

**Report under section 125(4) of the Fair Trading Act 1973 of the
Director General of Fair Trading to the Secretary of State for
Trade and Industry under section 76 of the Fair Trading Act**

1 September 2000

Acquisition by Interbrew SA of assets of Bass Plc, namely Bass Holdings Limited

Assessment

This is a completed transaction involving the acquisition by Interbrew SA of the UK brewing interests of Bass plc, namely Bass Holdings Limited (BHL). Interbrew also acquired certain Bass interests outside the UK but these aspects of the merger, together with the supply of flavoured alcoholic beverages (FABs) in the UK, have already been dealt with by the European Commission. Prior to acquiring BHL, Interbrew had acquired the UK brewing interests of Whitbread plc (the Whitbread Beer Company (WBC)). The current merger therefore brings together two of the four major national beer brewers and distributors in the UK.

Jurisdiction

This merger originally fell within the ambit of the European Community Merger Regulation but the UK elements of the transaction (excluding the supply of FABs) were repatriated to the UK authorities on 22 August. The merger satisfies both the assets test and the share of supply test in the Fair Trading Act.

Relevant markets

Interbrew contended that the relevant markets were: the production of beer for supply to the on-trade in the UK; and the production of beer for supply to the off-trade in the UK. In previous cases it has been suggested that this wider product market might be segmented both by type of beer—ale, lager and stout—and between the ‘standard’ and ‘premium’ categories. In support of these narrower market definitions, third parties have pointed to: the difficulties of switching production at the brewing level; the tendency of brewers to promote their brands against such type and category definitions; the lack of substitutability of a lager brand for an unavailable ale brand at the retail level; and the price premium at both the wholesale and the retail levels for ‘premium’ types of lager and ale. However, market shares are high, whether one considers the broad or narrow markets and I do not consider it is necessary to reach a firm conclusion either way.

In considering the geographic market, some third parties have argued that certain features of the on-trade in Northern Ireland and, to a lesser extent, Scotland suggest that they should be considered as distinct markets. Prior to this merger, Interbrew had no representation in Northern Ireland and little in Scotland. However, reaching a view on these matters is not crucial to this initial assessment of the effect of the merger on competition in the UK beer market. (There is, however, one potential issue arising out of the distribution of beer in Scotland that I touch upon below.) There is general agreement that supply to the on-trade should be considered separately from supply to the off-trade.

Horizontal issues

The parties are two of the four major national brewers and distributors of beer in the UK. At the brewing level, the merger gives Interbrew a market share of some [details omitted] % (increment [details omitted] %)—if the production of the Heineken and Murphy’s brands are attributed to Interbrew—[details omitted] % if they are excluded. This share of supply would make Interbrew the market leader ahead of

Scottish & Newcastle (S&N), at [details omitted] %, and considerably ahead of Carlsberg-Tetley (C-T), at [details omitted] %. The two market leaders would have around [details omitted] % of the brewing market.

At the distribution level, the parties' share of supply is likely to be higher, since they also wholesale beer brewed by others. Prior to its acquisition by Interbrew, WBC sub-contracted the distribution of its beers in Scotland to S&N, which would reduce its share of the distribution market. However, now that Interbrew will have access to the distribution network of BHL it might be expected to take this business in-house. Various estimates put Interbrew's share of distribution at above [details omitted] %, with it and S&N together accounting for between [details omitted] % of the market.

The merger would, thus, significantly increase the level of concentration within both the markets for brewing and distribution and may isolate and weaken C-T as a potential third force. Interbrew has pointed out that its share of supply might be expected to fall when the transitional Heineken & Murphy's arrangements come to an end. These arrangements have, however, several years before they completely unwind and Interbrew can, in any case, be expected to seek to substitute another standard lager from within its portfolio. Interbrew also contends that the pub groups will continue to exercise considerable buyer power. The major pub groups undoubtedly have some buyer power but no group has more than about 8.5% of the pub market and substantially less (<3%) in terms of beer supply, which indicates that this power is not great. It seems to me insufficient to act as an effective constraint to the market power that Interbrew will gain as a result of this merger.

Vertical issues

There appear to be two potential vertical issues arising out of the merger. These are: the broad range of major brands which Interbrew will control as a brewer, with the risk that it may be able to foreclose the market to other brewers at the distribution level; and the collective benefits it will have, as a brewer/distributor, as a result of the beer supply agreements with Whitbread and BLR. Third parties have indicated that one of the features of the current market structure has been that no brewer controlled a complete range of the major brands across product types. This provided market entry opportunities for other brewers and provided additional choices for pub tenants since a brewer without, for example, a premium lager product, then had a vested interest, as a distributor, in providing its customers with a range of options outside its portfolio.

