

**REFERENCE RELATING TO THE COMPLETED ACQUISITION BY LONG CLAWSON DAIRY LIMITED OF MILLWAY, BEING THE STILTON AND SPECIALITY CHEESE BUSINESS OF DAIRY CREST GROUP PLC**

**Statement of issues**

**The reference**

1. Our terms of reference require us to consider the completed acquisition of Millway, being the Stilton and speciality cheese business of Dairy Crest Group plc (Millway) by Long Clawson Dairy Limited (Long Clawson). The inquiry group (the Group) must decide:
  - (a) whether a relevant merger situation has been created; and
  - (b) if so, whether the creation of that situation has resulted or may be expected to result in a substantial lessening of competition (SLC) within any market or markets in the UK.
2. To enable it to do this, the Group will consider the following issues.

**Market definition**

3. Long Clawson and Millway produce and sell cheese directly to retailers as well as to wholesalers for distribution to retailers. In addition, they sell white Stilton to blenders, who use it as an input into the production of blended cheeses, and they sell blue Stilton to food manufacturers as a flavouring. The Group will consider at which level(s) of the supply chain it is necessary to define an economic market(s) affected by the merger (the relevant market(s)). In defining the relevant market(s), the Group will take into account the feasibility of both supply- and demand-side substitution.
4. The Group will consider the appropriate definition of the product market affected by the merger and, in particular:

with regard to blue Stilton, whether:

  - (a) there is a separate product market for blue Stilton cheese; or
  - (b) the relevant market is wider than blue Stilton cheese and includes other types of blue cheese;

with regard to white Stilton, whether:

  - (a) there is a separate product market for white Stilton cheese; or
  - (b) the relevant market is wider than white Stilton cheese and includes other types of cheese used as a base for blended (speciality) cheeses;

with regard to blended cheese, whether:

  - (a) there is a separate market for blended cheese based on white Stilton cheese; or
  - (b) the relevant market includes other types of blended cheese; and

with regard to all cheese, whether:

(a) the relevant market includes all cheese.

5. The Group will also examine whether there are separate product markets for the supply of cheese to intermediary companies and the supply of cheese to retailers.
6. It will also consider the geographic extent of the relevant market(s).

### **Assessment of the competitive effects of the merger**

7. The Group will consider the possible competitive effects of the merger within each of the relevant markets it identifies, compared with the counterfactual situation (ie the situation that would have arisen in the short to medium term, had the merger not occurred).

### **Counterfactual**

8. To determine the appropriate counterfactual against which to assess the proposed merger, the Group will consider what is likely to have happened in the relevant market(s) in the absence of the merger, including whether the Millway Stilton and speciality cheese business would have:
  - (a) remained an independent and viable business, whether owned by Dairy Crest or by another company not already active in the relevant market(s);
  - (b) been purchased by a party already active in the relevant market(s) other than Long Clawson; or
  - (c) ceased trading, and, if so, what would have happened to its assets and customer relationships.

### **Theories of harm**

9. To focus analysis of the competitive effects of the merger, the Group has so far identified three possible ways in which the merger might result in an SLC, which it will investigate further. These theories of harm are not mutually exclusive, and their identification does not mean that the Group has reached any conclusions. The three theories of harm identified by the Group to date are:
  - (a) *Unilateral horizontal effects*. The Group will consider whether, as a result of the merger, the reduction in the number of cheese producers in the relevant market(s) has resulted in or might be expected to create or increase market power, leading to higher prices, and/or lower levels of service or innovation than would otherwise be the case.
  - (b) *Coordinated effects*. The Group will consider whether the merger has resulted in or may be expected to increase the likelihood of coordination between Long Clawson and other cheese producers in the relevant market(s) (for example, in relation to prices or customer allocations), leading to higher prices, lower levels of service, or less innovation than would otherwise be the case.
  - (c) *Partial or full input foreclosure*. The Group will consider whether the merger has resulted in or might be expected to increase the ability and incentive for Long Clawson to foreclose the supply of white Stilton to other cheese producers,

resulting in fewer producers being active in the relevant market and higher prices, lower levels of service, or less innovation than would otherwise be the case.

10. The identification of these theories of harm does not preclude an SLC being identified on another basis following further work by us or the receipt of additional evidence.

### **Related competition issues**

11. Among the issues the Group will consider when deciding whether any of the theories of harm set out above are likely to be realized (and whether the merger has resulted in or may be expected to result in an SLC in any relevant market compared with the counterfactual situation) are:

(a) the extent of competition between Millway and Long Clawson before the merger;

(b) the ability and incentive of other existing or potential competitors to undermine any price increases or reductions in service levels by Long Clawson following the merger;

(c) the extent of barriers to entry or expansion in the relevant market(s);

(d) customer-related matters such as:

(i) the ease with which customers can switch between producers of cheese in the relevant market(s);

(ii) how prices paid by customers are determined;

(iii) the relative importance to customers of price and non-price factors (such as product specification, reliability and speed of supply); and

(iv) the extent of buyer power in the relevant market(s);

(e) the effect of any capacity constraints in Stilton production, packaging or distribution;

(f) factors relating to the likelihood of coordination following the merger such as:

(i) the degree of concentration in the relevant market(s) and companies' awareness of their competitors' behaviour;

(ii) the cost to companies of deviating from any prevailing coordinated behaviour; and

(iii) the strength of competitive constraints in the market.

### **Possible remedies and relevant customer benefits**

12. Should the Group conclude that the completed merger has resulted or may result in an SLC, it will consider whether and, if so, what remedies might be appropriate, and will issue a further statement.

13. In any consideration of possible remedies, the Group will take into account whether any relevant customer benefits<sup>1</sup> might be expected to arise as a result of the merger and, if so, what these benefits are likely to be and which customers would benefit.

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<sup>1</sup>'Relevant customer benefits' are defined in section 30(1) of the Enterprise Act 2002.