

Presentation at the American Antitrust Institute Conference on  
"Buyer Power and Antitrust", Washington D.C. June 22nd, 2004

---



# Buyer Power in the EU

**Lars-Hendrik Röller\***  
**European Commission, DG Competition**

(\*) The views expressed are those of the author and not necessarily reflect those of the European Commission

# Outline

---



- I. Buyer Power in the EU Horizontal Merger Guidelines**
- II. Buyer Power: some basic economics**
- III. EU Case law and practice**
- IV. Policy implications**

# I. Buyer Power in the EU Horizontal Merger Guidelines

---



.....Buyer Power appears three times

- U **May harm consumers**

1. Creation or strengthening of buyer power in upstream markets (section IV.4)

- U **May benefit consumers**

2. Countervailing buyer power (section V)
3. Purchasing efficiencies (§62 and section VII in general)

# 1. Creation or Strengthening of Buyer Power in Upstream Markets

---



- s *“The merged firm may be in a position to obtain lower prices by reducing its purchase of inputs. This may, in turn, lead it also to lower its level of output in the final product market, and thus harm consumer welfare”*
- s *“Such effects may in particular arise when upstream sellers are relatively fragmented”*
- s *“Competition in the downstream markets could also be adversely affected if, in particular, the merged entity were likely to use its buyer power vis-à-vis its suppliers to foreclose its rivals”*

## 2. Countervailing Buyer Power

---



- s *“The Commission will consider to what extent customers will be in a position to counter the increase in market power that a merger would otherwise be likely to create”*
  
- s Three sources of countervailing buyer power :
  - s *“immediately switch to other suppliers”*
  - s *“credibly threaten to vertically integrate into the upstream market*
  - s *“sponsor upstream expansion”*

### 3. Purchasing Efficiencies

---



- s *“The Commission considers any substantiated efficiency claim in the overall assessment of the merger.” (§77) provided “efficiencies are to the benefit of consumers, merger-specific and verifiable.” (§78)*
  
- s *“Increased buyer power may be beneficial for competition. If increased buyer power lowers input costs without restricting downstream competition or total output” (§62)*



---

## **II. Buyer Power: some basic economics**

# Buyer Market Power - Monopsony Power

---



- U **Monopsony is the “mirror image” of Monopoly**
  - w upward sloping input supply curve, uniform posted prices
- U **Effects in Upstream Market**
  - w A monopsonist restricts its input purchases to reduce prices below competitive levels, creates allocative inefficiency
  - w Buyer extract supplier surplus
- U **Effects in Downstream Markets**
  - w Consumers do not benefit: reduced input prices do not lead to reduced output prices. Monopsonist reduces input purchases and output sales, leading to higher downstream prices (depends on analysis of: competing downstream firms ability to expand output, the degree of product differentiation, etc.)
- U **No allocative inefficiency if the monopsonist price discriminates perfectly. Only a redistribution effect.**



# Bilateral Market Power

---



- U **Assuming that either seller or buyer sets price and the other responds competitively is not appropriate**
- U **Trading partners will acknowledge mutual interdependence**
  - w Some input level will maximize combined profits (i.e. all the gains from trade)
  - w Buyer and Seller then bargain over the input price to split this maximum profit
  - w If bargaining is efficient there is no allocative inefficiency and no consumer harm
- U **The welfare consequences of bilateral market power may be less severe than the cases where market power is unopposed.**
  - w There may be bargaining costs

# Predatory Buying



- ⌋ **Buyers pay higher than competitive prices – analogous to a form of investment – in an effort to raise competing buyers' costs. Once competing buyers exist, recoupment through lower than competitive prices.**
- ⌋ **Standard**
  - w Predatory pricing standards may not be appropriate (buyers can engage in predatory buying and still sell output at a price that is above average variable costs).
  - w Economically sound standard: whether the price offered was in excess of the marginal revenue product
    - Ø requires focusing on the marginal productivity of one or more inputs
- ⌋ **What to do with the additional input?**
  - w Predatory buying combined with predatory pricing can be very effective to foreclose rivals but also very costly

# Analysis of Buyer Power under Downstream Concentration

---



## Effect on Consumer Welfare....

- W Analysis of market power in downstream markets
- W Analysis of efficiency gains (e.g. purchasing efficiencies)
- W Analysis of upstream markets

