

Competition Commission  
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Victoria House  
Southampton Row  
London WC1B 4AD  
Attn TJ Oyler, Inquiry Secretary

26 June 2006

Dear Mr Oyler,

**IIED submission to the Competition Commission inquiry on the supply of groceries by retailers in the UK**

The International Institute for Environment and Development is an international policy research institute, working to promote more sustainable and equitable global development. Based in London, we are a non-governmental body, which works with an extensive network of colleagues and collaborators around the world. For over 30 years, we have analysed the position of smaller scale producers as the cornerstone of both broad-based, equitable economic development and the sound stewardship of natural resources.

From this standpoint, we are focussing our submission on three elements: (1) the impact of supply chain management and market structure on the overall working of the groceries market; (2) implications for producers in developing countries, and (3) need for modernisation of the Office of Fair Trading.

**1. The impact of supply chain management and market structure on the overall working of the groceries market**

You are aware from earlier inquiries that in the UK, supermarkets have implemented advanced supply chain management, characterised by long-term vertical coordination between producers, supplier-integrators, processors and retailers. The resulting closed supply chains have substantial barriers to entry, such as 'voluntary' standards, codes and benchmarks. Suppliers are faced with both the 'chain-insider' benefits and 'one buyer' risks. Farmers working outside these closed chains, such as those who do not have sufficient scale of production to be able to sell directly, can become relegated to the position of residual or top-up suppliers, or suppliers to the shrinking wholesale market. Farmers who supply wholesale markets, especially in marginal areas, are the most economically vulnerable sector.

With a large proportion of supply being traded through non-cash methods of trade, including contracts and marketing agreements, traditional cash markets are disappearing and there is no opportunity for price discovery. As price competition declines in importance and volume actually marketed declines, cash and wholesale

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IIED, 3 Endsleigh Street, London WC1H 0DD, UK. Tel: +44 (0)20 7388 2117; Fax: +44 (0)20 7388 2826, Email: [info@iied.org](mailto:info@iied.org) <http://www.iied.org/>  
IIED, 4 Hanover Street, Edinburgh EH2 2EN, UK. Tel: +44 (0)131 226 7040; Fax: +44 (0) 131 624 7050

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price data become increasingly suspect and represent the price of residual production which is surplus to supermarket quantity and quality requirements. Pricing becomes subject to manipulation, and hence its role in regulating the economy, by establishing equilibrium between supply and demand, is greatly weakened.

In other words vertical coordination can bring about a closing-off of market opportunities and becomes a barrier to pricing efficiency. 'Perfect competition' depends on a free flow of information among market participants, which does not correspond to the reality of buyer-driven chains. The potential anti-competitive outcomes of supply chain management have only recently begun to be explored.<sup>1</sup> There is a risk that farmer access to markets becomes so restricted that processors and retailers can reduce farm product prices even further,<sup>2</sup> in effect capping farm gate prices against target retail margins.

We are strongly of the opinion that the Competition Commission should include this perspective on the wider workings of concentrated grocery markets in the scope of the inquiry.

## **2. Impact on southern producers and farm labour**

"Making markets work for the poor" is key to the development policy of the UK and many other donor countries. Long-term business relationships with small enterprises in Africa are, as the Commission for Africa states "one of the most important ways in which larger companies can promote the participation of poor people in growth". Farmers in developing countries can escape the low and volatile prices of commodity markets by entering value-added sectors, such as export horticulture. The rapid rise in exports of horticultural produce from sub-Saharan African countries to UK supermarkets has been a development success story. But private sector standards for quality and food safety can, in the way in which they are measured and certified, be unnecessarily exclusionary.

The demands of private standards, and the cost-price squeeze of ever higher standards and ever lower prices, present a serious threat to (a) the continued participation of smallholders in these chains, and (b) the welfare of farm labourers, who feel the brunt of supermarket price wars. The banana price war, for example, has been described as a "perverse transfer of wealth, by some of the supermarkets, from farmers and farm workers of developing countries to the consumers of developed countries. This is anti-development and regressive"<sup>3</sup>.

The Inquiry would be well advised to include the position of developing country suppliers in its terms of reference.

## **3. Need for modernisation of the Office of Fair Trading**

In referring the grocery market to the Competition Commission, the OFT echoed the limited scope of earlier inquiries, concentrating on consumer choice ("product

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<sup>1</sup> Hildred W and Pinto J (2002) Impacts of supply chain management on competition. *Working Paper Series 02-10*, College of Business Administration, Northern Arizona University.

<sup>2</sup> Levins RA (2001). An Essay on Farm Income. Staff Paper P01-1, Department of Applied Economics, University of Minnesota April 2001.

<sup>3</sup> Interview with Bernard Cornibert, CEO of Windward Islands Banana Development and Exporting Company Limited, Eurofruit Magazines, April 2004

variety and choice of fascia”) rather than overall fairness and justice in trading relations. IIED is strongly of the opinion that the consumer welfare mandate of the OFT reflects an era which sees the problem in terms of powerful producers and manufacturers and atomised retailers. This is echoed in a response to a letter, by Bob MacDowall, OFT Markets and Policy Initiatives Division on 25 August 05, where he stated bluntly that “Our role is to make markets work well for consumers”. However, this is not the architecture of the retail sector we face today.

We hope that this Inquiry will at last recommend that the OFT’s mandate is modernised in line with the shift in market power downstream from producers, to recognise the issue of buyer power in its own right.<sup>4</sup>

Thank you for the opportunity to share these views with you.

With kind regards

Dr Camilla Toulmin  
Executive Director

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<sup>4</sup> See Tallontire A and Vorley B (2005). International Institute for Environment and Development Achieving fairness in trading between supermarkets and their agrifood supply chains. UK Food Group Briefing: [www.ukfg.org.uk](http://www.ukfg.org.uk)