

A report into the Monopolies and Mergers Commissions findings on Bird Eye Wall's conduct relating to the supply of wrapped ice cream

The case:

This case study concerns the Monopolies and Mergers Commission's report into Birds Eye Wall's Ltd. (BEW) distribution of wrapped ice creams in 1998. BEW were alleged to have been acting anti-competitively.

The details:

BEW in 1998 were the leading supplier of wrapped ice creams in the UK and had a market share of 70 per cent (Monopolies and Mergers Commission, 1998). Due to the Market power of BEW and its monopoly position within the wrapped ice cream market, BEW were able to use their power to dictate to their suppliers the conditions of supply they desired. When monopolies emerge there can be numerous problems, because the monopoly firm is the key player within the market and so can impose the conditions and the prices it desires upon the market. Monopolies gain the power to become price makers by restricting output. This can be done through various means; sometimes through naturally gained economies of scale or through vertical restraints or in some circumstances when backed up by force (bovination.com). All of these restrictions make it difficult for competition to survive, and so have the effect of deterring new entrants, and reducing competition. When output is restricted the price monopolies charge for the good is more than marginal cost, super normal profits are made, and so the product the monopoly sells is valued higher than what it is actually worth. This creates what is known as a deadweight loss for society and is not seen as favourable as 'Pareto optimality' is never achieved (Sloman, 2000).

The Monopolies and Mergers Commissions report was largely concerned with the distribution of wrapped ice creams and how the conditions BEW's imposed upon distributors in turn affected the supply of wrapped ice cream for immediate consumption to the end consumer.

All BEW wrapped ice creams were sold through wholesalers or dedicated distributors, BEW chose to distribute its wrapped ice cream primarily through dedicated distributors. The dedicated distributors stocked and distributed BEW's products only, and consequently, these distributors were given preferential terms and benefits over normal wholesalers who stocked BEW's as well as competitors products. Essentially this meant that BEW were selling the same product to its dedicated distributors at a lower cost than they were selling to its wholesalers. When a firm sells the same product at differing prices it is known as price discrimination (Sloman, 2000), and is seen as unfair and unjustifiable unless there is a benefit to society. BEW gave out discounts to its direct customers only when supply was done through a dedicated distributor. Similarly BEW also gave discounts to retailers who

purchased from dedicated distributors, but not to retailers who purchased from wholesalers who supplied competitors wrapped ice cream.

Were BEW's actions against the public interest?

As a result of BEW's chosen distribution system it meant that in order to buy BEW wrapped ice cream at the best price with preferential terms (e.g. exclusive freezer cabinets); supply had to come through a dedicated distributor. Obviously this had an impact upon the competition between wholesalers, as wholesalers who supplied BEW wrapped ice cream in addition to BEW competitors wrapped ice cream did not get as favourable price or conditions from BEW. At the time of the report this was skewing competition between wholesalers, because as BEW had a 70 per cent market share, wholesalers who stocked both BEW products and its competitors could not compete effectively on BEW products, so were often losing out on 70 per cent of the wrapped ice cream line of business. On top of this, the Monopolies and Mergers Commission research found that some retailers preferred to use only one distributor of ice-cream, and because BEW had 70 per cent of the market, inevitably many suppliers purchased from dedicated distributors who could supply them with the most competitive conditions. As a direct result of BEW giving discounts to direct customers through dedicated distributors, competitors wrapped ice creams were not being sold in some retail establishments.

BEW's chosen model of supply is a good example of a monopoly using its power and leverage to create barriers to squeeze out competition, and barriers to discourage entry within the market (Marvel and McCafferty, 1996). The Monopolies and Mergers Commission was established to ensure markets are competitive, and functioning as far as possible without vertical restraints that restrict competition. A vertical restraint refers to when a supplying firm imposes conditions to its supplier or customer (Sloman, 2000). Here it is evident that the vertical restraint within the case is BEW's selective distribution model. Although vertical restraints can be anti-competitive, they are not always necessarily, and it is only if the Monopolies and Mergers Commission finds the restraints working against public interest that the restraint will be deemed illegal.

Since BEW competitors wrapped ice cream were not being sold in some retail establishments, in effect consumer choice was reduced as a result of the way BEW chose to distribute. The commission's research showed that 44 per cent of outlets sold on only one brand of wrapped ice cream. The problem was not only limited to choice, the Monopolies and Mergers Commission attributed the lack of price competition at the retail level between manufacturers to have been influenced by BEW's anti-competitive behaviour.

