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Session III - Competition Issues in the Groceries Sector: Focus on Conduct

-- Background paper by the OECD Secretariat --

23-24 September 2015, Montego Bay, Jamaica

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MARKET STRUCTURE, GROWTH AND COMPETITION IN THE SUPERMARKET SECTOR IN LATIN AMERICA

-- BACKGROUND PAPER BY THE OECD SECRETARIAT* --

Abstract

Supermarkets play a limited but increasingly important role in Latin-America groceries retail markets. Traditional grocery retailers still play a substantial role in most Latin American countries and the penetration of supermarkets is still behind the developed countries. Paradoxically, within the supermarkets sector, concentration is high and a small number of large players are present in several countries. As personal income increases, the size of the middle class grows and the logistics and transport infrastructure develops, supermarkets are expected to expand further becoming the main gatekeeper for most grocery products. As supermarkets penetration increases, there is generally a process of transfer of market power from manufacturers and producers to retailers. In Latin America, producers and manufacturers still have substantial market power (and, consequently, bargaining power) in several product markets. However, recent cases and commercial practices show that such bargaining power is eroding in favour of large supermarket chains, changing the competitive dynamics of retail markets.

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1. Introduction

1. The retail grocery sector has undergone a drastic process of transformation all over the world in the last decades. Three simultaneous demand and supply factors have triggered this process:

1. On the demand side, the changes in shoppers' habits that have switched to one-stop shopping mostly due to time constraints;

2. On the supply side, innovation in logistics and distribution technologies that involve decreasing distribution costs and a better management of stocks; and

3. The increasing size of supermarket chains and the economies of scale and scope involved in their expansion.

2. The speed of this process differs from country to country and is strongly related to the development of other demand and supply factors. Demand-side factors affecting the development of supermarkets include socioeconomic factors such as the degree of urbanisation (supermarkets are mostly a urban phenomenon), the level of income (low-income shoppers might not adopt a one-stop shopping habit since they usually buy less and more frequently due to stricter daily budget constraints), the size of the middle class (the middle class constitutes the natural market for supermarkets) and the incorporation of women to the labour market. On the supply side, factors such as the development of transportation infrastructure and the existence of supermarket-friendly regulation (e.g., low restrictions to establishment operation) are determinant for the growth of the supermarket sector.

3. In developed countries, supermarkets have increasingly become the main gate to the market for an important number of products. This phenomenon has generated positive efficiencies but has also introduced risks for competition:

1. On the one hand, the innovation in logistics and distribution technologies and the economies of scale of supermarket chains have implied efficiency gains from which consumers have benefitted through better prices and wider product availability.

2. On the other hand, the increasing size of supermarket chains and the increasingly important role of supermarkets as market gatekeepers might present certain risks to competition which can lead to a decrease in social welfare.

4. The impact of the growth of the supermarket sector on consumer welfare depends on the balance of those two forces: a fair degree of competition will allow consumers to benefit from the efficiency gains derived from the expansion of the so-called "modern retailing" (which includes a wide variety of store formats such as supermarkets, hypermarkets, hard discount stores and convenience stores).

5. Latin America has also gone through a process of transformation of the groceries retail industry, especially during the last two decades. The object of this paper is to review how competition and the existence of anticompetitive practices have recently evolved in the supermarket sector in Latin America. Needless to say, that the evolution of competition has differed from country to country and it is not possible to talk about a "Latin-American competition model" in the supermarkets sector. However, the paper attempts to identify common sectoral features and common risks to competition. The paper starts by discussing the determinants of modern groceries retailing and what the state of play of those determinants in Latin America is. In view of the sectoral evolution, the paper analyses the economics of competition in the groceries retail distribution market and how they apply to Latin America. Finally, the paper presents an overview of recent competition cases in multiple Latin-American jurisdictions affecting the groceries retail industry.

2. The determinants of the expansion of supermarkets in Latin America

6. The arrival of modern retail in Latin America occurred in three successive waves (Reardon and Hopkins, 2006; Reardon and Berdegue, 2007). The first wave took place in the early to mid-1990s in South America (e.g., Argentina, Brazil, and Chile). The second wave happened during the mid to late 1990s in Mexico and Central America (e.g., Ecuador, Colombia, and Guatemala). The third wave begun in the late 1990s and early 2000s in some other countries in Central and South America (e.g., Nicaragua, Peru, and Bolivia).

7. In most cases, the process was triggered by the liberalization of trade and foreign direct investment (FDI). For example, in the case of Mexico, the transformation of the retail sector was mostly driven by Mexico joining the North American Free Trade Agreement (NAFTA). As a consequence of trade liberalization, domestic price controls became ineffective and thus domestic trade was also de facto liberalised and the system of official prices and widespread subsidies was dismantled.[1]

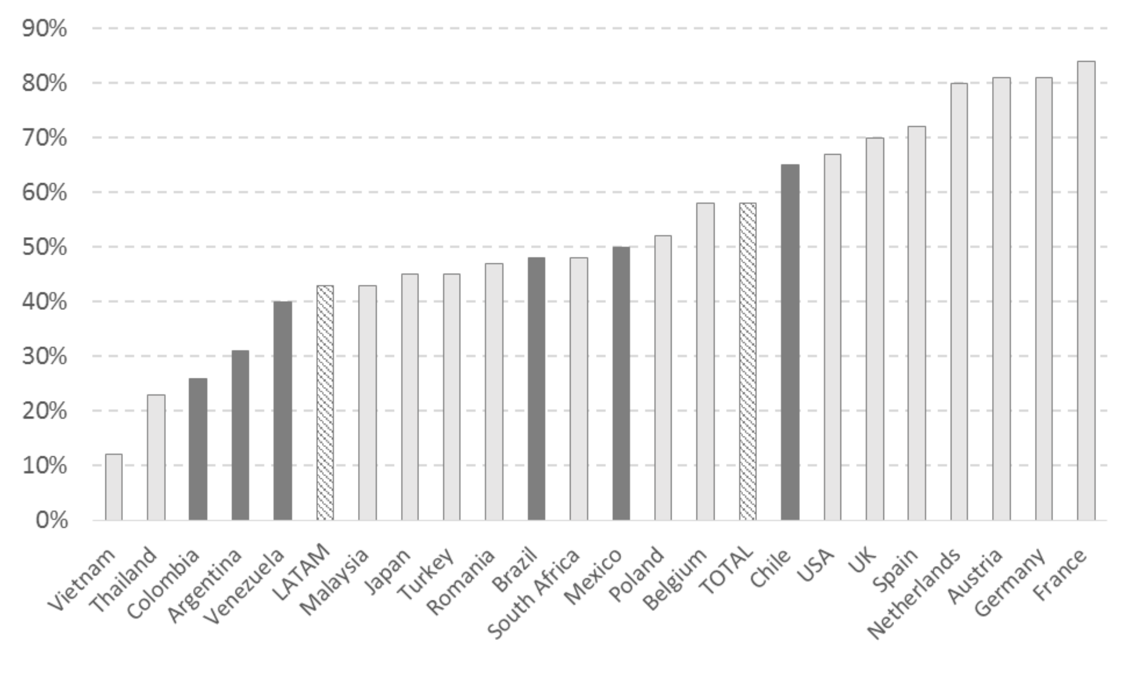
8. FDI has played a crucial role in the expansion of supermarket chains all over Latin America through the expansion of foreign supermarket chains in Latin America or the association of local groups with foreign chains. World retail leaders such as Walmart (in México, Central and South America), Carrefour, Auchan, Costco and Ahold initiated a process of rapid expansion.

9. Supermarket development in Latin America is however still behind the development in richer countries. Grocery sales through the modern channel still represent a percentage of the total grocery sales below 50% in comparison with figures above 70-80 per cent in Western Europe and the US. Only in Chile more than half of the grocery sales are made through supermarkets (65%), while the average of the Latin-American countries is just 43%[2] (See Figure 4 in Appendix 1).