It seems likely that, as a result of the mergers and the two supply agreements, the ex-Whitbread beers [details omitted] will be made available to the BLR pub estate and the ex-Bass beers [details omitted] to the Whitbread pub estate. While, on the one hand, this may initially increase the choice of beers available to those estates, it may also reduce the number of third party beers that are currently, or may be in the future, made available to them. This may, to some extent, reduce product diversity at the retail level and simply result in existing strong brands becoming stronger, as their supply base becomes wider, and a reduction in penetration of third party beers. This effect might become less pronounced once the supply agreements have ended, but they are capable of renewal.

Other issues

I have referred above to the increase in concentration at both the brewing and the distribution levels arising as a result of this merger. Third parties have expressed concerns regarding the potential for oligopolistic or duopolistic behaviour arising from the strength of the brand portfolios of both Interbrew and S&N as well as the control they will have over the route to market. The fact that both have similar high market shares in brewing and distribution; both have a similar range of products including major brands in most categories; the market for beer is static or in decline (particularly the on-trade); there has been no recent significant market entry; the transparency of prices in the market, [details omitted] all indicate, it is argued, that the market may be susceptible to oligopolistic or duopolistic behaviour.

Interbrew has, however, highlighted the differences between itself and S&N and the strategies they are likely to follow as indicating that such behaviour would not be viable or attainable. It has pointed to the presence of other international brewers within the UK; the strength of and competition provided by the regional brewers; and the level of imports to the UK.

While I have considered Interbrew's arguments, I do not feel persuaded by them. I accept that it is not possible, at this stage, to be certain that oligopolistic or duopolistic behaviour will result from this merger. The level of imports is quite low and overseas brewers do not generally make ale, which remains an important feature of the UK market. The regional brewers have relatively small market shares (only one regional brewer has noticeably more than one per cent of the brewing market) and through their strength at the distribution level the main players could inhibit their further growth. Given the indicators above the concerns of third parties and other uncertainties within the market, I find it impossible to dismiss this as a potential adverse effect.

Third party views

I have received representations from a number of interested third parties. While a few of those responding have contended that the merger would have pro-competitive effects, the majority have raised concerns about the potential adverse effects of the merger upon competition. In the main these concerns related less to the simple increase in market share in brewing and distribution, more to the effect upon the structure of the market in the UK and the pressure this might place on C-T as the remaining third player.

Another concern was the increase in concentration in the ownership of major beer brands (the 'portfolio' effect) and the potential foreclosure that might result both at the brewing and retail levels. In brewing, other brewers would be unable to secure access to market through an effective national distribution system; in retailing, customers might be encouraged by Interbrew to take a full range of its products (to which S&N might be expected to respond similarly) thus making it increasingly difficult for other brewers to gain access for their products.

Conclusion

It is not, in my view, necessary at this stage to reach a firm conclusion on whether the market should be viewed broadly, as embracing all beers, or narrowly, subdivided by product type and quality, nor to decide whether there are geographical subdivisions. Whichever view is taken, this merger raises significant competition concerns.

At the brewing level, the merger: reduces the number of national brewers from four to three; creates a new market leader and significantly increases the level of concentration in the hands of the top two brewers. I have some concerns as to how effective a competitor C-T and the smaller regional brewers will be against the market power of Interbrew and S&N. At the distribution level, similar concerns relating to market share and concentration arise with the additional concerns about potential foreclosure to market and the potential effects of the two beer supply agreements. The merger appears to give rise to a situation in which oligopolistic or duopolistic behaviour might be the result and, while this is far from certain, the potential adverse effect upon competition of such a situation are too significant to ignore.

In my view, therefore, the merger gives rise to potential competition concerns justifying reference to the Competition Commission.

Undertakings in lieu of reference

Having reached such a view, I have considered whether there are undertakings in lieu of reference that Interbrew might be able to give. I have discussed this issue with Interbrew but they have offered no undertakings. Given the tight timetable in cases referred back to the UK under Article 9, it is necessary to have fairly complete and agreed undertakings before you take a decision on reference. I am therefore, unable to recommend undertakings that you might seek in this case.

Recommendation

I therefore conclude and recommend that you should refer this transaction to the Competition Commission and that you should make an Order under section 74 of the Act, to prevent the integration of the BHL business with that of Interbrew.