

Competitive effects in the liquid egg market

Introduction

1. In Appendix D we defined the following relevant markets:
 - (a) the supply of free-range liquid eggs to customers in the UK for whom imports represent a poor substitute.
 - (b) the supply of intensive liquid eggs to customers in the UK for whom imports represent a poor substitute.
2. The CC considered that there may be insufficient marginal customers to warrant a wider product market definition which includes powdered eggs or a wider geographic market definition to include northern Europe.
3. In any event, as discussed in Appendix D, the parties negotiate prices individually with their customers, and have knowledge of which customers are willing to source from outside the UK. In addition, we were told that pasteurised liquid eggs had a very short shelf life, which would limit customers' opportunities for arbitrage.¹ It would therefore be possible for Noble foods to price discriminate between marginal and infra-marginal customers.

Market shares

4. Industry statistics do not allow for the production of market share estimates separately for free range liquid eggs and for intensive liquid eggs.
5. The parties provided a number of estimates of their market shares based upon various definitions of the relevant market. The parties told us that, based on a

¹We were told by Northern Foods that the shelf life of pasteurised liquid egg was nine to twelve days.

market definition which includes supplies of liquid eggs from northern continental Europe their shares of supply would equal [X] per cent for Deans and [X] per cent for Stonegate, giving a combined share of supply of [X] per cent.² The parties also estimated that a UK market which included the liquid equivalent of powdered egg imports would result in market shares of [X] per cent for Deans and [X] per cent for Stonegate respectively. This would result in a combined market share of [X] per cent.

6. However, for the reasons noted in Appendix D, the CC has defined the appropriate markets as the supply of free range liquid eggs to customers within the UK for whom imports represent a poor substitute and the supply of intensive liquid eggs to customers within the UK for whom imports provide a poor substitute.

7. The CC's own estimates of market shares, and the shares of supply outlined in the parties' own internal documents result in market shares higher than those provided by the parties. CC estimates of the parties' market shares, based on information provided by the parties are listed in Table 1 below.³

²These estimates are based on 2004 production figures for the UK, Germany, the Netherlands and France

³We note that the parties' estimates of their production of liquid egg in 2005 in their internal documents provided at Table 2 vary from those provided at 4.11 of their submission. The parties also submitted information on the 18 October which estimated their total production of liquid egg for 2005 to be [X] tonnes for Deans and [X] tonnes for Stonegate respectively.

TABLE 1 **Market shares of liquid egg supply in the UK (2005)**

<i>Company</i>	<i>Current production tonnes/year</i>	<i>Market share %</i>
✂		

Source: CC study from information supplied by the parties.

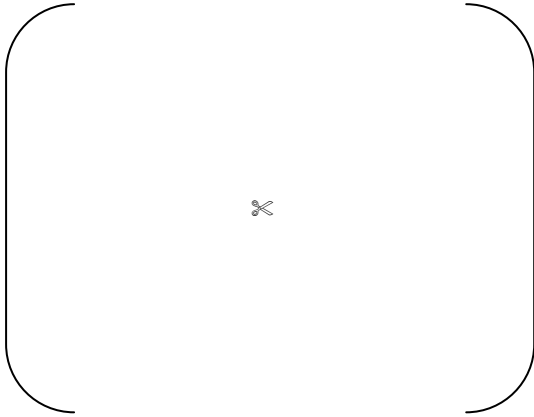
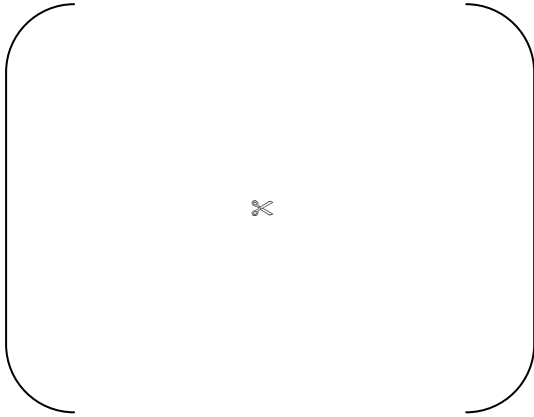
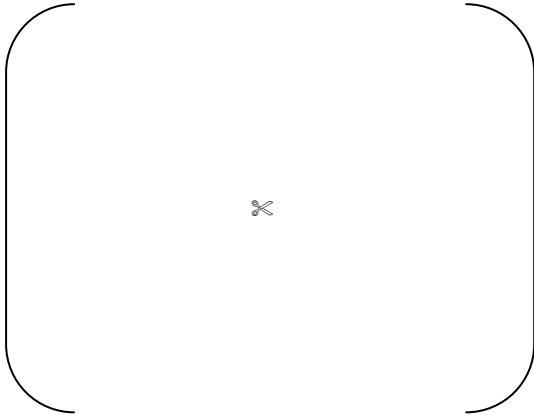
*Source: Main submission 4.11.