[1] FAO (2009) describes the process of liberalization of the agrofood industry in Mexico.

[2] Unweighted Average of countries with available data: Argentina, Brazil, Chile, Colombia, Mexico and Venezuela.

Figure 1. Groceries sales through modern retail in selected countries 2011



Source: Own elaboration based on Euromonitor

10. What determines the size of the modern retail grocery sector? There are different demand and supply factors that affect the development of the modern retail grocery industry (See Reardon and Gulati, 2008). Demand-side factors such as the income growth, the urbanization rate, the size of the middle class and the participation of women in the labour market (as a proxy of the opportunity cost of time for women) are necessary but not sufficient for the expansion of modern retailing (Reardon et al., 2003). Other supply factors such as policy factors, infrastructure development, the modernisation of the supply chain (through the development of modern wholesalers and centralised purchasing mechanisms) and the level of FDI are also very relevant. Supply-side factors are normally more heterogeneous and more difficult to systematize but, as mentioned above, not less important.

11. This section analyses where Latin America stands in relation to other countries of the world with respect to the demand and supply-side factors that determine the development of the modern retail industry.

12. On the demand side, income and urbanization rates have been proved to be relevant in explaining supermarket development. Traill (2006) shows that a one percentage point increase in urbanization rate results in a USD2.5 increase in annual per capita supermarket sales, while a USD1 increase in disposable income would raise supermarket sales by USD0.27.

13. There is a clear positive relation between the development of modern retailing and the level of personal income (See Figure 3 in Appendix 1). As income per person increases, modern retailing becomes the prevalent mean of grocery purchasing. The penetration rate of supermarkets, measured as the percentage of grocery purchases made in supermarkets, of Brazil and Mexico seems to be in line with other countries with similar purchasing power per capita such as South Africa, Turkey, Romania and Malaysia.

14. The explanatory value of this factor seems to diminish as countries become richer reinforcing the fact that income growth is a necessary condition but not sufficient to explain the development of

supermarkets, e.g. the penetration of supermarkets in Japan and Germany differs by 35 percentage points despite having similar levels of income.

15. Latin American countries seem to fit relatively well with the relation between both variables (with the exception of Argentina). The relatively lower penetration of the modern retailing industry is generally consistent with the lower income per capita of Latin American countries.

16. The relation between the share of urban population and the penetration of modern retailing is weaker (See Figure 4 in Appendix 1) although this could be due to the fact that most countries in the sample have high urbanization rates. In countries such as Ireland and Romania this seems to be a relevant factor to explain the low degree of penetration of supermarkets. The Latin American countries in the sample have high urban population rates similar to other richer countries in the sample. Thus, the rate of urban population does not seem to explain the lower penetration of modern retailing in Latin America.

17. The size of the middle class (measured as the percentage of population living in households with daily per capita incomes of between USD10 and USD100 in PPP terms)[3] also seems relevant in explaining the rate of penetration of supermarkets (See Figure 5 in Appendix 1). However, at high-income levels, this link seems to fade out. In the case of Latin America, the size of the middle class in Mexico and Chile is larger than in Colombia and Venezuela and so the penetration of modern retailing.

18. On the supply side, the lack of modernization of the fresh produce supply chain, where supermarkets still use the traditional wholesale supply chain for an important part of their purchases of fresh products, and the lack of wholesale distribution structures (in most countries only backward integrated supermarkets benefit from economies of scale and scope, but other actors have no access to an efficient distribution network) are relevant factors in explaining the rate of penetration of supermarkets[4]. The development of modern wholesale platforms and the adoption of centralized purchasing systems would favour the expansion and the development of competition in the supermarket industry.

19. An important share of fresh produce supply in Latin America is done through traditional wholesale markets (the so-called "centrales de abasto"). The "centrales de abasto" are logistic distribution centres for fresh produce where producers and retailers physically meet to buy and sell their products. Most of these institutions were created in the period 1960-1980 as mechanisms to guarantee food security of supply of large cities (see Cunha, 2012)[5]. Currently, they constitute the main supply channel for traditional retailing. Supermarkets often complement their own logistic platforms with purchases from these wholesale traditional markets. Traditional wholesale markets are less efficient and more costly than modern logistics platforms (in terms of transport logistic efficiencies, stocking, product manipulation and sorting and waste management).

20. In terms of logistics development, Latin America is well behind other emerging economies. The World Bank Logistics Performance Index[6] has remained practically unchanged between 2007 and 2012 for

3 Kharas (2010).

4 Reardon et al (2006).

5 Similar institutions were also created in the post-WW II period in several countries of the South of Europe such as France, Italy and Spain and they still play a relevant role in wholesale trading. The role of wholesale markets in other European countries such as Germany, UK and The Netherlands is residual. In Europe, traditional wholesale markets have evolved into modern platforms through the integration of multimodal transport including refrigerated transport, including traceability technologies and looking for new market niches such as specialized shops, hotels and restaurants (Cunha, 2012).

6 See http://lpi.worldbank.org/

the whole region while other emerging economies (such as South Africa, Morocco, Turkey, China, Philippines and Vietnam) have made substantial progress. Also the logistics costs of the region are high (about 12% of GDP), compared to developed economies (8 to 10% of GDP)[7].

21. Policy factors might be playing a role in the low penetration of supermarkets in Argentina and Venezuela. Political uncertainty, price controls and other operational restrictions might refrain investment in the industry. Argentina and Venezuela's problems with inflation have triggered some measures that have limited the ability of supermarkets (amongst other economic agents) to freely set their prices.

22. Venezuela has created a strong price control system with its "Precios Justos"-scheme ("fair prices"). Under this system, companies must send accounting information to the government in order to justify the prices that they set as "Precios Justos". Profits above 30% are not allowed. SUNDEE[8] is in charge of implementing this regulation and it has extended powers to fine companies, expropriate its assets and incarcerate its management.

23. Argentina's system is less interventionist, as prices are not directly regulated. However, Argentina has implemented a system in which companies and the government agree on prices for a certain basket of products ("Precios Cuidados"). Even if this system is based on voluntary negotiations, the "Ley de Abastecimiento"[9], which allows the government to directly intervene to set prices, disciplines companies in their negotiation with the government.

24. In conclusion, in Latin-American countries modern retailing still plays a limited role in comparison to other countries such as the US or Western Europe. Having said that, it is expected that as countries grow and their per-capita income increases and the size of the middle class converges, the penetration of supermarkets will increase. Also, some supply factors seem to be holding back investment and growth of the supermarket industry. The adoption of policies that remove obstacles to competition, promote the development of wholesalers and incorporate fresh produce into the modern supply chain will contribute to the development of the supermarket sector.

3. Market trends and implications for competition

25. Although the degree of competition in the modern retailing industry differs from country to country, there are five general features that seem to be common in several countries in Latin America:

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7 See CAF (2013).

8 Superintendencia Nacional para la Defensa de los Derechos Socioeconómicos or Superintendencia de Precios Justos.

9 This law allows government to intervene prices in any market, and it has already been applied in several industries, such as:

- The car industry. http://www.diariodemocracia.com/notas/2014/10/23/gobierno-aplica-abastecimiento-contra-automotrices-peugeot-renault-91455.asp.
- The wheat market http://lapistaoculta.com.ar/3/2/c/item/4386-gobierno-aplica-la-ley-de-abastecimiento-al-trigo.html.
- Gasoline market http://www.perfil.com/economia/Aplican-la-Ley-de-Abastecimiento-en-los-combustibles-20100816-0006.html.

1. As analysed in the previous section, there is generally a low penetration of supermarkets in comparison to rich countries. Traditional grocery shops still play an important role in most Latin American countries. This low penetration might be temporary and the role of supermarkets will likely become more important as the above-mentioned demand and supply factors evolve.

