profile of the remedy requires it, for example where the OFT has reasonable doubts with regard to the ongoing viability of the divestment package and/or there is only a small number of candidate suitable purchasers for the divestment business that would remedy the competition concerns. Such doubts may arise, for example, because there are questions about the commercial attractiveness of the divestment business in question or where the field of suitable potential candidate purchasers is very limited.[56]

181. Princes has indicated that it does not consider an upfront buyer requirement appropriate since there is, in their view, a large range of purchasers available and the remedy is not complex in nature. The OFT however has residual concerns over both the remedy package offered and the actual number of suitable purchasers for the brand. In particular, the OFT considers that the nature of the remedy which involves the sale of a brand and discrete manufacturing assets to have a higher risk profile than a divestment remedy and that there is a need to approve the purchaser in these circumstances. Based on information supplied by Princes, the OFT

[56] Mergers - *'Exceptions to the duty to refer and undertakings in lieu of reference guidance'* (OFT1122 paragraph 5.33

considers that the number of purchasers with appropriate expertise may be limited. The OFT therefore considers that the requirement for an up-front buyer is both reasonable and proportionate in seeking to ensure that competition concerns are remedied.

182. The OFT considers that it is only appropriate to suspend its duty to refer on the basis that it will seek an upfront buyer for the divestment of this case. The OFT will therefore only accept undertakings, following consultation, when Princes has agreed to a provisional sale with a purchaser who has the necessary finance, expertise and business plans to acquire the brand and continue the sale of canned food products under the Fray Bentos brand.

Conclusion on Undertakings in lieu

183. Princes has offered undertakings in lieu of a reference to the Competition Commission that the OFT considers are, in principle, clear-cut and capable of restoring pre-merger levels of competition. The OFT therefore considers it appropriate to suspend its duty to refer this case while it considers further whether to accept these undertakings in lieu of a reference under Section 73 of the Act.

DECISION

184. The OFT considers that there is a realistic prospect of a substantial lessening of competition arising as a result of the anticipated acquisition by Princes of the canned foods product business of Premier to the Competition Commission pursuant to section 33 of the Act. The OFT has, however, suspended its duty to refer while it is considers whether to accept undertakings in lieu of reference from Princes pursuant to section 73 of the Act.