†Source: Main submission 3.21.

8. We note that, there are a number of inconsistencies in the information provided by the parties' on which Table 1 is based.⁴ We therefore consider the parties' estimates of their market shares in Table 2 below, based on their internal documents, to be more reliable.

⁴[✂]

TABLE 2 Market shares of liquid egg supply in the UK (2005)

Company	Current production (tonnes/week)	Current Production (tonnes/year)	Market Share (%)
Deans			
Stonegate			
Combined			
Manton			
Framptons			
Freshfayre (Oaklands)			
Bumble Hole			
Nive (Holland)			
D Wise			
Eipro			
Lowrie foods			
Parker foods			
Total			
HHI pre merger			
HHI post merger			
Increment			

Source: The parties' internal documents. [REDACTED]

9. However, even using the parties' preferred methodology, based upon the market definition outlined above, the parties' post merger share of supply is high and the increment to that share of supply is significant. In addition, the next largest competitors to the merged entity, Manton Coldstorage Ltd (Manton) and Framptons would be less than [REDACTED].

10. [REDACTED]

11. In addition the market shares included in Table 2 include importers, who would not represent a viable alternative for those customers who would be unwilling or unable to source from a supplier outside the UK. The choice of available suppliers for these customers is likely to be smaller.

12. Relatively few of the parties' liquid egg competitors listed in Table 2 supply significant volumes of free-range liquid eggs. Deans's own assessment of its competitors' strengths and weaknesses shows that the remaining alternative suppliers are relatively weak in the supply of free-range liquid eggs.

13. Deans's internal documents note that of the competitors listed in Table 2 only [REDACTED] are listed as having 'free range supply' as a strength.⁵ [REDACTED] is listed as having 'no UK free-range', [REDACTED] is listed as having 'limited free-range', [REDACTED] 'no free-range' and [REDACTED] 'limited free range'.
14. As a result of their competitors' limited free-range supplies, we consider that were market shares available for free-range liquid eggs separately, the parties' market shares would be considerably higher than shown in Table 2 above.
15. Finally, the parties' internal documents note that [REDACTED].⁶ The competitive constraint imposed upon the parties by smaller suppliers may also be further limited by their relative lack of vertical integration.

Switching

16. The parties do not consider themselves to be close competitors in the supply of liquid eggs.⁷ [REDACTED]
17. This argument is supported by the switching data provided by the parties. The parties' switching data (see Annex 1) shows that although there is [REDACTED]
18. However, the parties' switching data shows that switching suppliers is relatively infrequent. Switching to or from Deans appears to have occurred on only [REDACTED] occasions since 2002 and switching to or from Stonegate appears to have occurred on only [REDACTED] occasions since 2001. In addition, despite an apparently high degree of switching to suppliers outside the UK, these suppliers still supply very small volumes of liquid eggs to the UK compared to the volumes of Deans and Stonegate.

⁵Note however that suppliers outside the UK, such as [REDACTED] are outside our market definition.

⁶Source: Parties' presentation to the banks.

⁷Main submission, paragraph 5.66.

19. Finally, as discussed in Appendix D, there are a large number of customers for whom suppliers outside the UK are unlikely to provide a viable alternative. The ability of some customers to switch to suppliers outside the UK would not, given the parties' ability to price discriminate, protect these customers from an increase in price.

Capacity

20. The parties stated that there was abundant spare processing capacity, even within the UK. The parties estimated that a large number of their competitors in the UK had sufficient capacity to increase their output significantly.

