

Domestic electrical goods: I

A report on the supply in the UK of televisions, video cassette recorders, hi-fi systems and camcorders

Volume I: Summary and Conclusions



MONOPOLIES AND MERGERS COMMISSION

Domestic electrical goods: I

A report on the supply in the UK of televisions,
video cassette recorders, hi-fi systems and
camcorders

Volume I: Summary and Conclusions

**Presented to Parliament by the Secretary of State for Trade
and Industry by Command of Her Majesty
July 1997**

Members of the Monopolies and Mergers Commission as at 30 April 1997

Sir Graeme Odgers (*Chairman*)
Mr P H Dean CBE (*Deputy Chairman*)
Mr D G Goyder CBE (*Deputy Chairman*)
Dr D J Morris (*Deputy Chairman*)
Professor J Beatson
Professor M Cave
Mr A T Clothier
Mr P G Corbett CBE
Mr R H F Croft CB¹
Mr R O Davies
Professor S Eilon¹
Mr J Evans CBE
Mr N H Finney OBE¹
Sir Archibald Forster
Sir Ronald Halstead CBE
Mr D B Hammond¹
Miss J C Hanratty
Ms P A Hodgson CBE
Mr D J Jenkins MBE
Mrs D P B Kingsmill
Mr H H Liesner CB¹
Mr R Lyons
Mr P Mackay CB
Mr N F Matthews
Professor J S Metcalfe CBE
Mrs K M H Mortimer
Mr R J Munson
Professor D M G Newbery
Dr G F Owen
Professor J F Pickering¹
Mr M R Prosser
Professor J A Rees
Mr T S Richmond
Dr A Robinson
Mr J K Roe
Dr L M Rouse
Mr C R Smallwood
Mr G H Stacy CBE
Mrs E C Tritton QC¹

Miss P A Boys (*Secretary*)

¹These members formed the Group which was responsible for this report under the chairmanship of Mr H H Liesner.

Note by the Department of Trade and Industry

In accordance with section 83(3) and (3A) of the Fair Trading Act 1973, the Secretary of State has excluded from the copies of the report, as laid before Parliament and as published, certain matters, publication of which appears to the Secretary of State to be against the public interest, or which she considers would not be in the public interest to disclose and which, in her opinion, would seriously and prejudicially affect certain interests. The omissions are indicated by a note in the text.

Contents

	<i>Page</i>
<i>Chapter</i> 1	Summary 1
2	Conclusions: Televisions 7
	List of signatories: Televisions 90
3	Conclusions: Video cassette recorders 91
	List of signatories: Video cassette recorders 171
4	Conclusions: Hi-fi systems 172
	List of signatories: Hi-fi systems 254
5	Conclusions: Camcorders 255
	List of signatories: Camcorders 333
<i>Appendices</i>	(The numbering of the appendices indicates the chapters to which they relate.)
2.1	Suppliers which recommend or suggest television retail prices 334
2.2	Suppliers which engage in selective distribution of televisions 335
3.1	Suppliers which recommend or suggest VCR retail prices 336
3.2	Suppliers which engage in selective distribution of VCRs 337
4.1	Suppliers which recommend or suggest hi-fi system retail prices 338
4.2	Suppliers which engage in selective distribution of hi-fi systems 339
5.1	Suppliers which recommend or suggest camcorder retail prices 340
5.2	Suppliers which engage in selective distribution of camcorders 341
	Glossary 342

1 Summary

1.1. On 27 April 1995 the Director General of Fair Trading (DGFT) asked us to investigate whether a monopoly situation exists in the UK in relation to the supply (other than by retail sale or hire) of televisions and, if so, to determine whether practices relating to two matters:

- (a) steps taken, by recommending or suggesting prices to be charged by dealers, or otherwise, to influence the prices at which dealers resell televisions; and
- (b) withholding supplies of televisions from dealers;

operate or may be expected to operate against the public interest. In addition the DGFT referred to us, in similar terms, the supply of three other 'brown' goods, video cassette recorders (VCRs), hi-fi systems and camcorders which are also the subject of this report, and four 'white' goods which are the subject of a separate report. The full terms of reference for the four reference brown goods are at Appendix 6.1.

1.2. Our separate conclusions on each of the four reference brown goods are set out in Chapters 2 to 5 respectively. This summary deals with all four, noting any relevant and significant differences between them.

