



COMPETITION COMMISSION

Interbrew SA and Bass PLC

A report on the acquisition by Interbrew SA
of the brewing interests of Bass PLC

**Presented to Parliament by the Secretary of State for
Trade and Industry by Command of Her Majesty
January 2001**

Cm 5014

£22.15

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¹These members formed the Group which was responsible for this report under the Chairmanship of Professor Geroski.

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 he considers would not be in the public interest to disclose and which, in his opinion, would seriously and prejudicially affect certain interests.

The omissions are indicated by a note in the text or, where space does not permit, by the symbol ✂.

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Part I

Summary and Conclusions

1 Summary

1.1. The acquisition by Interbrew SA (Interbrew) of the brewing interests of Bass PLC (Bass), known as Bass Brewers, was referred to the UK competition authorities by the European Commission in July 2000. Subsequently, the Secretary of State for Trade and Industry (Secretary of State) asked us to investigate and report on whether the merger operates, or may be expected to operate, against the public interest. Our terms of reference are set out in Appendix 1.1.

1.2. Interbrew is a quoted Belgian company, which in May 2000 acquired the brewing business of Whitbread PLC, known as the Whitbread Beer Company (WBC). Prior to the WBC acquisition, Interbrew's involvement in the UK beer market was primarily through a licence agreement with Whitbread to brew and distribute Stella Artois.

1.3. On 14 June 2000 Interbrew announced that it had reached agreement with Bass to purchase Bass Brewers and on 22 August it announced that the transaction had become unconditional. Bass Brewers in the UK comprises brewing and export operations.

1.4. The merger would make Interbrew the largest brewer in Great Britain, with an overall market share of between 33 and 38 per cent and a portfolio of leading beer brands. In terms of the wholesaling and distribution of beer, Interbrew would have a market share of approximately 33 per cent.

1.5. The merger would strengthen Interbrew's portfolio of leading brands and lead to the creation of a duopoly between Interbrew and Scottish & Newcastle plc (S&N). Because Interbrew and S&N share a common interest in raising operating margins, and because we believe conditions of the market work to facilitate it, we think it likely that net wholesale prices would increase as discount levels are reduced. Given that most consumers do not place a high value on price when choosing a beer brand, we expect that retailers would pass higher wholesale prices through to consumers. We think that there would also be an increased emphasis on non-price competition (advertising and marketing), which would raise barriers to entry and expansion by competing brands. We expect that more emphasis would be placed on the promotion of the leading brands, which in turn would lead to a greater degree of brand rationalization, and less consumer choice, than might otherwise occur.

1.6. As a result of the merger, Interbrew and S&N would have the largest and most efficient wholesaling and distribution operations in Great Britain. While competing brewers may be able to rely on the centralized wholesaling and distribution arrangements offered by some multiple retailers, this will not enable entrants or smaller brewers to access either multiple retailers that do not offer such services or the independent free trade. For these customers, Interbrew and S&N would effectively control the route to market.

1.7. Interbrew charges different prices according to the type of customer with whom it is dealing; the differences are only in part explained by differences in costs incurred. Interbrew offers more attractive prices to multiple retailers than it does to the independent free trade or independent wholesalers. As a result, the independent free trade is less competitive with the multiple retailers than would be the case if the price differences were attributable only to cost

differences. Independent wholesalers find it difficult, if not impossible, to compete for the business of the multiple retailers. And they are unable to offer low prices to the independent free trade. We expect that the merger would enhance Interbrew's ability to price discriminate.

1.8. Interbrew expects that the merger would result in synergy benefits and cost savings amounting to approximately £[§] million a year after four years. It assessed the cost of implementing these cost savings to be £[§] million. Interbrew told us that the synergies would enable it to continue to offer competitive pricing to all channels without further erosion of already tight margins.

1.9. Interbrew paid £[§] million more for Bass Brewers than its own estimate of fair value and considered this a reasonable premium to pay in order to achieve the synergistic savings. The payment of this premium limits any beneficial effects that consumers would experience from those synergies even if Interbrew realized all the synergies it claims are available.

1.10. We have considered nine behavioural and structural remedies. The behavioural remedies would not address the adverse public interest effects and they would be difficult, if not impossible, to enforce. Similarly, a number of the structural remedies would either not address the adverse effects or they would be impracticable.

1.11. We believe that it would be extremely difficult successfully to divest from Bass Brewers a suitable combination of brands, brewing capacity, and wholesaling and distribution capacity in a manner that would not seriously damage Bass Brewers as a competitor. We also think it would be undesirable to attempt artificially to create a new business in this manner.

1.12. Interbrew told us that it was prepared to undertake that it would not close any breweries before 2003 and that it would maintain its current brand portfolio until 2003. We do not believe that these remedy the adverse effects we have identified.

1.13. In our view, the behavioural remedies and most of the structural remedies we considered, individually or in combination, would not remedy the adverse effects we have identified. This, in turn, means that we believe that there are no options short of divestment which would remedy the adverse effects of this merger. This left us with two final structural remedies.

1.14. We all believe that without the rights to Stella Artois, WBC would not be a viable stand-alone business, nor would it be an attractive proposition for another brewer. Nor were we able to give brands to WBC from the portfolio of Bass Brewers that would compensate for the loss of Stella Artois. The divestment of WBC without Stella Artois would not, therefore, allay the adverse public interest effects.

1.15. We have given careful consideration to whether the divestment of WBC with the licence rights to Stella Artois would remedy the adverse effects. One of us believes that it would, with certain undertakings regarding the licence rights to Stella Artois, arguing that this remedy effectively would recreate the pre-merger situation; it would make WBC a viable business and a strong competitor; and it would make WBC an attractive merger or alliance partner for another brewer, in which case it would become a more formidable competitor and this would render less effective a potential duopoly between Interbrew and S&N.

1.16. Three of us believe, however, that it would not be a sufficient remedy. We are not convinced that any undertakings in respect of the Stella Artois licence would be effective. Moreover, without Stella Artois in its portfolio, Interbrew would be forced to develop another premium lager, possibly Grolsch. We do not believe that Interbrew would use a licensed brand to compete actively with a brand that it owns, but is licensed to a competitor, and on which it was receiving a stream of royalties. We think that separating the management of a brand from its ownership will undermine the long-term health of the brand in a market where the brand

manager and owner are both operating and where brands are of increasing importance. Furthermore, we are concerned that Interbrew would use its position as owner of the Stella Artois brand to persuade WBC not to compete as vigorously against Grolsch as it otherwise might do. Finally, we believe that WBC on its own would be a weak competitive force (being very reliant on Stella Artois for sales and profits) and an unattractive platform for other brewers to use as a vehicle for large scale entry into the market.

1.17. Three of us believe that Bass Brewers is a viable business that can be disposed of without complications. We also believe that there are a number of international brewers who would find it an attractive vehicle for entry or expansion in the UK. Further, disposal of Bass Brewers would leave Interbrew owning and managing its major brand and it would make WBC, owned by Interbrew, a stronger competitor than it would be as a stand alone business.

1.18. The three of us considered whether it would be proportionate to require the disposal of what would amount to 75 per cent of Interbrew's business in the UK. We would have recommended another remedy, or combination of remedies, if we were satisfied that to do so would have remedied the adverse effects of the merger. However, we believe that no individual remedy, or combination of remedies, would have this effect. Accordingly, the majority recommend that Interbrew should be required to divest the UK business of Bass Brewers to a buyer approved by the Director General of Fair Trading.