TABLE 3 The parties' estimates of current output and capacity

<i>Competitor</i>	<i>Current production tonnes/week</i>	<i>Estimated spare capacity tonnes/week</i>	<i>Total capacity</i>
Framptons*	())	()
Manton			
Freshfayre			
Bumble Hole			
D.Wise			
Lourie			
Parker Foods			
Oaklands			
McEwan			
Total			

Source: The parties.

*[REDACTED]

21. However, it would appear that the ability of the parties' competitors to expand is more limited than processing capacities alone would indicate. The parties' remaining competitors rely on the spot market to source their raw eggs for breaking, particularly to source free-range shell eggs for breaking.

22. Northern Foods (the parties' largest customer) told us that food manufacturers needed to be confident that a supplier could meet their needs, as supply outages were very costly, and because it was difficult to store liquid eggs.⁸

⁸Source: Transcript of hearing with Northern Foods.

23. [REDACTED]⁹
24. [REDACTED]¹⁰
25. For one competitor, [REDACTED], Deans noted that ‘raw material supply’ was a strength. However, a key weakness listed for [REDACTED] was its ‘limited free-range’.
26. Eipro, a key continental competitor, appears to have free range egg supply, [REDACTED]. However, [REDACTED].
27. In addition, the parties’ competitors are particularly constrained in their ability to source free range eggs for breaking. [REDACTED]

Entry and expansion

28. The parties claimed that entry into liquid egg production was relatively easy. They also cited a number of recent entrants including Just Egg (Chilled Foods) Ltd (Just Egg), Oaklands, and Manton.
29. However Oaklands, a recent entrant, told us that it had set up its processing plant in the wake of the avian flu crisis in 2003, [REDACTED].¹¹ The parties’ internal documents also indicate that the avian flu crisis caused an unprecedentedly high level of egg prices followed by a protracted downturn. This may have been a reason for the relatively large number of recent entrants.¹²
30. This would seem to indicate that although entry is possible, we would not expect large scale entry in the event of (for example) a 5 per cent increase in price.

⁹[REDACTED]

¹⁰Response to market questionnaire question 79.

¹¹[REDACTED]

¹²Source: Deans Egg Products business plan June 2005.

31. In any event, any new entrant would appear to be constrained by the availability of eggs for breaking as discussed above. A key barrier to entry and expansion would appear to be that incumbent suppliers with their own shell eggs (in house or contracted) production enjoy economies of scope as their shell egg division provides a stable source of second quality eggs for breaking.
32. The parties told us that their competitors are not reliant on the spot market to source eggs for breaking. They said that Deans does not rely heavily on internal production or contracted producers to source raw material for liquid eggs. [REDACTED]
33. The parties also told us that its major international competitors do not have their own internal egg production and do not experience problems gaining access to raw material. They also said that one of their competitors in the UK, Oaklands, has an internal supply of cage eggs, and that there are a number of uncontracted UK suppliers who produce seconds which will be available to competitors. The parties also said that their competitors can import shell eggs for breaking. They noted that there was an internet association called Ex-Trade based in Denmark for the placement of eggs for breaking across Europe and that Bumble Hole, Parker Foods Ltd (Parker) and D Wise were members.
34. However, the parties' arguments are contradicted by their own internal documents which note [REDACTED] (see paragraph 15) and the fact that, until recently, Deans sourced [REDACTED] of its eggs for breaking in-house. Deans's internal documents note that the vast majority of their inputs of raw material for breaking are sourced internally. [REDACTED]¹³
35. The parties told us that the comments in their internal documents reflected a perception that customers considered the traceability of the raw eggs to be of the

¹³Source: [REDACTED]

highest priority and a decisive factor in the choice of supplier. The parties stated that subsequent research through discussions with customers had led Deans to conclude that this strategy was flawed.

36. Responses from customers however, support the contention that for some customers at least, traceability of the raw eggs used to produce liquid eggs is of a high priority. For example [X] told us that “the demands of the UK retailers are very exacting and smaller UK based suppliers still have some way to go before they reach the level whereby they would readily meet current standards for quality, reliability, security of supply and economies of scale that would allow them to compete on all fronts.”