2. Despite the small size of the supermarket sector compared to other countries, the sector is very concentrated and few actors dominate the domestic markets. The three most important players hold a joint market share above 70-80 % in most countries (see Table 2). Moreover there is a small number of large operators that are present in several countries (Cencosud in Argentina, Brazil, Chile, Peru and Colombia; Wal-Mart in Argentina, Brazil, Chile, Honduras and Mexico; Casino in Brazil and Colombia; Falabella in Chile and Peru and Carrefour in Argentina and Brazil).

Table 1. Main supermarket chains and concentration index

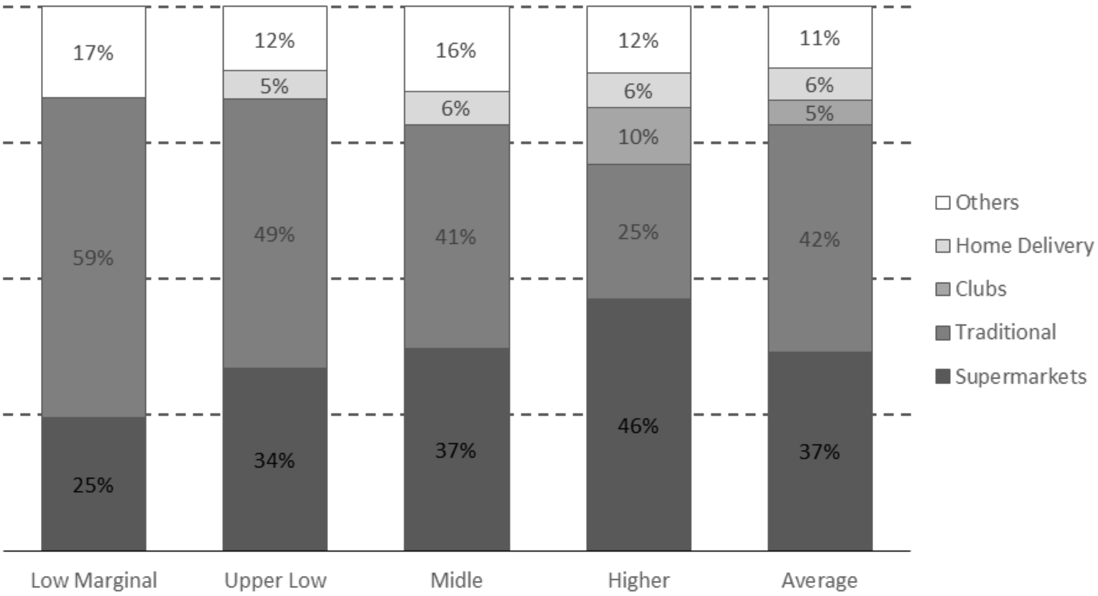
COUNTRY	Argentina	Brazil	Colombia	Chile	Honduras	Mexico	Peru
Chain	*Carrefour*	*Casino (CBD)*	*Casino (Éxito)*	*Walmart*	*Walmart*	*Walmart*	*Cencosud (Wong)*
	Cencosud (Jumbo)	*Carrefour*	*Cencosud (Jumbo)*	*Cencosud (Sta. Isabel)*	*La Colonia*	*Soriana-Comercial Mexicana*	*Iberbank*
	Walmart	*Walmart*	*Olímpica*	*Falabella (Tottus)*	*Price Smart*	*Chedraui*	*Falabella*
		Cencosud (Gbarbosa)		*SMU (Unimarc)*			
C3	*>80%*	*>60% (C4)*	*>70%*	*>90%*	*>95%*	*>90%*	*>95%*

Source: Own elaboration. In brackets, main brand under which each company operates in each country.

3. Supermarkets are increasingly spreading to broader groups of population but are still mostly supplying middle and high-class consumers. This implies that traditional and modern retail outlets are not always competitors since they target different groups of shoppers. In México for example, poorer citizens shop mostly at traditional shops (59 % of their food expenditure) and make only 24 % of their food expenditure in supermarkets while richer citizens shop mostly at supermarkets (46 %) and less often in traditional shops (25 %) (Figure 2)[10].

10 This pattern exists in other countries, such as Argentina, where 64% of rich people shop in supermarkets, while just 25% of poor citizens shop in supermarkets. http://sitiosargentina.com.ar/notas/2006/octubre/compras.htm

Figure 2. Share of expenditure in groceries by socioeconomic group and outlet in México 2013



Source: Own elaboration based on data from Nielsen. October 2013.

Available at http://www.nielsen01.com/hsfacts/_2013/131007_NSEB/

4. The Latin American region has different upstream buying structures. For example, in Brazil, buying is centralized and vertically integrated, with supermarket groups banding together to improve their purchasing power, bypassing wholesalers and negotiating directly with suppliers. In Chile, there are two supermarket buying associations — Mas and Cadesur, which negotiate with suppliers and distribute to supermarkets. In México, supermarkets are vertically integrated and negotiate directly with suppliers. Wholesalers are practically non-existent which makes the entry of smaller competitors difficult since they do not have access to efficient logistics and distributors.

5. In most Latin American countries, fresh food products (mostly fruits and vegetables but also meat and fish) are not fully integrated in the modern retail sector and an important part of the wholesale supply of fresh products is channelled through traditional local or regional wholesale markets ("mercados mayoristas" and “centrales de abastos”). Even supermarkets make part of their purchases instead of negotiating directly with producers as it happens with other food products in Latin America or with fresh products in other parts of the world.

26. The specific characteristics of the retail grocery industry in Latin America means that the competition concerns are not identical to those in countries where modern retailing is the dominant distribution channel. The industry structure of the grocery retail industry in Latin America has a number of implications that should be incorporated into the analysis of competition:

1. Since the size of the modern retail sector is smaller in Latin American countries, industry buyer power will be lower as compared to more developed countries. Since producers have access to a large traditional distribution channel, the power of supermarkets as market gatekeepers will be reduced. On the other hand, concentration within the modern retail channel in most Latin American countries is high and few players, which are present in several countries, have substantial market shares., Individual buyer power by large supermarket chains will be thus high

within the modern supply chain. The competitive effect of both forces will depend on the size of the modern retail sector and on the level of concentration of the industry: a high concentration of the supermarket industry might be irrelevant from a competition point of view if the role of supermarkets is not significant.

2. Given the high concentration of the supermarkets industry, coordination between competitors could be in principle easier. A small number of competitors reduces the cost of coordination and also the gains from deviations from a potential agreement (Motta, 2004). This does not imply that the existence of a small number of firms will necessarily lead to collusion.

3. The socioeconomic segmentation of the market might encourage discriminatory pricing by supermarkets: since supermarket clients enjoy higher incomes and have a lower price elasticity of demand, supermarkets might decide to charge them higher prices. This would imply that supermarkets might not fully transfer to final consumers their efficiency gains. Large supermarkets might obtain a product at a lower price from manufacturers and distribute it at a lower cost but, knowing that their clients are less price-sensitive, they might set a higher margin offsetting the efficiency gains and depriving final consumers from the cost benefits of modern retailing.

4. The power of producers and manufacturers' brands still dominates over the power of retail brands which makes that vertical backward integration of manufacturers by retailers and supermarket private brands (or store brands) are rare in Latin America. While the penetration rate of private labels in Europe is between 20 and 40 % of total groceries expenditure (or even above 40 % in the UK, Spain and Switzerland) and is about 18 % in the US and Canada, such penetration is generally below 10 % in Latin America (with the exception of Colombia where the weight of private labels reaches 15 %). The role of private labels in Chile (10 %), Brazil (5 %), Mexico (8 %), Argentina (9 %), Peru (7 %) and Venezuela (3 %) is limited but growing steadily[11]. The growth of private labels goes generally hand in hand with the concentration of the industry: For example, Switzerland has both the highest retailer concentration and private-label dollar share and, in fact, 15 of the 18 most concentrated markets in the world are found in Europe, where private labels are also more successful.