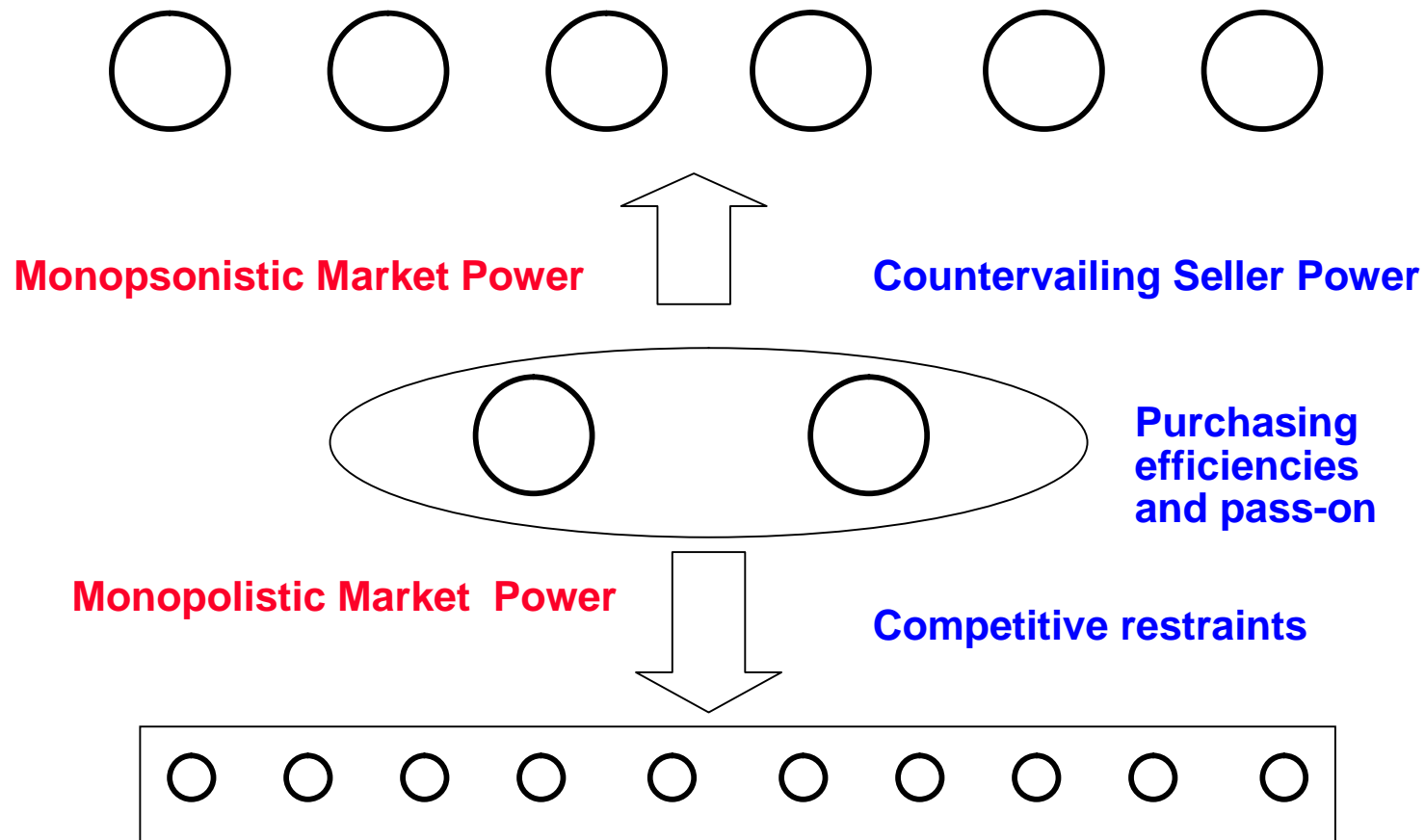
### 1. Buyers have market power relative to suppliers

- § Monopsonistic power => restrict output
- § Raising rivals costs (e.g. through predatory buying)

### 2. Sellers have market power relative to buyers

- § Countervailing seller power (not in the HMG)