Bargaining power

37. The parties have not made the argument that their liquid egg customers enjoy buyer power. We have no evidence that they do or would enjoy buyer power. Consequently this area is not discussed further.

Unilateral effects

38. The merger between Deans and Stonegate appears to remove an important competitive force. The merger results in a large combined market share, with a significant increment. After Deans, Stonegate was the next largest supplier of liquid eggs, and therefore was likely to have been a significant competitor. The parties' remaining competitors are relatively small, and the competitive constraint that they impose is limited due to security of supply problems, as they appear to rely on spot purchases of eggs to break to a greater extent than the parties. In addition, very few of the parties' competitors appear to have a consistent supply of free range eggs.
39. Given the available evidence, it does not seem likely, that the threat of new entry or expansion is sufficient to offset the reduction in rivalry as a result of the merger.

40. A number of customers, particularly some larger customers such as Alembic, [REDACTED] and [REDACTED] may be able to resist any post merger price rise or other anticompetitive effects through their ability to source liquid eggs outside the UK. However, a large number of customers would not appear to have this ability and would be vulnerable to a price rise as a result of the merger.

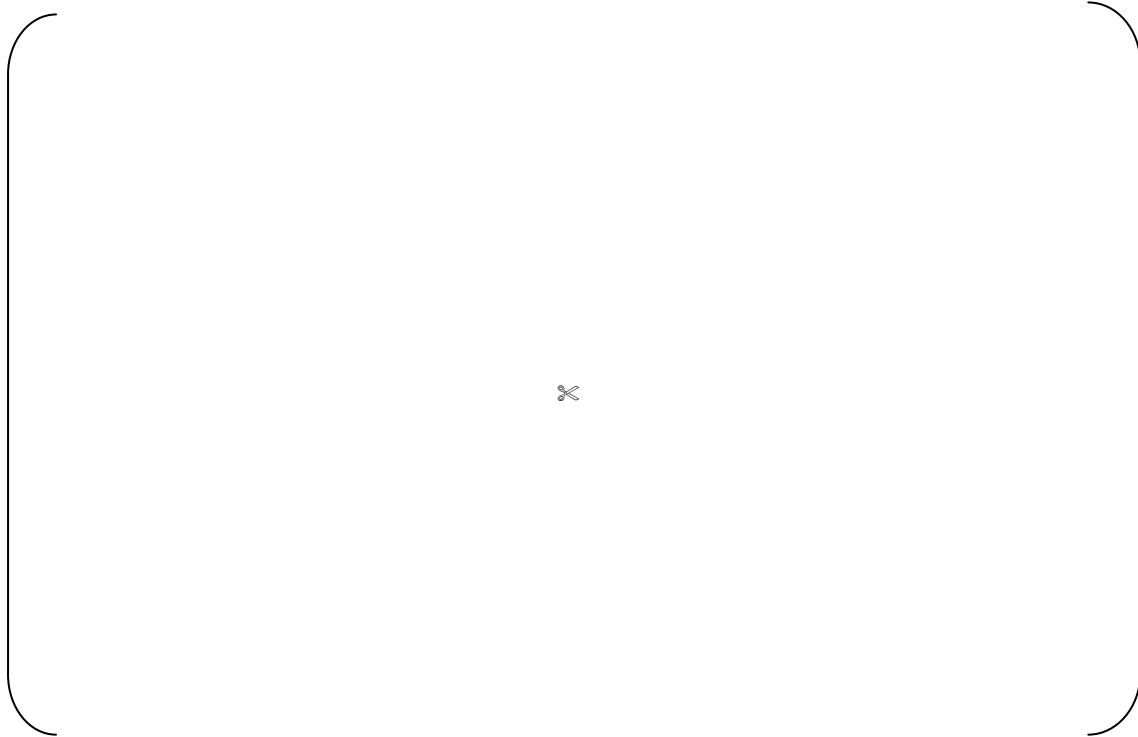
The parties' switching data

TABLE 1 Business won and lost: processed egg products (Stonegate)



Source: The parties.

TABLE 2 **Business won and lost: processed egg products (Deans)**



Source: Deans.