   In many product segments, concentration is high at manufacturing level and there are few suppliers with large market shares. For example, the Mexican company Bachoco claims to hold a 35 % of the chicken production in Mexico. Other product categories such as beer[12], chilled processed food[13], baby food[14] and dairy products[15] are also highly concentrated partially countervailing the potential buyer power of supermarkets. In Chile, Unilever controls 70% of detergent sales through supermarkets and three companies (Agrosuper, Ariztía and Don Pollo) account for 80% of the poultry market. In Argentina, also Unilever accounts for 71% of the detergent market, two brewers (Cervecería Quilmes and CCU Argentina) account for 96% of the beer market and two firms (Mastellone and Sancor) account for the 77% of milk producers[16].

11 Data for 2013 obtained from Nielsen (2014).

12 Grupo Modelo (AB Inbev) and Cuauhtémoc Moctezuma (Heineken), jointly accounted for 99 per cent of the market share.

13 Sigma Alimentos SA de CV accounts for 42% of the market.

14 Nestle accounts for 61% of the market.

15 Grupo Industrial Lala SA de CV accounts for 20.50% of the market.

16 See more examples in “PODER DE COMPRA EN LA CADENA ALIMENTICIA EN LA REPÚBLICA ARGENTINA”

5. The lack of wholesale traders in some countries such as Brazil and Mexico prevents access to modern retailing by independent supermarkets and small regional chains which reinforces the cost advantages and the market power of large supermarket chains. Entry and competition in the supermarket industry might be limited in the absence of wholesale suppliers that allow small supermarket chains to benefit from modern retailing efficiencies.

6. The lack of integration of fruits and vegetables into the modern retail supply chain might prevent consumers from benefitting from the advantages that such channel is able to offer. On the other hand, exclusionary conducts will be less likely to appear in the fresh produce sector since large supermarkets chains will not be able to exercise their market power in this market segment.

4. Recent competition cases in the groceries retail sector in Latin America

27. This section reviews anticompetitive practices reported by antitrust and competition cases and investigations in the groceries retail distribution industry across several jurisdictions in Latin America. The aim of this section is to illustrate a variety of anticompetitive conducts that have been recently investigated by competition authorities in the supermarkets sector in Latin America.

28. Recent interventions of competition authorities in the supermarket industry in Latin America have not been very numerous. However, as the industry grows, the risks of anticompetitive behaviour might increase and so the number of antitrust interventions in the industry.

29. There have been several interventions related to consumer protection (since some competition authorities, such as the Peruvian agency Indecopi and the Colombian Superintendencia de Industria y Comercio (SIC), also have consumer protection powers), unfair competition (such as the ongoing investigations in Colombia[17] and Chile[18] regarding misleading price comparisons) and merger analysis.

30. The focus of this paper is on anticompetitive conducts from an antitrust perspective. The current section focuses on recent interventions related to market screening activities and to the investigation of anticompetitive practices.

31. The section presents both a broad classification of potential anticompetitive conducts in the supermarket industry and reviews some recent cases (for a review of older cases see Basker and Noel, 2013).

4.1 Market Screening

32. The analysis of competition in the groceries retail industry has become a popular topic amongst competition authorities. The increasing concentration of the industry and the important role of the industry in the daily life of citizens have attracted the attention of antitrust agencies with the objective of guaranteeing the well-functioning of groceries retail markets. Several Antitrust Agencies all over the world have conducted comprehensive market investigations in the groceries retail industry in order to detect

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available in http://www.sela.org/media/264681/t023600006273-0 poder_de_compra_de_la_cadena_alimenticia_argentina_.pdf.

17 See http://www.sic.gov.co/drupal/sites/default/files/estados/Resolucion_14749_Archivo_Averiguacion_Preliminar_Cafam_Carrefour.pdf.

18 See http://www.tdlc.cl/Portal.Base/Web/VerContenido.aspx?ID=1320.

potential obstacles to the functioning of the market in the form of barriers to entry and anticompetitive behaviour[19].

33. Most of these studies analyse the structural characteristics of the industry, the existence of barriers to entry (in the form of economic and legal obstacles to the establishment and operation of supermarkets) and the existence of commercial practices that could hinder the development of competition (although not necessarily constituting infringements of competition law).

34. Special attention has been directed to the relations between producers and manufacturers on one side and retailers on the other side and, in particular, to the potential exercise of buyer power by retailers. Most of these initiatives have led to the elaboration of industry voluntary codes of conduct (as in the UK and Australia) or even to the passing of sector specific legislation regulating suppliers-retailers relations (as in Spain).

35. In Latin America, just a few competition authorities have conducted market investigations in the groceries retail industry which is consistent with the increasing but still limited role of supermarkets as market gatekeepers for the purchase of groceries. Chile's Fiscalía Nacional Económica was an early-bird and analysed the industry in 2007 concluding that, on the one hand, market entry was having an impact on prices but, on the other hand, the increasing concentration of the market through mergers and acquisitions could be offsetting such effects. The report found evidence of the potential exercise of buyer power at upstream level and proposed the adoption of certain measures to limit the exercise of buyer power by retailers (see Box 1). Colombia's Superintendencia commissioned a report in 2013 to examine the competitive conditions in the supermarket industry. The report concludes that despite the efficiencies introduced by large supermarket chains, the competition authority should be vigilant on the increasing concentration of the industry that could lead to potential abuses of buyer power of retailers versus producers and manufacturers.

36. Perhaps the most ambitious project in this field is the one currently being conducted by the Mexican COFECE that in 2014 commissioned a number of long-ranging studies in the agri-food industry including the whole production and supply chain (from competition in agricultural markets to retail markets). The results of the studies are expected to be published by the end of 2015[20].

Box 1. Groceries Retail Market Investigation in Chile (2007)

The Chilean Competition Authority (Fiscalía Nacional Económica, FNE) opened a competition investigation in the Supermarket sector which was published in 2007. The report analysed the market forces both in the downstream market (retailers-consumers) and the upstream market (suppliers).

Regarding downstream markets, the reports' objective was to evaluate the degree of concentration in the industry and whether its evolution had had any influence on industry prices and margins. Regarding upstream markets, the report analysed the relation between supermarkets and suppliers from three different point of views: (i) the degree of suppliers' market power, (ii) the degree of supermarkets' buyer power and (iii) the development of supermarkets' private labels and its effect on the market competition.

19 Reports on the groceries retail market have been produced by competition authorities in Germany, France, Spain, Portugal, Italy, Austria, Australia, Ireland, UK and Nordic countries. The European Commission has also commissioned several reports in the context of several taskforces dealing with the better functioning of the food supply chain.

20 See webpage "Estudio sobre la competencia y libre concurrencia en el sector agroalimentario" http://www.cofece.mx/d3sarroll0/index.php/prensa/noticias/estudio-sobre-la-competencia-y-libre-concurrencia-en-el-sector-agroalimentario**.**

The report concluded that the evolution of prices (and margins) in the sector had been characterized by constant reductions due to the expansion of the different chains through the country and the strong competition between the entrants and the regional incumbents. However, once that the market had been captured by the main supermarket chains the effect on prices has been reversed. Furthermore, the report found that the concentration process that occurred around 2005 had led to higher prices and margins.

The FNE also concluded that concentration in the sector was high which could be evidence of the existence of supermarkets' market power. As a consequence the Authority advised to (i) limit payments from suppliers to supermarkets to certain payments for specific services and to discounts; (ii) obligations to signed contract for any transaction between suppliers and supermarkets and (iii) forbid payments periods longer than 30 days.

Source: Análisis Económico de la Industria de Supermercados en el marco de la Causa Rol Nº 101/2006.

www.fne.gob.cl/wp-content/uploads/2013/02/Analisis-economico.pdf.