The markets

1.3. Relevant statistics about the markets for each of the reference brown goods are given in Table 1.1.

TABLE 1.1 **Markets for reference brown goods in 1995**

	<i>Televisions</i>	<i>VCRs</i>	<i>Hi-fi systems</i>	<i>Camcorders</i>
Total value of UK retail sales (£m)	931	611	522	204
Average unit value (to nearest £10)	310	270	260	590
Percentage of households with these goods, 1995/96	98	79	60	10
Number of suppliers with market share of 1% or over	14	15	13	8
				<i>per cent</i>
Market share of Sony Corporation	15.9	10.6	33.1	24.6
Market share of Matsushita	14.4	20.8	17.9	27.1
Aggregate market share of top four suppliers	52.6	45.6	65.2	81.4
Retail market share of Dixons	20.9	22.4	22.6	34.5
Retail market share of Comet	10.6	9.3	11.5	8.4
Retail market share of RECs*	10.4	10.7	14.5	9.8

Source: MMC, based on data from GfK Marketing Services Ltd (GfK), multiple retailers, Office for National Statistics and Market Assessment Publications Ltd.

*For convenience we use the acronym 'RECs' to refer collectively to electrical goods retailing operations which were owned, for most of our inquiry, by one or more of the English and Welsh regional companies, the two Scottish electricity companies and Northern Ireland Electricity, and to Powerhouse, Powerstore and Homepower which bought retailing businesses from regional electricity companies.

1.4. In 1995 the two leading suppliers of each of the four reference brown goods were the Sony Corporation of Japan (Sony Corporation), which owns Sony United Kingdom Limited (Sony) and is the majority shareholder of the Japanese parent of Aiwa (UK) Ltd (Aiwa), and Matsushita Electric Industrial Co Ltd (Matsushita), which owns Panasonic UK Ltd (Panasonic) and is the majority shareholder of the Japanese parent of JVC (UK) Limited (JVC). We were told that Sony and Aiwa operated wholly independently of each other in the UK, as did Panasonic and JVC.

1.5. The most important retail channels for each of the reference brown goods in 1995 were Dixons Group plc (Dixons) and Comet Group plc (Comet). Wholesalers play only a minor part in these markets. The only important retailer buying group is Combined Independents (Holdings) Ltd (CIH).

1.6. It was put to us that each of the markets for the reference brown goods is highly competitive at both the supply and the retail levels. In support of this claim it was argued that prices for these goods were highly visible and consumers shopped around; there were no substantial barriers to entry; the profitability of suppliers and retailers was low; there was continuing downward pressure on prices which had fallen in real terms in recent years; and prices for the goods in the UK were below those in other European countries.

1.7. We have reservations about these arguments. We saw evidence to suggest that many consumers did not engage in substantial search activity, and that brand loyalty was strong. The transparency of the market for consumers is limited by different retailers stocking different models from the extensive ranges of the main suppliers; by the difficulty of establishing objectively the relative performance and reliability of different models; and by the widespread use of non-price offers which are hard to evaluate.

1.8. The brand strength of the incumbent major suppliers will constrain the ability of a new entrant supplier to achieve a substantial market share. On the retail side, small retailers' growth may be held back by problems of procuring the reference brown goods as cheaply as larger, better-established competitors.

1.9. We received limited evidence about profitability, and that which we did examine was inconclusive. Moreover we decided that the level of profit of suppliers and retailers did not bear to a material extent on the matters referred to us.

1.10. We accept that the real price of each of the reference brown goods has declined in recent years, but we think this reflects improvements in manufacturing efficiency generally rather than a highly competitive market in the UK. For several detailed reasons we think the evidence about international price comparisons is inconclusive and of little relevance to the matters we have investigated.

Evidence on prices

1.11. We obtained evidence about pricing practices from a range of sources including suppliers and retailers, large and small. We carried out an analysis of retail prices. For all the reference brown goods we found that:

- (a) larger suppliers sought the views of major retailers about the retail prices that their goods were likely to fetch;
- (b) nearly all suppliers (but not Aiwa, from 1 April 1997) informed dealers of a recommended or suggested retail price (RRP);
- (c) most retailers took account of RRPs in setting their own prices, but of those who said that they did not do so, for example Dixons, most agreed that their prices often coincided with RRPs;
- (d) retailers frequently complained to suppliers about price cutting by their competitors;
- (e) suppliers sometimes contacted dealers who sold at discounted prices; suppliers denied that their

intention was to influence retail prices but we identified several cases where, in our view, suppliers had discouraged discounting;

- (f) most suppliers started from the RRP when negotiating a dealer's net buying price, and this established the dealer's gross margin when the goods were sold at the RRP; if the supplier subsequently reduced the RRP, it normally also reduced the dealer's net buying price so that the agreed margin was broadly maintained;
- (g) some of the discounts (for example, advertising and promotional allowances) offered by suppliers were paid at the discretion of the supplier, or retrospectively, or both, giving the supplier the means of influencing retailer behaviour;
- (h) retail prices tended to be at or close to the RRP; and
- (i) most suppliers provided mail order companies with suggested catalogue prices that were higher than RRP; over 80 per cent by value of mail order sales of each of the reference brown goods were at these suggested prices in 1995.