In essence therefore, BEW used their distribution system as a vertical restriction. This restraint on supply could if it continued perpetuate the growth of BEW's market share, and so increase their already colossal power within the market. This vertical restriction is likely to have deterred potential entrants into the industry, and made it near impossible for entrants to establish distribution channels (Carlton

and Perloff, 1999). Without doubt, if retailers only wanted to have one supplier of wrapped ice cream, they would choose a supplier offering the majority of wrapped ice creams (BEW) at the lowest price. This meant to enter into the market of being a supplier of wrapped ice creams and within that role establishing channels of distribution, in competition to other suppliers, it would have proved a very difficult task, and the cost of entry into the market would have been raised substantially.

Were BEW's actions in favour of public interest?

Although at the outset of the case, it seems very clear that in fact the way BEW was behaving was anti-competitive, as the supply system seems to be a vertical restriction deterring entry and reducing consumer choice, in BEW's defence the distribution system set up was very effective. It was recognised at the time that there was a 'high standard of performance achieved by the dedicated distributors' (Monopolies and Mergers Commission, Birds Eye Wall's Ltd, p28). This business efficiency gained by BEW provides evidence that in fact this vertical restraint did have desirable effects. Carlton and Perloff (1999) comment that it is within the manufacturer's interest to distribute the product the cheapest way possible, as distribution is just seen as an input necessary to make a sale. The way in which BEW chose to distribute its wrapped ice creams was very efficient, thus some economists (such as the economists of the Harvard school of thought) would argue, that because BEW was doing what was most efficient, the savings made in distribution would be 'passed down the ladder' and thus in the long run benefit the consumer by lowering price or increasing services related to the product (Carlton and Perloff, 1999). Within the Commission's report, it is stated that there is no real competition on the retail level, however some would argue in theory, if BEW were allowed to keep on pursuing the same distribution, inevitably as the brand would be restricted among the retailers, competition across the brand would be encouraged, and thus retailers would have to compete with each other on price. Effectively this way of thinking would have meant that although BEW would maintain and grow in their monopoly position, the field of competition for BEW wrapped ice cream on the retail side would be over price. Price was an issue the Commission were concerned over, and if they had followed the Harvard school of thought, it would have benefited the consumer in terms of price as it would have led to reductions in price of the product as retailers competed over it.

Furthermore, it was also acknowledged by the Commission that inter brand competition decline within the wrapped ice cream market could not just be put down to BEW's supply system, as the impulse ice cream market as a whole was showing general signs of contraction. This fact could have led the Commission to allow BEW's actions to continue as it would have meant that competition on the retail level would have been over price. If the market was showing general signs of contraction anyway with inter brand competition, a decision to permit BEW's monopoly position to be maintained and grow, would not affect the long term future of the market, but encourage competition over price to happen sooner.

The Commissions verdict

The Monopolies and Mergers Commission found that the vertical restraints BEW were engaged in relating to distribution were restrictive to competition at the wholesale level, and reduced competition and choice at the retail level. BEW were instructed by the Commission by the 1st March 1999 to supply wholesalers on the same terms and conditions as their dedicated distributors and that the terms of supply should be fully terms transparent and to stop offering discounts to retailers which were only available when they purchased only from dedicated distributors.

The Commission also reported following their inquiry, that wider concerns at the whole wrapped ice cream market were made apparent during the research. As a result the Monopolies and Mergers Commission investigated the industry as a whole the following year.

Was the Commissions verdict correct?

When reviewing the Monopolies and Mergers Commission verdict, it can be seen they viewed BEW's monopoly position to be dangerous, and the distribution system outside the public interest. Whether or not this was a correct decision could be debated through the economical standpoints which have been touched upon so far. The Harvard side arguing market power and monopolies leads to efficiency in comparison to the Chicago school of thought arguing that restrictive measures should be emplaced to encourage business efficiency and competition within the market.

The true test as to whether or not the Monopolies and Mergers Commission made the correct decision is to be found by looking at how the market for wrapped ice creams has changed since the Commissions recommendations, and if the actions taken by the Commission were effective in reducing the power and leverage of BEW over its suppliers.