4.2 Abuse of Dominance

37. Despite the increasing concern about the growing market and buyer power of supermarket chains, there have been few cases regarding the abuse of dominant positions in this industry[21]. Not even in Europe, where supermarkets concentration is higher than in Latin America, have there been relevant competition cases involving the abuse of market power in the groceries retail industry. The increasing concern about the potential abuse of buyer power by large supermarket chains has not been followed by a concomitant opening of antitrust cases. The concerns about the imbalance of power between retailers and suppliers have been mostly addressed through the signing of voluntary industry codes of conduct. Such codes of conduct exist in Australia, the UK, Canada, Italy and Portugal. In Latin America, Mexico, Colombia and Ecuador have adopted industry codes of conduct[22].

38. As reported in section 0, a distinctive feature of Latin America is the high concentration in the production of certain products, which countervails the increasing buyer power of supermarkets. Contrary to what has happened in Europe where there has been a process of transfer of market power from brand manufacturers to retailers, manufacturers in some industries still retain in Latin America high degrees of market power. Such high concentration in suppliers' markets makes that cases implying the abuse of a dominant position are more likely to involve manufacturers imposing conditions on retailers rather than the opposite. This was the case of the case against Unilever in Chile in 2013 for imposing exclusivity clauses on retailers for the sale of soap that had an exclusionary effect on competitors (see Box 2). A decision in a similar case but involving a beer manufacturer was adopted by Brazilian's CADE in 2009. The investigation, initiated in 2004, involved a loyalty programme developed by AmBev, Brazil's largest beer producer (with a 70 % market share). The programme, named 'To Contigo', awarded points to retailers for purchases of AmBev products, which could then be exchanged for gifts. CADE concluded that the

21 Basker and Noel (2013) report the case against Makro supermarkets in Argentina in 1997 for predatory pricing that was finally closed without sanction and the case against Corporación Supermercados Unidos (CSU), the largest supermarket chain in Costa Rica with a market share of 60–80% of the Costa Rican supermarket sector, five times its nearest competitor, for imposing certain commercial conditions to suppliers that had an exclusionary effect on competitors.

More recently, other two predatory cases has been investigated. Cadena Comercial Sancarleña S.A in Costa Rica (2012) and D&L in Chile (ongoing) were investigated for selling under costs. However, the first case was not found guilty and the second one, which also includes accusations of unfair competition, is still ongoing.

22 See OECD (2013) for some examples.

programme created incentives for exclusive dealing, foreclosing competitors from accessing the market[23]. CADE imposed AmBev the largest fine till that date amounting to USD160m (see Martinez, 2013).

39. Similar cases involving vertical foreclosure by manufacturers' supermarkets are the 2012 Ice-Cream refusal to supply case in Costa Rica where a firm supplying supermarkets refused to supply local stores (shelved)[24], and the exclusionary rebates in the liquor market in Costa Rica, where a dominant liquor company offered discounts to large supermarkets that could have exclusionary effects on small retailers (shelved)[25].

Box 2. Suppliers' Market Power: Unilever in Chile (2014)

In 2013, the Chilean FNE initiated an investigation on Unilever, the main soap manufacturer (70% of sales through supermarkets). The company was accused of engaging in anticompetitive exclusionary conducts which limited competitors' ability to compete and enter the market, such as exclusivity agreements and retroactive rebates.

The FNE initially referred the case to the competition court (Tribunal de Defensa de la Libre Competencia) asking the court to fine the company USD20 million for imposing anti-competitive clauses that excluded on suppliers. However, the case was finally settled and Unilever agreed to change its distribution and commercialization practices, in order to allow third parties to compete.

Unilever's commitments included (i) abolishing exclusivity agreements with dealers, including wholesalers and supermarkets; (ii) not offering any discounts or premiums to encourage the exclusive sale of its own brands; (iii) not offering financial incentives to suppliers subject to meeting sales goals; and (iv) not paying for supermarket shelves space during a period of three years.

Source: C 249-13 Requerimiento de la FNE contra Unilever Chile S.A.

http://www.tdlc.cl/Portal.Base/Web/VerContenido.aspx?ID=4007.

40. In Brazil, CADE has also dealt with a number of cases involving exclusivity agreements between shopping malls and retailers which, although not dealing strictly with supermarkets, might have implications for supermarkets based in shopping malls. In particular, CADE dismissed in 2014 the allegations against McDonald's for abusing its dominant position by including an exclusivity clause in its contract with the Brazilian shopping mall Iguatemi. The clause prevented the shopping mall from entering into lease arrangements with McDonald's main domestic competitor, Brazilian-owned food chain Bob's. However, exclusivity clauses have been declared illegal by CADE when imposed by shopping malls on their tenants, forbidding the tenant from locating a store within a specified distance from the mall[26].

23 CADE´s Administrative Proceedings No 08012003805/2004-10 against Companhia de Bebidas das Américas – Ambev.

24 http://www.coprocom.go.cr/resoluciones/2012/voto-15-2012-calificacion-denuncia-contra-helados-charo-ang.pdf

25 Bars and small retailers considered that they could not compete with supermarkets, as they could never achieve the sufficient scale to get the rebates offered by the Company. http://www.coprocom.go.cr/resoluciones/2010/voto-06-2010-fanal-resolucion-final.pdf

26 08012.000751/2008-64 Reporta suposta infração à ordem econômica praticada pela Representada MC Donald's comércio de alimentos Ltda.

http://www.cade.gov.br/Default.aspx?1b1bec3bfb11e53ed648d574cc

4.3 Horizontal Agreements

41. In addition to conventional price fixing or market sharing agreements, there are two types of horizontal agreements which are observed frequently in the supermarket industry: (i) the so-called three-party, ABC or hub-and-spoke cartels; and (ii) the purchasing alliances.

42. Hub-and-spoke cartels are price fixing agreements in which both competitors and suppliers/buyers participate. In this sense, they are horizontal agreements with a vertical element. In such cartels, price coordination between competitor A and C takes part through buyer/supplier B. In order for this to be anticompetitive, there must be intent of player A to reveal its prices to player C and player C knows the object of such price information disclosure[27]. Hub-and-spoke cartels can involve the price coordination of manufacturers that communicate through retailers or the price coordination of retailers that communicate through manufacturers.

43. The theory of harm associated to this conduct is that the communication of future prices reduces uncertainty and facilitates the coordination between competitors. There have been cases of hub-and-spoke cartels between supermarkets in the UK (dairy products)[28] and in Belgium (Drugs, perfume and hygiene products)[29]. In Uruguay, the competition authority sanctioned four frozen food manufacturers for coordinating their prices through a supermarket chain (that was also fined). The supermarket chain was in charge of verifying the implementation of the agreement (see Box 3).

44. Price agreements between the main supermarket chains (Walmart, Cencosud, SMU y Tottus) are currently being investigated in Chile by the FNE. The investigation was initiated in 2011 and to date there is no yet a final decision[30].

Box 3. Hub and Spoke Cartel in the frozen food market in Uruguay (2014)

Uruguay's Competition Authority (Comisión de Promoción y defensa de la Competencia) fined four frozen food manufacturers for fixing minimum resale prices, and also one supermarket chain (Supermercados Disco del Uruguay S.A.) for asking for such minimum resale prices.

The four manufacturers had designed a system to set Minimum Resale Prices, linked to a strict control system and penalties for companies breaking the deal.

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27 See “Decision of the Office of Fair Trading CA98/03/2011 Dairy retail price initiatives 26 July 2011 (Case CE/3094-03)”. Available at http://webarchive.nationalarchives.gov.uk/20140402142426/http:/www.oft.gov.uk/shared_oft/ca-and-cartels/dairy-decision.pdf .

28 “Decision of the Office of Fair Trading CA98/03/2011 Dairy retail price initiatives 26 July 2011 (Case CE/3094-03)”.