Evidence on withholding supply

1.12. We defined a selective distribution system as one under which a supplier selects dealers to be supplied by taking account of criteria that it deems appropriate. Nearly all the larger suppliers of the reference brown goods had such distribution systems. The supply criteria which many took into account included the provision of pre- and post-sales service. These criteria were often used as grounds for refusing to supply warehouse clubs. Another common selection criterion was whether the locality was already adequately supplied with the products of the supplier in question. This criterion had frequently been used as a reason to withhold supply.

1.13. CIH supplied only those retailers who were members of its local groups (which own it). Local groups would admit as members only those retailers who could submit audited accounts for a period of three years. Some required new members to be acceptable to existing members.

Monopoly situations

1.14. We find that there are two complex monopoly situations for each reference brown good.

1.15. The first complex monopoly situation involves all suppliers who suggest or recommend retail prices; for each of the reference brown goods, the suppliers concerned supply more than one-quarter by value of those goods supplied in the UK. It also involves all retailers who take account of RRP in setting their own retail prices, or take part in discussions with suppliers which influence the RRP suggested by those suppliers, or both. Such conduct and the influence that, in our view, RRP have on transaction prices have the effect of restricting or distorting competition in the supply of each of the reference brown goods in the UK. For each reference brown good this complex monopoly situation exists in favour of the suppliers and retailers referred to in this paragraph.

1.16. The second complex monopoly situation involves all suppliers who select dealers to be supplied with the reference brown goods on the basis of certain criteria and refuse to supply dealers who are not selected. For each reference brown good the suppliers concerned supply more than one-quarter by value of those goods supplied in the UK. For each reference brown good this second complex monopoly situation exists in favour of the suppliers referred to in this paragraph and of dealers selected to receive supply from those suppliers.

1.17. In 1995, supply by Sony Corporation to the UK hi-fi market and supply by Matsushita to the UK camcorder market each exceeded one-quarter of the total market for each of those goods, and more than one-quarter of the camcorders sold in the UK were supplied to Dixons. Three 'scale' monopoly situations therefore exist, one in favour of Sony Corporation, Sony and Aiwa, one in favour of

Matsushita, Panasonic and JVC and one in favour of Dixons.

Public interest findings on prices

1.18. Many suppliers and retailers argued that the clustering of transaction prices we observed was not associated with the use of RRPs and that, to the extent that transaction prices and RRPs coincided, it was because RRPs followed these prices. We are not persuaded by these arguments. Our analysis indicates that there is an association between RRPs and transaction prices. Given the evidence we received about suppliers' and retailers' practices, we believe that the most convincing explanation of this association is that transaction prices are influenced by RRPs.

1.19. The influence of RRPs on retail prices results from the strength of the relationship between suppliers and retailers. Aspects of this relationship include a shared antipathy to unrestrained price competition (often expressed as a preference for 'orderly markets'): an antipathy associated with an emphasis on non-price offers and reinforced by the steps taken by some suppliers to encourage adherence to RRPs; and the pervasive use by suppliers of RRPs to determine dealers' buying prices, coupled with discretionary and retrospective discounts.

1.20. We conclude that the following actions are steps taken by at least some suppliers to influence the prices at which dealers resell each of the reference brown goods which operate or may be expected to operate against the public interest:

- (a) the setting of RRPs;
- (b) reducing or threatening to reduce discounts to dealers who advertise or display prices regarded by the supplier as substantially below the RRP;
- (c) making support for dealer advertising costs conditional upon the advertisement not quoting prices below those approved by the supplier;
- (d) contacting dealers who advertise prices considered by the supplier or other dealers or both to be too low;
- (e) providing point-of-sale material that includes the display of RRPs;
- (f) not permitting 'price on application' advertising; and
- (g) suggesting catalogue prices to mail order companies.

1.21. In addition we found that certain actions undertaken by one supplier, Sony, and two retailers, Dixons and Empire Stores Group plc (Empire), operated or may be expected to operate against the public interest.

1.22. The adverse effects of the actions set out in paragraphs 1.20 and 1.21 are to cause retail prices to be higher than they otherwise would be; to reduce the choice for consumers between lower prices/fewer non-price benefits on the one hand and higher prices/more non-price benefits on the other; and to discourage innovation in retailing.