In 1998, BEW had a market share of 70 per cent, however following the Monopolies and Mergers Commission into distribution this has fallen consistently since 1998. As can be seen from the table on the next page, BEW has seen an estimated fall in sales of 24.9 per cent.

Figure 1: Manufacturers' shares in the wrapped impulse ice cream market, 1999-2001

	1999		2000		2001 (est)		% change 1999- 2001
	£m	%	£m	%	£m	%	
BEW	201	69	164	65	151	63	-24.9
Mars	32	11	33	13	31	13	-3.1
Nestlé	31	11	26	10	27	11	-12.9
Richmond/Treats	15	5	13	5	13	5	-13.3
Other brands	12	4	16	6	17	7	+41.7
Total	291	100	252	100	239	100.0	-17.9

Data may not equal totals due to rounding

Source: Mintel International Group Limited: Impulse Ice Cream - UK - February 2002

The Mintel report on impulse ice cream for 2002 concluded that the Commissions recommendations had loosened BEW's grip on the market. Indeed, when viewing the market now, it appears that the market is more open to competition, and this has been shown from the number of new entrants into the market. Cadbury's has recently entered the wrapped ice cream market after proving itself successful in the take-home ice cream sector. It is certain that the market has grown to be more competitive following the Commissions findings.

Mars was one of the companies that asked the Monopolies and Mergers Commission to investigate BEW's distribution policy, and they seem to have come off favourably as a consequence, as their market share increased 2% following the Commission's conclusions. Following the Commissions recommendations Mars was able to know for certain that its products could be distributed, and so it was able to launch new products and since 1999 has become very innovative. The market as a whole has become more innovative. In 2001, Mars launched four new products for the impulse ice cream sector, and similarly Nestle, Cadbury's and BEW have all launched new products. The BBC have commented post the Commissions decision and note that the market has been seen to have operated more fairly; as prices have fallen and variety and availability of rival brands has increased (BBC, 1999).

So, the market of wrapped ice cream has become fairer and more advantageous for the consumer; prices have fallen, and variety has increased. One can conclude therefore that the Monopolies and Mergers Commission recommendations were correct and have had the impact that was desired. In accordance therefore, one may ask the question whether as a rule one can assume that monopolies do not act within the public interest. Essentially the actions of the Commission were to limit and take away BEW's power within the wrapped ice cream industry. The issue of competition, and monopolies, oligopolies, perfect competition, and other models of competition is a highly contentious issue within Economics. Through this case study, it is obvious that the Monopolies and Mergers Commission decision to limit competition has been favourable for the market as a whole, however there are occasions where monopolies have had desirable impacts upon markets, and there are numerous ways in which monopolies can bring advantages to the consumer.

Gillmor (2003) acknowledges that monopolies can lead to innovation not happening as much under other competition models, however writes that monopolies can lead to stability within markets. However 'stability within markets' is only really desirable within technological markets, and the full weight of Gillmor's statement doesn't carry for markets such as impulse ice cream, stability is not really an issue. Nevertheless, there are still some 'pure' libertarians who believe that there should be no rules imposed to prevent monopolies. Economists with this view argue that in practice monopolies are not a problem at all, and that a monopoly occurs because of economies of scale, and these are actually beneficial. Realistically however with the case that has been examined, the Monopolies and Mergers Commission made a decision which has had a desirable impact on the market now. This therefore suggests that for the market of wrapped ice cream, a consumable good, a monopoly position is not desirable in order for there to be a good variety and low price. Discussed earlier was the Harvard school of thought, which in this case would argue that by allowing BEW to gain a complete monopoly position, the cost to the consumer of wrapped ice cream would be lowered as it would be the only way retailers could compete with each other. However if the Commission had taken the Harvard school of thought, although prices may have been lower, variety would not have increased to the extent it has done.

In hindsight therefore, the Monopolies and Mergers Commission appear to have made a decision that has had a good effect upon competition within the market place of wrapped ice creams. Since the Commission's report, the market has been plagued with fall in prices, innovation and new entrants, all contributing to a healthier, more competitive market. In economic terms this has meant that as the market has become less dominated by one monopoly, the price the consumer pays for the product has moved closer to marginal cost, so the deadweight loss to society has been reduced because the monopoly no longer has the power to restrict output. This has only happened as a direct result of the Monopolies and Mergers Commission actions in removing the vertical restraint that BEW were able to impose through their distribution system.

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