29 “Décision de l'Autorité Belge de la Concurrence n° ABC-2015-I/O-19-AUD du 22 juin 2015 Affaire CONC-I/O-06/0038 – Hausses coordonnées des prix de vente de produits de parfumerie, d’hygiène et de droguerie”. Available at: http://economie.fgov.be/fr/binaries/D%C3%A9cision%20transaction%20version%20publique%20finale_tcm326-268756.pdf.

30 See "Investigación del FNE por colusión de supermercados continúa vigente" at: http://america-retail.com/industria-y-mercado/investigacion-del-fne-por-colusion-de-supermercados-continua-vigente

Supermercados Disco del Uruguay S.A. acted as coordinator of the agreement and reported the deviations by the upstream companies. The supermarket chain even threatened to impose penalties on manufacturers and stop buying from them if they did make the deal effective. The competition authority did not accept the efficiency allegations argued by the parties.

Source: Nº 18/2010 – MERCADO DE ALIMENTOS CONGELADOS.

http://www.mef.gub.uy/9847/5/areas/resolucion-n%C2%BA-80-14---asunto-n%C2%BA-18_2010-alimentos-congelados-148-kb--20_08_2014.html.

45. Purchasing alliances between supermarket chains have the objective of aggregating purchases of one or several products with the aim of reaching larger economies of scale in distribution and increasing bargaining power vis-a-vis suppliers. Purchasing alliances might allow independent supermarkets and small supermarket chains to access the modern distribution channel and benefit from more efficient transport and distribution. However, as purchasing agreements are agreements between competitors, they might lead to coordination in retail markets.

46. Several competition authorities have analysed the competitive impact of supermarket purchasing alliances[31]. Purchasing alliances are not only limited to national players but also often involve players from several countries[32].

47. Purchasing alliances are rare in Latin America. They could however play an important role in providing access to the modern distribution channel to small chains and independent supermarkets. Therefore, in most cases, they would be likely to have procompetitve effects. Purchasing alliances exist in Chile (Mas and Cadesur) and, to a limited extent, in Mexico (Sinergia). In Mexico, a purchasing alliance by three supermarket chains was initially blocked by the competition authority CFC in 2003 and was later approved on efficiency grounds (see Box 4).

Box 4. Buying Alliances: Sinergia de Autoservicios in Mexico (2004)

In 2003, three Mexican supermarket chains (Gigante, Soriana and Controladora Comercial Mexicana) announced the creation of a joint purchasing and distribution alliance (Sinergia).

The three supermarket chains argued that individually they could not get prices from the suppliers that allowed them to compete with the industry leader Walmart. Walmart's market share was at that moment over 50% of the supermarket industry and its large volume of purchases allowed to get important discounts from suppliers.

The three chains argued that the alliance would be welfare enhancing, as the alliance would imply lower prices for final consumers and would increase the competitive pressure on the main market player (Walmart). Moreover, the alliance purchasing volume would be still smaller than Walmart's purchases.

31 See for example the report prepared by RBB for the UK OFT "The competitive effects of buyer groups OFT Economic Discussion Paper January 2007" (Available at: http://www.rbbecon.com/downloads/2012/12/oft863.pdf); the report of the French Authorité de la Concurrence "Avis n° 15-A-06 du 31 mars 2015 relatif au rapprochement des centrales d'achat et de référencement dans le secteur de la grande distribution" (Available at: http://www.autoritedelaconcurrence.fr/pdf/avis/15a06.pdf); and the numerous cases of upstream cooperation between German supermarket chains. In Germany, there exist several purchasing alliances between regional supermarket chains such as Edeka, Rewe, Bünting y Bartels Langness.

32 Por ejemplo, la alianza CORE creada en 2014 incluye la segunda mayor cadena de supermercados de Alemania Rewe, la cadena de descuento belga Colruyt, y las cooperativas italiana y suiza Conad and Coop.

The alliance was initially blocked by the former competition authority (CFC) due to concerns that it would lead to price coordination. Later that year, following an appeal, the CFC approved the joint venture under the condition that no price coordination take place, allowing Sinergia to coordinate wholesale purchasing and distribution to stores.

Source: CNT-97-2003. Controladora Comercial Mexicana / Gigantes / Tiendas Soriana / Sinergia de Autoservicios. http://189.206.114.203/docs/pdf/ra-22-2004.pdf.

48. Finally, there have been cases of cartels between manufacturers and producers in highly concentrated industries. As mentioned above, the high concentration in some product markets makes more likely the existence of anticompetitive conducts in upstream markets rather than in retail markets. An example is the poultry cartel in Chile where the three sanctioned companies had a joint market share of 80 % (see Box 5). Other cases of horizontal agreements in producers' markets are the case against onion producers in Colombia (shelved)[33], egg producers in Mexico (pending) or tortillas producers in Mexico (sanctioned)[34].

33 "Inicia COFECE investigación en el mercado del huevo "

http://www.sic.gov.co/drupal/sites/default/files/estados/Resolucion_32150_Archivo_Averiguacion_Preliminar_Cebolla.pdf.

34 "CFC sanciona prácticas monopólicas en tortillerías"

http://www.2006-2012.economia.gob.mx/comunidad-negocios/notas-relevantes/8606-cfc-sanciona-practicas-monopolicas-en-tortillerias.

Box 5. Suppliers' market power: The Poultry Cartel in Chile (2014)

In 2014, the Chilean Competition Tribunal (Tribunal de Defensa de la Libre Competencia) fined three poultry producers (Agrosuper, Ariztía and Don Pollo) with USD 61 million for integrating a cartel during at least 10 years. The three companies, which accounted for 80 % of the market, where found guilty of "agreeing to limit the production of chicken meat supplied in the national market and allocating market quotas in the production and commercialization of that product".

The Tribunal, for the first time, also ordered the dissolution of the Trade Association, as it concluded it had played an important role in coordinating, implementing and monitoring the compliance with the agreement.

The ruling also required the companies to consult with antitrust officials prior to any future market concentration efforts or before participating in any new trade association.

Source: C 236-11. Requerimiento de la FNE contra Agrícola Agrosuper S.A. y otros.

http://www.tdlc.cl/Portal.Base/Web/VerContenido.aspx?ID=2947

4.4 Vertical Agreements

49. The process of growth an expansion of supermarkets often involves the vertical backward integration of the distribution chain and even, in some cases, of production facilities. Large supermarket chains are often integrated backwards controlling the transport and distribution of the products through their own logistics platforms. In some cases, retailers also control the production of some products through the direct ownership of production facilities or through exclusive distribution agreements with manufacturers (that may or may not include the production of supermarkets' private labels).

50. Vertical integration of production facilities by supermarkets and private labels are not widespread phenomena in Latin America. However, there are cases of common ownership of production and retail facilities and also exclusive distribution agreements between manufacturers and retailers. A particular case is the case of OXXO, which is a convenience store chain with more than 13,000 points of sale in Mexico. OXXO was created by FEMSA, which owned Cervecería Cuauhtémoc Moctezuma, the second largest brewer in Mexico. OXXO was an exclusive distributor of FEMSA beer brands. In 2010, FEMSA sold its beer business to the multinational Heineken but maintained the exclusive distribution agreement through OXXO until 2020. The exclusive beer distribution agreements in Mexico have been investigated by the COFECE which set limits to such agreements (see Box. 6).

Box 6. Exclusive distribution agreements for beer in Mexico (2013)

In 2010, the beer multinational Heineken bought the second larger Mexican brewery Femsa Beer Business (which included beer brands such as Sol, Dos Equis, Indio...). Femsa also owned OXXO the largest convenience store chain in Latin America. OXXO distributed exclusively FEMSA's beer brands.

Under the terms of the deal, Heineken secured a 10 years extension of the exclusive distribution agreement with OXXO, which would only sell Heineken beers until 2020.

Initially, the Mexican CFC cleared the merger (and the exclusive distribution agreement). However, the Authority opened later a comprehensive investigation in the beer market, that was highly concentrated and where exclusive distribution agreements were widespread.