# Creation or Strengthening of Monopsonistic and Monopolistic Market Power



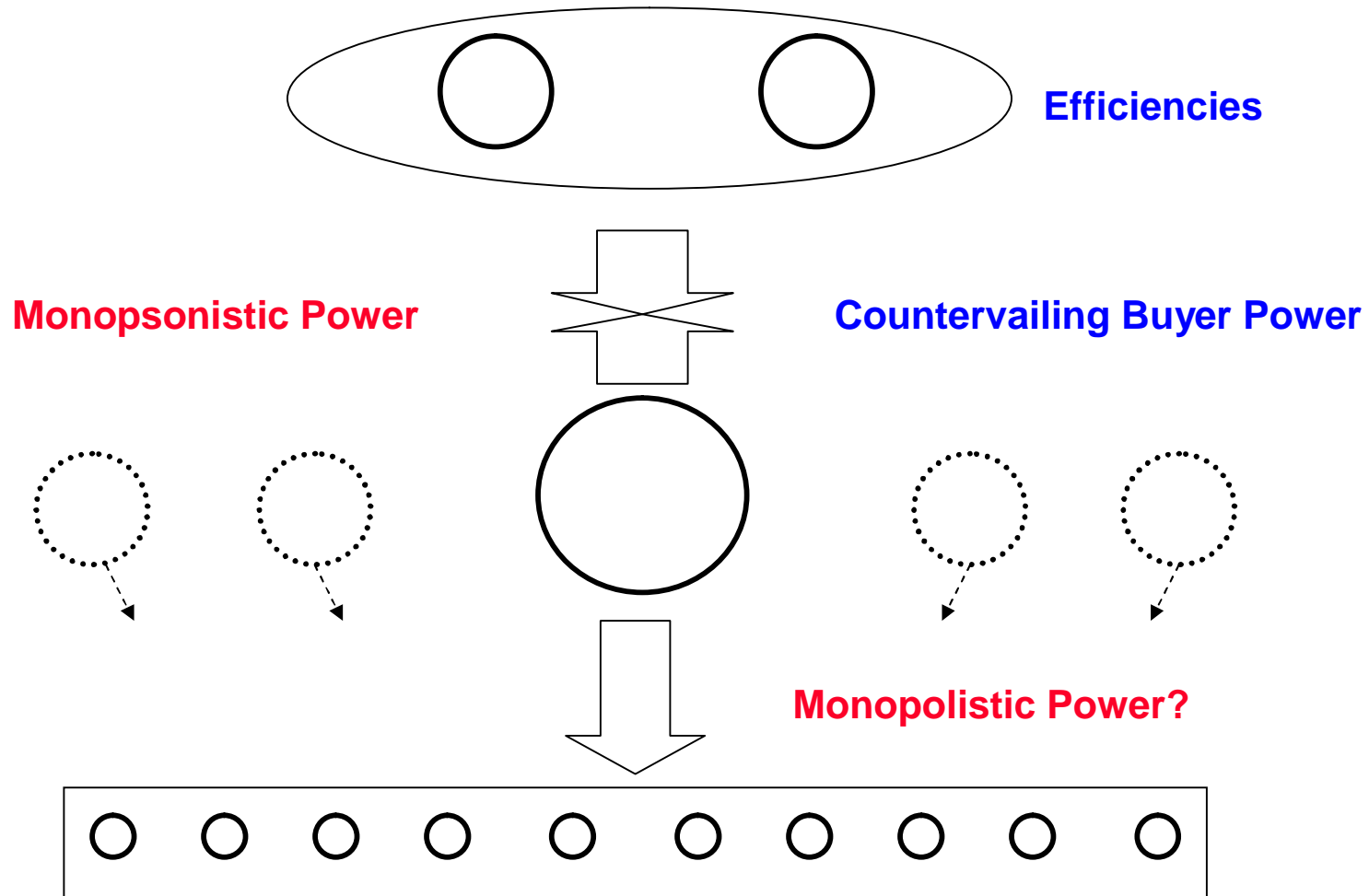
# Analysis of Buyer Power under Upstream Concentration