Public interest findings on withholding supply

1.23. Suppliers who had refused to supply warehouse clubs generally told us that they were not satisfied with the clubs' pre- and post-sales service. However, we noted that such suppliers sold the reference brown goods to mail order companies whose level of pre-sales service was not significantly different from that of warehouse clubs. Other evidence, such as the payment by suppliers of sales incentives to retailers' staff, also made us doubt the validity of this reason for refusing to supply warehouse clubs. We found that the post-sales service offered by warehouse clubs was not necessarily less satisfactory than that offered by high street retailers. More generally, we believe that consumers should be able to choose how much pre- and post-sales service they obtain.

1.24. We conclude that the withholding of supply of the reference brown goods from warehouse clubs by suppliers represents a discriminatory application of the criteria which suppliers use to select dealers for supply, and operates or may be expected to operate against the public interest. The adverse effects are the restriction of entry to the retail market, a loss of choice for consumers, higher retail prices than would otherwise be the case, and the discouragement of retail innovation.

1.25. We also conclude that, in the context of the following actions by CIH's local groups, the withholding of supply by CIH to non-members of local groups operates or may be expected to operate against the public interest by preventing some retailers from taking advantage of CIH's purchasing power and thus restricting entry into retailing:

- (a) the requirement by local groups that prospective new members must submit audited accounts for three years; and
- (b) the requirement by some local groups that new members be acceptable to existing members.

1.26. In addition, recommendations by CIH that retailers should not resell goods bought from CIH to dealers who are not members of CIH's local groups operate or may be expected to operate against the public interest.

Recommendations on prices

1.27. We believe that the use of RRP's is so entrenched in the way business is conducted in the UK reference brown goods markets that nothing short of their prohibition would deal effectively with the adverse effects we have found. We therefore recommend that:

- (a) suppliers should be prohibited from publishing, or otherwise notifying to dealers, the prices that suppliers recommend or suggest that dealers advertise, display or charge when they seek to resell the reference brown goods;
- (b) suppliers should be prohibited from taking any action to compel or influence dealers to resell the reference brown goods at prices higher than those decided on by the dealers; and
- (c) dealers should be prohibited from taking steps to persuade suppliers to:
 - (i) suggest or recommend prices at which dealers should resell the reference brown goods; and
 - (ii) encourage or influence other dealers to resell the reference brown goods at prices different from those at which the other dealers themselves wish to resell.

1.28. We also recommend the prohibition of certain other practices which influence dealers to adhere to RRP's, and the introduction of a requirement for suppliers to send compliance statements to the DGFT.

1.29. Some of our recommendations cover similar ground to certain provisions of the Resale Prices Act 1976 (RPA) but we were told by the Office of Fair Trading (OFT) that shortcomings in the RPA made it difficult to enforce. Our recommendations would remedy some of these shortcomings in relation

to the reference brown goods.

Recommendations on withholding supply

1.30. We recommend that suppliers should be prohibited from applying the criteria they use to select dealers to receive supply in a manner which discriminates against particular dealers or categories of dealers; that suppliers should be required to notify would-be dealers in writing of the criteria they use to select dealers; and that any dealer who is refused supply should be given a written statement of the reasons for refusal by the supplier concerned.

1.31. These recommendations might not prevent a supplier, determined to withhold supply from warehouse clubs, devising selection criteria specifically designed to exclude this type of dealer. To prevent this, we further recommend that suppliers should be required to supply all creditworthy warehouse clubs which request supply, on terms which are not less favourable than those on which other dealers in similar circumstances are supplied, unless the supplier concerned can satisfy the DGFT that the criteria used to refuse supply do not have as their object or effect the prevention, restriction or distortion of competition and that these criteria have been applied in a non-discriminatory manner.

1.32. We further recommend that suppliers should be prohibited from withholding supply from retailers of the reference brown goods on the grounds that the locality is already supplied.

1.33. We consulted the European Commission about our recommendations, in view of its responsibilities under Article 85 of the EC Treaty. It told us that there was no general objection arising from EC law to our making these recommendations.

1.34. In addition to these general recommendations, we recommend that CIH's local groups should be prohibited from refusing membership to any retailer who applies for it and who can demonstrate the ability to pay for any reference brown goods he may order; and that CIH should give undertakings that it would not in future make any recommendations restricting the resale of such goods purchased from it.

1.35. We see our recommendations on RRP's and on withholding supply as complementing each other, so that together they reduce suppliers' influence on retail prices.