The Mexican beer market was controlled in Mexico by two companies, Grupo Modelo (AB Inbev) and Cuauhtémoc Moctezuma (now part of Heineken), which jointly accounted for 99 % of the market share. The two companies held exclusive dealing agreements with restaurants, bars and convenience stores (Modelo owned the convenience store chain Extra with more than 600 outlets).

The CFC concluded that the two companies monopolized the beer market in Mexico, and that exclusive agreements where hindering entry in the market. To resolve the issues, both brewers committed to limit the number of exclusive contracts with bars, restaurants and corner shops. However, exclusive agreements were allowed with convenience stores, hotels as well as sponsored events.

Under the agreement, the total number of exclusive contracts could not represent more than 25 % of either brewer's points of sale, and the volume of exclusivity contracts should be reduced to 20 % within five years time.

Source: CFC-08-2013. ESTABLECE LA CFC CONDICIONES A EMPRESAS CERVECERASPARA ABRIR EL MERCADO DE VENTA AL MENUDEO DE CERVEZA.

https://forumm.files.wordpress.com/2013/07/cfc-08-2013.pdf.

51. Finally, the the Uruguayan Comisión de Promoción y Defensa de la Competencia opened a case against the main supermarket chain in Uruguay for refusing to sell certain juices in its stores arguing that they only sold those products that were listed by Nielsen. Juice companies denounced Nielsen and Supermercados Disco, as they understood those companies wanted to exclude them from the market. The case was finally dismissed, as the Competition Authority did not find evidence of anticompetitive behaviour[35].

5. Conclusions

52. There is an increasing concern all over the world about the impact of supermarkets growth and concentration on consumer welfare. The modernisation of the distribution chain provides obvious benefits to consumers in the form of lower transportation and distribution cost and larger product availability. The subsequent process of industry concentration also involves competition risks: as the supermarket industry acquires a more important role in groceries retailing and becomes more concentrated, the risk of anticompetitive behaviour becomes higher.

35 ASUNTO Nº 7/2014: MISTERIL S.A Y MODINAR S.A. C/SUPERMERCADOS DISCO DEL URUGUAY S.A. Y NIELSEN URUGUAY – DENUNCIA https://www.mef.gub.uy/innovaportal/file/15684/2/resolucion-35-15-misteril-y-modinar-c-disco-y-otros.pdf

53. The main antitrust concerns in the supermarket industry relate to potential abuses of market power with exclusionary effects on smaller competitors and/or abuses of buyer power vis-a-vis suppliers. There are also concerns about the configuration of purchasing alliances between potential or actual competitors and the existence of sophisticated market-sharing and price-coordination mechanisms. The groceries retail industry is under close monitoring by competition authorities in several jurisdictions all over the world.

54. In Latin America, supermarkets are well represented in urban areas and remain as the main point of sale for groceries for the middle and high class. However, a large part of the population still shops in traditional shops and local markets. Supermarkets play a limited but increasingly important role in the groceries retailing map but, within the supermarket industry, the sector is highly concentrated and a small number of players hold large market shares and are present in several countries.

55. Competitive concerns have started to arise in several countries as supermarket chains expand and the industry becomes more concentrated. However, this does not affect all products: in a number of products, the industry concentration at manufacturer level is high and the exercise of market power is more likely to be observed at manufacturing level rather than at retail level. As it has happened in other countries, the expansion of supermarkets will imply a transfer of market power from manufacturers to retailers and the likelihood of observing anticompetitive conducts at retail level will increase.

56. At present, there has been limited intervention of Latin-American competition authorities in the groceries retail industry (apart from cases of consumer protection, unfair competition and mergers). Cases of abuse of a dominant position and horizontal agreements are more frequently observed at manufacturer level and vertical restraints are often imposed by large manufacturers rather than by retailers.

57. A number of authorities are starting to analyse in depth the structure of the industry and the risks for competition and consumer welfare. However, the number of cases strictly dealing with supermarkets behaviour is still limited. There are practically no cases of abuse in the supermarkets sector. Some countries have adopted a preventive strategy to avoid supermarkets squeezing suppliers and have introduced voluntary codes of conduct that regulate softly the relation between manufacturers and retailers (Mexico, Ecuador and Colombia).

58. Regarding horizontal agreements, a relatively sophisticated price agreement has been recently sanctioned in Uruguay and there is an on-going investigation in Chile against the four largest supermarket chains for the potential coordination of their pricing strategies. Surprisingly, there are few purchasing alliances between competitors in Latin America. Purchasing alliances might be procompetitive since they allow small supermarket chains to reach the necessary economies of scale and bargaining power that allow them to compete with larger supermarket chains. They might also rise competitive concerns if they involve coordination at retail level.

59. Finally, there are few vertical restraint cases where restrictions are imposed by retailers. In those products where exclusivity agreements exist, such agreements are often imposed by manufacturers rather than by retailers.

60. Supermarkets are gaining importance in Latin America. No doubt that their expansion will imply efficiency gains and will benefit consumers. But, their expansion also means higher industry concentration and the emergence of competition concerns. Competition authorities should be especially aware of the competitive risks that such process presents. The real challenge for competition authorities is how to promote the modernisation of the groceries retailing industry while guaranteeing that the market remains competitive and that consumers fully benefit from the modernisation process.