---



- W **Analysis of market power in downstream markets less important**
- W **Analysis of upstream markets**
  1. **When buyers have market power relative to suppliers**  
**=> countervailing buyer power (in the HMG)**
  2. **When sellers have market power relative to buyer**  
**=> effect on final consumer (Pass-on, efficiencies, etc.)**

# Creation or Strengthening of Seller Power





---

## **III. EU Case law and practice**

# Monopsonistic Power



## U **Kesko/Tuko (Nov 1996)**

- w Commission prohibited the merger of two large Finnish supermarket chains accounting for 55% of daily consumables retail space.
- w The merged entity would obtain lower input prices “to an extent that no rival could match” making new entry onto the market “more difficult”
- w Commission concluded that “Kesko’s purchasing power [over its suppliers]” would make it dominant in the retail market.

## U **Blokker/Toys “R” Us (June 1997)**

- w Commission prohibited the merger of two Dutch toy retailers accounting for 55-60% of Dutch toy sales.
- w Blokker’s power over suppliers enhanced by unmatched economies of scale in purchasing

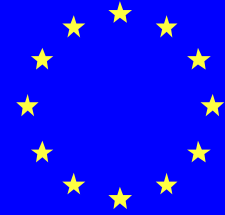
## U **Rewe/Meinl (Feb 1999)**

- w Merger of two Austrian firm retailers accounting for 30% of retail food sales. Approved with conditions.
- w Source of buyer power: a unique centralised structure to take full advantage of any efficiencies and economies of scale created by the merger



# Monopsonistic Power (2)

---



## U **Carrefour/Promodes (June 2001)**

- w No single firm dominance: combined share of around 30% of food retail distribution in France
- w Spiral effect: Buyer power -> discounts -> predation -> higher market shares -> increased buyer power

[The greater size of the merged firm would lead to a larger volume-related discount. This would enable it to offer lower prices, undercutting those offered by smaller rivals. This in turn would increase the merged firm's market share, which in turn would raise the volume of its purchases, which would enhance its buyer power through a higher volume-related discount and so on.]

# Countervailing Buyer Power



## U **Guinness/Grand Metropolitan**

- w small number of buyers account for large share of sellers profits
- w bargaining skill and technical ability to use buyer power
- w alternative suppliers are available

## U **Valeo/ITT**

- w major EU car producers exercise countervailing power over producers of automotive parts.

## U **Public Utility cases:**

- w Alcatel/Telettra: Telefonica was sole purchaser of telecom equipment in Spain
- w Thomson CSF/Deutsche Aerospace: military and defence case.
- w ABB/Daimler Benz: Offsetting monopsony power from Deutsche Bahn

## U **Coca-Cola/Carlsberg A/S: Countervailing power of retailers insufficient**

## U **GE/Honeywell: Airbus and Boeing compete fiercely and face a free-riding problem when it comes to sustain upstream competition in the long-term**



---

## **IV. Policy Implications**

## ... some Implications for Antitrust

---



- ⌋ **Monopsonistic power can raise important competition concerns**
- ⌋ **Markets must be defined from the sellers point of view**
- ⌋ **The distortion in the input market induced by a dominant buyer is greater, all other things equal:**
  - w The larger the dominant buyer's share of total purchases
  - w The lower the responsiveness of input supply to changes in input price (e.g. few alternative applications)
  - w The lower the ability of fringe buyers to increase purchases when input prices fall (e.g. capacity constrained)

# Buyer Power under a Consumer Standard

---



- When considering monopsonistic market power and the effect on consumers one must also analyze the degree of competition in downstream markets. This makes the analysis more complex.
- In reaching bargaining solutions there will likely be significant non-linearities in pricing and other constraints in contracts. Such aspects of contracts should not necessarily be treated with suspicion as they may increase efficiency
- The creation of countervailing seller power requires further consideration
- A proper efficiency analysis must identify the *source* of the input price reduction (*increased efficiency vs. restriction in input purchases*)

# A German's view on Buyer power

---



**SIR – After living in Germany for a decade, my husband and I relocated to Florida in 1998. We were both reluctant Wal-Mart shoppers at first. However, after the opening of a supercentre near our house, we hardly shop anywhere else. I can get everything under one roof and all at unbeatable prices.**

**Cynthia Spidell (Odessa, Florida)**

**Apr 29th 2004, From The Economist print edition**