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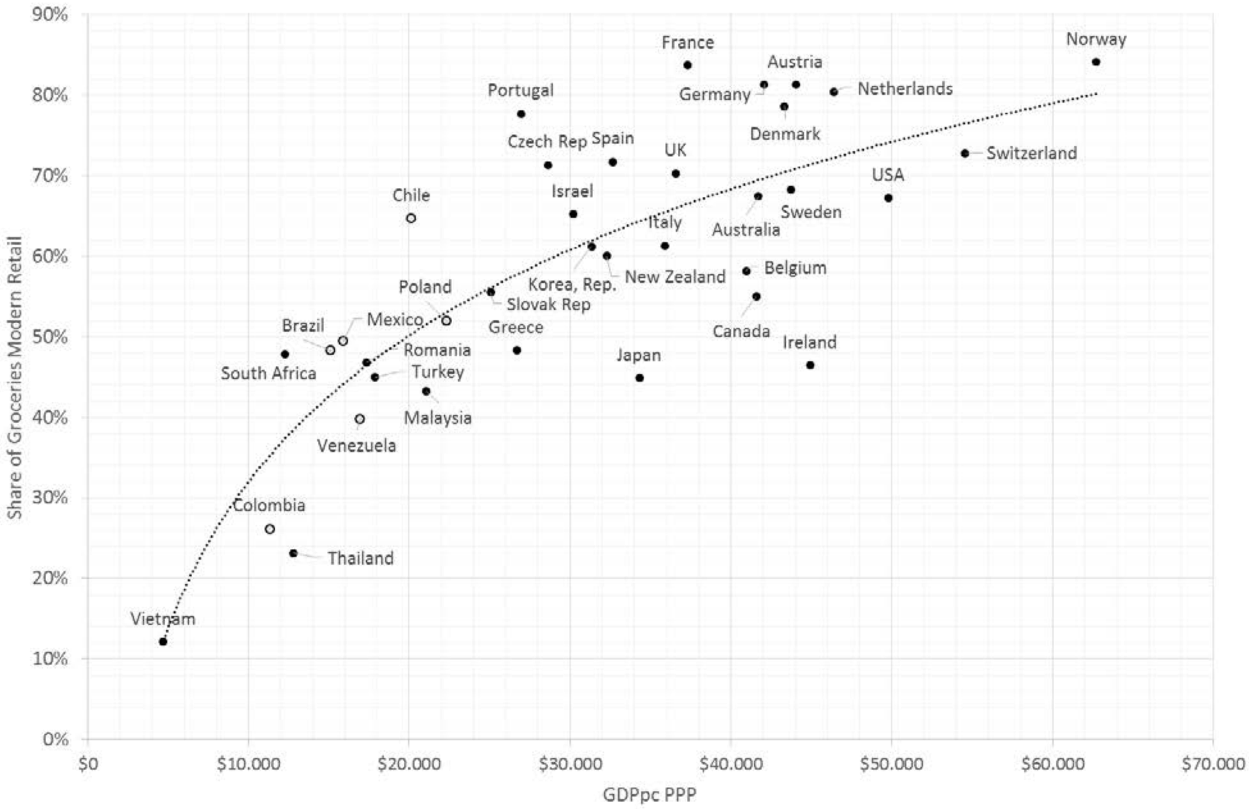
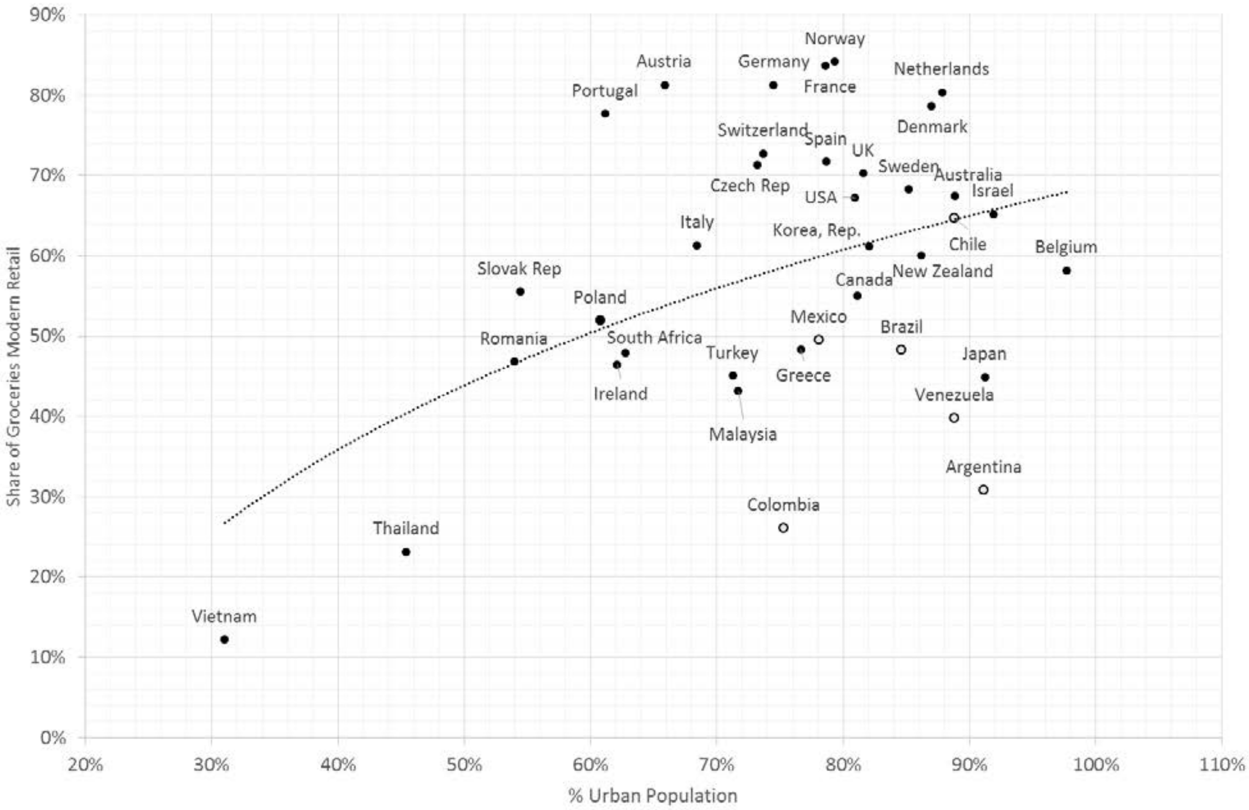
APPENDIX 1. DETERMINANTS OF THE SHARE OF GROCERIES MODERN RETAIL IN LATIN AMERICA

Figure 3. Share of Groceries Modern Retail and GDP per capita (PPP) (2011)



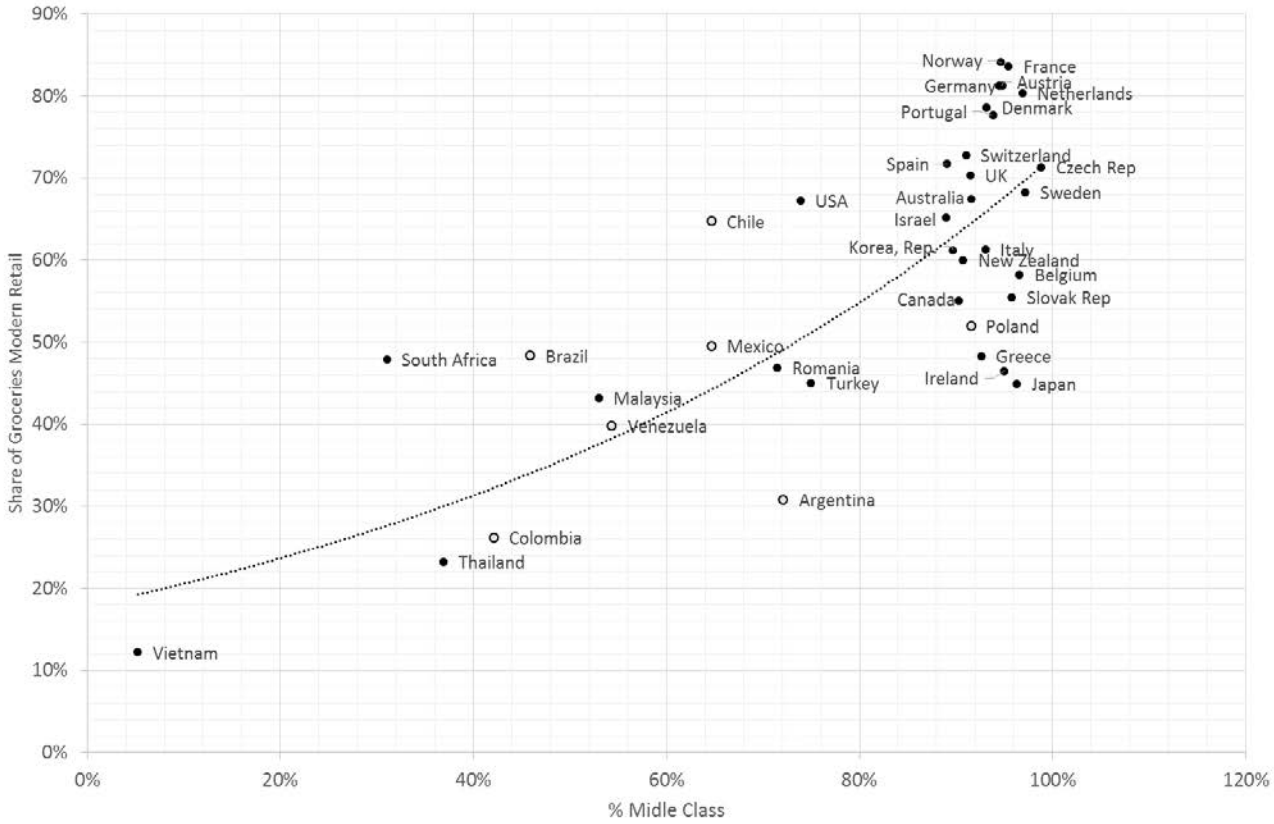
Source: Own elaboration based on Euromonitor and WorldBank.

Figure 4. Share of Groceries Modern Retail and Urban Population Rate (2011)



Source: Own elaboration based on Euromonitor and WorldBank.

Figure 5. Share of Groceries Modern Retail and Size of the Middle Class (2011)



Source: Own elaboration based on Euromonitor and WorldBank